



Australian Government
Inspector-General of Taxation

Review into the Australian Taxation Office's Fraud Control Management

A report prepared at the request of the
Senate Economics References Committee

Inspector-General of Taxation

June 2018

Review into the ATO's Fraud Control Management

A report prepared at the request of the
Senate Economics References Committee

Inspector-General of Taxation

© Commonwealth of Australia 2018

ISBN 978-1-925504-89-7

Ownership of intellectual property rights in this publication

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

Creative Commons licence

With the exception of the Coat of Arms (see below), the IGT logo and ATO sourced material, this publication is licensed under a Creative Commons Attribution 3.0 Australia Licence.



Creative Commons Attribution 3.0 Australia Licence is a standard form licence agreement that allows you to copy, distribute, transmit and adapt this publication provided that you attribute the work. A summary of the licence terms is available from: <http://creativecommons.org/licenses/by/3.0/au/deed.en>. The full licence terms are available from <http://creativecommons.org/licenses/by/3.0/au/legalcode>.

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

Source: Licensed from the Australian Government Inspector-General of Taxation under a Creative Commons *Attribution 3.0 Australia* Licence.

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

Use of the Coat of Arms

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



Australian Government
Inspector-General of Taxation

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

GPO Box 551
Sydney NSW 2001

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

Dear Minister

Review into the ATO's Fraud Control Management

I am pleased to present you with my report of the above review which was commenced at the request of the Senate Economics References Committee and examines the ATO's management of internal and external fraud risks. This review was requested due to the events connected with Operation Elbrus and, necessarily, involves detailed examination of relevant ATO practices, procedures and structures to detect and address fraud and corruption risks.

The review has not found evidence of systemic internal fraud or corruption. The ATO, generally, has sound systems in place for managing risks of internal fraud, however, a number of areas have been identified which require improvement. Aspects of ATO's management of external fraud risks have also been examined, complementing other initiatives aimed at addressing tax and financial crime, for example the Phoenix and Black Economy Taskforces. In this regard, certain case studies were examined such as the ATO's response to alleged fraud in the precious metals industry as well as its management of tax evasion referrals from the community.

Overall, I have made 13 recommendations to the ATO, to all of which it has agreed in full or in part and some that it has advised have already been implemented. There is one recommendation for the Government to consider a review of the framework for interagency collaboration to combat tax crime.

I offer my thanks to taxpayers, tax practitioners, industry associations and professional bodies, academics, current and former ATO officers, legal and risk professionals as well as government agencies, such as the AFP, CDPP, AGD, ACLEI, AUSTRAC, ACIC, AIC and Department of Home Affairs, who contributed and supported this review.

Yours faithfully,

A handwritten signature in black ink, appearing to read 'Ali Noroozi', with a long horizontal line extending to the right.

Ali Noroozi
Inspector-General of Taxation

TABLE OF CONTENTS

- EXECUTIVE SUMMARY VII**
- LIST OF RECOMMENDATIONS XI**
- CHAPTER 1 – INTRODUCTION 1**
 - Conduct of the review 1
 - Focus of this review 3
 - Structure of this report 6
- CHAPTER 2 – BACKGROUND 9**
 - Fraud, corruption, integrity and conflict of interest 9
 - Risk management across the Commonwealth public service 12
 - The roles and responsibilities of key agencies 14
 - ATO’s Enterprise Risk Management Framework 17
 - International approaches 23
- CHAPTER 3 – PREVENTION OF INTERNAL FRAUD 35**
 - Maintaining integrity through recruitment and ongoing staff monitoring 35
 - Rotation of staff 54
 - Fraud training and awareness 57
 - Controls in relation to conflicts of interest 64
 - Controls in relation to senior officers’ intervention in cases 82
 - Controls in relation to settlements 87
 - Controls in relation to letters of comfort 92
 - Predictive models 95
- CHAPTER 4 – DETECTION OF AND RESPONSE TO INTERNAL FRAUD 103**
 - Detection methods 103
 - FPII investigations of internal fraud 114
- CHAPTER 5 – GOVERNANCE, STRUCTURE AND OVERSIGHT FOR MANAGING INTERNAL FRAUD RISK 129**
 - Governance arrangements, integrity framework & reporting 129
 - Expansion of the Private Groups & High Wealth Individuals business line 138
 - External oversight 141
- CHAPTER 6 – THE ATO’S APPROACH TO EXTERNAL FRAUD 145**
 - Prevention 145
 - Detection 155
 - Staff capability for criminal investigation 179
- CHAPTER 7 – INTERAGENCY COLLABORATION 183**
- APPENDIX A – TERMS OF REFERENCE 201**
- APPENDIX B – OPERATION ELBRUS 205**

APPENDIX C – OTHER RELEVANT REVIEWS	223
APPENDIX D – PRECIOUS METALS	227
APPENDIX E – ILLICIT TOBACCO TRADE	251
APPENDIX F – PANAMA PAPERS	257
APPENDIX G – PARADISE PAPERS	261
APPENDIX H – ATO RESPONSE	263
SHORTENED FORMS	265

EXECUTIVE SUMMARY

The Inspector-General of Taxation's (IGT) review into the Australian Taxation Office's (ATO) fraud control management was commenced at the request of the Senate Economics References Committee. It followed events connected to Operation Elbrus including allegations of tax fraud that may be linked to abuse of position by a public official.

The review has not found evidence of systemic internal fraud or corruption. Generally, the ATO has sound systems in place for managing risks of internal fraud, however, the review has uncovered a number of areas which require improvement.

One of the areas identified for improvement concerns the ATO controls to appropriately identify and manage conflicts of interest as inadequate management of such conflicts can lead to risk of corruption. In this regard, following Operation Elbrus, the ATO has made significant improvements to its staff instructions and guidance, however, further improvements are required.

The IGT is of the view that, in determining whether conflicts of interest has occurred, the ATO should consider the nature of the interest, such as the closeness of the personal relationship giving rise to a potential conflict, the seniority of the officers' roles and the nature of the official duties, such as relevant transactions or other responsibilities. A recommendation has been made which is aimed at ensuring undeclared conflicts are systematically captured, appropriate action is taken in respect of identified conflicts and former colleagues of current ATO officers do not obtain information or exert influence by reason of their previous association.

Another area identified as requiring improvement relates to senior ATO officer intervention in individual cases. A recommendation has been made to improve the transparency of such interventions by clearly specifying when they may occur, requiring appropriate documentation of all resulting actions in an accessible form and periodically reviewing compliance with such policies.

The IGT particularly considered the ATO's controls with respect to medium to high risk roles. A number of recommendations have been made such as periodic rotation of officers in these roles and bolstering the induction for new SES officers, recruited from outside the ATO, to focus on the ethical standards and highest levels of integrity that an organisation such as the ATO must exemplify.

Other IGT recommendations aimed at achieving significant improvements to the ATO's management of internal fraud risk include:

- bolstering the independence of its Audit and Risk Committee by ensuring that the majority of its members, including the chair are external to and independent of the ATO;
- maintaining the role of the Integrity Advisor and enabling ATO staff to discuss ethical or fraud related concerns with him or her;
- conducting periodic reviews of its corporate integrity indicators and providing results and actions arising from them to the Commissioner;

- strengthening the ATO's staff recruitment processes, ongoing checks and mandatory fraud awareness training to ensure its workforce maintains integrity and engenders continuing public confidence;
- acting on the advice, received from corruption risk experts, to improve its ability to detect internal fraud and corruption risks by such means as enhancing staff ownership of the risks;
- requiring staff to make contemporaneous notes of any requests made by one officer to another to access taxpayer information (so-called 'access by proxy');
- conducting periodic quality reviews of internal fraud investigations as well as the appropriateness of associated disciplinary actions;
- enhancing its analysis of behavioural events to assist in detecting serious misconduct; and
- increasing transparency of settlement processes.

The review also examined aspects of the ATO's management of the risks posed by external parties who seek to exploit the tax system and commit fraud against the Commonwealth ('external fraud'), in particular those attracting criminal sanctions. In this regard, the IGT examined certain areas and conducted case studies to identify areas of improvement which would complement other recent initiatives aimed at addressing tax and financial crime, for example the Phoenix and Black Economy Taskforces.

The specific areas examined include the ATO's tax evasion referral (TER) process which involves receiving and acting on intelligence provided by the community. It was already the subject of an IGT own-initiative investigation as a result of complaints made by dissatisfied taxpayers who had referred those they suspected of tax avoidance to the ATO. The IGT has concluded that TERs are a valuable source of information for detecting external fraud. A recommendation has been made for the ATO to formalise and document consistent processes, across all business lines, for dealing with TERs as well as better informing the public and reporting on resulting outcomes to enhance public confidence and thereby improve the quality and quantity of TERs.

Another area of particular focus in this review was the ATO's response to alleged fraud in the precious metals industry, where \$2.5 billion was estimated to be at risk due to weaknesses in the GST regime. The IGT found that there were lessons to be learnt from this experience such as identifying risks early and taking prompt whole of ATO action to prevent the propagation of fraud.

More broadly, the IGT has made recommendations to improve processes aimed at prevention of external fraud and these include ATO officers routinely considering whether the source of risks encountered in their case work are potential weaknesses in the system and ensuring that such risks and weaknesses are prioritised and investigated.

The review also considered ATO's collaboration with other agencies to combat serious tax crime. Through the Serious Financial Crimes Taskforce (SFCT), which is responsible for identifying and addressing the most serious and complex tax and financial crimes, law enforcement agencies and the ATO share information and coordinate their activities. Some recent steps have been taken to improve the quality of ATO referrals to the SFCT and the ATO's capability to conduct criminal investigations jointly with the Australian Federal Police (AFP). The IGT has identified further improvement opportunities and has recommended to the Government to review the current arrangements for interagency collaboration including

optimal models for sharing specialist capabilities and information as well as the management, structure and funding of taskforces.

In addition to the above recommendation to Government, the IGT has made a total of 13 recommendations to the ATO who has agreed with all them in whole or in part. The ATO has indicated that some of these recommendations have already been implemented and this would be verified by its Audit and Risk Committee. The implementation of the agreed recommendations should significantly bolster the ATO's management of fraud and corruption risks. However, the full benefit of the package of improvements may not be realised due to disagreement with certain aspects of recommendations.

In closing, it should be noted that the review has ensured that the matters, relating to Operation Elbrus, which are currently before the courts have not been prejudiced in any way. To this end, relevant parts of this report were provided to the AFP and the Commonwealth Director of Public Prosecutions for their consideration and their comments have been taken into account.

LIST OF RECOMMENDATIONS

RECOMMENDATION 3.1

The IGT recommends the ATO:

- a) *conduct a risk assessment of every position in the organisation to determine the level of pre-employment and ongoing checks required and periodically reassess the risk associated with moderate to high risk positions;*
- b) *use criminal intelligence databases to determine whether candidates for high risk positions are known to law enforcement, either by reason of their own conduct or that of their associates or relatives;*
- c) *as part of its pre-employment checks:*
 - i) *depending on the level and types of risk associated with the relevant position, require candidates to provide declarations about matters such as their financial circumstances; and*
 - ii) *request information, such as that relating to misconduct, from previous employers of external candidates; and*
- d) *require all employees to make an annual disclosure about matters that are assessed in the pre-employment checks of their current position and periodically check such disclosures at a frequency rate reflective of the risk associated with the relevant position.*

RECOMMENDATION 3.2

The IGT recommends the ATO formalise its fraud risk controls relevant to SES officers and officers in high risk roles including the periodic rotation of officers.

RECOMMENDATION 3.3

The IGT recommends the ATO strengthen its fraud awareness and ethics training by:

- a) *requiring new staff to complete the mandatory fraud training during their induction process and prior to allowing them access to taxpayer information;*
- b) *withdrawing access to ATO systems for contractors who fail to complete the mandatory training package within a reasonable timeframe;*
- c) *incorporating into the assessments of mandatory training packages, a series of practical scenarios that requires staff to apply ethical principles;*

RECOMMENDATION 3.3 (CONTINUED)

- d) requiring managers to discuss with new starters ethical matters as they apply to their work area, including by way of practical scenarios, and ensuring that those managers receive sufficient guidance and support for this process to take place shortly after new starters have completed the mandatory fraud training; and*
- e) increasing the level of staff interaction in its mandatory fraud training particularly those delivered by the Fraud Prevention and Internal Investigations unit.*

RECOMMENDATION 3.4

The IGT recommends that the ATO:

- a) update its conflict of interest guidance document to clarify ambiguities and provide further explanation, including practical examples, as well as require officers to register their conflicts of interest as soon as they become aware of them;*
- b) bolster its processes for ensuring that former colleagues of current ATO officers do not obtain information or exert influence by virtue of their previous associations;*
- c) improve awareness and compliance with its conflict of interest policies and guidance including through its active promotion by the Commissioners and other senior executives;*
- d) conduct periodic reviews on the central conflicts of interest register to identify trends, verify the accuracy of the declared information as well as ensure that the appropriate management actions have been taken to address the conflict; and*
- e) seek ways to capture and analyse information for detecting undeclared conflicts of interest as part of some of its existing checks as well as from other sources.*

RECOMMENDATION 3.5

The IGT recommends the ATO improve the policies regarding senior officer intervention by:

- a) specifying the circumstances in which senior officers are authorised to intervene in individual matters;*
- b) where senior officers receive requests to intervene in matters outside their area of responsibility, requiring such requests to be transferred to their counterpart in the relevant area;*
- c) requiring intervening officers to document the initial request and all subsequent actions, including the details of decisions made, supporting reasons and resulting outcomes as well as briefings provided to the original decision maker on a single centralised system and in a form which is transparent and easily accessible; and*
- d) periodically reviewing senior officers' compliance with such policies.*

RECOMMENDATION 3.6

The IGT recommends that the ATO publish more information about its Independent Assurance of Settlements process such as identified improvement opportunities and work undertaken to implement them.

RECOMMENDATION 3.7

The IGT recommends the ATO consider incorporating, into its Organisational Behavioural Assessment process, other data sets including employees' technology usage and conflicts of interest disclosures.

RECOMMENDATION 4.1

The IGT recommends the ATO improve its ability to detect internal fraud and corruption by such means as:

- a) acting on the advice it received in its 2017 Corruption Risk Review, including requiring each business line to describe, in detail, potential fraud and corruption events in their area;*
- b) retrospectively analysing events surrounding any significant internal fraud case and recording all findings and resulting actions in one central library for future use; and*
- c) contemporaneous recording of officers' requests to access information about a particular taxpayer and ensuring availability of such records to its Fraud Prevention and Internal Investigations Unit.*

RECOMMENDATION 4.2

The IGT recommends that, with respect to its internal fraud investigations, the ATO:

- a) periodically review the appropriateness of sanctions imposed;*
- b) conduct appropriate and periodic external and internal quality assurance reviews and publish the results of such reviews;*
- c) provide more public information about the investigation process such as timeframes and procedural safeguards; and*
- d) develop a formal complaints handling process as well as inform its staff about the process and how such complaints may be lodged.*

RECOMMENDATION 5.1

The IGT recommends the ATO strengthen its oversight of internal fraud risks by:

- a) bolstering the independence of its Audit and Risk Committee by ensuring that, at the very least, the majority of its members, including the chair, are external to and independent of the ATO;*
- b) maintaining the role of the Integrity Advisor and providing him or her with all necessary access and support as well as enabling ATO staff to discuss ethical or fraud related concerns with him or her;*
- c) requiring the Assistant Commissioner of Fraud Prevention and Internal Investigations to regularly report internal fraud risk trends and issues to the Commissioners and other ATO Executives;*
- d) conducting periodic reviews of the ATO's corporate integrity indicators and providing the results and actions arising from them to the Commissioners and other ATO Executives; and*
- e) augmenting the existing induction program for new SES officers, recruited from outside the ATO, with specific training on ethical standards and the highest level of integrity expected at such an organisation.*

RECOMMENDATION 6.1

The IGT recommends that the ATO improve the prevention of external fraud by:

- a) requiring its officers to routinely consider whether risks encountered in their case work indicate a potential weakness in the system, ensure such risks are promptly prioritised and investigated as well as publicly reporting the outcomes where appropriate; and*
- b) improving its media strategy to increase the reporting of its tax crime investigations, prosecutions and recoveries of proceeds of crime.*

RECOMMENDATION 6.2

The IGT recommends the ATO:

- a) better inform the public about making tax evasion referrals including by specifying the type of information required and assuring them of confidentiality;*
- b) formalise and document consistent processes, across all business lines, for dealing with tax evasion referrals; and*
- c) publically report aggregate data about the outcome of its investigations of tax evasion referrals including the extent to which they give rise to compliance activities, any identified trends and the most common types of referrals.*

RECOMMENDATION 6.3

The IGT recommends that the ATO consider:

- a) reporting ATO officer referrals, about potential fraud, which have led to successful prosecution along with appropriate recognition; and*
- b) requiring all its officers to complete more in-depth training about the range of behaviours and events which may be indicators of fraud being perpetrated.*

RECOMMENDATION 7.1

The IGT recommends that Government consider a broad review of the current arrangements for interagency collaboration for combating tax fraud including the following key issues:

- a) optimal models for information sharing between agencies;*
- b) the extent to which specialist capabilities should be shared amongst agencies and mechanisms to ensure that each agency has appropriate access to such capabilities;*
- c) structure and funding for interagency taskforces including whether they should be headed by an independent leader with appropriate powers and secretariat;*
- d) permitting the ATO to use telecommunication interception information obtained in joint investigations of prescribed taskforces in raising assessments for those who are subjects of such investigations; and*
- e) in appropriate circumstances, allowing the ATO to issue production orders to third parties such as financial institutions who hold relevant information about persons or transactions of interest.*

CHAPTER 1 – INTRODUCTION

CONDUCT OF THE REVIEW

1.1 On 20 June 2017, the Senate Standing References Committee on Economics (the Committee) requested that the Inspector-General of Taxation (IGT) review the Australian Taxation Office's (ATO) fraud control management. This request followed certain events including those relating to Operation Elbrus and allegations of tax fraud that may be linked to an abuse of position by a public official.

1.2 The IGT accepted the Committee's request on 27 June 2017 and shortly afterwards commenced this review.¹ In doing so, the IGT acknowledged the Committee's concerns and that the community is entitled to expect the highest level of integrity in the administration of the tax system. Such a review would be aimed at restoring community confidence by providing independent assurance and making recommendations for improvement as necessary.

1.3 The IGT invited and received many submissions² to this review from a broad range of stakeholders. The IGT also met with them including academics, legal and risk professionals as well as taxpayers, tax practitioners and their representative bodies.

1.4 To gain a better understanding of the issues and areas requiring further investigation, the IGT also held discussions with current and former ATO officers³ as well as senior staff in other Commonwealth government agencies such as the Australian Federal Police (AFP), Attorney-General's Department (AGD), Australian Commission for Law Enforcement Integrity (ACLEI), Australian Transaction Reports and Analysis Centre (AUSTRAC), Australian Securities and Investments Commission (ASIC) and Australian National Audit Office (ANAO).

1.5 The issues raised in the above submissions and discussions were further tested during the IGT's analysis of ATO controls, processes and procedures. This analysis included examining case records on the ATO's case management system, Siebel, ATO internal fraud investigation case files as well as related statistics. The IGT also interviewed ATO officers across a range of business units including Fraud Prevention and Internal Investigations (FPII), Public Groups and International (PGI), Private Groups and High Wealth Individuals (PGH), ATO Corporate (ATOC), ATO People (ATOP) and other business lines.

1.6 It should be noted that whilst this review considers both internal and external risks of fraud and corruption, there is a stronger focus on the internal risks given that it

¹ The review was commenced pursuant to paragraph 8(3)(d) of the *Inspector-General of Taxation Act 2003*.

² Terms of reference are reproduced in Appendix A of this report.

³ In accordance with subparagraph 8(2A)(b)(iii) of the *Ombudsman Act 1976* which applies by virtue of subsection 15(h) of the *Inspector-General of Taxation Act 2003*.

was initiated largely due to the events related to Operation Elbrus. In addition, there are other reviews and processes dealing with risks of external fraud such as the Phoenix Taskforce⁴ and the Black Economy Taskforce⁵. The discussion of external risks in this review is limited mainly to the work the IGT has conducted in this area to date as well as a brief consideration of some specific issues.

1.7 Importantly, the review was conducted in a manner which ensured that the prosecutions, commenced as a result of Operation Elbrus, were not prejudiced in any way. For example, before finalisation of the review, the relevant parts of this report, including Appendix B were provided to the AFP and Commonwealth Director of Prosecutions (CDPP) for their consideration and comment all of which have been taken into account. Furthermore, the IGT has expressed no views on whether the events connected to Operation Elbrus amounted to fraud or corruption as this is a matter for the courts.

1.8 The review has found no evidence of actual internal fraud or corruption of a systemic nature. Generally, the ATO has sound systems in place for managing risks of internal fraud and, specifically, in relation to Operation Elbrus, they did restrict unauthorised access to taxpayer information. However, the detailed examinations of relevant ATO practices, procedures and structures and how they are enforced has identified a number of areas that require improvement, some of which are already being addressed as a result of reviews which the ATO itself has undertaken since Operation Elbrus.

1.9 Given the public interest in Operation Elbrus and related issues, Appendix B sets out, in some detail, the IGT's understanding of the relevant events. In summary, Operation Elbrus concerns a joint agency operation to investigate an alleged tax evasion syndicate. It is understood that the syndicate may have used a payroll service provider as a vehicle to obtain approximately \$157 million of Pay As You Go (PAYG) amounts, withheld from payments to thousands of contractors, and other taxes. A phoenix type arrangement may have been employed to dissipate assets through a complex process under the insolvency laws.

1.10 Operation Elbrus revealed that two of the alleged key syndicate members were children of the ATO's then Deputy Commissioner for the PGH business line. The latter was also the Chair of the Government's Phoenix Taskforce.⁶ The PGH business service line is the very area in the ATO tasked with investigating 'those who criminally defraud the [tax] system or deliberately avoid their tax obligations' and collaborates with regulatory and law enforcement agencies in doing so.⁷ The Deputy Commissioner was subsequently charged with abuse of position of a public official.

⁴ The Hon. Kelly O'Dwyer, MP, Minister for Revenue and Financial Services, 'A comprehensive package of reforms to address illegal phoenixing' (Media release, 12 September 2017); Australian Government, *Budget Paper No. 2* (May 2018) p 37.

⁵ See, the Treasury, 'Black Economy Taskforce Overview' <www.treasury.gov.au>.

⁶ Commonwealth, *Inquiry into insolvency in the Australian construction industry*, Senate Economics References Committee, 28 September 2015, p 26 (Deputy Commissioner of the PGH business line).

⁷ Commissioner of Taxation, *Annual Report 2016-17* (2017) p 59.

FOCUS OF THIS REVIEW

1.11 As mentioned earlier, the main focus of this review is internal integrity or internal fraud risks. The IGT has avoided directly commenting on specific matters in Operation Elbrus as they are currently before the courts. However, events relating to Operation Elbrus, as well as concerns raised by stakeholders and the IGT's own analysis have led this review to consider risks including the following:

- the suitability of personnel for the roles they perform including vetting and consideration of an officer's family or associates;
- length of time staff remain in high risk roles;
- risk awareness, or integrity, culture including training;
- conflicts of interest;
- unauthorised access by ATO officers, related security controls and senior officer intervention in ATO compliance activities; and
- ATO capability in detecting and investigating staff fraud and misconduct.

1.12 As mentioned already, this review also considers risks of external fraud but to a lesser extent. It draws on recent IGT work in this area. For example, at the time that this review was commenced, a separate IGT review was being conducted into Goods and Services Tax (GST) refunds verification.⁸ In that review, one aspect of the ATO's approach to fraud in the precious metals industry was examined. The broader risks of fraud in this industry have been explored in this review together with the ATO's treatment approach including interagency collaboration – refer to Appendix D.

1.13 Similarly, as a result of a number of complaints being made to the IGT, an investigation was already initiated into the ATO's management of tax evasion referrals (TERs) by the community before the commencement of this review.⁹ Given their direct relevance to this review, the results of that investigation are incorporated into Chapter 6 of this report.

1.14 This review also briefly considers the ATO's approach to certain other compliance risks, such as illicit tobacco and offshore tax evasion, as was exposed by the Panama Papers leaks. It also examines cooperation with other agencies to deal with financial crime, including information sharing arrangements.

Relevant IGT investigations

1.15 During the review, the IGT received a number of complaints which alleged or suggested ATO fraud and/or corruption. Such complaints were investigated where sufficient information was provided, or could be obtained, to at least make initial inquiries. The investigations were conducted in parallel to this review and insights from them have also been incorporated into this report.

⁸ Inspector-General of Taxation (IGT), *Review into GST Refunds* (2018).

⁹ The investigation was commenced pursuant to subsection 8(1) of the *Inspector-General of Taxation Act 2003*.

1.16 Where complaints were made anonymously, insufficient information was provided or the IGT had no other means of verifying the concerns, broader inquiries were made during the review to determine whether ATO controls were sufficiently robust to deal with the allegations raised. Any identified weaknesses were treated as areas requiring improvement. Complaints which related to previous ATO practices or processes were treated in the same manner, i.e. the allegations were tested against current practices.

1.17 The remainder of complaint investigations that raised valid concerns were isolated instances and did not, of themselves, suggest criminal culpability, for example, an ATO officer's conduct in private interactions with members of the public. The ATO has confirmed consideration of disciplinary action in such cases and the IGT used the insights in these cases as part of a broader consideration of the ATO's culture regarding integrity issues.

Relevant reviews by other agencies

1.18 In conducting this review, the IGT also considered a number of reviews and inquiries conducted by other bodies and agencies including those conducted by the ATO itself. The key reviews are described below whilst a list of reviews which were also considered, together with a short description, is provided in Appendix C.

ATO internal reviews

1.19 Subsequent to the events in Operation Elbrus, the ATO commenced a number of reviews relating to the detection and investigation of internal fraud risks. These include the following:

ATO Corruption Risk Review (2017)

1.20 The objective of this ATO commissioned review¹⁰ was to evaluate the current areas of corruption risk within the ATO and to identify potential areas of emerging risk to inform future mitigation efforts. It was found that whilst the ATO's FPII unit was a key pillar in the ATO's corruption resistance framework, the ownership of corruption risk was also concentrated in that unit rather than being more widely accepted by the ATO's business lines as a shared responsibility.

The ATO September 2017 Report

1.21 The ATO September 2017 Report was the outcome of an internal review¹¹ which examined the ATO's arrangements in relation to conflicts of interest, security clearances and positions of trust to assess whether they appropriately addressed integrity risks. A number of recommendations were made including improvements to

¹⁰ Professor David Lacey and Jane Bailey, 'ATO Corruption Risk Review 2017', report to the ATO (2017).

¹¹ Australian Taxation Office (ATO), 'Review of ATO Conflict of Interest and Security Clearance Processes - Management Initiated Report' (Internal ATO document, 6 September 2017).

how conflicts of interest are reported and monitored as well as a need to identify high risk roles and associated controls beyond those related to security clearances.

Phoenix Taskforce

1.22 The issue of combatting illegal phoenix activity was the subject of an interagency government taskforce with a range of proposed measures recently being announced by the Government.¹² Accordingly, in this report, the IGT has only provided some information on these issues, allowing some time for the measures to be implemented and bear fruit before making further recommendations.

Black Economy Taskforce Report

1.23 The Black Economy Taskforce has examined issues which overlap with those in the terms of reference for this review and the IGT has sought to complement the matters raised in the Taskforce's report.¹³

Performance audit of the ATO's use of settlements

1.24 The ANAO has recently conducted a performance audit of the ATO's settlement of tax liabilities with a number of recommendations being made.¹⁴ Once again, some time should be afforded before further review of the processes involved in such ATO activities. However, it is noted that it may be necessary for the IGT to review ATO senior officers' assessment of 'litigation risk' in the future. The ATO's key control in this respect is the retrospective analysis conducted by retired judges in major settlement cases. It is noted that very few cases have been subjected to this process thus far.¹⁵

Review of the Public Interest Disclosure Act 2013

1.25 The Public Interest Disclosure (PID) regime, which enables current or former public servants' allegations of misconduct or wrongdoing to be reported and investigated, was recently reviewed by the Department of the Prime Minister and Cabinet. This review found that whistleblowers did not have a positive experience after making a disclosure and that the relevant agencies believe the *Public Interest Disclosure Act 2013* (PID Act) has been difficult to apply. One of the recommendations involved certain agencies, including the IGT, being considered as 'investigative agencies' to encourage disclosers to come forward.¹⁶ Elements of the PID regime are discussed in this report where relevant.

¹² Above n 4, pp 37–38.

¹³ The Treasury, *Black Economy Taskforce – Final Report* (October 2017).

¹⁴ Australian National Audit Office (ANAO), *ANAO Report No. 21 2017–18 Performance Audit - The Australian Taxation Office's Use of Settlements* (2017).

¹⁵ Above n 7, p 68.

¹⁶ Mr Philip Moss, 'Review of the Public Interest Disclosure Act 2013', report to the Government (15 July 2016) p 13 rec 2.

Australian Commission for Law Enforcement Integrity—inquiry into jurisdiction

1.26 A Parliamentary Joint Committee inquiry into the jurisdiction of ACLEI considered whether the ATO should be included within ACLEI's remit.¹⁷ The inquiry recommended an independent assessment of the ATO's corruption risk profile, together with an examination of the feasibility of including the ATO within ACLEI's jurisdiction. The current role of ACLEI is explained in more detail in Chapter 5.

STRUCTURE OF THIS REPORT

1.27 This report is divided into two main sections: internal fraud and external fraud. However, the IGT recognises that fraud and corruption events may result from the convergence of these two risks. This is also known as 'complex fraud'.¹⁸ For example, an outsider intending to commit external fraud may seek the assistance of an ATO officer to commit internal fraud such as providing tip-offs to evade detection. This report addresses such convergence in the most relevant sections.

1.28 Chapter 2 of the report begins by explaining a range of integrity-related concepts, such as fraud, corruption and conflict of interest. It proceeds by describing the Commonwealth Fraud Control Framework, including the role of other key Commonwealth government agencies, followed by the general ATO arrangements under that framework. Finally, a summary of relevant approaches adopted by other revenue agencies in comparable jurisdictions is outlined.

1.29 Chapters 3 and 4 of the report consider issues relating to internal fraud and corruption risks, including those raised by Operation Elbrus, and the discussion is aligned with the broad requirements of the Commonwealth Fraud Control Framework, namely:

- fraud and corruption prevention measures (Chapter 3), including:
 - controls in recruitment processes and vetting of staff more generally;
 - rotation of staff into other roles;
 - risk awareness culture including training;
 - management of conflicts of interest;
 - appropriateness of senior officer intervention in audits and reviews;
 - integrity of settlement decision-making and issuing of letters of comfort; and
 - prevention through predictive models; and

¹⁷ Joint Committee on the Australian Commission for Law Enforcement Integrity, Parliament of Australia, *Inquiry into the jurisdiction of the Australian Commission for Law Enforcement Integrity* (5 May 2016).

¹⁸ Attorney-General's Department (AGD), *Preventing, detecting and dealing with fraud, Resource Management Guide No. 201* (August 2017) p 7 para [20].

- fraud and corruption detection and response (Chapter 4), including:
 - the FPII unit's detection methods and investigations; and
 - the ATO's Fraud and Corruption Control Plan.

1.30 Chapter 5 is the final chapter that discusses internal fraud and corruption issues and it focuses on governance and oversight.

1.31 The last two chapters of this report (Chapters 6 and 7) focus on key risks posed by external parties who seek to exploit weaknesses in the tax system for their own gain. Chapter 6 examines the ATO's own prevention, detection and response whilst the ATO's collaboration and cooperation with other agencies in addressing major external fraud risks is examined in Chapter 7.

CHAPTER 2 – BACKGROUND

2.1 This chapter describes a number of key concepts such as what constitutes fraud, corruption and conflict of interest, before considering the Commonwealth Fraud Control Framework and the role of other key Commonwealth agencies within the Framework. The ATO's own fraud risk management and governance arrangements are also explained, followed by a summary of approaches to fraud risk management adopted by other revenue agencies in comparable jurisdictions.

FRAUD, CORRUPTION, INTEGRITY AND CONFLICT OF INTEREST

2.2 Those trusted with regulatory power are expected to exercise that power effectively and ethically. Public confidence is lost when institutions are ineffective in fulfilling their public role or fail to address unethical staff conduct. As a result, an institution loses its legitimacy and power to engender voluntary compliance with the laws that it regulates.

2.3 Unethical behaviour, such as fraud and corruption, threatens the funds available to deliver public goods and services, distorts the decision-making process of public officials, weakens public confidence in Government and undermines the financial integrity of public institutions. In a 2017 Australian Institute of Criminology (AIC) report¹⁹, Commonwealth losses attributable to fraud had totalled approximately \$1.203 billion over four financial years, from \$119 million in 2010–11 increasing to \$673 million in 2013–14. However, over this period, Commonwealth agencies had only recovered \$75.3 million previously lost to fraud and the number of reported incidents more than doubled, rising from 52,127 in 2010–11 to 110,698 in 2013–14, with the most common types of external fraud related to government entitlements, including revenue, visa/citizenship and social security frauds.

2.4 The main types of unethical behaviour, namely: fraud, corruption and conflict of interest, are described in more detail below.

Fraud

2.5 In a criminal law context, fraud has been defined as 'dishonestly obtaining a benefit, or causing a loss, by deception or other means'²⁰, for example, theft or knowingly providing false or misleading information to the Commonwealth, or failing to provide it when there is an obligation to do so.²¹

¹⁹ Australian Institute of Criminology (AIC), *Fraud against the Commonwealth: Report to Government 2013–14* (2017).

²⁰ *Criminal Code Act 1995* s 134.2.

²¹ AGD, *Commonwealth Fraud Control Framework 2017* (2017) p C7 para [15].

2.6 The 'benefits' obtained may be tangible, such as obtaining monetary benefits, or intangible, such as obtaining information. A benefit may also be obtained by a third party through unauthorised disclosure of information or provision of access.²²

2.7 'Dishonesty' focuses on a person's intent and is based on whether a reasonable person would consider an act or omission to be honest or dishonest at the time it occurs. Therefore, accidents and inefficient work practices would not meet the definition of fraud.²³

2.8 In the tax context, fraud may be contrasted with 'non-compliance' whereby activities such as a taxpayer incorrectly reporting their income may be the subject of administrative penalties by the ATO without the need to establish the taxpayer's state of mind. Fraud, by contrast, may be prosecuted through the criminal justice system and requires evidence of actual intent to obtain a benefit through dishonest means.²⁴

Corruption

2.9 In the Australian Public Service (APS) context, corruption has been defined as 'the abuse of a public position for private gain' or 'the dishonest or biased exercise of a Commonwealth public official's functions'.²⁵ Such conduct amounts to 'abuse of public office', which is a criminal offence, where:

- (a) the public official:
 - (i) exercises any influence that the official has in the official's capacity as a Commonwealth public official; or
 - (ii) engages in any conduct in the exercise of the official's duties as a Commonwealth public official; or
 - (iii) uses any information that the official has obtained in the official's capacity as a Commonwealth public official; and
- (b) the official does so with the intention of:
 - (i) dishonestly obtaining a benefit for himself or herself or for another person; or
 - (ii) dishonestly causing a detriment to another person.²⁶

2.10 Other examples of corrupt conduct include bribery, embezzlement, insider trading, nepotism or cronyism.²⁷

²² *ibid.*

²³ *ibid.*

²⁴ McLaren, J, 'The distinction between tax avoidance and tax evasion has become blurred in Australia: Why has it happened?' (2008) 3(2) *Journal of Australasian Tax Teachers Association* p 143.

²⁵ Senate Select Committee on a National Integrity Commission, Parliament of Australia, *Report* (2017) paras [2.5] and [2.6].

²⁶ *Criminal Code Act 1995* s 142.2.

²⁷ AGD, *Managing the insider threat to your business* (2014) p 6.

2.11 The Senate Select Committee on a National Integrity Commission also noted that ‘corruption’, and ‘corrupt conduct’ carry different meanings in different contexts.²⁸

2.12 It could be said, therefore, that corruption refers, not to a particular offence necessarily, but rather to a range of behaviours which may or may not amount to criminal conduct. Although an event may amount to both fraud and corruption, not all cases of corruption will amount to fraud nor will all cases of fraud involve corruption. Fraud and corruption can also involve collusion between officials and external parties who work together in secret for a dishonest purpose.²⁹ As noted by the Victorian Independent Broad-based Anti-corruption Commission:

When a public servant can be persuaded to cooperate with a criminal group, they offer the group ongoing access while employing inside knowledge of the public bodies’ systems to avoid detection. Obtaining information and access from insiders is an efficient and cost-effective means of facilitating major criminal enterprises.³⁰

Conflict of interest

2.13 A conflict of interest arises when an official’s interest or relationship, real or perceived, conflicts with a duty they hold or where they have a role that conflicts with another role.³¹ For example, a conflict of interest may arise where:

- a decision maker considers an appeal of a decision which they had made;
- an official has family or intimate personal relationships with a person they are supervising in the workplace; or
- an official is considering a decision which may benefit or cause detriment to that official or to a person to whom they are related or with whom they have a relationship.³²

2.14 Real or perceived conflicts of interest may adversely affect an official’s or agency’s integrity or reputation.³³ Public confidence in the Government may be jeopardised if the public perceives that officials are working to serve their own agendas.³⁴ The Organisation for Economic Co-operation and Development (OECD) notes that it is not practical to prohibit public officials from having private interests but recognises that ‘an unresolved conflict of interest may result in abuse of public office.’³⁵

²⁸ Above n 25, para [2.8].

²⁹ ATO, ‘Fraud Awareness e-Learning Training Booklet – Text Version’ (Internal ATO document, undated) p 11.

³⁰ Victorian Independent Broad-based Anti-corruption Commissioner, *Organised crime group cultivation of public sector employees* (2015) < www.ibac.vic.gov.au>.

³¹ ANAO, *Managing Conflicts of Interest in FMA Agencies* (2014) para [1.7].

³² Independent Commission Against Corruption (ICAC) NSW, ‘Conflicts of interest’, <www.icac.nsw.gov.au>.

³³ Above n 29, p 16.

³⁴ Australian Public Service Commission (APSC), ‘In whose interests? Preventing and managing conflicts of interest in the APS’ (23 October 2013) <www.apsc.gov.au>; APSC, ‘Values and Code of Conduct in practice Section 5: Conflict of interest’ (August 2017) <www.apsc.gov.au>.

³⁵ Organisation for Economic Co-operation and Development (OECD), *Managing Conflict of Interest in the Public Sector: A Toolkit* (2005) p 96.

2.15 It should be noted that bias is not the same as a conflict of interest as a bias can affect a public official's judgment irrespective of any conflict of interest. For example, an official conducting job interviews may place importance on a university education and will therefore have a bias towards candidates who have completed their university degree. The public servant, however, may not have any financial or other interest with universities. As such they may make a biased decision to hire a candidate with a university education without any conflict of interest.

2.16 Unlike fraud and corruption, conflicts of interest may not amount to a criminal offence. However, it may evidence unethical conduct which attracts a disciplinary sanction as APS employees are required to:

- take reasonable steps to avoid any conflict of interest (real or perceived) in connection with their APS employment; and
- disclose details of any material personal interest in connection with their employment.³⁶

2.17 Before turning to how the ATO manages the specific risks of fraud and corruption, this report considers a range of other factors that influence how Commonwealth agencies generally manage risks including fraud and corruption.

RISK MANAGEMENT ACROSS THE COMMONWEALTH PUBLIC SERVICE

2.18 Commonwealth public service agencies have general risk management obligations under the *Public Governance, Performance and Accountability Act 2013* (PGPA Act) which is administered by the Department of Finance. Each agency gives effect to these requirements by setting out its expectations of staff decision-making and conduct through corporate policies known as Chief Executive Instructions (CEIs).³⁷ They are lawful directions to staff for the purposes of the *Public Service Act 1999*.³⁸ Staff who do not comply with the CEIs may be in breach of the APS Code of Conduct³⁹, potentially resulting in the imposition of disciplinary sanctions.⁴⁰ Non-compliance by contractors may result in breach of the terms of their contract with the ATO.⁴¹

2.19 Section 16 of the PGPA Act requires an 'accountable authority', which is the Commissioner in the case of the ATO, to establish and maintain an appropriate system of risk oversight and management.⁴² To that end, the Commonwealth Risk Management Policy⁴³ requires Commonwealth entities, such as the ATO, to comply with nine elements in order to satisfy this part of the PGPA Act. One of these elements is the mandatory establishment of a risk management framework that provides 'the

³⁶ *Public Service Act 1999* s 13(7).

³⁷ APSC, *Building better governance* (2012).

³⁸ *Public Service Act 1999* s 13(5).

³⁹ The APS Code of Conduct is set out in *Public Service Act 1999* s 13.

⁴⁰ *Public Service Act 1999* s 15.

⁴¹ ATO, 'Chief Executive Instructions - Corporate Governance (CEI 2014/11/02)' (Internal ATO document, 3 November 2014).

⁴² *Public Governance, Performance and Accountability Act 2013* s 16.

⁴³ Department of Finance, *Commonwealth Risk Management Policy* (2014).

arrangements for designing, implementing, monitoring, reviewing and continually improving risk management throughout the entity.⁴⁴

2.20 The PGPA Act also authorises the making of rules through legislative instruments such as the *Public Governance, Performance and Accountability Rule 2014* (PGPA Rule). Section 10 of the PGPA Rule requires Commonwealth entities to take 'all reasonable measures to prevent, detect and deal with fraud relating to the entity.' This section, known as 'the Fraud Rule', also lists specific requirements such as the need for the agency to develop and implement a fraud control plan.⁴⁵

2.21 The Fraud Rule forms part of the Commonwealth Fraud Control Framework administered by the AGD.⁴⁶ The Commonwealth Fraud Control Framework consists of:

- the Fraud Rule, which is described above;
- the Fraud Policy⁴⁷, which sets out procedural requirements for specific areas of fraud control such as investigations and reporting; and
- the Fraud Guidance⁴⁸, which all agencies are expected to follow, as appropriate, in meeting the requirements of the Fraud Rule and Fraud Policy.⁴⁹

2.22 Commonwealth agencies publicly demonstrate their compliance with the Commonwealth Fraud Control Framework by reporting on fraud control matters in their Annual Reports⁵⁰ and reporting⁵¹ information on fraud perpetrated against the Commonwealth to the AIC by 30 September each year. Such reporting, however, is not required to include incidents of suspected fraud, incidents under investigation and whether the fraud was proven or not although reporting agencies are encouraged to do so.⁵²

2.23 There is no specific requirement for agencies to report fraud matters to their responsible Minister. However, there is a legislative requirement that the Minister be kept informed about significant issues that may affect the agency⁵³, for example, information regarding fraud risks.⁵⁴

⁴⁴ *ibid.*, para [14].

⁴⁵ *Public Governance, Performance and Accountability Rule 2014* s 10(b).

⁴⁶ AGD, 'Fraud Control' <www.ag.gov.au>.

⁴⁷ The Fraud Policy is also known as the Commonwealth Fraud Control Policy: above n 21.

⁴⁸ Above n 18.

⁴⁹ Above n 21.

⁵⁰ *Public Governance, Performance and Accountability Act 2013* s 17AG.

⁵¹ AGD, *Commonwealth Fraud Control Policy* (2016) paras [12] and [14].

⁵² Above n 18, para [93].

⁵³ *Public Governance, Performance and Accountability Act 2013* s 19.

⁵⁴ Above n 21, para [94].

THE ROLES AND RESPONSIBILITIES OF KEY AGENCIES

2.24 The Fraud Policy and Fraud Guidance sets out the roles and responsibilities of key agencies some of which, as well as those of other relevant bodies, are outlined below.

Attorney-General's Department

2.25 The AGD is responsible for providing high level policy advice to the Government about fraud control arrangements within Commonwealth agencies. This includes developing and reviewing general policies of Government with respect to fraud control, such as the Commonwealth Fraud Control Framework, advising agencies about the content and application of those policies, and reporting to Government on compliance with the Fraud Rule.⁵⁵

Australian Federal Police

2.26 The AFP is the primary law enforcement agency for the Commonwealth and its responsibilities include investigating serious or complex fraud against the Commonwealth.⁵⁶ If a fraud is not serious or complex, the affected agency will remain responsible for investigating that fraud.⁵⁷

2.27 Agencies must refer all instances of potential serious or complex fraud offences to the AFP in accordance with the Australian Government Investigation Standards (AGIS)⁵⁸ and AFP referral process. However, agencies are not required to make such referrals if legislation sets out alternative arrangements or where agencies have the capacity, appropriate skills and resources needed to investigate the matter as well as meet the AGIS requirements for evidence gathering and the Commonwealth Department of Public Prosecutions' (CDPP) requirements in preparing briefs of evidence.⁵⁹

2.28 Generally, where a referral is made to the AFP, the referring agency completes an AFP Referral Form and sends it to the AFP Operations Monitoring Centre in the State or Territory in which the suspected offences occurred. In exceptional circumstances where immediate action by the AFP is required, the AFP will consider the referral over the telephone but a written referral must follow within 24 hours.⁶⁰ Referrals are considered in accordance with the criteria set out in the AFP Case Categorisation and Prioritisation Model (CCPM) in deciding whether to undertake an

⁵⁵ Above n 18, p C5.

⁵⁶ *ibid.*

⁵⁷ *ibid.*, para [71].

⁵⁸ Above n 51, para [4].

⁵⁹ *ibid.*, para [8].

⁶⁰ Australian Federal Police (AFP), 'Referrals - Referring matters to the AFP - services for government' <www.afp.gov.au>.

investigation into the matter, undertake a joint investigation with the agency or reject the referral.⁶¹

2.29 For the ATO, however, there are specific processes which prescribe how such referrals may be made to the AFP and how their priority is determined. These processes are set out in detail in Chapter 6.

Australian Commission for Law Enforcement Integrity

2.30 The ACLEI assists the Integrity Commissioner to detect, investigate and prevent corrupt conduct in designated Government agencies with law enforcement functions.⁶² The ATO is not subject to ACLEI's jurisdiction. In administering the tax laws, however, the ATO does access information of other law enforcement agencies which do fall under ACLEI's jurisdiction.

Australian National Audit Office

2.31 The ANAO audits the financial statements of Commonwealth agencies and may conduct performance audits to assess how agencies meet their fraud control responsibilities.⁶³ For example, the ANAO conducted a performance audit on the ATO's fraud control arrangements in 2000 as well as a broader performance audit of fraud control arrangements for selected Commonwealth entities in 2014.⁶⁴

Commonwealth Director of Public Prosecutions

2.32 The CDPP is responsible for prosecuting offences against Commonwealth law.⁶⁵ Agencies are encouraged to consider criminal prosecution in appropriate circumstances as an important deterrent to future instances of fraud and to educate the public generally about the seriousness of fraud.⁶⁶ Agencies are also encouraged to take reasonable measures to recover financial losses from fraud through proceeds of crime and civil recovery processes or through administrative remedies.⁶⁷

2.33 When referring matters to the CDPP for consideration of prosecution action, agencies are encouraged to prepare briefs in accordance with the guidelines for dealings between Commonwealth investigators and the CDPP.⁶⁸

2.34 Where a brief of evidence has been referred to the CDPP, the brief will be examined to decide whether a prosecution should be instituted and, if so, on what

⁶¹ ANAO, *Fraud Control in Australian Government Entities* (2011).

⁶² Above n 18, p C5.

⁶³ *ibid.*

⁶⁴ ANAO, *Fraud Control Arrangements, Across Entities, Performance Audit, 2014* (2014).

⁶⁵ Above n 18, p C5.

⁶⁶ Above n 21, para [83].

⁶⁷ *ibid.*, para [86].

⁶⁸ Referred to in above n 18, p 83.

charge or charges.⁶⁹ In addition to the evidentiary requirements for prosecution, the CDPP has the discretion to consider whether it is in the public interest to prosecute the offender(s). The factors for such consideration vary from case to case, but may include:⁷⁰

- whether the offence has been determined to be serious or trivial in nature based on the agency's case selection and prioritisation policies;
- the need for deterrence; and
- the likely outcome in the event of a finding of guilt.

Australian Institute of Criminology

2.35 The AIC is responsible for conducting an annual fraud survey of agencies and producing reports on fraud against the Commonwealth, the compliance of Commonwealth agencies with the Commonwealth Fraud Control Framework as well as fraud trends.⁷¹ In doing so, the AIC must annually report on fraud against the Commonwealth and fraud control arrangements within six months of receiving the information it collects from agencies.⁷²

Australian Securities and Investments Commission

2.36 The ASIC regulates Australian companies, financial markets, financial services organisations and professionals who deal with and advise on investments, superannuation, insurance, deposit-taking and credit under a number of Commonwealth laws. ASIC uses enforcement powers to detect and deal with unlawful conduct and responds to breaches of law ranging from minor regulatory offences through to serious misconduct.⁷³

Commonwealth Ombudsman

2.37 The Commonwealth Ombudsman's role includes monitoring the operation of the PID Act.⁷⁴

Parliament

2.38 Parliament, and its committees, also perform a key role in scrutinising all government activities including fraud or corruption-related matters.

⁶⁹ Commonwealth Director of Public Prosecutions (CDPP), *Prosecution Policy of the Commonwealth* (2008) s 3.4, p 11.

⁷⁰ CDPP, *Prosecution Policy of the Commonwealth – Guidelines for the making of decisions in the prosecution process* (2014).

⁷¹ Above n 18, p C5.

⁷² Above n 51, para [13].

⁷³ Above n 18, p C5.

⁷⁴ Commonwealth Ombudsman, 'Public Interest Disclosure scheme' <www.ombudsman.gov.au>.

ATO'S ENTERPRISE RISK MANAGEMENT FRAMEWORK

2.39 Pursuant to the Commonwealth Risk Management Policy, the ATO's Enterprise Risk Management Framework comprises of a range of components including a risk matrix, to assist with rating risk according to likelihood and consequence, and a risk register to record different categories of risk hierarchically.⁷⁵

2.40 During the review, the ATO began to change its risk management framework. However, to date, not all risks and responsibilities have been migrated to the adjusted framework and, in any event, the risks and responsibilities relevant to this review are likely to remain substantially the same. Accordingly, this report refers to the framework prior to the commencement of such migration.

2.41 The risk register contains 21 'Level 0' risk categories within which are more specific 'Level 1' risks.

2.42 In accordance with the third element of the Commonwealth Risk Management Policy⁷⁶, the ATO allocates responsibilities for the each of these Level 1 risks to various officers within the ATO. These include a Senior Executive Service (SES) Band 1 officer as the 'risk steward' who is responsible for 'managing a discrete risk population or group (risk pool) within an enterprise risk category' and an executive level (EL) officer as the 'risk manager' who has day-to-day responsibility for managing that risk.⁷⁷

2.43 For example, under the Level 0 risk category 'Major Tax Integrity Threats', there are Level 1 risks such as 'Aggressive Tax Planning', 'Cash Economy' and 'Tax Crime'. Under 'Tax Crime' are four risks, namely: GST Evasion, Phoenix, Refund Fraud and Tax Crime. The risk of Tax Crime is described as the 'Failure to adequately identify and respond to major criminal threats to Australia's tax and superannuation system which have the potential to undermine community confidence in the integrity of the system'.⁷⁸ The risk steward for Tax Crime is the Assistant Commissioner (SES Band 1) for the Tax Evasion and Crime (TEC) area whilst the risk manager is a Director (EL officer) within the Tax Crime Risk Management unit. Both of these positions are located within the PGH business line. Further information about how the ATO addresses the Tax Crime risk is contained in Chapter 6.

2.44 Similarly, the Level 0 risk 'Governance', contains the Level 1 risk 'Internal Fraud and Corruption' which is described as 'Failure to minimise internal fraud and corruption through timely and effective prevention, detection and investigative activities'.⁷⁹ The risk steward is the Assistant Commissioner for the FPII unit (the FPII Assistant Commissioner), whilst the risk manager is a Director within that unit.

⁷⁵ Information about the ATO's management of enterprise risk was also explored in the IGT's *Review into aspects of the Australian Taxation Office's use of compliance risk assessment tools* (2013) Chapter 2.

⁷⁶ Above n 43, para [15].

⁷⁷ ATO, 'Chief Executive Instruction 2015/03/01 Risk Management' (Internal ATO document, 16 March 2015).

⁷⁸ ATO, 'Risk Register, Tax Crime Risk Level 1' (Internal ATO document, ATO database, accessed January 2018).

⁷⁹ ATO, 'Risk Register, Internal Fraud and Corruption Level 1' (Internal ATO document, ATO database, accessed January 2018).

2.45 The risk register captures other details about the risk such as any mitigation details or risk assessments which may be attached as documents. In relation to the Internal Fraud and Corruption risk, for example, one of the documents included is the Fraud and Corruption Control Plan. This plan is discussed later in this chapter.

2.46 By contrast, for 'Privacy' risks⁸⁰, which is a Level 1 risk, the mitigation details refer to the CEI on Privacy and Taxpayer Confidentiality. The following section addresses the role of CEIs within the ATO.

ATO's Chief Executive Instructions

2.47 The Commissioner has issued a number of CEIs giving instructions to staff in a variety of areas such as asset management, work health and safety as well as a range of integrity-related issues such as conflicts of interest⁸¹ and appropriate access to taxpayer records.⁸²

2.48 For example, the CEI 2014/05/08 on 'Internal Fraud and Corruption' requires ATO staff to:

actively [assist] in preventing, detecting and reporting internal fraud and corruption by:

- Ensuring your mandatory training for dealing with fraud and ethics is complete and remains current
- Referring any suspicion of fraud and corruption to either your manager, or [the FPII unit], leaving a message on the ... hotline ... or completing the Anonymous Fraud Alert Form
- Not overlooking fraud or corruption, not hindering an investigation, and not attempting to investigate fraud or corruption yourself. If you have any concerns talk to your manager or Fraud Prevention and Internal Investigations
- Complying with the APS Code of Conduct including behaving honestly and not making improper use of inside information
- Participating in fraud control activities, such as risk assessment activities
- Respecting the confidentiality of others who may report or are involved in a fraud investigation
- Assisting and supporting fraud and corruption reporting, investigation and prosecution, including providing information or acting as a witness.⁸³

⁸⁰ Described as 'The failure of ATO staff and/or contractors to prevent taxpayer information from being unlawfully collected, used or disclosed.'

⁸¹ ATO, 'Chief Executive Instruction 2014/06/10 Conflict of Interest' (Internal ATO document, 12 October 2017).

⁸² ATO, 'Chief Executive Instruction 2014/04/02 Access to Taxation Records in the Possession of the Commissioner' (Internal ATO document, 16 April 2014).

⁸³ ATO, 'Chief Executive Instruction 2014/05/08 Internal Fraud and Corruption' (Internal ATO document, 29 January 2015).

ATO Fraud and Corruption Control Plan

2.49 The ATO has developed a fraud control plan as required by the Fraud Rule. Consistent with developments in international and Australian standards⁸⁴, the ATO's fraud control plan also addresses corruption as a risk and, accordingly, it is known as the Fraud and Corruption Control Plan.⁸⁵ This publicly available document sets out the range of ATO strategies to prevent, detect and respond to internal and external fraud and corruption risks as well as the associated oversight and reporting mechanisms.⁸⁶ These strategies include:

fraud and corruption prevention strategies that are targeted at building a strong integrity culture within the ATO, and fraud awareness in those who interact with the ATO [which] is based on [a number of factors, including]: a strong awareness of what fraud is and what to do about it;... robust recruitment and vetting processes ...[; and] regular training and communication...

... fraud and corruption detection activity [that] is based around [the following including]: system monitoring and scanning, and associated control scenarios ... systematic review and analysis of fraud referrals to identify possible trends ... a strong culture of reporting, and awareness of how to report [; and] ...PIDs... [which are made by those who suspect wrongdoing by ATO officers]...

...[responding] in the following ways [including]: assessment of all reports and allegations to determine an appropriate response;... undertaking investigations in accordance with [AGIS; and] pursuing disciplinary, administrative, civil or criminal actions as appropriate...⁸⁷

2.50 The Fraud and Corruption Control Plan also considers that all ATO officers have an obligation to report incidents of suspected fraud or corruption and provides the details for the community and law enforcement agencies to report suspected tax crime regarding external fraud.⁸⁸ The obligation for ATO officers to report external fraud is also outlined in the CEI on Tax Crime and External Fraud which imposes a number of requirements including the responsibility for staff to refer suspected tax crime matters, after consultation with their manager, to the TEC area within PGH.⁸⁹

2.51 Since the 2014-15 financial year, the ATO has reviewed its Fraud and Corruption Control Plan annually.

⁸⁴ Standards Australia, *Australian Standard AS 8001-2008 Fraud and Corruption Control* (2008).

⁸⁵ A fraud control plan is required by s 10(b) of the Fraud Rule. However, agencies may incorporate corruption risks into their plans to create a fraud and corruption control plan.

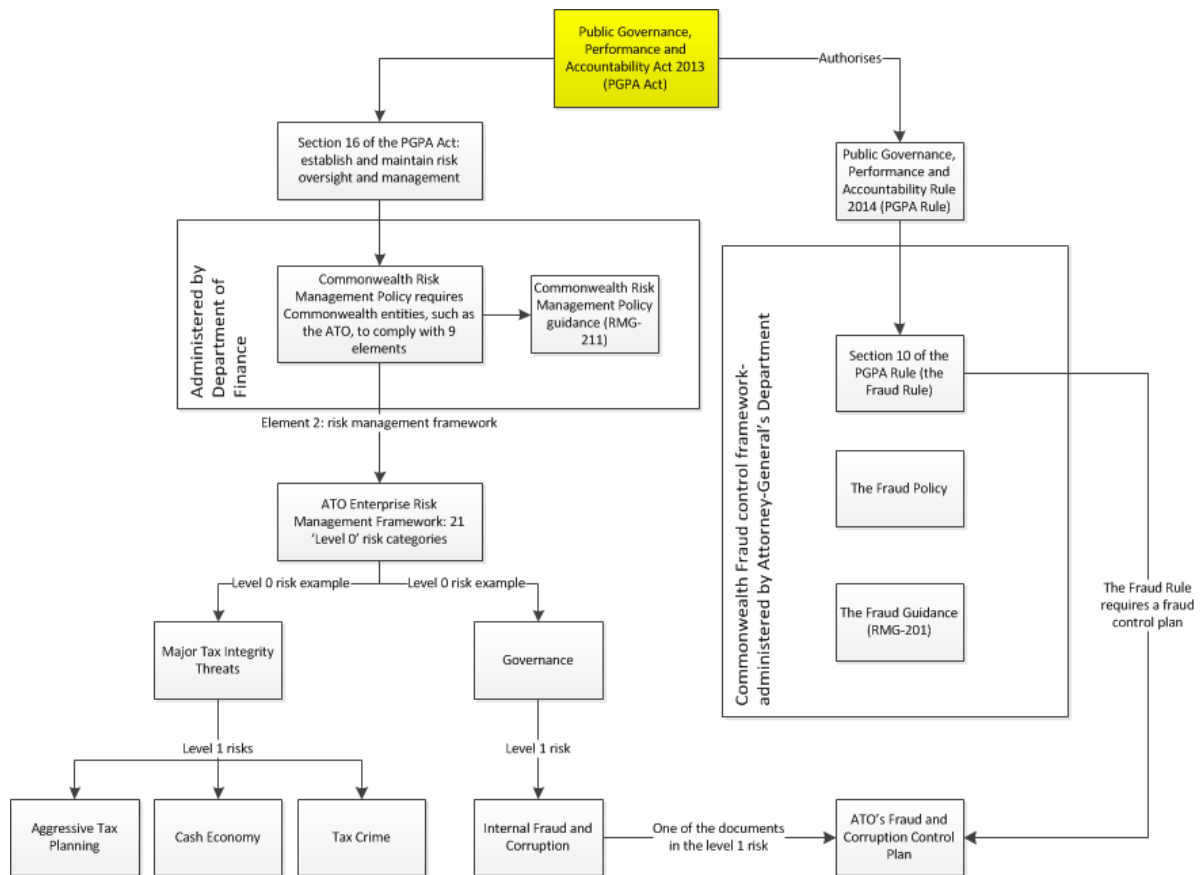
⁸⁶ ATO, 'ATO Fraud and Corruption Control Plan 2017-18' (15 September 2017) <www.ato.gov.au>.

⁸⁷ *ibid.*

⁸⁸ *ibid.*

⁸⁹ ATO, 'Chief Executive Instruction 2014/05/09 Tax Crime and External Fraud' (Internal ATO document, 9 May 2014).

Figure 2.1 – Overview of Commonwealth and ATO risk management framework



Source: ATO⁹⁰, AGD and Department of Finance.

ATO's governance of fraud and corruption risk management

2.52 Generally, the ATO's governance structure consists of a number of committees, program boards and consultation groups.⁹¹ In relation to the management of fraud and corruption risks, the current critical functional areas and positions include the following:

- The Audit and Risk Committee (ARC) oversees the development and implementation of the Fraud and Corruption Control Plan and provides independent assurance to the Commissioner on fraud and corruption risks and controls as part of its role of providing assurance and advice on broader risks, controls and compliance frameworks.⁹²
- The Internal Audit (IA) unit, headed by the Chief Internal Auditor, supports the work of the ARC.⁹³ The IA unit conducts a program of risk-based audits and

⁹⁰ Note that during this review the ATO's Enterprise Risk Management Framework was in a state of change.

⁹¹ Above n 7, p 127.

⁹² *ibid.*, p 135.

⁹³ *ibid.*

assessments of the effectiveness of the ATO's governance and control frameworks and reports to the ARC. Among the reports provided, the following are the most relevant:

- Independent Review of the Internal Audit Function and Fraud Prevention and Investigations Function (2015)⁹⁴; and
- The Integrity Framework (Integrity Arrangements) – Assessment of the framework and recommendations for future arrangements (2015).⁹⁵
- The FPII unit is responsible for the implementation of measures to effectively prevent, detect and respond to internal fraud and corruption.⁹⁶ The unit is headed by the FPII Assistant Commissioner who is also responsible for the development of the Fraud and Corruption Control Plan and reporting to the ARC on a quarterly basis.
- The Client Engagement Group, headed by a Second Commissioner, identifies 'potential instances of non-compliance [with the tax and superannuation laws] and assures that the right amount of taxes are paid, at the right time'. Various areas within this Group may deal with taxpayer fraud. In particular, the PGH business line focuses on 'those who criminally defraud the system or deliberately avoid their tax obligations'. This area works in collaboration with regulatory and law enforcement agencies.⁹⁷
- The Deputy Commissioner of ATOC is ultimately responsible for managing the risk of internal fraud, which includes monitoring and providing assurance on the effectiveness of controls as well as assessing the performance of the FPII unit.⁹⁸

ATO's risk reporting

2.53 To track compliance with certain legal obligations as well as whole-of-government and internal requirements, the ATO conducts the 'conformance with obligations program'.⁹⁹ This program monitors and reports on the level of conformance in areas of identified risks. These reports include quarterly qualitative conformance statements from the responsible areas.

2.54 Quarterly corporate integrity indicator reports are also produced for areas of risk, priority or identified improvement.¹⁰⁰ These are:

a rolling program of quantitative reports in some predetermined areas of risk, priority or where the ATO needs to improve concerning reputation, people, information practices, resources and security.¹⁰¹

⁹⁴ RSM Bird Cameron, 'ATO – Independent Review of the Internal Audit Function and FPII Function', report to the ATO (December 2015) p 35.

⁹⁵ ATO, 'The Integrity Framework Integrity Arrangements – Assessment of the framework and recommendations for future arrangements (2015)' (Internal ATO document, 2015).

⁹⁶ Above n 86.

⁹⁷ Above n 7, pp 9 and 59.

⁹⁸ Above n 86.

⁹⁹ ATO, 'CEI 2014/05/07 ATO's Conformance with Obligations' (Internal ATO document, 6 June 2014).

¹⁰⁰ *ibid.*

¹⁰¹ ATO, 'Corporate integrity indicators' (Internal ATO document, 31 March 2017).

2.55 Table 2.1 below describes these reports in more detail by outlining the indicators and what is being measured.¹⁰²

Table 2.1: ATO corporate integrity indicators

Corporate integrity indicator	Measurement
Aged complaints	Aged complaints over 50 business days old
Conflicting Information Technology (IT) access roles	Medium and high risk conflicting IT tax systems where access combinations pose financial and/or fraud risks
Security incidents	Overview of security incidents by type and site across the ATO
Unauthorised access to taxpayer records	The number of occurrences of unauthorised access to taxpayer records
Comcare claims	The costs and number of Comcare claims
Workforce absence	The level of workforce absence across the ATO compared to the APS large agency median of 12.4 days and the ATO's internal rate of unscheduled leave compared to the same time last year.
Mandatory training	Completion rates for ATO staff and new starters' mandatory training in Security, Privacy, Fraud and Work Health Safety

Source: ATO

2.56 Summaries from the conformance statements, integrity indicator reports and other relevant materials are reported to the ATO Executive, the ARC and are made available across the ATO.¹⁰³

2.57 The FPII Assistant Commissioner also provides detailed reports to the ARC which includes identified trends and work that the FPII unit may be conducting internally or with other agencies in Australia and overseas. The reports to the ARC also include an overview of the FPII unit's prevention, detection and response activities for the relevant period, including:¹⁰⁴

- the number of allegations of fraud, corruption or misconduct received by the FPII unit;
- the number of investigations conducted as a result of the allegations as well as the proportion that are substantiated;
- high level trend analysis of the allegations investigated and the types of allegations received;
- the status of any court action underway for fraud, corruption or misconduct;
- the progress of FPII reviews and risk assessments in its forward work plan; and
- the progress of the FPII unit's proactive detection and communication activities.

¹⁰² *ibid.*

¹⁰³ Above n 99.

¹⁰⁴ ATO, 'FPII Snapshot of key activities and outcomes for DC ATO Corporate 1 January–31 March 2017' (Internal ATO document, 2017).

2.58 The FPII Assistant Commissioner also reports on a monthly basis to the Deputy Commissioner, ATOC, on the FPII unit's performance, including progress of reviews, trends and status of individual FPII investigations.¹⁰⁵ The ATO has also advised the IGT that the FPII Assistant Commissioner may also report directly to the Commissioner or Second Commissioners on issues of significant risk or misconduct.

2.59 Furthermore, as noted above, the ATO publicly demonstrates its compliance with the Commonwealth Fraud and Corruption Control Framework by reporting on fraud control matters in the Commissioner's Annual Reports¹⁰⁶, to the AIC annually on fraud perpetrated against the ATO¹⁰⁷ and to the Commonwealth Ombudsman regarding its compliance with the PID regime.¹⁰⁸

INTERNATIONAL APPROACHES

2.60 The following section briefly describes the approaches taken by revenue authorities in some comparable countries within the OECD to address risks of internal fraud and corruption. While they all have their own priorities and focus areas in relation to the management of external fraud, the need for sound management of internal fraud is a ubiquitous concern across all jurisdictions.

United States of America

2.61 Responsibility for the management of fraud risks within the Internal Revenue Service (IRS) is shared between the IRS itself and the Treasury Inspector General for Tax Administration (TIGTA), which is an independent office having oversight responsibilities of the IRS and reporting directly to the Treasury Secretary and Congress.¹⁰⁹ Generally, TIGTA's Office of Investigations (OI) conducts a comprehensive program of investigating potentially fraudulent activities that have been detected or reported, whilst the IRS is responsible for fraud prevention through training programs and adopting internal controls. The responsibility for detecting internal fraud is shared by TIGTA and the IRS, with the former focusing on areas such as unauthorised access while the latter has its own projects in place to detect fraud and impropriety in areas such as procurement and human resources (HR). Due to the structures in place, any potentially fraudulent conduct detected by the IRS's detection projects is referred to TIGTA's OI.

Internal Revenue Service

2.62 With respect to recruitment, the IRS has a two-stage checking process aimed at safeguarding the integrity and trustworthiness of the workforce. Initial pre-screening is conducted by the IRS prior to the employee's commencement date, while a much more

¹⁰⁵ ATO, 'FPII - Reporting Matrix' (Internal ATO document, 31 March 2017).

¹⁰⁶ *Public Governance, Performance and Accountability Rule 2014 s 17AG.*

¹⁰⁷ Above n 51, p 3 paras [12] and [14].

¹⁰⁸ Above n 105.

¹⁰⁹ Treasury Inspector General for Tax Administration (TIGTA), *Office of Investigations* (24 May 2013) <www.treasury.gov/tigta/oi.shtml>.

thorough 'suitability investigation' is conducted under the jurisdiction of the Office of Personnel Management within the first year of employment.¹¹⁰

2.63 The extent of both the pre-screening and the suitability investigation will depend on the position's risk level. Any position in the IRS that involves access to federal tax information is designated to be at least moderate risk and subject to fingerprinting, a credit search, Federal and local law enforcement checks and a personal subject interview. Written inquiries are also made to the employee's previous employer(s) and/or place of study with references being sought for the past five years.¹¹¹ Employees in positions designated to be high risk, such as criminal investigators, are subject to more comprehensive checks. There is a separate but similar screening regime for contractors.¹¹²

2.64 Although the extensiveness of the background checks can be quite time consuming, the IRS's two-stage process means that a portion of the checks can be completed while the employee has already commenced employment. In this way, the IRS is able to balance the need for a thorough vetting process while minimising the delay in deploying human resources that such a process would typically entail.

2.65 Furthermore, the IRS's screening process is not limited to a point-in-time check which occurs when an employee enters the organisation. For moderate and high risk positions, the background investigation is repeated once every five years to provide assurance that the employees remain suitable for their role from an integrity perspective.¹¹³

2.66 Once an employee or a contractor joins the IRS, measures are also taken to instil within them the ethics and values of the organisation. Employees are required to complete annual mandatory training which includes modules on ethics, unauthorised access and conflicts of interest. To ensure the robustness of online training, some of the mandatory modules are created using software that have set time frames per slide or require staff members to interact with the screen to ensure that they are working through the content.¹¹⁴ The training packages also use real and relevant examples from actual investigations to provide more practical and useful guidance. After working through the module, the employee or contractor needs to complete a test which, if failed, would require the employee or contractor to repeat the entire module before they could attempt the test again. Staff will also be prevented from accessing certain IRS systems if the associated training modules are incomplete or not passed.¹¹⁵

2.67 The IRS also adopts various internal controls to reduce the likelihood of fraud. For example, the team responsible for case selection has no involvement in audit or compliance activities and vice versa. Similarly, senior officers with more extensive decision-making powers are only privy to high level information and generally do not have any direct involvement in individual audit cases. While it is an option for the

¹¹⁰ Internal Revenue Service (IRS), *Internal Revenue Manual*, Parts 10.23.3.3 and 10.23.3.5 (28 June 2016).

¹¹¹ TIGTA, *The Office of Safeguards should Improve Management Oversight and Internal Controls to Ensure the Effective Protection of Federal Tax Information*, Reference Number 2014-20-059 (15 September 2014) p 6.

¹¹² Above n 110, Part 10.23.2 (27 April 2016).

¹¹³ *ibid.*, Part 10.23.3.4 (28 June 2016).

¹¹⁴ The IRS uses software called Articulate.

¹¹⁵ Tax Executive Staff, 'Elevating Examination Concerns Within the New LB&I - The Expert: Rosemary Sereti', *Tax Executive*, (1 February 2018) <www.taxexecutive.org>.

taxpayer to escalate issues to such officers, these officers encourage the taxpayer to raise and resolve their concerns with the manager of the audit team directly. In instances where senior officers are involved in cases, the IRS has a set of principles which guides these interactions.¹¹⁶ Furthermore, the right of US taxpayers to appeal to an independent Office of Appeals, which is separate and independent from the IRS's compliance function, operates as a further check on the senior officer's decision-making powers.

2.68 The IRS also treats management of conflicts of interest very seriously as public servants in the US are prohibited, by law, from participating in an official capacity in any matter in which they have a financial interest if the matter will have a direct and predictable effect on that interest.¹¹⁷ Senior executives are required to make a Public Financial Disclosure which outlines their assets, liabilities, financial transactions and gifts received and those of their spouse.¹¹⁸ Such disclosures must be made upon commencement of employment and annually thereafter. Employees who are not senior executives but are deemed to be employed in a position that has a direct and substantial economic effect on the interests of a non-federal entity, such as auditors, are instead required to lodge a Confidential Financial Disclosure Report upon commencement of their role and annually thereafter. This report requires the employee to disclose their assets, liabilities and gifts and those of their spouse and dependent children.¹¹⁹

2.69 Conflicts of interest are not simply restricted to situations where there may be financial gain but also extends to other types of personal benefits. As such, IRS employees are specifically expected to recuse themselves from participating in matters related to a particular taxpayer if the employee is currently seeking employment from that taxpayer.¹²⁰

2.70 The rules that seek to prevent IRS employees from being exposed to conflicts of interest extend into the period after the employee has left the organisation. Broadly speaking, under US legislation, a former IRS employee would be permanently prohibited from dealing with the IRS on a matter if they previously participated personally and substantially in the matter while being employed by the IRS. That IRS employee would also be prohibited for a period of two years from dealing with the IRS if they did not substantially participate in the matter but it was under their official responsibility. Senior executives also have an additional restriction placed upon them after they leave the organisation known as the 'no contact rule,' which effectively prohibits the former executive from dealing with the IRS in connection with any matter for a period of one year.¹²¹

¹¹⁶ Above n 110, Parts 4.46.4.4 and 4.46.1.4.3 (3 September 2016).

¹¹⁷ United States, 5 C.F.R. § 2635.402 and 18 U.S.C. § 208.

¹¹⁸ US Office of Government Ethics, *Executive Branch Personnel Public Financial Disclosure Report - OGE Form 287e* (1 March 2014) <www.oge.gov>.

¹¹⁹ US Office of Government Ethics, *Confidential Financial Disclosure Report - OFE Form 450* (January 2017) <www.oge.gov>.

¹²⁰ United States, 5 C.F.R. § 2635.601.

¹²¹ United States 18 U.S.C § 207.

Treasury Inspector General for Tax Administration

2.71 The reasons why allegations of fraud or corruption by IRS staff are investigated by a structurally independent agency are based in the history of TIGTA and its predecessor, the IRS Inspection Service. In response to allegations of corruption, the IRS Inspection Service was established in 1951 as the IRS's internal affairs division.¹²² However, perceptions of conflicts of interest remained as the IRS Inspection Service was within the IRS. These conflict of interest perceptions and allegations of abuse of power by the IRS led to the ultimate transfer of all the functions of the IRS Inspection Service to the newly created independent TIGTA.¹²³

2.72 The purpose of severing the internal fraud investigation function from the IRS was to promote impartiality by preventing such investigations from being unduly influenced by IRS senior management. The fact that TIGTA has its own reporting channels to the Treasury Secretary and to Congress further supports the separation of roles and responsibilities.

2.73 As noted earlier, TIGTA may receive referrals about fraud or other misconduct by IRS employees. TIGTA may also be alerted to these matters through its fraud, waste and abuse hotline or online reporting form.¹²⁴ While the majority of TIGTA's investigations originate by these channels, the OI also proactively engages in monitoring activities to detect potential wrongdoing, such as unauthorised access and the misuse of IRS systems.¹²⁵ For example, TIGTA has put in place certain automated safeguards and is able to detect IRS employees who look up records of their family, neighbours and high profile taxpayers. In addition, TIGTA is also able to detect employees who have potentially made adjustments to tax accounts.

2.74 As noted earlier, the above investigations are conducted by TIGTA's OI whose staff are Federal law enforcement officers and possess both the capability and the broad range of powers including the authority to carry firearms, to execute and serve search warrants, and to make arrests.¹²⁶ In addition, TIGTA does not need to obtain permission from the US Department of Justice to commence its investigations.

2.75 Not all allegations made to TIGTA involve criminal allegations. Approximately 30 per cent of all allegations are referred back to the IRS for action¹²⁷ as they involve less serious administrative concerns such as employee performance issues or unauthorised absences.

2.76 During each six month reporting period, the OI typically conducts around 1,500 investigations. When an investigation into an IRS employee has been completed, TIGTA presents the outcomes to the IRS who determines the appropriate disciplinary action to take. In circumstances where the outcome of the investigation uncovers a

¹²² TIGTA, *History* (24 May 2013) <www.treasury.gov>.

¹²³ *Internal Revenue Service Restructuring and Reform Act of 1998* s 1103.

¹²⁴ TIGTA, *Report Fraud, Waste, & Abuse* (5 October 2016) <www.treasury.gov>.

¹²⁵ TIGTA, *Audit trails did not comply with standards or fully support investigations of unauthorised disclosure of taxpayer data*, Reference Number 2012-20-099 (20 September 2012) p 2.

¹²⁶ United States 26 U.S.C § 7608.

¹²⁷ TIGTA, *Semiannual Report to Congress October 1, 2016 – March 31, 2017* (5 June 2017) p 67.

criminal element, TIGTA will refer the matter to the Department of Justice for prosecution.¹²⁸

2.77 TIGTA also has some involvement in fraud prevention. For example, TIGTA conducts a variety of proactive activities, such as presentations to groups of IRS employees. These activities provide TIGTA with the opportunity to meet face-to-face with IRS employees and their managers to make them more aware of TIGTA's role and responsibility and to help them feel more comfortable about approaching TIGTA to provide information.¹²⁹ The IRS also publishes the number of staff terminated, suspended, fined and prosecuted for unauthorised access on posters to remind its staff of the seriousness of the offence and to act as a deterrent.

2.78 In addition, TIGTA has a review function that is performed by its Office of Audit and Office of Inspections & Evaluations. Such reviews are designed to promote efficiency and effectiveness in the administration of the US revenue system and sometimes touch on integrity issues. For example, in the past five years TIGTA has reviewed topics such as the hiring of former employees¹³⁰, the controls over outside employment¹³¹, and the violation of tax laws by IRS employees¹³².

United Kingdom

2.79 Her Majesty's Revenue and Customs (HMRC) adopts a range of measures to manage the risk of internal fraud. These include preventative measures, such as vetting processes and detection activities which monitor suspicious use of information technology (IT) systems.

2.80 A prospective employee is subject to a vetting process that is similar to that adopted in Australia. At a minimum, the prospective employee must undergo a Baseline Personnel Security Standard pre-engagement check which involves an identity check, a nationality check, employment history verification for the past three years and a criminal record check for unspent convictions.¹³³ An applicant for a higher risk position will need to obtain a security clearance, of which there are three levels, in addition to the Baseline pre-engagement check. Unlike the later check, which is only performed once upon entry into HMRC, security clearances are subject to a review process every 7 to 10 years, depending on the security clearance level. Clearance holders are also required to report any relevant changes in their circumstances.¹³⁴

2.81 HMRC's two primary methods for detecting internal fraud are referrals, which can be made by employees, managers or other government agencies, and

¹²⁸ *ibid.*, pp 28 and 67.

¹²⁹ TIGTA, *What is TIGTA* (11 December 2014) <www.treasury.gov>.

¹³⁰ TIGTA, *Additional Consideration of Prior Conduct and Performance Issues is Needed When Hiring Former Employees*, Reference Number 2015-10-006 (30 December 2014); TIGTA, *The Internal Revenue Service Continues to Rehire Former Employees With Conduct and Performance Issues*, Reference Number 2017-10-035 (24 July 2017).

¹³¹ TIGTA, *Controls Over Outside Employment Are Not Sufficient to Prevent or Detect Conflicts of Interest*, Reference Number 2014-10-073 (29 September 2014).

¹³² TIGTA, *Review of the Internal Revenue Service's Process to Address Violations of Tax Law by Its Own Employees*, Reference Number 2015-10-002 (14 April 2015).

¹³³ UK Cabinet Office, National Security and Intelligence and Government Security Profession, *Her Majesty's Government Baseline Personnel Security Standard* (1 April 2014) p 12 <www.gov.uk>.

¹³⁴ Her Majesty's Revenue and Customs (HMRC) communication to the IGT, 30 August 2017.

proactive risk profiling activities, such as data mining practices which incorporates the logging and analysis of its staff's keystrokes to detect suspicious activity. A proportion of HMRC's internal investigations also originate from its risk profiling activities.¹³⁵ HMRC has indicated that it constantly seeks opportunities to further improve its detection mechanisms. In its most recent Internal Fraud and Corruption Strategy document, HMRC indicated that it will be adopting a 'test and learn' based approach with the aim of making its data mining practices more flexible in dealing with emerging risk areas.¹³⁶

2.82 In relation to managing conflicts of interest, HMRC currently relies on employees' self-disclosures. However, HMRC is testing a pilot that seeks to match such self-disclosures with information regarding employees' and their family's shareholdings and directorships.¹³⁷ This information would assist to identify potential conflicts of interest and prevent actual conflicts from arising.

2.83 If HMRC detects a potential integrity issue with an employee, or decides to investigate an allegation about an employee, the matter is referred to Internal Governance, an area within HMRC's Fraud Investigation Service Unit responsible for managing internal fraud. The matter is either examined by the Internal Governance area's civil investigative team, which typically actions between 300 and 350 cases per year, or the Internal Governance area's criminal investigative team, for more serious matters. Officers in the criminal investigative team are law enforcement officers who have the power to apply for search warrants and make arrests. Approximately 25 cases are referred each year to the Crown Prosecution Service by this team.¹³⁸ If the prosecution results in a successful conviction, the details of the investigation are published on HMRC's intranet as a deterrent, including the name of the offender, the nature of the offence and the length of the sentence.¹³⁹

2.84 The outcomes of investigations are also used by HMRC as part of its overall fraud management strategy to drive its 'upstream' prevention and detection activities. For example, investigative outcomes are used to design specific educational and communication packages with the aim of providing HMRC employees with fraud and ethics training that is both relevant and practical. Investigative outcomes are also used to inform HMRC's key risk areas with the aim of ensuring that its detection activities remain up-to-date and responsive.¹⁴⁰

New Zealand

2.85 In October 2015, New Zealand's revenue authority, the Inland Revenue Department (IRD), introduced a new fraud and corruption control policy and framework which involved the creation of a fraud risk register.¹⁴¹ The register is aimed

¹³⁵ HMRC communication to the IGT, 26 September 2017.

¹³⁶ HMRC, 'HMRC Internal Fraud and Corruption Strategy: A Cross Departmental Collaborative Approach' (Internal HMRC document, date unknown).

¹³⁷ HMRC communication to the IGT, 30 August 2017.

¹³⁸ *ibid.*

¹³⁹ HMRC, 'Playboy fraudster's luck runs out' (Internal HMRC document, date unknown); HMRC, 'Former employee and husband sentenced for tax fraud' (Internal HMRC document, date unknown).

¹⁴⁰ Above n 136.

¹⁴¹ Inland Revenue Department (IRD), *Annual Report 2016 (2016)* p 42 <www.ird.govt.nz>.

at ensuring that the organisation maintains a holistic, up-to-date understanding of its risk profile and adopts a differentiated approach to account for the variance in risk in each of the organisation's business groups.

2.86 All prospective IRD employees, at a minimum, undergo a pre-employment suitability check to examine the candidate's criminal history and their compliance with tax, student loan and child support obligations. If the role is in a sensitive area with higher risk, the applicant will also be subject to a more comprehensive vetting process to obtain one of the three levels of security clearances. Security clearances are reviewed every five years and when a significant change in circumstances is reported to ensure currency.¹⁴²

2.87 After the prospective employee has passed all of the relevant checks and joins the IRD, they will undergo an induction process with his or her manager. On the first day, the manager is required to have a discussion with the new starter about the IRD's culture and values and go through the IRD's Code of Conduct. A signed form acknowledging that this has occurred must be filled out and attached to the new starter's personnel files. If relevant, a conflict of interest disclosure will also need to be submitted. During the first week, the new starter must complete online training packages on the IRD's Code of Conduct, security awareness and unauthorised access. After these have been completed, the manager is required to discuss the training with the new starter with the aim of ensuring that the new starter has a proper understanding of the content of the modules and allowing the manager to provide some context on how the content applies specifically to the new starter's role.¹⁴³

2.88 Due to the relatively small size of the organisation and the geographical proximity of its offices, scheduled and ad hoc fraud training throughout the year can be presented face-to-face by members of the IRD's Integrity Assurance team. The IRD sees this type of fraud awareness training as having a greater impact on employee behaviour when compared with online learning, which, in the IRD's experience, can be treated as a 'tick-and-flick' exercise. Furthermore, the training provides IRD employees with an opportunity to interact directly with the Integrity Assurance team. Establishing this kind of rapport is aimed at creating a sense of trust and familiarity which may give the employee the greater confidence to report fraud should the need arise.¹⁴⁴

2.89 The IRD's internal controls impose an annual requirement for senior officers to disclose financial assets that they or their family possess.¹⁴⁵ These controls have the aim of preventing the IRD's decision makers from being inappropriately influenced by their interests and relationships and are further supplemented by segregation of duties. For example, as senior officers in the IRD do not typically have any direct interest or involvement in audit cases, it makes it more difficult for taxpayers or their representatives to use their relationships with senior officers to inappropriately influence decision-making. If a taxpayer were to contact an IRD senior officer directly about a particular audit and request intervention, the expected behaviour would be for

¹⁴² New Zealand Security Intelligence Service, *Protective Security Requirements* (18 December 2014) <www.protectivesecurity.govt.nz>.

¹⁴³ IRD, 'Navigating IR: Your Induction Journey - Hiring Leader's Induction Checklist' (Internal IRD document, date unknown).

¹⁴⁴ IRD communication to the IGT, 17 August 2017.

¹⁴⁵ IRD, 'Disclosure & Conflict of Interest Policy' (internal IRD document, July 2017).

the senior officer to decline and refer the matter to the complaint management service, being the appropriate channel for the investigation of such concerns.¹⁴⁶

2.90 Furthermore, IRD senior managers with high decision-making power would typically not be able to access individual taxpayer data.¹⁴⁷ Those intending to access data would likely need to give instructions to subordinate staff to perform access by proxy. In such a situation, it would be expected that the employee report the matter if they suspect any impropriety, as the IRD's focus on fraud awareness and training is aimed at making its employees more comfortable with reporting improper conduct.¹⁴⁸

2.91 The investigation of employee misconduct within the IRD is undertaken internally by its Integrity Assurance team. The majority of these investigations stem from reports from its own staff while proactive detection measures play a comparatively small role. The typical methods for IRD staff to report improper conduct are an online form and a referral hotline. The IRD also has a separate intranet report option for staff which allows for anonymous referrals, however, usage of this option is low when compared to the other channels.¹⁴⁹

2.92 It should be noted that there are regular meetings between the IRD's Integrity Assurance manager with the Commissioner's Executive Advisors on internal fraud risks as well as regular briefings and reports to the Deputy Commissioner.¹⁵⁰

Canada

2.93 Similar to the models in the other jurisdictions above, all prospective Canada Revenue Agency (CRA) employees must undergo personnel security screening before they are permitted to work for the organisation, with higher risk positions requiring more stringent checks. At a minimum, CRA employees are required to obtain a 'reliability status' clearance which involves the verification of their identity, background and credentials, mandatory fingerprinting, a credit check, and a criminal record check. Some employees may also require a security clearance at the secret or top secret level, requiring both a security assessment and an assessment of loyalty to Canada undertaken by the Canadian Security Intelligence Service. A security screening is deemed effective after the employee has signed a security briefing certificate. This certificate specifies the security requirements attached to the granted level of screening and signifies that the employee understands and agrees to abide by those requirements.¹⁵¹

2.94 Once an employee has been deemed suitable for employment and hired, they must comply with a number of obligations upon initial hire. Firstly, they are required sign an Oath or Affirmation in relation to secrecy. The CRA considers any information which is acquired in consequence of employment by the CRA, that is not publicly available, to be protected information. The disclosure of such information at any time

¹⁴⁶ IRD communication to the IGT, 17 August 2017.

¹⁴⁷ IRD communications to the IGT, 17 August 2017 and 6 March 2018.

¹⁴⁸ IRD communication to the IGT, 17 August 2017.

¹⁴⁹ IRD communication to the IGT, 17 October 2017.

¹⁵⁰ IRD communication to the IGT, 6 March 2018.

¹⁵¹ Treasury Board of Canada Secretariat, *Standard on Security Screening* (20 October 2014) <www.tbs-sct.gc.ca>.

will constitute a breach of either the *Income Tax Act*¹⁵² or the *Excise Act*¹⁵³ and may result in criminal sanctions.¹⁵⁴ Furthermore, employees are required to review the *CRA Code of Integrity and Professional Conduct*,¹⁵⁵ the *Values and Ethics Code for the Public Sector*,¹⁵⁶ and the *Directive on Conflict of Interest, Gifts and Hospitality, and Post-employment*.¹⁵⁷ These documents are considered part of the conditions of employment and must be reviewed by CRA officers annually and whenever the employees change roles within the CRA.¹⁵⁸

2.95 Specific obligations in relation to preventing, identifying, disclosing and managing conflicts of interest are outlined in the conflicts of interest directive. One such obligation requires employees to disclose private interests and outside activities in a confidential disclosure form within 60 working days of initial appointment. The definition of private interest is comprehensive and includes investments, interests in partnerships and companies, rental properties and commodities. The definition of outside activities is similarly comprehensive and includes all paid or unpaid employment, membership on a board of directors, and public speaking engagements. Any changes to an employee's private interests and outside activities which occur during the period of employment must also be disclosed, even if the change occurs during periods of leave, with or without pay. In addition, the directive also requires CRA employees to disclose all offers or acceptance of prohibited and reportable gifts.¹⁵⁹

2.96 When a CRA employee makes a disclosure under the directive, the information is submitted to a delegated manager at the director level or higher. The delegated manager is responsible for reviewing the submission in accordance with the criteria outlined in the directive. If a real, apparent or potential conflict of interest is found to exist, the delegated manager may consider appropriate measures such as the restriction, removal or reassignment of specific duties, directing the employee to cease, curtail or modify the outside activity, and/or directing the employee to relinquish, divest, or make other arrangements to manage the private interest. The employee would then be required to carry out the measures within 120 days of his or her initial appointment or change in circumstances.¹⁶⁰

2.97 If a CRA employee observes that a fellow employee has engaged in behaviour that is contrary to the obligations in the conflict of interest directive, or any other form of misconduct, the employee is obliged to report the matter. The misconduct can be reported directly to the CRA's Internal Affairs and Fraud Control Division for investigation, to the observing employee's manager who may then refer the matter on to the Internal Affairs and Fraud Control Division, or to the CRA's anonymous internal fraud and misuse reporting line which is operated by a third party.¹⁶¹ Statistics

¹⁵² *Income Tax Act* R.S.C. 1985 (Canada) c. 1 (5th Supp.).

¹⁵³ *Excise Act* R.S.C. 1985 (Canada) c. E-14.

¹⁵⁴ Canada Revenue Agency (CRA), *Directive on conflict of interest, gifts and hospitality, and post-employment* (16 December 2016) <www.canada.ca>.

¹⁵⁵ CRA, *Code of Integrity and Professional Conduct* (20 September 2016) <www.canada.ca>.

¹⁵⁶ *ibid.*, Appendix B.

¹⁵⁷ Above n 154.

¹⁵⁸ *ibid.*, s 6.

¹⁵⁹ *ibid.*, Appendix A.

¹⁶⁰ *ibid.*, Appendix B.

¹⁶¹ Above n 155, s 2.

provided by the CRA indicate that the lowest source of internal investigations was the anonymous tip line whilst the highest source of investigations was referrals from management.¹⁶² The CRA also commences investigations into misconduct that it detects on a proactive basis. The unauthorised access of taxpayer data, for example, is something which can be automatically detected on the CRA's Enterprise IT systems.¹⁶³

2.98 In addition to the internal controls outlined previously, the conflict of interest directive also imposes rigorous post-employment rules on employees who are leaving the organisation to manage the risk of potentially preferential treatment, inappropriate disclosure of CRA information, and other conflict of interest situations. The context for these controls is the increased recruitment of the CRA's senior officers since 2010 by private sector firms such as the Big Four accounting firms. This has been an issue which has been reported in newspapers¹⁶⁴ and discussed in the House of Commons¹⁶⁵ and is a major concern for the CRA.

2.99 Any CRA employee who has accepted an offer of outside employment, including self-employment, must make a disclosure. Such disclosure may lead to them being assigned to other duties and responsibilities for the remainder of their employment. Members of the CRA's executive group are subject to an additional requirement to lodge a confidential disclosure form whenever they receive any firm offer of outside employment.¹⁶⁶

2.100 Furthermore, after an employee has left the CRA, they are not permitted to act for, or on behalf of any taxpayer in relation to any ongoing matter in which they had been involved while still employed at the CRA. The directive also specifically prohibits former employees from contacting current CRA employees in any manner that could be perceived as seeking preferential treatment or privileged access.¹⁶⁷ The directive also prohibits current employees from dealing with any former employee unless the delegated manager has been advised and approval has been granted.¹⁶⁸

2.101 Once an employee leaves the CRA, they are prohibited from accepting employment from any entity outside the public service if they had official dealings with them during one year immediately prior to termination. Furthermore, during this period, the former employee is prohibited from dealing with the CRA as a representative of any entity if they had any official dealings with the entity during the one year immediately prior to termination. The former employee is also required to disclose to the CRA's Senior Officer for Post-employment any offer or acceptance of employment during the limitation period.¹⁶⁹

2.102 In order to manage the risk of former employees disclosing the CRA's risk thresholds and other strategically important information to private sector firms, it is

¹⁶² CRA, '2016-17 Annual report on internal investigations', (internal CRA document, undated).

¹⁶³ CRA, *Internal controls to ensure privacy and security* (13 June 2016) <www.canada.ca>.

¹⁶⁴ Harvey Cashore, Kimberly Ivany and Katie Pedersen, 'Senior federal tax enforcer joined KPMG as its offshore 'sham' was under CRA probe', *CBC News*, 11 April 2016.

¹⁶⁵ Evidence to Standing Committee on Finance, House of Commons, Canada, 5 May 2016, (Diane Lorenzato, Assistant Commissioner, Human Resources Branch, CRA).

¹⁶⁶ Above n 154, Appendix D.

¹⁶⁷ *ibid.*

¹⁶⁸ *ibid.*, s 7.1.

¹⁶⁹ *ibid.*, Appendix D.

the CRA's standard practice to provide a reminder letter to all departing employees, outlining their ongoing obligation and the restrictions that apply.¹⁷⁰

¹⁷⁰ Above n 165.

CHAPTER 3 – PREVENTION OF INTERNAL FRAUD

3.1 Pursuant to the Commonwealth Fraud Control Framework, described in the previous chapter, the ATO must have in place measures to prevent, detect and respond to fraud. This chapter examines key ATO prevention measures in relation to internal fraud, namely:

- maintaining integrity through recruitment and ongoing staff monitoring;
- limiting the time that staff stay in high risk positions (rotation);
- fraud and ethics training;
- managing conflicts of interest;
- ensuring senior officer intervention in cases is appropriate and transparent;
- considering settlements and issuing letters of comfort; and
- predicting potentially fraudulent behaviour.

3.2 In exploring the above measures, the IGT has considered ATO practices and processes alongside those of other Commonwealth government agencies as well as revenue authorities in other jurisdictions. Stakeholders' concerns in this regard have also been examined in analysing the information obtained from the ATO.

3.3 The IGT's analysis has included scrutinising a sample of the ATO's FPII investigations into officers' alleged breaches of relevant APS Code of Conduct and/or ATO procedures. In total, 39 investigations, which were completed between 2011 and 2018, were reviewed and they covered areas such as conflicts of interest, unauthorised access, misuse of ATO property, abuse of position and unauthorised release of information.

3.4 Approximately half of the allegations in the above investigations were substantiated and, of these, 30 per cent were referred for management action, 20 per cent were referred to the CDPP or state police and the remainder were to be considered for misconduct by the ATO's HR area, namely the ATOP business line.

MAINTAINING INTEGRITY THROUGH RECRUITMENT AND ONGOING STAFF MONITORING

3.5 The ATO is integral to the fabric of Australian society. In addition to its primary role of revenue collection, it performs a variety of ancillary, but critical, functions. These include holding one of the largest repositories of highly personal and commercially sensitive information about individuals and businesses operating in Australia and overseas.

3.6 The ATO is also afforded significant powers, including coercive information gathering and interrogation, restricting movements of individuals and garnishee notices, many of which are exercised without the need for judicial authorisation.¹⁷¹

3.7 Australia's comparatively high level of voluntary compliance relies on the public's continuing confidence in the ATO and its officers to exercise its considerable powers in a fair and equitable manner and use the extensive information at their disposal only for the purpose for which it was obtained. One measure through which the ATO can achieve these outcomes is through appropriate staff recruitment processes and ongoing checks to ensure its workforce maintains integrity and shares the values that such an organisation must possess.

3.8 Relevantly, both the Australian Standard on Fraud and Corruption and Control¹⁷² and the ATO's Fraud and Corruption Control Plan highlight the importance of employment screening as a preventative control.

Stakeholder concerns

3.9 In submissions to this review, stakeholders cited publicly known examples of former ATO staff who had been involved in unethical behaviour, including fraud. Almost all examples took place many years ago and at a time when the ATO's recruitment and vetting processes were limited to conducting a criminal history check, contacting nominated referees and carrying out a security clearance check. However, some stakeholders believed that the ATO's recruitment processes have not changed substantially since that time.

3.10 Stakeholders believed that improved ATO recruitment processes, including vetting, may have identified a history of questionable behaviour which had become evident years after they were recruited. For example, an ATO staff member, whose employment had been terminated by the ATO, was rehired through a recruitment exercise conducted by external recruiters on behalf of the ATO.

3.11 Stakeholders also expressed concern that there appeared to be insufficient enforcement of staff's obligation to disclose changes to their circumstances which could impact their ongoing suitability to perform roles. They commented that the regime was not effective to address staff forgetfulness. Therefore, at times, changes in circumstance would only be detected at the next security clearance check which occurs every five years.

Relevant materials

3.12 The ATO is an agency that employs one of the largest numbers of staff in the APS. As at 30 June 2017, it employed 20,435 staff.¹⁷³ Whilst the number of positions

¹⁷¹ IGT, Submission to the House of Representatives Standing Committee on Tax and Revenue, *Inquiry into the External Scrutiny of the Australian Taxation Office* (March 2016) p 7.

¹⁷² Above n 84.

¹⁷³ Above n 7, p 115.

advertised historically may have been lower during 2013 when the government introduced temporary measures to restrict new hiring,¹⁷⁴ the ATO has advertised over 650 positions and received over 140,000 job applications in response to those job advertisements since 1 January 2015.¹⁷⁵

Recruitment

3.13 The ATO's CEI 2015/05/01 outlines the ATO's general principles for recruitment, selection and mobility for all ATO employees, including SES officers. In particular, this instruction requires the ATO to 'use fair, transparent processes that are in accordance with APS legislation, redeployment and employment principles and value the candidate experience'.¹⁷⁶ In addition, the ATO's CEI 2014/06/07 on security practices requires managers to ensure that appropriate integrity checks are completed prior to and during the engagement of staff.¹⁷⁷ The ATO has advised that the intensity of integrity and security clearance checks is based on the nature and seniority of the position as well as the level of responsibility and the sensitivity of information associated with the position.

3.14 To assist in the handling of the high volume of job applications, the ATO has centralised the management of its recruitment processes, including the associated integrity checks, in the ATOP business line.

3.15 Once an ATO business line has identified the need to fill a position and confirmed the requirements for the role, such as the level of security clearance, the ATOP business line assists the business area with the recruitment process by coordinating the following:¹⁷⁸

- provides overall support for the recruitment process including advertising the role, briefing the selection panel members for interviews on their roles and responsibilities, managing the candidates through pre-engagement checks and coordinating relevant approvals;
- undertakes pre-employment police and security checks including requesting the FPII unit to assist with certain aspects; and
- assists the candidate with the on-boarding process after the letter of offer has been issued.

3.16 Where a candidate's written application is considered suitable by the selection panel, the ATOP business line will check whether the candidate has prior employment history with the ATO. If so, further checks are conducted against the ATO's People

¹⁷⁴ APSC, *State of the Service 2012-13* (2013) p 3; Ben Packham, 'Hiring freeze imposed on Australian Public Service', *The Australian*, 31 October 2013.

¹⁷⁵ ATO communication to the IGT, 24 November 2017.

¹⁷⁶ ATO, 'Chief Executive Instruction 2015/05/01 Recruitment, Selection and Mobility' (Internal ATO document, 1 December 2016).

¹⁷⁷ ATO, 'Chief Executive Instruction 2014/06/07 Security' (Internal ATO document, 31 March 2015) pp 1-2.

¹⁷⁸ ATO communication to the IGT, 12 October 2017.

Issue Escalation System database¹⁷⁹ for records of any fraud, misconduct or performance concerns and this information is provided to the selection panel at the interview stage. These checks were previously performed just before an offer of employment was made. Furthermore, prior to June 2016, these checks were not required to be performed for external candidates, however, since that time procedures have been put in place so that they are applied to all candidates.¹⁸⁰

3.17 All ATO job applications request current supervisors/managers to be listed as a referee and the ATOP business line contacts the nominated referees of suitable candidates. The steps involved in these checks, however, differ between large and small scale recruitment exercises.¹⁸¹ The ATOP business line has advised that referee reports are conducted as 'best business practice' and recommended for all external engagements but may not be necessary for internal promotions or if the selection panel and/or the delegate already have sufficient knowledge about the candidate.¹⁸² Completed referee checks are provided to the selection committee as part of the selection committee report.¹⁸³

3.18 Once the selection committee report has been approved and the preferred candidate identified, the ATOP business line will conduct a Pre-Engagement Integrity Check (PEIC) before an offer of engagement is made.¹⁸⁴

Pre-Engagement Integrity Checks

3.19 The ATO requires a PEIC for all individuals who are engaged by the ATO in any employment capacity¹⁸⁵, including those transferred from other APS agencies¹⁸⁶, contractors and consultants¹⁸⁷, as almost all positions would need access to information that would be considered sensitive.¹⁸⁸

3.20 A PEIC seeks to verify whether the candidate is 'honest, responsible, trustworthy and willing to comply with policies and procedures to safeguard Australian Government resources'.¹⁸⁹ Such verification is achieved through checking identity and any criminal convictions which are not 'spent'¹⁹⁰ by conducting a police

¹⁷⁹ Note that on 26 August 2017 the ATO migrated the People Issue Escalation System database to a new case management database called 'People Connect'.

¹⁸⁰ ATO communication to the IGT, 12 October 2017; 'Standard external recruitment template: information flow' (Internal ATO document, undated).

¹⁸¹ ATO communication to the IGT, 24 November 2017.

¹⁸² ATO, 'Referee reports' (Internal ATO document, 24 November 2017).

¹⁸³ ATO communication to the IGT, 24 November 2017; ATO, 'Selection Committee Report template' (Internal ATO document, January 2017).

¹⁸⁴ ATO, 'Standard external recruitment template: information flow' (Internal ATO document, undated).

¹⁸⁵ ATO, 'Pre-engagement integrity check' (ATO intranet, 24 October 2017).

¹⁸⁶ Transfer between agencies pursuant to section 26 of the *Public Service Act 1999*.

¹⁸⁷ Above n 185.

¹⁸⁸ AGD, *Information security management guidelines - Australian Government security classification system* (2015).

¹⁸⁹ Above n 185.

¹⁹⁰ A conviction is 'spent' under subsection 85ZM(2) of the *Crimes Act 1914* if 'the person has been granted a pardon for a reason other than that the person was wrongly convicted of the offence' or 'the person was not sentenced to imprisonment for the offence for more than 30 months and the waiting period' (i.e. 10 years since the date of conviction or 5 years for juvenile offenders: *Crimes Act 1914* s 85ZL) for the offence has ended.

check and residential address history for the past five years.¹⁹¹ Successful completion of a PEIC allows candidates to access ATO information appropriate to their level of security clearance.

3.21 For EL positions, shortlisted candidates undergo an ‘enhanced PEIC’ which involves additional checks to confirm the candidate’s qualifications, employment history, digital footprint, professional memberships and company directorships.¹⁹² As part of this employment history check, subject to the candidate’s consent, the ATOP business line will contact the HR area of the previous employer to identify whether any unethical behaviour was reported.¹⁹³

3.22 Since November 2017, enhanced PEICs are also required for all APS 6 positions and for more junior staff where the relevant business line determines the position to be of high risk.¹⁹⁴

3.23 As set out in Table 3.1 below, the ATO has conducted over 24,300 PEICs and over 200 enhanced PEICs since 1 July 2015 at a cost of over \$474,000.¹⁹⁵

Table 3.1: Numbers and costs of pre-employment integrity checks

	2015–16	2016–17	1 July 2017 – 6 October 2017 (YTD)	TOTAL
No. of PEICs	11,579	10,223	2,556	24,358
No. of Enhanced PEICs	18	158	58	234
Cost	\$191,804.82	\$244,409.90	\$38,155.00	\$474,369.72

Source: ATO

3.24 Generally, a successful candidate will not start work until a PEIC or an enhanced PEIC has been completed. However, the ATO has advised that it will allow a candidate to start their role before the PEIC has been completed¹⁹⁶ where the Director of the ATOP Security and Vetting team has provided approval based on the submission of a business case from the director of the relevant business line.¹⁹⁷ The ATO has advised that in the period 1 July 2016 to 19 October 2016, it had allowed 18 candidates to begin their role without first completing a PEIC.¹⁹⁸

3.25 There are also positions where the ATO considers a PEIC is generally not required.¹⁹⁹ Such positions include certain secondments and delivery or attendance at official meetings (or training) by foreign nationals who would have no access to ATO systems or taxpayer information. In these cases, the relevant business line must obtain and retain a declaration of secrecy from the person who has not been required to

¹⁹¹ The address history is checked through proof of identity documents provided by the candidate such as their driver’s licence and bank statements.

¹⁹² Above n 185.

¹⁹³ ATO communication to the IGT, 24 January 2018.

¹⁹⁴ ATO, ‘Enhanced checks’ (Internal ATO document, undated).

¹⁹⁵ ATO communication to the IGT, 12 October 2017.

¹⁹⁶ ATO, ‘Fraud and Corruption Control – Exemptions/exceptions to Pre-Engagement Integrity Checks’ (Internal ATO document, submitted to the ARC on 23 March 2017).

¹⁹⁷ Above n 185.

¹⁹⁸ Above n 196.

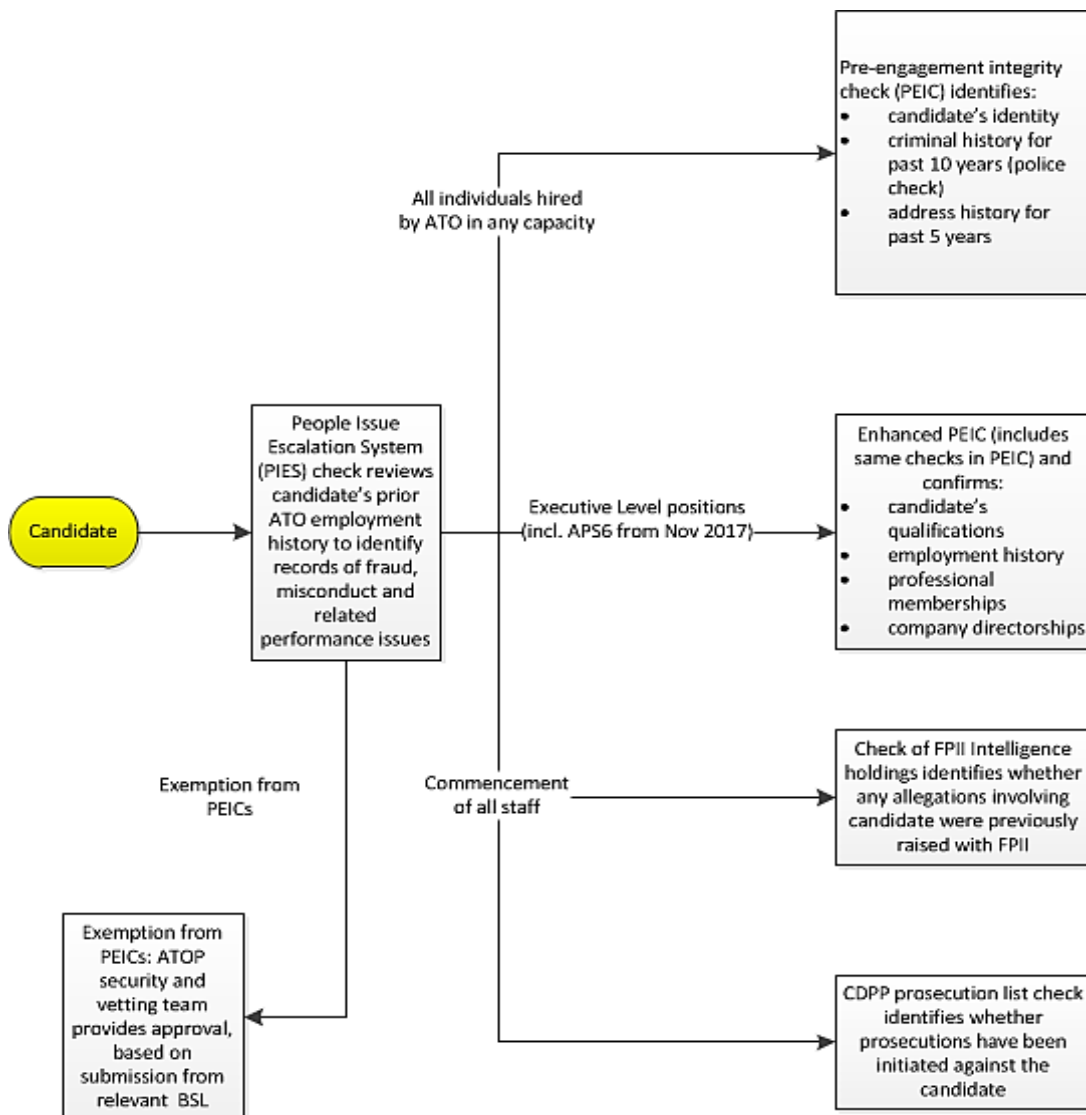
¹⁹⁹ *ibid.*

undergo a PEIC.²⁰⁰ The ATO has advised that it has processed 230 applications to not conduct a PEIC since July 2015.²⁰¹

3.26 In addition to the PEIC and enhanced PEIC, the ATOP business line requests the FPII unit to check candidate’s details against its records. The FPII unit is also requested to conduct searches to determine if the candidate’s name is on the CDDP Prosecution List (i.e., whether the Commonwealth has initiated a prosecution against the candidate on behalf of the ATO). If there is a match, the FPII unit will review the case information and share any relevant information with the ATOP business line.²⁰²

3.27 The figure below summarises the above checks.

Figure 3.1 – Outline of ATO integrity checks during recruitment



Source: ATO

²⁰⁰ Above n 185.

²⁰¹ ATO communication to the IGT, 12 October 2017.

²⁰² *ibid.*; ATO, 'Integrity checks' (Internal ATO document, undated).

Declarations by employees

3.28 Candidates who are subject to PEICs are also required to complete a declaration regarding their compliance with tax and superannuation obligations as well as any conflicts of interest they have, for example by also being registered as a tax or Business Activity Statement (BAS) agent.²⁰³

Security clearances

3.29 Positions which have access to security-classified information are known as 'designated security assessed positions' (DSAPs).²⁰⁴ Those holding a DSAP are required to obtain a security clearance before they can begin work. Security clearances are conducted by the Australian Government Security Vetting Agency (AGSVA) in the Department of Defence.

3.30 The type of clearance required will depend upon the type of information that may be accessed. The information itself is classified according to the level of damage that may be sustained as a result of its unauthorised release. Where such release results in:

- 'exceptionally grave damage to the National Interest' the information will be classified as 'Top Secret' and a Negative Vetting Level 2 (NV2) security clearance will be required;
- 'serious damage to the National Interest, organisations or individuals' the information will be classified as 'Secret' and thus a Negative Vetting Level 1 (NV1) clearance will be required; and
- 'significant' or 'limited damage to the National Interest, organisations or individuals' (Confidential and Protected information) a Baseline security clearance will be required.²⁰⁵

3.31 A Baseline security clearance is required to be renewed at least every 15 years and generally confirms an applicant's identity, citizenship, background for the past five years (residential addresses, employment and overseas travel history), qualifications and professional referees as well as police records (excluding spent convictions), financial history (including a summary of assets, income, liabilities and expenditure) and that an official secrets declaration and relevant statutory declarations have been completed.²⁰⁶

3.32 A NV1 security clearance is required to be renewed at least every 10 years. It is granted after completion of a suitability screening questionnaire by the applicant, an assessment by the Australian Security Intelligence Organisation, verification of the

²⁰³ ATO, 'ATO pre-engagement documentation' (Internal ATO documentation, 4 April 2012).

²⁰⁴ Security classified information is information, the unauthorised release of which, could cause damage to the National Interest, organisations and/or individuals: see, above n 188.

²⁰⁵ Department of Defence, 'Clearance Subject FAQs' <www.defence.gov.au>.

²⁰⁶ AGD, *Personnel security guidelines - Vetting Practices* (2017) p 20.

applicant digital footprint, financial position and police check as well as the same checks associated with Baseline security clearance.²⁰⁷

3.33 A NV2 security clearance is required to be renewed at least every 5–7 years. The processes involved in obtaining NV2 clearances are the same as those in NV1 with more referee checks and an additional security interview.²⁰⁸

3.34 Once a person has been granted a security clearance, they are required to disclose to the ATO's security section, security advisor or directly to AGSVA any changes or events which are relevant to the security clearance, for example, entering/leaving a significant relationship, material change in finances or being the subject of a criminal investigation ('notifiable events').²⁰⁹

3.35 Irrespective of whether a person occupies a DSAP, an ATO officer may be required to obtain a security clearance where the position involves access to aggregations of information (for example an Information and Communications Technology administrator) or is otherwise a 'Trusted Position'. A Trusted Position is one where the abuse of the position would cause a level of harm.²¹⁰ For example, where the abuse of that position would result in a level of harm to the agency operations, commercial entities or members of the public, a Baseline security clearance will be required. Where the level of harm could be expected to seriously damage national security (a 'medium to extreme business impact level') the position will require a NV1 security clearance.

3.36 An ATO flowchart outlining how it determines the security clearance level for positions is provided in the figure below.

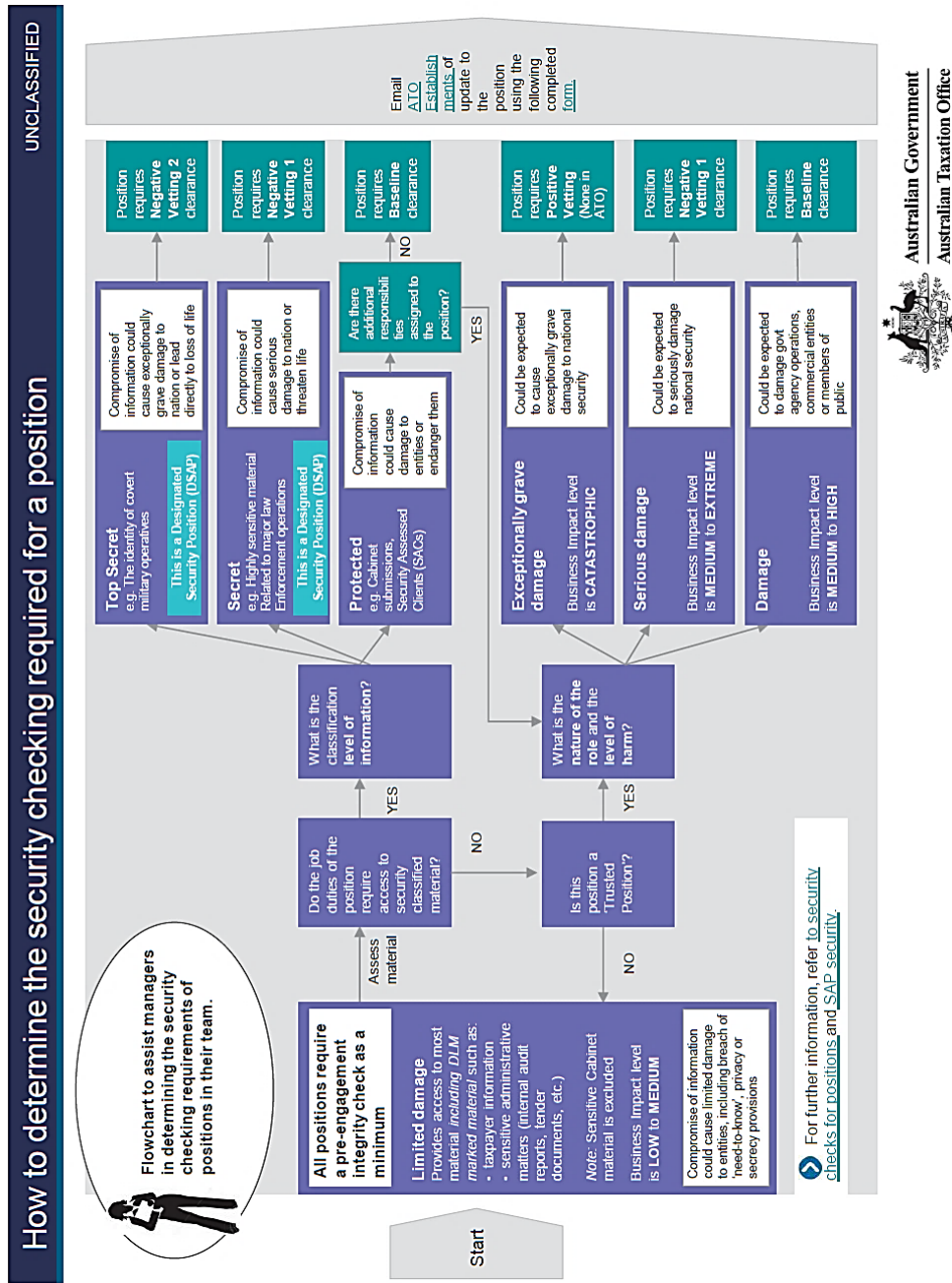
²⁰⁷ *ibid.*

²⁰⁸ *ibid.*

²⁰⁹ Department of Defence, 'Maintaining your clearance' <www.defence.gov.au>.

²¹⁰ AGD, *Australian Government Personnel Security Protocol* (2017) p 16.

Figure 3.2: How the ATO determines which positions require a security clearance



Source: ATO

3.37 Following the events associated with Operation Elbrus, the ATO has more recently examined high risk positions in its own review into conflicts of interest and security clearance processes. The report of this review (ATO September 2017 Report) makes the following observations and recommendation about high risk positions:

...internal integrity related processes and controls should be strongly geared towards those individuals or position holders that, for varying reasons, present a heightened level of risk to the organisation. That is, organisational efforts ... should strongly focus on those positions where non-compliance would result in an unacceptable consequence. As such, we have suggested the development of an approach to identify and manage 'high risk roles', which will further support the existing measures in place. The development of this approach should be informed by work undertaken by FPII in 2015 which identified some 'job 'families' such as those with IT administrator access that may be considered to be of higher fraud and corruption risk....

... Recommendation 6: It is timely for the ATO to identify those positions that would be deemed to be high risk. The identification of high risk roles should consider whether additional scrutiny or controls should be in place to appropriately manage the risks related to those specific roles. Example of controls could include the rotation of roles, dual signoff or security checks above the existing security clearance requirements.²¹¹

3.38 As a result of the above recommendation, the ATO has commenced a process of identifying high risk positions, which is in addition to DSAPs and Trusted Positions, and determining suitable level of checks for those positions. Further risk mitigation measures are also being considered where misconduct by the occupant of those positions would 'seriously undermine the confidence in the ATO's integrity'. The ATO considers that such positions will include those that require officers to:²¹²

- deal with high risk taxpayers;
- liaise with law enforcement agencies to tackle serious criminality, including tax evasion and money laundering;
- have significant access to government data, funds (including significant financial delegations) or assets;
- have administrator access to ATO systems, data or other sensitive information;
- deal with significant or sensitive legislative change; and
- deal with significant or sensitive public or private rulings.

3.39 The ATO must identify, record and review positions that require a security clearance as well as the level of clearance required for those positions.²¹³ The ATO has advised that the level of requisite security clearance associated with the relevant roles is recorded on its HR system, 'SAP'.²¹⁴ Both DSAPs and Trusted Positions are included in this register which is reproduced in Table 3.2 below.

²¹¹ Above n 11, pp 3 and 7.

²¹² ATO, 'ATO Office Minute' (Internal ATO document, 26 September 2017).

²¹³ AGD, *Protective Security Policy Framework*, (9 May 2016) PERSEC 3.

²¹⁴ ATO, 'Security checks for positions' (Internal ATO document, 29 November 2016).

Table 3.2: Number of security assessed positions, by type and functional area

Functional area/Group	Business line	Type of security clearance assessed		TOTAL
		Trusted Positions	DSAPs	
Enterprise Solutions & Technology (EST)	All BSLs	2,642	285	2,927
Client Engagement	PGH	702	251	953
	Smarter Data	575	62	637
	PGI	179	41	220
	Other BSLs	1,064	148	1,212
Corporate and Enabling Services	ATOC	241	60	301
	ATO Finance	431	45	476
	Other BSLs	218	77	295
Law Design and Practice	All BSLs	412	94	506
Service Delivery	All BSLs	786	103	889
Office of Commissioners	N/A	14	0	14
ACNC (a)	N/A	19	29	48
TPB (a)	N/A	26	2	28
TOTAL (b)		7,309	1,197	8,506

Source: ATO, as at 20 February 2018.

Note (a): In accordance with the Schedule 1 of the PGPA Rule the Commissioner of Taxation is the Accountable Authority for the Australian Charities and Not-for-profits Commission (ACNC) and the Tax Practitioners Board (TPB).

Note (b): When comparing this total against the totals in the subsequent tables, please note that since October 2017, there was an increase in the positions requiring a security clearance: ATO communication to the IGT, 20 February 2018.

3.40 As indicated by the Table above, over 85 per cent of security assessed positions are for Trusted Positions. The majority of Trusted Positions are in the Enterprise Solutions & Technology (EST) and Client Engagement Groups.

3.41 Table 3.3 below sets out the total number of staff with security clearances by functional area as at 10 October 2017. The greatest number of staff with higher level security clearances, i.e. NV1 and NV2, are located in the EST, Client Engagement, and Corporate and Enabling Services Groups as well as those in the Office of the Commissioners. The Law Design and Practice and Service Delivery Groups have the lowest number of staff with NV1 and NV2 security clearances.

Table 3.3: Number of staff with security clearances by level and functional area

Functional area/Group	Business line	Security clearance level			TOTAL
		Baseline	NV 1	NV 2	
Enterprise Solutions & Technology	All BSLs	2,694	102	20	2,816
Client Engagement	PGH	670	215	9	894
	Smarter Data	588	12	5	605
	PGI	201	12	2	215
	Other BSLs	1,176	16	0	1,192
Corporate and Enabling Services	ATOC	210	42	4	256
	ATO Finance	442	13	3	458
	Other BSLs	287	31	0	318
Law Design and Practice	All BSLs	505	5	0	510
Service Delivery	All BSLs	867	10	0	877
Office of Commissioners	N/A	4	5	5	14
ACNC (a)	N/A	37	10	3	50
TPB (a)	N/A	28	1	0	29
TOTAL		7,709	474	51	8,234

Source: ATO, as at October 2017

Note (a): In accordance with Schedule 1 of the PGPA Rule the Commissioner of Taxation is the Accountable Authority for the ACNC and the TPB.

3.42 Since September 2016, the ATO has conducted three assessments to determine if staff held the appropriate security clearance levels for their positions.²¹⁵

Table 3.4: Numbers of mismatched security clearances

	Sept 16 – Feb 17	Mar 17 – Aug 17	Sept 17
No. of staff with mismatched clearances	397	243	103
Total no. of security clearances	8,352	8,200	8,200
% of mismatched clearances	4.8%	3.0%	1.3%

Source: ATO, as at September 2017

3.43 Table 3.4 above shows that the percentage of staff who held a security clearance of a lower level than that required for their position ('mismatched security clearance') has declined with each assessment from 4.8 per cent in February 2017 to 1.3 per cent in September 2017. Data from the August 2017 security mismatch report indicates that these mismatches were the result of officers not holding security clearances at all or holding lower security clearance than the positions they held required.²¹⁶

²¹⁵ ATO communication to the IGT, 12 October 2017.

²¹⁶ *ibid.*

3.44 It should also be noted that the ATO September 2017 Report makes the following observations and recommendation about improving the analysis of security clearance mismatches to enable the relevant areas to take appropriate action:

...opportunities have been identified to strengthen the monitoring, reporting and actioning of security clearance mismatches and mandatory training completion rates. Currently these processes are treated as standalone.

Recommendation 7: Opportunities for improvement include better collaboration between Security Vetting and Workforce Analytics to adopt a joint risk based approach to security clearance mismatches and mandatory training. This could consider combining data to identify higher risk situations (e.g. long periods without the required clearance and/or training, or significant mismatches in security clearance held versus those required, failure to obtain required clearances/training, etc.). This analysis should then inform appropriate areas for escalation, including staff managers/SES and FP&II.²¹⁷

3.45 As a result of the above recommendation, the ATO has commenced a process to develop an analytical tool to improve the 'automation and efficiency of producing security clearance mismatch reports'.²¹⁸

3.46 The ATO has since advised that it has improved quarterly security mismatch reporting and, since September 2017, they are being sent to relevant Assistant Commissioners who determine whether the relevant position holders should obtain the requisite security clearance or adjust the security clearance level of the roles.²¹⁹

Waivers for aspects for the security clearance process

3.47 The ATO can seek endorsement from AGSVA for a waiver of parts of the eligibility criteria for holding a security clearance in two circumstances, namely: where the candidate is not an Australian citizen or where they have an 'uncheckable background' which can occur if the candidate has spent time outside of Australia during the 'checkable period'. Furthermore, the Commissioner must form the view that the candidate is 'necessary to the agency meeting its outcomes' and 'the role cannot be redesigned so that access to classified information or resources is restricted to existing personnel with the appropriate clearance'.²²⁰

3.48 The ATO is required to include all waivers within its Annual Protective Security Policy Framework compliance reports.²²¹ The ATO has advised that since July 2015, it had granted 14 waivers (based on citizenship grounds) for Baseline and above security clearances. Waivers were provisionally approved by a Director of the ATOP

²¹⁷ Above n 11, pp 3 and 8.

²¹⁸ *ibid.*

²¹⁹ ATO communication to the IGT, 24 November 2017.

²²⁰ AGD, *Personnel security guidelines – Agency personnel security responsibilities* (2015) pp 37–38.

²²¹ *ibid.*, p 37.

business line but any ratification of the waiver rests with AGSVA.²²² The ATO has advised that it conducts annual reviews of all security clearance waivers issued.²²³

3.49 For non-Australian citizens, a citizenship employment waiver may also be granted where the vacancy requires specialist skills, knowledge or qualifications that are seen to be in limited supply in the Australian labour market and the Deputy Commissioner, ATOP, has approved the waiver. The ATO has advised that it had also recently implemented a policy where non-citizens are not permitted to be employed as permanent employees.²²⁴

3.50 The ATO has also advised that it has employed 28 non-Australian citizens since July 2015.²²⁵ On 6 September 2017, the ATO approved the establishment of a register to record business cases for employment citizenship waivers as well as any work-related visa restrictions. This register is required to be kept up-to-date and is required to be monitored by the Personnel Security Team.²²⁶

Ongoing suitability checks

3.51 In addition to all the security checks described thus far, the ATO has advised that all its employees, who were recruited since 1 July 2016, may be subject to ongoing suitability checks as a condition of their employment:

To be eligible for employment in the ATO, you must be an Australian citizen (at the time you begin employment with the ATO) and agree to have a criminal history records check... You may also be required to undergo further integrity checks during the course of your engagement with the ATO.²²⁷

3.52 It should be noted that employees who were recruited prior to 1 July 2016 are not required to undergo ongoing suitability checks as it had not been incorporated into their conditions of employment when they accepted the position.²²⁸

3.53 For employees who hold a security clearance from AGSVA, the ATO had been relying solely on AGSVA's periodic security clearance renewals as an ongoing suitability check. However, recently, the periods for security clearance renewals was extended by AGSVA, for example the seven year period for a Baseline security clearance renewal was extended to 15 years.

3.54 In mid-2017, the ATO piloted a 'Security Health Check'²²⁹ in the ATOP and ATO Finance business lines which required managers to discuss with staff the currency of their assigned security clearance, identify any notifiable events and confirm that they had completed their security awareness training. Where these steps are not

²²² Department of Defence, 'Security Officer' <www.defence.gov.au>.

²²³ ATO communication to the IGT, 12 October 2017.

²²⁴ ATO, 'ATO Office Minute' (Internal ATO document, 17 August 2017).

²²⁵ Above n 223.

²²⁶ Above n 224.

²²⁷ Above n 223.

²²⁸ *ibid.*

²²⁹ *ibid.*; note that the name of this process was later changed to "Annual Security Clearance Check".

completed by the due date or the relevant requirements are not satisfied, there would be follow-up action, including revocation of the security clearance sponsorship.²³⁰ On 9 March 2018, the ATO rolled out this pilot to all areas of the ATO and such checks are now required to be completed on an annual basis.²³¹ From this date, managers must also provide written confirmation that their staff have complied with this requirement.²³²

3.55 In total, approximately 67 per cent of the ATO workforce undergo one of the above forms of ongoing suitability checks with the remainder (33 per cent) not being subject to such checks.

IGT observations

3.56 As stated earlier, recruitment processes and ongoing monitoring of staff is one preventative measure against internal fraud. The recruitment and retention of suitable individuals upholds the integrity and high ethical values of the organisation, fostering an environment where committing wrongdoing is a rare event.

Establishing the level of checks required for each position

3.57 Appropriate checks conducted at recruitment and on an ongoing basis assists in maintaining the integrity of the workforce. No such system of check can completely eliminate risk of fraud but it can significantly minimise it.

3.58 A balance must be struck between the levels of checks required against the time, cost and intrusiveness associated with such checks. For example, an NV1 clearance has a benchmark processing time of 121 days.²³³ The level of checks has to reflect the risk associated with an unsuitable person filling a particular position.²³⁴ Accordingly, each position has to be assessed to determine the level of risk associated with it and the level of checks required to mitigate those risks.

3.59 As mentioned earlier, the ATO has traditionally conducted pre-employment checks of staff and required staff to obtain a security clearance for those in DSAPs or Trusted Positions. The ATO September 2017 Report indicates that it will be reassessing the security vetting that is needed for 'high risk positions', together with any risk mitigation work needed to address risks if a gap is found to exist.²³⁵ The ATO's work in this area is in its early stages and its outcomes are unclear at this stage. For example, the extent of the reassessment is not clear nor are a number of other related issues such as the distinguishing features of DSAPs, Trusted Positions and 'high risk positions'. It is also not clear whether positions of influence, such as those that involve influencing or coordinating the activities of many staff, would fall within one of these three categories when appropriately risk-assessed.

²³⁰ Above n 11, p 3.

²³¹ ATO communication to the IGT, 1 May 2018.

²³² *ibid.*

²³³ Department of Defence, *AGSVA Key Performance Indicators* < www.defence.gov.au>.

²³⁴ NSW ICAC, *Strengthening employment screening practices in the NSW public sector* (February 2018) p 14.

²³⁵ Above n 212.

3.60 The IGT is of the view that all or the vast majority of the positions at the ATO should be risk-assessed at least once and for areas that present moderate to high risk, a reassessment should be required periodically. It is acknowledged that the ATO has begun to conduct such reassessment for those positions which require a security clearance.

3.61 Having determined the risk levels of each position, appropriate pre-engagement and ongoing checks should be devised and conducted. In doing so, it may be necessary to look beyond the position itself and consider the interactions that a person in such a position has with other staff. For example, roles such as executive assistants should have the same level of security clearance as the positions that they support as they are likely to view and have access to the same security-classified information. It is unclear if the ATO has imposed such a requirement on its support staff. For example, it would be reasonable to expect that all executive and personal assistants to the four Commissioners have the same level of security clearance as the Commissioners they support, for example a NV2 clearance level. However, information provided by the ATO indicates that only five of the fourteen positions in the Office of Commissioners are required to have such security clearances.

Checks conducted at recruitment

3.62 As mentioned earlier, the ATO conducts a number of checks to identify potential issues of concern at the recruitment stage. The ATO has access to its own HR records to check some of these issues for internal candidates but for external candidates, it has to rely on information provided by third parties.

3.63 One of the checks is contacting referees which, in some cases, is done by the ATOP business line rather than the selection panel. Where such checks are performed by the ATOP business line, it provides a degree of independence in the process and mitigates the risk of 'confirmation bias' where the selection panel may not 'place sufficient weight on any red flags because a positive impression of the candidate has already been formed'.²³⁶ However, contacting referees is not mandatory for internal promotions or where the selection panel and/or the delegate already have sufficient knowledge about the candidate.²³⁷ Whilst this may be efficient, it may give rise to perceptions of bias.

3.64 The ATO also obtains the contact details of candidates' current supervisors who are an important, contemporaneous source of information as they may alert the ATO of any suspected fraud or unethical behaviour. However, they may be motivated not to disclose any knowledge of a candidate's impropriety for a number of reasons, such as a desire to help the candidate to relocate, notwithstanding the advice of the Australian Public Service Commission (APSC) to provide 'an honest assessment of work performance, attendance and behaviour'.²³⁸ The risk of such incomplete

²³⁶ Above n 234, p 20.

²³⁷ Above n 182.

²³⁸ APSC, *Managing Integrity Risks in the Workplace – A toolkit* (2016) para [2.1.4].

disclosure by a supervisor may be ameliorated, however, if an enhanced PEIC process is conducted. The latter also assists to address the limitations of referees' feedback.

3.65 It should be noted, however, that since November 2017 the enhanced PEIC process is not conducted for positions at the APS 5 level and below or for contractors unless specifically requested by the relevant business line. As a result, the ATO is limited to confirming the veracity of a candidate's claimed employment history. In such circumstances, the ATO would not be made aware of any misconduct in their previous employment unless disclosed by the nominated referees. It should be noted that, in a wider context, it has been found that eight per cent of employees involved in fraudulent conduct have a known history of dishonesty with a previous organisation.²³⁹

3.66 Accordingly, the IGT is of the view that, for all external candidates, the ATOP business line should obtain relevant information, such as that relating to misconduct, from the HR department of their prior employers as part of the pre-engagement checks. Such action would be consistent with proposed legislation²⁴⁰ to authorise Commonwealth agencies to collect, use, and disclose personal information for the purposes of preventing, detecting, investigating or dealing with fraud or corruption against the Commonwealth.

3.67 Another check conducted at recruitment is the police check where the candidates' names are checked against the Australian Criminal Intelligence Commission's (ACIC) National Police Checking system to identify if they have any 'disclosable court outcomes', such as court convictions, findings of guilt and appearances subject to spent convictions and non-disclosure legislation. However, this police check does not identify connections to organised crime through family members.

3.68 As highlighted by the NSW Independent Commission Against Corruption (ICAC)²⁴¹, for positions that have access to high level security-classified information or have a high 'business impact' risk, it is important to extend employment screening to an applicant's family and associates. For example, Operation Elbrus and related events have revealed that a senior ATO officer has close family members who may have had business and social connections to a number of people known to law enforcement agencies. Unfortunately, the revelation came too late for the ATO to avoid reputational damage.

3.69 Other criminal intelligence holdings, such as the ACIC's National Criminal Intelligence System, contains a valuable source of information which would assist the ATO to ascertain whether candidates for a higher risk position, or their relatives, are known by law enforcement bodies either by reason of their own conduct or that of their associates. Accordingly, the IGT is of the view that the ATO should explore using other criminal intelligence holdings for candidate vetting where it may lawfully do so.

²³⁹ KPMG, *Fraud and Misconduct Survey Australia and New Zealand* (2010) p 15.

²⁴⁰ Schedule 7 to the Crimes Legislation Amendment (Powers, Offences and Other Measures) Bill 2017.

²⁴¹ Above n 234, p 26.

3.70 It is important to note that candidates should be afforded opportunity to address any unsubstantiated allegations against them that are uncovered in the vetting process. It is acknowledged that in some circumstances such information cannot be disclosed to prevent putting others at risk or jeopardise the investigations of law enforcement agencies.

3.71 In addition to the above checks, candidates are currently required to provide a declaration about the state of their tax affairs as part of their applications. If the declaration is later found to be incorrect, the candidate may be subject to disciplinary proceedings. However, these declarations cannot be verified against taxpayer information held by the ATO due to tax secrecy laws which effectively prohibit using such information for employment purposes, notwithstanding any consent for such use.²⁴²

3.72 Public confidence would likely be affected if ATO officers were found to be non-compliant with the very laws that they are tasked with enforcing. For example, if ATO officers were making decisions about late lodgment of income tax returns of others whilst not being compliant themselves, the community would view that as 'double standards'.²⁴³

3.73 An exemption to tax secrecy laws may be required to allow the Commissioner to verify the tax compliance history of candidates before they are offered employment with the ATO.

3.74 In addition to tax compliance declaration, it would be prudent for the ATO to require candidates to also make declarations about their financial circumstances. The ATO's experience shows that problem gambling, for example, may increase the risk of unethical behaviour and fraud.²⁴⁴ In fact, it is an issue amongst all Commonwealth agencies. A census of the most costly fraud incidents in 2014 indicated that gambling was amongst the primary motivations for committing fraud²⁴⁵ whilst some studies estimate that 10 to 25 per cent of problem gamblers commit gambling-related offences, the most common being fraud.²⁴⁶

3.75 Further checks which may be helpful include identifying pre-existing personal relationships with ATO officers as well their financial interests and those of their partners or close family members that may later give rise to conflicts of interest. As stated earlier, the extent of such further checks depends on the level of risk associated with the position in question.

²⁴² *Taxation Administration Act 1953* (TAA 1953) sch 1 s 355-35 and *Privacy Act 1988*, APP 10.

²⁴³ Treasury, *Review of Taxation Secrecy and Disclosure Provisions* (2006).

²⁴⁴ See, for example, Graeme Webber, 'ATO officer jailed', *The Age*, 20 September 2003.

²⁴⁵ See also, AIC, 'Fraud within the Commonwealth: A census of the most costly incidents' (March 2017) *AIC Statistical Bulletin* where gambling is indicated as one of a number of primary motivations.

²⁴⁶ AIC, 'Gambling-motivated fraud in Australia: who, why and how', *AIC Crime Reduction Matters*, No. 72(19) (2008).

Ongoing checks

3.76 After candidates commence employment at the ATO, it is important to conduct ongoing checks to ensure that no subsequent changes or events negatively impact their suitability for their roles. Ongoing checks also provide a safety net where previous checks may not have uncovered all relevant issues.

3.77 The ATO has advised that it has recently implemented a process where managers annually remind employees, who hold security clearances, to report any relevant changes in their circumstances. Managers must also now provide written confirmation that their staff have complied with these requirements. The IGT is of the view that, whilst such reminders and confirmation are helpful, a more rigorous process is needed. Employees should be required to make an annual disclosure, including nil responses, about all matters that are assessed in the pre-employment checks for their current position. Such disclosures should also be periodically checked. Such ongoing checks could also include verification against Australian criminal records, bankruptcies, directorships as well as a social media search. The frequency of these checks may vary depending on the level of risk associated with each position.

RECOMMENDATION 3.1

The IGT recommends the ATO:

- a) *conduct a risk assessment of every position in the organisation to determine the level of pre-employment and ongoing checks required and periodically reassess the risk associated with moderate to high risk positions;*
- b) *use criminal intelligence databases to determine whether candidates for high risk positions are known to law enforcement, either by reason of their own conduct or that of their associates or relatives;*
- c) *as part of its pre-employment checks:*
 - i) *depending on the level and types of risk associated with the relevant position, require candidates to provide declarations about matters such as their financial circumstances; and*
 - ii) *request information, such as that relating to misconduct, from previous employers of external candidates; and*
- d) *require all employees to make an annual disclosure about matters that are assessed in the pre-employment checks of their current position and periodically check such disclosures at a frequency rate reflective of the risk associated with the relevant position.*

ATO RESPONSE

(a) Agree

The ATO will conduct the risk assessments using the various job types to assess the likely integrity risks.

(b) Agree

The ATO will utilise such information for high risk positions to the extent that it is lawful and considered appropriate.

(c) (i) Agree**(c) (ii) Disagree**

The ATO undertakes thousands of engagements each year, the bulk of which are not considered to be in high risk positions. Existing processes involve the declaration of past misconduct by candidates and referee checks with the candidate's current manager / employer. Verification over and above this is done using a risk based approach. A range of other controls are also in place to reduce the risk of fraud from those working for or on behalf of the ATO.

(d) Disagree

All staff undergo security, privacy and fraud training to ensure they are aware of their integrity obligations and the ATO undertakes regular awareness campaigns to remind staff to disclose any changes in their circumstances. Additionally, 40% of ATO staff are subject to annual security discussions with their manager as a result of holding a security clearance. This is reflective of the higher risk involved. To further assure the ongoing suitability of ATO personnel, the ATO proposes to introduce a declaration process for all staff as part of the building pass renewal process (every five years).

ROTATION OF STAFF

3.78 In addition to ongoing checks, risk of internal fraud or other unethical behaviour that may arise post commencement of employment may be further minimised by ensuring that staff do not stay in high risk positions for prolonged periods of time.

Stakeholder concerns

3.79 Certain stakeholders noted that, in relation to the events of Operation Elbrus, Michael Cranston occupied the same positions, including Deputy Commissioner of the PGH business line, for a considerable period and questioned the general appropriateness of officers holding such positions for extended periods. Stakeholders believed that regular rotation of very senior and specialist staff as well as those in high risk positions is important for avoiding the development of enclaves and reducing the risk of undetected fraud. They were also of the view that regular rotation also benefits the organisation and the individual provided that the positions continue to be filled by those with the necessary skillset and interest.

Relevant materials

3.80 The ATO Executive conducts annual discussions following the mid-year performance appraisal process of SES officers.²⁴⁷ The opportunity for SES Band 1

²⁴⁷ ATO, 'SES Moves and Vacancy Discussion' (Internal ATO document, 3 March 2017).

officers to move to different areas is considered during these discussions. The decision to move SES Band 1 officers will depend on factors such as performance as well as whether the officer has 'had a change in role or higher duties opportunities in recent times'.²⁴⁸ The ATO has advised that while there is no set timeframe for the rotation of SES officers there is a 'rough guide' of three years in a role before an SES officer may be required to rotate to a new area.²⁴⁹

3.81 The ATO September 2017 Report made a number of recommendations including the need to identify high risk roles and to consider additional scrutiny or controls for these positions.²⁵⁰ Subsequently, a newly established team within the ATOP business line, called the ATO Integrity Unit, commenced a pilot to address this recommendation.²⁵¹ The pilot developed a range of proposed controls for such positions which include 'fixed term in role (given effect by contract position or staff rotation)' and 'mandated time out of role (minimum continuous stretch of leave or short term at level rotation)'.

3.82 In relation to Michael Cranston's tenure within the PGH business line, as noted in Appendix B, Michael Cranston was the Deputy Commissioner of the Serious Non-Compliance (SNC) business line from 2007-08 until 2011-12 when he became the Deputy Commissioner of the Small and Medium Enterprises (SME) business line. When the SNC and part of the SME business lines were amalgamated into the PGH business line in 2013-14, Michael Cranston became the Deputy Commissioner of PGH. Thus until the events of Operation Elbrus in May 2017, Michael Cranston held the senior position of Deputy Commissioner of SNC and its successor business line, PGH, for eight years.

IGT observations

3.83 Those in senior positions have high levels of influence over decisions and the individuals who report to them. Such influence is not limited to senior officers. Specialists holding vital knowledge about the inner workings of the organisation, such as IT, also wield considerable influence. The prolonged stay of officers in such positions may heighten the risk that subcultures may form under their influence which are out of step with the organisation's values.²⁵² The ACLEI has noted that, within the law enforcement context:

²⁴⁸ *ibid.*; ATO, 'SES Band 1s (including those on CLP Program) to be considered for moves' (Internal ATO document, undated).

²⁴⁹ ATO communication to the IGT, 26 October 2017.

²⁵⁰ Above n 11, p 7.

²⁵¹ ATO, 'High Risk Roles - Integrity risk susceptibility pilot' (Internal ATO document, undated).

²⁵² Australian Commission for Law Enforcement Integrity (ACLEI), Griffin, M, *Integrity Leadership: Countering corruption impulses in difficult environments*, Speech to the Australian Public Sector Anti-Corruption Conference (2015) p 2.

strong bonds that exist amongst staff ... may result in sub-cultures of misplaced loyalty and accompanying loss of objectivity, which in turn may lead to a reluctance to report misconduct or, in some cases, to a propensity to cover-up wrongdoing.²⁵³

3.84 In order to effectively manage the risks of either misplaced loyalties or team values diverging from those of the ATO, consistent with practices of enforcement agencies, it would be prudent for the ATO to implement strategies such as regular rotation of staff in high corruption risk areas.²⁵⁴

3.85 As noted above, the ATO also considers 'length of time in position' for determining the movement of SES Band 1 officers. It does not appear, however, that such formal considerations occur for SES Band 2 officers, i.e. Deputy Commissioner level. The current consideration of 'period in position' for SES Band 1 officers also appears to focus purely on the career progression of officers.

3.86 It is encouraging, however, that the ATO September 2017 Report and subsequent actions are looking at rotations for high risk roles. The IGT supports such an initiative and is of the view that the ATO should formalise its rotation process for SES Band 1 and SES Band 2 officers as well as any other high risk roles, not only for career progression purposes but also for addressing integrity risks.

3.87 It is acknowledged that rotations may present challenges for a large organisation like the ATO that relies on both IT to service the public as well as tax technical and commercial knowledge to respond to an increasingly complex environment.²⁵⁵ Therefore, succession planning would be required to ensure multiple officers have the expertise and ability to fill these roles.

3.88 Accordingly, the IGT is of the view that the ATO formalise its rotation process for SES Band 1 and SES Band 2 officers as well as for high risk roles. IGT is also of the view that the ATO proactively identify qualified and experienced individuals as part of succession planning arrangements to facilitate such rotation.

RECOMMENDATION 3.2

The IGT recommends the ATO formalise its fraud risk controls relevant to SES officers and officers in high risk roles including the periodic rotation of officers.

ATO RESPONSE

Agree

²⁵³ ACLEI, *Resistance to corruption: A pilot review of the internal anti-corruption arrangements of the Australian Crime Commission and the Australian Federal Police* (2009) p 2.

²⁵⁴ ACLEI, 'Integrity framework checklist for law enforcement agencies' <www.aclei.gov.au>.

²⁵⁵ The risk with long tenures is likely to heighten as senior roles within the ATO may become more specialised in the future, making them difficult to replace or rotate. For future trends, refer to the IGT's current *Review into the Future of the Tax Profession* (2018).

FRAUD TRAINING AND AWARENESS

3.89 Fraud training performs an important function in communicating to staff the organisation's values as well as raising awareness of the types of behaviour that constitute fraud.²⁵⁶ A clear understanding of fraud and reminders of its serious consequences help to foster an ethical culture where internal fraud is a rare event and, if it arises, staff can promptly identify and report it.

Stakeholder concerns

3.90 Stakeholders have raised a number of concerns about the content and enforcement of fraud awareness and ethics training that is delivered to ATO officers. In particular, the effectiveness of online training packages was questioned and the difficulty of ensuring that they are appropriately completed by ATO officers was also raised. For example, stakeholders have observed that recent refresher training allowed officers to simply book the online training module and 'click confirm participation' to satisfy the requirements. By contrast, other stakeholders recalled that there was a previous requirement for SES officers to provide assurance to the relevant Deputy Commissioners that their staff had completed the training. It was also linked to the performance pay of SES officers.

3.91 In relation to the regularity of the ATO's fraud training and communications, some stakeholders were of the view that the ATO had not reinforced the importance of fraud awareness for a long time. Others, however, recalled that the ATO previously conducted training and refresher courses on such topics as conflicts of interest for all ATO officers and that prior to the commencement of certain sensitive audits, the team involved would need to ensure that the training was completed.

Relevant materials

3.92 All new starters at the ATO, including casual staff and contractors²⁵⁷, are required to complete a Security, Privacy and Fraud online training package (Standard SPF Training) within one month of commencement.²⁵⁸ Thereafter, refresher training must be completed every two years.²⁵⁹

3.93 All managers with direct reports are also required to complete the online 'Security, Privacy and Fraud: Managers' training package (Managers' SPF Training) in addition to the Standard SPF Training.²⁶⁰

3.94 The Standard SPF Training takes approximately one and a half hours to complete and covers topics such as security classifications, IT security, passwords,

²⁵⁶ Above n 84, p 38.

²⁵⁷ ATO, 'Mandatory training in the ATO' (Internal ATO document, 24 October 2017).

²⁵⁸ ATO, 'Manager - Employee new to the ATO' (Internal ATO document, undated) p 4.

²⁵⁹ Above 257.

²⁶⁰ *ibid.*

fraud and fraud reporting.²⁶¹ The Managers' SPF Training covers topics such as threatening behaviour, breach of information disclosure rules, security classification, working from home and other security concerns.²⁶² Both of these packages also cover a range of other integrity-related topics such as conflicts of interest and unauthorised access as well as the acceptance and declaration of gifts.²⁶³

3.95 The ATO reviews and updates both training packages annually, with the aim of improving the package's readability, and when needed to take into account changes in legislation and policy.²⁶⁴ The current versions of these training packages deliver content through interactive slides, videos and workplace scenarios which are aimed at engaging the user and improving memory retention. By contrast, previous versions of these training packages were delivered as textual documents for the officer to study.²⁶⁵

3.96 Once a new starter has completed reviewing the content of the Standard SPF Training package, they are required to complete a multiple choice assessment. Some scenario-based decision-making questions are included in the Managers' SPF Training assessment but are not included in the Standard SPF Training assessment.²⁶⁶ For both training packages, the assessment is comprised of ten questions which are selected from a pool of 20.

3.97 For both training packages, the officer must correctly answer at least seven questions in the assessment (70 per cent pass mark) to successfully pass and complete the training package. If the officer does not pass the assessment, they are able to access and attempt the assessment two additional times. If the officer is not able to successfully pass after three attempts, access to the assessment will be locked. Access to the assessment can be reset after the officer's team leader has been provided with assurance that the officer has learned the material.²⁶⁷

3.98 The ATO retains records of completion of mandatory training on its electronic employee record system. Since June 2017, the ATO sends quarterly reminder e-mails to staff to notify them of any outstanding training requirements that they may need to meet. From July 2017 onwards, completion records have been automatically provided to team leaders in monthly manager reports that cover the officers within their reporting line.²⁶⁸ Prior to the implementation of these changes, the training completion records were manually extracted from the ATO's electronic employee record system and passed on to business line representatives who were responsible for monitoring conformance with the training requirements by staff in their area.

²⁶¹ ATO, 'Security, Privacy & Fraud Assessment questions - August 2017' (Internal ATO document, August 2017) pp 2-3.

²⁶² ATO, 'SPF Managers Assessment questions - August 2017' (Internal ATO document, August 2017) p 2.

²⁶³ ATO, 'Security, Privacy and Fraud - Accessible version' (Internal ATO document, June 2017).

²⁶⁴ ATO, 'Publishing Checklist' (Internal ATO document, undated).

²⁶⁵ ATO, 'Security Awareness - Security Essentials' (Internal ATO document, undated circa 2011); ATO, 'Security, Privacy and Fraud' (Internal ATO document, undated circa 2011).

²⁶⁶ Above n 261, pp 3-10; Above n 262, p 2.

²⁶⁷ Above n 261, p 1; Above n 262, p 1.

²⁶⁸ ATO communication to the IGT, 20 October 2017.

3.99 It is a manager's responsibility to use the reporting systems in place to identify and address any instances of non-completion of training amongst their staff.²⁶⁹ If such training has not been completed within a 'few weeks' of being required, the ATO's People Support Team (PST) will contact the relevant manager and, if required, follow up with staff directly in the following month.²⁷⁰

3.100 The completion rate of the Standard SPF Training is monitored on an organisational basis by the ATO's leadership as a quantitative indicator of the overall integrity of the organisation.²⁷¹ An ATO Executive Report from May 2017 indicates that the completion rate by internal ATO employees meets the target of 97 per cent but the completion rate by external workers was significantly below this benchmark at 56 per cent.²⁷² As a result, the ATO has been seeking to implement strategies to improve these figures, such as using third-party software to improve external system access to training materials, sending regular targeted e-mails to the managers of contractors who have not completed the required training and confirming with vendors the ATO's training requirements and expectations.²⁷³ The ATO has recently advised the IGT that as at 31 January 2018, there were 1,464 contractors who had not completed the Standard SPF Training and assessment. Of these 1,464 contractors, 896 had the necessary systems access to complete the training and assessment.²⁷⁴

3.101 The ATO also provides non-mandatory fraud and ethics training via other channels such as targeted face-to-face training²⁷⁵, telepresence²⁷⁶, webinars²⁷⁷, live streaming and online discussion forums²⁷⁸. In addition, the ATO has recently advised the IGT that in 2016-17, FPII attended 22 site visits which included multiple interactive sessions attended by a total of 1,537 participants – an increase from 2015-16 where three sessions were held and attended by 350 participants.²⁷⁹ Staff can also participate in external training sessions run by other government organisations or private sector providers to obtain a range of fraud and security qualifications.²⁸⁰

3.102 In addition, the ATO undertakes a number of awareness raising activities through multiple channels as part of the FPII unit's communication strategy, which seeks to achieve 90 per cent awareness amongst ATO staff regarding the activities

²⁶⁹ ATO, 'Supporting mandatory Security, Privacy & Fraud training completion' (Internal ATO document, undated).

²⁷⁰ ATO, 'Non-completion of training' (Internal ATO document, 22 August 2017) p 1.

²⁷¹ Above n 101, p 2.

²⁷² ATO, 'ATO Executive Report Quarter 3, 2016-17' (Internal ATO document, May 2017) p 47.

²⁷³ *ibid.*, p 44.

²⁷⁴ ATO communication to the IGT, 20 February 2018.

²⁷⁵ For example, the FPII unit will conduct on-site awareness sessions in the Perth office as a result of increased counter workplace behaviours observed in the 2017 Organisational Behavioural Assessment; ATO, 'Australian Taxation Office Organisational Behavioural Assessment - 2017' (Internal ATO document, 2017) p 14.

²⁷⁶ ATO, 'Fraud and corruption project engagement and advice' (Internal ATO document, submitted to the Audit and Risk Committee (ARC), on 6 September 2017) p 3.

²⁷⁷ ATO communication to the IGT, 20 October 2017.

²⁷⁸ *ibid.*

²⁷⁹ ATO communication to the IGT, 1 December 2017.

²⁸⁰ ATO, 'Fraud/Security Awareness, Privacy and Investigations External Training Programs' (1 July 2015 to 30 September 2017) (Internal ATO document, undated); ATO, 'Fraud/Security Awareness, Privacy and Investigations Conferences and Forums' (1 July 2015 to 30 September 2017) (Internal ATO document, undated).

which indicate fraud and corruption, including the consequences of involvement in these activities.²⁸¹ Examples of such awareness raising activities include regular staff newsletter articles, digital signage within ATO office buildings, 'kNOw fraud' messaging on officers' log-on and lock screens, content on the ATO intranet²⁸² and special events such as 'security, integrity and fraud awareness week'.²⁸³

IGT observations

3.103 As mentioned earlier, fraud training and awareness programs can perform a very important role in shaping a positive organisational culture by recalibrating individuals' judgements of improper conduct. While there is usually common agreement that certain egregious actions will constitute fraud and/or corruption, for actions which are at the fringes, there may be disagreement and a need for clarity. As the ATO recognised in its 2017 Corruption Risk Review:

individuals who undertake corrupt conduct may themselves not identify or rationalise such activity as being in itself corrupt. Some individuals may in fact be deceived into performing or enabling corrupt acts without knowing (such as responding to a manager's request for what appears to be a legitimate need).²⁸⁴

3.104 The ATO's fraud and prevention training and awareness programs can help to guide staff conduct and prevent unethical behaviour. Importantly, they can provide staff with the confidence to proactively refer matters to the FPII unit when they identify fraud and corruption risks. As will be discussed in the following chapter, such referrals are one of the main sources for FPII investigations – more than two-thirds of investigations were initiated as a result of staff referrals.²⁸⁵ Without an effective training program, a key pillar of the ATO's integrity framework would be eroded as ATO officers are better placed to detect certain risks, such as conflicts of interest, than automated detection systems.

3.105 In the IGT's view, fraud training should be completed soon after commencement of employment so that new starters begin their career at the ATO on the right footing. The current situation where new starters have one month to complete the Standard SPF training which is not part of induction tasks, such as obtaining wi-fi access, referring to the ATO's social media guidelines and arranging to provide systems access²⁸⁶, may create a perception that completion of fraud training is not considered to be as high a priority as the other tasks.

3.106 Furthermore, there is a risk that new starters may be able to access taxpayer information before the ATO is able to assure itself that staff understand their obligations regarding fraud, privacy and security issues. Relevantly, New Zealand's

²⁸¹ ATO, 'Fraud Prevention & Internal Investigations Communication Strategy (2016-2017)' (Internal ATO document, undated).

²⁸² ATO, 'FPII Communication Strategy (2016-2017)' (Internal ATO document, undated).

²⁸³ ATO, 'Security, Integrity and Fraud Awareness Week 2017 Schedule' (Internal ATO document, undated).

²⁸⁴ Above n 10, p 7.

²⁸⁵ ATO, 'Internal Investigations Analysis Breakdown of Reasons since 1 July 2015' (Internal ATO document, undated).

²⁸⁶ ATO, 'Induction checklist for managers with new employees' (Internal ATO document, 12 February 2018).

IRD requires all three mandatory online training packages on code of conduct, security and privacy to be completed within the first week. Accordingly, the IGT is of the view that the mandatory Standard SPF training package should be completed by new starters as soon as they obtain access to the ATO's systems and before they have access to taxpayer information.

3.107 The above approach would ensure no one who has not undertaken the SPF training would have access to taxpayer information. It is acknowledged that the ATO currently performs well in this area with respect to its officers, 97 per cent of whom have successfully completed the necessary training. However, the completion rate for contractors engaged by the ATO is only 56 per cent and is a concern.²⁸⁷ The ATO is currently trialling solutions to allow contractors to complete training without the need to log onto the ATO's systems. However, the IGT believes that this is only a partial solution as 61 per cent of contractors who had not completed the mandatory training had access to ATO systems to complete the training.²⁸⁸ The IGT is of the view that, where a contractor has access to the ATO's systems but fails to complete the mandatory training package after a reasonable timeframe of follow-up, the ATO should withdraw their access to its systems.

3.108 Successful completion of mandatory training packages, however, does not of itself guarantee that staff have absorbed the material and refined their understanding of appropriate behaviours. The design of the assessment has significant impact on appreciation of the course content. For example, staff may feel a deep understanding is not required as the assessment is not particularly onerous or that the consequences of failure are insignificant.

3.109 The assessment of the Standard SPF Training package is designed such that staff may be deemed to have successfully passed the assessment despite three incorrect answers in each of three possible attempts. Such an assessment methodology increases the probability that questions which were posed in previous attempts will be raised again. As there are a limited number of potential answers in a multiple choice format, it is possible for staff to successfully pass the assessment without fully understanding the training package's content.

3.110 Furthermore, the learning outcomes for the Standard SPF Training package and its accompanying assessment do not contain any workplace specific examples.²⁸⁹ Therefore, even if staff have understood the content of the training, they may be uncertain as to how it applies in their particular work area. This view appears to be consistent with the results of the ATO's latest Fraud and Corruption Control Survey in which only 77 per cent of respondents indicated that they had the necessary levels of awareness to recognise fraud and corruption even though the completion rate of the Standard SPF Training for officers is 97 per cent.²⁹⁰ The IGT is of the view that the Standard SPF Training assessment could be improved by the inclusion of tailored

²⁸⁷ Above n 272, p 47.

²⁸⁸ ATO communication to the IGT, 20 February 2018.

²⁸⁹ Above n 261.

²⁹⁰ ATO, '2016 ATO Fraud and Corruption Control Survey' (Internal ATO document, 2016).

scenarios which deal with common ethical issues that arise in various ATO business areas.

3.111 The manner in which fraud training is delivered is equally important for staff engagement and understanding of risks of internal fraud. Both the Standard SPF Training and the Managers' SPF Training packages are delivered online. Whilst the ATO has sought to improve a reader's active engagement with the training through increased use of audio-visual materials and interactive elements, there is scope for further enhancement such as allowing staff to raise questions. In the IGT's view, fraud prevention training for new starters ought to provide opportunities to raise questions and receive immediate response as well as be able to engage in discussion where opinions differ. Such an approach would provide new starters with a deeper understanding and ethical conduct is more likely to become second nature to them.

3.112 The induction of new staff in New Zealand's IRD involves their manager conducting a guided discussion with them about general ethical matters as well as workplace scenarios relevant to their area of work. This allows the manager to gauge their new team member's understanding of their obligations and pave the way for the new starter to raise relevant issues with their manager in the future. It also reinforces the message that ethics and fraud awareness is an integrated aspect of their day-to-day work and not a separate 'corporate' obligation.

3.113 In the IGT's view, the ATO should adopt a similar approach by requiring its managers to conduct guided discussions on ethical matters with new starters as soon as they have completed their Standard SPF Training assessment. Such discussion should be aimed at testing the new starter's ability to identify ethical issues arising from practical scenarios in their area of work. For example, individuals in the TEC area of the PGH business line may be provided with a scenario designed to test their ability to identify an organised crime group's attempt to 'cultivate' a colleague. Alternatively, individuals working in the PGI business line may be provided with a scenario designed to test their ability to identify the ethical issues involved in auditing a company in which their parents may have a substantial financial interest.

3.114 The success of the above approach, however, depends on managers' ability to instil integrity values which are consistent with the ATO's. Research indicates a new starter's first supervisor is one of the most powerful factors in shaping his/her approach to integrity issues²⁹¹ and if the supervisor does not display loyalty to the ethical and professional standards of the organisation and instead conveys a 'that's the way we do things here' attitude, the written rules will be ignored by the new starter.²⁹² It has also been noted that workplace sub-cultures can result in misplaced allegiance to individuals over and above the organisation's professional standards.²⁹³ This highlights the importance of the supervisor's own ethical standards being aligned with that of the

²⁹¹ Queensland Crime and Misconduct Commission, 'Improving misconduct in the QPS: the importance of ethical culture' (2013) 11 *Research and Issues*.

²⁹² Queensland Police, *Taskforce Bletchley* (2015) p 21.

²⁹³ Philip Moss Integrity Commissioner, 'Matching measures to risks' (Speech delivered at the Corruption Prevention Network (CPN) Seminar Hosted by the ATO, 12 June 2009) p 8.

organisation.²⁹⁴ For this reason, the IGT considers that for such a discussion to take place, the ATO should provide adequate support for the relevant supervisors or managers.

3.115 Support for managers may be in the form of face-to-face training provided by the ATO's fraud and integrity experts, namely those working in the FPII unit. This unit is ideally suited to deliver such training to supervisors and managers as their daily work involves the investigation and resolution of ethical issues arising in the workplace. This includes providing instruction on the necessary skills they will need to instil the desired values in staff and in dealing with sensitive situations, such as when a staff member has been involved in, or has observed, misconduct.

3.116 Until recently, fraud training delivered by the FPII unit would have required officers to travel to the relevant locations to deliver/receive the training. However, travel is no longer a prerequisite with the ATO's increased use of videoconferencing, telepresence and webinars. Whilst it is ideal to deliver fraud training in person, there are costs associated with this, especially as the ATO offices are geographically dispersed.

3.117 It would be beneficial for the FPII unit to deliver the initial fraud training in person or through telepresence sessions as it helps the establishment of rapport and familiarity between FPII officers and new starters. In New Zealand's IRD, this kind of familiarity and rapport with the Integrity Assurance team was encouraged to give IRD officers greater confidence to report fraud should the need arise. There is a lesser need to deliver refresher training in person or through telepresence and these can be delivered through such means as webinars.

RECOMMENDATION 3.3

The IGT recommends the ATO strengthen its fraud awareness and ethics training by:

- a) requiring new staff to complete the mandatory fraud training during their induction process and prior to allowing them access to taxpayer information;*
- b) withdrawing access to ATO systems for contractors who fail to complete the mandatory training package within a reasonable timeframe;*
- c) incorporating into the assessments of mandatory training packages, a series of practical scenarios that requires staff to apply ethical principles;*
- d) requiring managers to discuss with new starters ethical matters as they apply to their work area, including by way of practical scenarios, and ensuring that those managers receive sufficient guidance and support for this process to take place shortly after new starters have completed the mandatory fraud training; and*
- e) increasing the level of staff interaction in its mandatory fraud training particularly those delivered by the Fraud Prevention and Internal Investigations unit.*

²⁹⁴ Above n 292, p 161.

ATO RESPONSE

(a) **Agree**

(b) **Agree**

(c) **Implemented**

(d) **Agree**

(e) **Agreed**

The ATO has already expanded the channels which employees engage, using internal communication products, which allows for real-time engaging discussions.

CONTROLS IN RELATION TO CONFLICTS OF INTEREST

3.118 The importance of managing conflicts of interest in the public sector is highlighted by the NSW ICAC:

The community has a right to expect that public officials at all levels perform their duties in a fair and unbiased way, and that the decisions they make are not affected by self-interest, private affiliations, or the likelihood that they, or those close to them, will financially gain or lose. The perception that a conflict of interest has influenced an outcome can undermine public confidence in the integrity of the organisation and the individual. Unresolved or badly managed conflicts of interest can actually lead to corruption or abuse of public office, or the perception that these exist.²⁹⁵

3.119 The OECD has also noted the connection between inadequately managed conflicts of interest and corruption.²⁹⁶ Accordingly, it is important for the ATO to have strong controls in place to ensure conflicts of interest are appropriately identified and managed to prevent unethical behaviour.

Stakeholder concerns

3.120 Stakeholders have raised a number of concerns about the adequacy of the ATO's management of conflicts of interest. In particular, stakeholders have observed that the controls which the ATO has in place for declaring and managing conflicts of interest do not compare favourably to those adopted by others, for example the courts or the private sector.

3.121 Stakeholders have suggested that the ATO should strengthen the above controls by requiring all staff to formally declare their interest with respect to the sensitive information to which they have access. Some officers, for example, have access to market sensitive information which provides them with an opportunity for insider trading. Other ATO officers may have been in the private sector previously and

²⁹⁵ NSW ICAC, *Identifying and managing conflicts of interest in the public sector* (2012) p 2.

²⁹⁶ Above n 35, p 96.

may now be dealing with former clients or colleagues. There is a concern that the ATO's current controls are not adequate for managing the risk of conflicts of interest inherent in these types of situations. The perception is that the only control is self-disclosure, which is not checked, analysed or otherwise monitored.

3.122 Stakeholders have also raised concerns about lack of controls where ATO officers leave the organisation to join the private sector. A number of submissions asserted awareness of situations where an ATO officer has signed off on a 'very advantageous' negotiated outcome for a taxpayer and, soon afterwards, that officer left the ATO to join the firm that was advising taxpayer in question. To address this potential issue, stakeholders have suggested a number of options such as the implementation of 'gardening leave' provisions. They have also suggested a system of 'changing the locks' to periodically change certain sensitive internal ATO information so that the latter cannot be advantageously used by those leaving the ATO.

3.123 Questions have also been raised about family members, spouses or partners who work in the same areas within the ATO or in related roles and the extent to which they may be allowed to influence one another's views or collude to achieve certain outcomes. There are perceptions that former associates were recruited from the private sector in preference to internal candidates who may have possessed more relevant experience and been better suited to the roles in question.

3.124 Stakeholders have also made general observations that the ATO, in its attempt to cut red tape, may have gone too far and weakened the pre-existing controls and integrity framework. There is a concern that the current ATO guidelines and CEIs may not provide staff with sufficient guidance to properly deal with a variety of problematic situations.

Relevant materials

3.125 There are three legislative sources which impose an obligation on ATO officers to declare conflicts of interest.

3.126 Firstly, section 42 of the PGPA Act requires financial statements to be prepared in accordance with the accounting standards. Since 1 July 2016, *Australian Accounting Standard AASB 124 Related Party Disclosures* applies to public sector entities with the result being that ATO SES officers are required to disclose any related party transactions that they or their close family members may have with the ATO.

3.127 Secondly, subsection 13(7) of the *Public Service Act 1999* requires APS employees to take positive steps to avoid conflicts of interest, as it requires them to:

- take reasonable steps to avoid any conflict of interest (real or apparent) in connection with their employment; and

- disclose details of any material personal interest they may have in connection with their employment.²⁹⁷

3.128 If an ATO officer does not comply with the above obligations and does not disclose material personal interests, they may be in breach of the APS Code of Conduct which may in turn result in disciplinary sanctions, including termination.²⁹⁸

3.129 Thirdly, subsection 13(5) of the same Act requires employees to ‘comply with any lawful and reasonable direction given by someone in the employee’s agency who has authority to give the direction’. The Commissioner has given direction to ATO officers, in the CEI 2014/06/10, to disclose conflicts of interest. Failure to follow a CEI may also result in the ATO officer being found to have breached the APS Code of Conduct.

3.130 CEI 2014/06/10 was implemented in June 2014 to replace an earlier ATO policy. Subsequently, it has undergone a substantial update in October 2017 as a result of an internal review which was conducted following the events connected with Operation Elbrus. A brief outline of the initial CEI, the findings of the internal review and resulting changes in the update are provided below.

ATO policy prior to October 2017

3.131 From November 2014 to October 2017, CEI 2014/06/10 had required all ATO officers to take all reasonable steps to identify, avoid and/or manage any conflicts of interest as well as ensure that they were not being improperly influenced by family, personal or other relationships. Where officers became aware of a conflict of interest, they were to discuss it with their manager and submit conflict of interest forms if their manager required it.²⁹⁹ It should be noted that until late 2016, such forms were kept in a register that each business line maintained themselves. Since late 2016, however, the ATO implemented a single ATO register which recorded, on a prospective basis, all such conflicts of interest forms.³⁰⁰

3.132 CEI 2014/06/10 defined a conflict of interest as a situation in which ‘a person’s personal interests could appear to, or are likely to inappropriately influence the performance of their duties. They may be real, perceived, or potential and may be financial or non-financial.’³⁰¹ The CEI also set out the test to apply in identifying a conflict of interest, namely ‘whether an impartial observer would reasonably question if the personal factors may inappropriately influence the way you behave and the way you carry out your duties’.³⁰²

3.133 ATO managers were required to ensure that their staff were aware of and complied with their obligations under the CEI. As the authorised decision makers, managers had to ensure that conflicts of interest were brought to their attention and

²⁹⁷ *Public Service Act 1999* s 13(7).

²⁹⁸ Above n 81; *Public Service Act 1999* s 15.

²⁹⁹ ATO, ‘Chief Executive Instruction 2014/06/10 Conflict of Interest’ (Internal ATO document, 1 May 2017).

³⁰⁰ Above n 11.

³⁰¹ Above n 299.

³⁰² *ibid.*

addressed promptly. Where the conflicts of interest involved contact with persons engaged in illegal conduct, that matter had to be brought before a Deputy Commissioner.³⁰³

3.134 CEI 2014/06/10 also outlined several other principles for managing conflicts of interest and made reference to the ATO's other existing CEIs regarding the receipt of gifts and engaging in outside employment. It did not contain any additional consolidated guidance or examples on how conflicts may manifest themselves in the workplace. It did, however, provide a link to an explanatory video on how to apply the policy. In total, the CEI was two pages long.

Internal ATO review of conflicts of interest policies and procedures

3.135 As stated earlier, prompted by the events of Operation Elbrus, the ATO commenced an internal review to assess 'the extent to which current [conflict of interest] policies and procedures are appropriate to address integrity risks [and] whether processes and systems are effective to ensure officers comply with policy requirements and their obligations'.³⁰⁴ The review examined, not only CEI 2014/06/10 and associated guidance, but also broader processes such as the administration of the conflicts of interest register. The CEI had been scheduled to be reviewed at a later time, however, the events in Operation Elbrus resulted in the review being brought forward.

3.136 The resulting ATO September 2017 Report made a number of recommendations, with four of these being about the ATO's management of conflicts of interest. One key aspect of these recommendations was the need to update guidance material for ATO officers. The guidance was believed to be 'a large volume dispersedly located'.³⁰⁵ Other key aspects of these recommendations related to increasing staff awareness of the ATO's policies and improving how the ATO handles the conflicts of interest declarations. These key aspects are summarised below:

- a central conflicts of interest register to be maintained that contains all conflicts of interest declarations made and that the declarations include the period for which the conflicts existed;
- declarations which had been previously made to be resubmitted by staff if they relate to ongoing conflicts:
 - [conflicts of interest] declarations relating to ongoing conflicts, even if previously reported, should be resubmitted by staff to ensure the current register is complete, and to assist current managers in meeting their conflict of interest responsibilities in relation to current staff³⁰⁶;
- periodic analysis of the register's contents to assess completeness and to identify broader themes for dissemination and response;

³⁰³ *ibid.*

³⁰⁴ ATO, 'Review of Integrity Measures' (Internal ATO document, 8 June 2017).

³⁰⁵ Above n 11, p 5.

³⁰⁶ *ibid.*, p 4.

- the 'associations' and 'reportable contact' that staff must declare to be more clearly documented and such declarations to be made in the same manner as a conflict of interest declaration;
- SES conflict of interest declarations to be made as part of the SES annual declaration process and their managers be required to acknowledge and approve them; and
- conflicts of interest and security clearance requirements to be included in the existing ATO-wide fraud and integrity awareness and other education campaigns to create awareness among staff and managers of their responsibilities regarding such requirements.

3.137 Management agreed with the recommendations in the ATO September 2017 Report and, as a result, CEI 2014/06/10 as well as supporting guidance was updated and released to all staff on 12 October 2017.³⁰⁷ As CEI 2014/06/10 and the associated guidance underwent significant change, these updated documents are considered in more detail below.

Updated CEI 2014/06/10 and associated guidance regarding conflicts of interest

3.138 The updated CEI made a number of significant changes to ATO staff responsibilities as well as the process for disclosing, considering and registering conflicts of interest. One of these changes was to expand the application of the CEI to Australian Charities and Not-for-profits Commission (ACNC) and Tax Practitioners Board (TPB) staff, including SES officers. Another change was to increase the responsibilities of officers by incorporating additional requirements and providing greater clarification of existing requirements, including the following:

- Review your declarations and management of conflicts of interest when your circumstances change. For example:
 - if there is a change to your role, duties or the clients you are dealing with
 - when you undertake a particular task such as a procurement or recruitment
 - when you acquire a new financial or personal interest
- Ensure you are not influenced by financial interests, family, personal or other relationships and manage situations where you would be perceived as being influenced.³⁰⁸

3.139 The additional officer requirements were further explained and include the following:

Conflicts may be ongoing or temporary. When you change roles you must review your financial and personal interests having regard to your new duties and identify and report any conflicts that arise due to a change. If you undertake a particular task such as a procurement, recruitment or writing a share market sensitive taxation ruling, you need to consider if your personal or financial interests might give rise to a conflict of interest in respect of that task that should be reported.

³⁰⁷ ATO communication to the IGT, 2 November 2017.

³⁰⁸ Above n 81, para [5].

Examples of the type of financial interests that may need to be declared include:

- Shares or options in a company to which your work[; and]
- An interest as a beneficiary of a trust to which your work relates.

Examples of personal interests or associations that may need to be declared include:

- Personal relationships or close associations with persons such as journalists or members of the tax profession, or employees of an organisation to which your work relates[; and]
- Close personal and/or family relationships between staff members that may give rise to perceptions of favouritism or nepotism.³⁰⁹

3.140 Managers were also given greater responsibilities and their existing responsibilities were clarified in the updated CEI. These included ensuring:

- conflicts of interest matters brought to [their] attention are dealt with promptly by discussion and notification via the ATO Integrity Register form and are escalated to the appropriate decision maker if it is not [themselves; and]
- mandatory training is current for [them] and all of [their] employees, including contractors.³¹⁰

3.141 The updated CEI was more than double the size of the previous version and also provided a link to a guidance document which emphasises the importance of managing conflicts of interest, including that ‘failing to effectively manage conflicts of interest can lead to improper decision-making and corruption and will expose employees to adverse consequences’.³¹¹ This document also provides more expansive guidance on a number of issues including the following.

Definitions of conflicts as well as interests

3.142 Whilst the CEI itself notes that conflicts of interest can be real, perceived or potential, the guidance document explains these terms in greater detail.

3.143 A real conflict of interest occurs where there is a ‘direct conflict between your public duties and responsibilities and your personal or financial interests’, whilst a perceived conflict arises where ‘it appears or is perceived that your personal or financial interests could improperly influence the performance of your duties at work’ even if there is no actual conflict. A potential conflict occurs where ‘your personal or financial interests could conflict with your official duties in the future’.³¹²

3.144 Greater guidance on the two main types of interests, namely personal or financial interest, is also provided and expansive definitions are applied. For example, personal interests are defined in the guidance document to include a person’s own interests as well as the interests of individuals and groups with which they associate. A

³⁰⁹ *ibid.*, para [3].

³¹⁰ *ibid.*, para [5].

³¹¹ ATO, ‘Conflicts of Interest’ a guidance document accompanying ‘Conflicts of Interest – CEI 2014/06/10’ (Internal ATO document, 12 October 2017) p 1.

³¹² *ibid.*, p 2.

person may not only have an interest in obtaining a benefit for themselves, friends or family, but they may also have an interest in bringing disadvantage to rivals or enemies.³¹³

3.145 Financial interests are defined to include a person's shareholdings, directorships, outside employment, involvement in their own or their family's business, trusts as well as offers and acceptances of gifts or benefits. For example, the guidance document notes that a conflict may arise due to an immediate family member's shareholdings, however, the family member's consent may be needed to disclose the details of the shareholding.³¹⁴

3.146 The guidance document also provides an expansive definition for non-financial interests as it advises ATO staff that such interest can arise from family and personal relationships, personal values or beliefs, involvement in community groups or activities, professional associations or former colleagues.³¹⁵

3.147 In addition to the definitions of key terms, the guidance document identifies a number of circumstances in which a conflict of interest may arise, including those involving personal relationships in the workplace, recruitment exercises and officers who are planning to leave the ATO for outside employment. The guidance for each of these circumstances is summarised below.

Application of CEI and declaration requirements

3.148 Whilst all officers, including SES and contractors, are required to identify and disclose conflicts of interest as and when they occur, there is a requirement for SES officers to make annual declarations about their financial and personal interests that could involve a real or perceived conflict of interest. Therefore, they have to make a positive declaration, even if there was no conflict to declare or no change to previous declarations. It should be noted that the Commissioner, an ATO Executive member or a Deputy Commissioner may also apply this requirement for non-SES officers if the role 'warrants a particular transparency about private interests'.³¹⁶

Personal relationships in the workplace

3.149 The guidance document states that 'it is generally not appropriate for couples, family members or close personal friends to have any direct supervisory or line responsibility over one another' and provides an example of two spouses who both work in the ATO.³¹⁷ The two spouses would not need to report their relationship merely because they work for the ATO but if they became involved in any work together they should submit a conflict of interest form and discuss the situation with their managers, even if the conflict is only perceived.³¹⁸ It is important to note that the

³¹³ *ibid.*, pp 2-3.

³¹⁴ *ibid.*, p 4.

³¹⁵ *ibid.*, p 12.

³¹⁶ *ibid.*

³¹⁷ *ibid.*

³¹⁸ *ibid.*, p 3.

updated CEI also specifically mentions ‘personal and/or family relationships between staff members that may give rise to perceptions of favouritism or nepotism’ as an example of a personal interest that may need to be declared.³¹⁹

Recruitment

3.150 With respect to recruitment, the guidance document provides an illustrative example where a member of an ATO recruitment selection panel discovers that a former colleague, with whom she remained in regular contact, had applied for the position. As the panel member’s association with the applicant is a perceived or real conflict of interest, the guidance document points out that the panel member ‘should advise the other selection panel members of the conflict, including the chair of the committee, the recruitment delegate and/or the recruitment campaign leader, her manager and submit a conflict of interest form’.³²⁰ The appropriate decision maker in this case, being the recruitment delegate or the recruitment campaign leader, will decide how the conflict should be managed. The CEI also specifically refers to participation in recruitment activities as a situation where officers will need to consider whether their personal or financial interests might give rise to conflicts of interest.³²¹

3.151 It should be noted that selection panels involved in the recruitment of SES officers have additional requirements imposed on them by section 21 of the *Australian Public Service Commissioner’s Directions 2016* (the APS Commissioner’s Directions). For example, the selection panel must include either the APS Commissioner or a representative of the APS Commissioner.³²² According to the APSC’s guide to engagement, mobility and separation of SES officers, the APS Commissioner’s representative is expected to be an APS employee from outside the portfolio and hold a position substantively at a level above the level of the relevant vacancy. The representative has a key role in assisting the selection panel in upholding merit and in ensuring that decisions are consistent with relevant APS Values, APS Employment Principles and the relevant legislative framework.³²³ At the end of the selection process and before an SES officer is promoted or engaged, the APS Commissioner’s representative is required to certify that the selection process complies with both the *Public Service Act 1999* and the APS Commissioner’s Directions.³²⁴

3.152 The participation of the APS Commissioner’s representative in such processes is intended to bring an external perspective to the selection panel as they consider the broader range of management and leadership capabilities required at SES level and avoid a narrower focus only on the particular requirements of the role concerned. This helps to ensure individuals selected to perform SES duties will possess the full range of skills required to operate at the SES level in the APS. The representative is expected to

³¹⁹ Above n 81.

³²⁰ Above n 311, p 11.

³²¹ Note: ATO employees, amongst other APS staff, are legally obliged to exercise their power in relation to the employment of others without patronage or favouritism: *Public Service Act* s 19; Above n 81.

³²² *Australian Public Service Commissioner’s Directions 2016* s 21.

³²³ APSC, *The Senior Executive Service: an HR practitioner’s guide to engagement, promotion, mobility and separation* (2015) p 7.

³²⁴ Above n 322.

be fully independent, impartial and not be a referee for any of the candidates, unless this is unavoidable. In addition, it is preferred that agencies nominate a different individual to represent the APS Commissioner on each occasion. This will help to maintain the independence of the representative, and to ensure this role is spread evenly across the APS.³²⁵

Officers leaving the ATO

3.153 ATO officers must submit a conflict of interest form as soon as they are aware that they will be taking a role in the private sector. The officer's Deputy Commissioner will then consider a number of issues including the importance and sensitivity of the officer's ATO role, the nature of the private sector appointment, the relationship between the future employer and the ATO as well as the period during which ATO information or contacts would be of value to the officer in their new role. The Deputy Commissioner is authorised to implement strategies to manage any conflicts such as changing the officer's duties, approving leave until the new appointment commences or making a determination that the officer is not to work through their notice period.³²⁶ An additional reminder to report this type of conflict of interest is provided to SES officers as part of their exit checklist when they leave the organisation.³²⁷

3.154 The guidance document also sets out the following expectations of former officers in external roles:

- You must not disclose or use internal or restricted knowledge acquired during the course of your work at the ATO without authority.
- Any work performed by you in the course of your employment with the ATO is the intellectual property of the Australian Government.
- As a former employee, do not seek to influence current ATO employees through pressuring ex-colleagues or subordinates to act partially by seeking to influence their work or to secure favours.
- Do not lobby the ATO on matters in which you were personally and substantially involved during your time at the ATO.³²⁸

3.155 Furthermore, SES officers who leave the ATO are prohibited from engaging in lobbying government representatives on any matters which they had previously worked on in the previous 12 months when at the ATO.³²⁹

³²⁵ Above n 323, p 7.

³²⁶ Above n 311, p 7.

³²⁷ ATO, 'Employee Certification' (Internal ATO document, undated); ATO, 'Obligations on Ceasing Tax Office Employment or Contract' (Internal ATO document, undated).

³²⁸ Above n 311, p 7.

³²⁹ Department of Prime Minister and Cabinet, *Lobbying Code of Conduct* (2013) p 4, cl 7 <<http://lobbyists.pmc.gov.au>>.

Security, derivatives or share ownership

3.156 Staff are alerted to conflicts of interest arising not only when they are working directly on a company in which they or an immediate family member holds securities, derivatives or shares, but also when they are involved in discussions or exposed to information about that company.³³⁰

Relationship or contact with persons involved in, or suspected of, illegal or criminal activity, or associates of such person

3.157 Although it is not strictly a conflict of interest, all officers are required to declare any relationship or contact that occurs between themselves and persons involved in, or suspected of illegal or criminal activity, or associates where such persons may affect the performance of their duties or the reputation of the ATO. For these declarations, the officer's Deputy Commissioner must be notified. Furthermore, the guidance states that:

...any unreported contact with these persons or their associates, which comes to the attention of the ATO will be fully investigated and may lead to misconduct proceedings.³³¹

3.158 It should be noted that the above guidance more closely reflects a prior detailed direction which had been given to all SNC business line staff in 2007.

Management of disclosed conflicts

3.159 Having assisted officers to identify conflicts of interests, the guidance describes options available to the decision makers to manage the conflicts of interest that are raised with them. Where there is a low risk that the conflict would improperly influence decisions or duties, the decision maker may decide to monitor the situation whilst allowing the officer to continue their normal duties. Where there is a higher risk, the decision maker may decide to restrict the involvement of the conflicted officer. This may be suitable where the conflict of interest occurs on an infrequent basis and where the officer can be practically separated from the relevant activity or decision.

3.160 The decision maker may also decide to involve other officers in the relevant process in order to provide supervision of the conflicted officer who cannot be easily removed from the situation.

3.161 Other options include reassigning the officer to another position within the organisation at the same level. This is more appropriate for ongoing conflicts of interest. The decision maker may also ask the officer to divest or relinquish their private interest that is causing the conflict of interest where the above options are not able to resolve the conflict.

3.162 Finally, if an officer does not accept the method chosen by the decision maker to manage the conflict, the officer may resign from the ATO. The guidance states:

³³⁰ Above n 311, p 9.

³³¹ *ibid.*, p 5.

This may be the case if the personal interest is more important to the employee than their employment and the decision maker considers the personal interest needs to be relinquished. It is important to note that this is not a decision made by the manager, but only by the employee.³³²

Verifying disclosures and non-disclosures

3.163 The ATO has relied on officers' self-disclosure of conflicts of interest as there has not been a reliable data source to independently obtain that information. However, following the completion of the ATO September 2017 Report, a new scan has been included in the 'FPII Detection Program' which is aimed at detecting undeclared conflicts of interest³³³ by analysing officers' digital footprints and FPII intelligence assessments.³³⁴

Conflict of interest disclosures and investigations within the ATO

3.164 The ATO had implemented a centralised register for conflict of interest declarations on 1 July 2015 and, by December 2017, that register contained declarations made by 177 officers. During this same period, the FPII unit had received allegations that 52 officers had a conflict of interest, including the following:

- officers performing official duties in relation to taxpayers with whom they had a personal relationship;
- incorrect procurement or recruitment processes suggesting an officer's conflict of interest with potential contractors;
- officers conducting a business or engaged in outside employment; and
- officers associating with people with known links to criminal organisations.³³⁵

3.165 In eight of the 52 cases raised with the FPII unit, the allegations were found to be substantiated. Of these substantiated cases, two were referred to the ATOP business line for potential misconduct proceedings, three were referred to the officers' managers for their action and in four cases no further action was taken. It should be noted that of the 52 cases raised with the FPII unit, only eight of the officers had lodged conflict of interest declarations on the central register.³³⁶

IGT observations

3.166 Effective management of conflicts of interest is of critical importance to the ATO. As the OECD has asserted, such conduct can lead to corruption:

³³² Above n 311, p 13.

³³³ ATO, 'Conflict of Interest Review – BSL Project Proposed Outline' (Internal ATO document, 25 October 2017).

³³⁴ Above n 11, p 3.

³³⁵ ATO communication to the IGT, 19 December 2017.

³³⁶ *ibid.*

While a conflict of interest is not ipso facto corruption, there is increasing recognition that conflicts between the private interests and public duties of public officials, if inadequately managed, can result in corruption.³³⁷

3.167 Furthermore, robust controls to appropriately manage conflicts of interest will foster greater community trust in the ATO and increased voluntary compliance. For such controls to be effective, however, staff must clearly understand the circumstances in which conflicts of interest arise and what the ATO requires of them.

3.168 As stated earlier, significant improvements have been made to CEI/2014/06/10 and the accompanying guidance document following Operation Elbrus. For example, the new guidance document provides a more complete definition of conflicts of interest and more expansive explanations including a number of examples that will better assist officers and their managers to identify conflicts of interest.

3.169 The guidance document also makes it clear that the requirement to avoid or declare such conflicts is ongoing and must be considered before beginning any work associated with external or internal client dealings, for example, before conducting work on settlements, audits and rulings. The new arrangements also provide clearer guidance on the respective responsibilities of managers and decision makers in managing conflicts of interest.

3.170 Transparency of such declarations is also promoted by the registration on a single register which should assist to promote a positive disclosure culture³³⁸, a fraud and corruption control in itself. Furthermore, the register should be periodically analysed not only to assess completeness and to identify broader themes but also to ensure that appropriate actions are taken to address the conflicts declared.

3.171 It should be noted that the above measures should be underpinned by an organisational culture that fosters ethical behaviour. Accordingly, a program of awareness raising is required, particularly because the emphasis on disclosure and management of conflicts of interest may not have been as pressing a priority in the past, as indicated by the low numbers of disclosures made. The challenge is to develop an environment where positive disclosure is the norm to address the difficulties in detecting undeclared conflicts of interest as many officers' personal and financial interests are not systematically captured.

Clarification of guidance material

3.172 Whilst CEI/2014/06/10 and accompanying guidance material have been much improved, there is room for further improvement. Such improvements may increase staff compliance by clarifying ambiguities which could otherwise result in non-disclosure, particularly because of previously formed habits based on the previous guidance. In the IGT's view the following areas in the guidance material require clarification.

³³⁷ Above n 35, p 96.

³³⁸ Above n 238, p 18.

Registration of conflict and discussion with manager

3.173 The CEI/2014/06/10 and accompanying guidance material require officers to discuss conflicts of interest issues with their managers as soon as they become aware of them and to register them by submitting an ATO Integrity Register form 'as required'. It is unclear, however, whether the form is to be submitted before or after such discussions, particularly as managers are required to promptly deal with matters raised and registration of the conflict of interest is listed as only one such option.³³⁹ Accordingly, there is a risk that managers may incorrectly advise officers not to register some conflicts of interest.

3.174 The CEI/2014/06/10 and guidance material should clearly require officers to register the conflicts of interest, using ATO Integrity Register Forms, as soon as they become aware of them. The contents of the forms would then become the basis for the discussion with their managers. The forms can be updated after the discussions to reflect the action to be taken to address the conflicts of interest. Such an approach will assist in normalising a practice which fosters positive disclosure and increase transparency on the ATO's management of an important corruption risk.

Management of disclosed conflicts

3.175 While the guidance document currently describes the options available to decision makers to manage conflicts of interest that have been raised with them, it provides limited details on factors that should be considered in choosing the most appropriate option. The decision makers should be required to consider factors such as:

- the nature of the interest, for example the closeness of the personal relationship giving rise to the conflict;
- the seniority of the officer's role; and
- the nature of the official duties, for example the transactions or other responsibilities affected by the conflict.

Types of conflicts

3.176 As noted above, the guidance document defines the different categories of conflicts of interest, namely 'real', 'perceived' or 'potential' conflicts of interest. However, there is some inconsistent use of these terms and introduction of new terms. For example, in relation to separation arrangements, officers are required to notify as soon as they become aware that the role they will be taking in the private sector may give rise to 'possible' conflicts of interest. However, 'possible' conflicts of interest is not defined in the guidance material and it may be better to use the defined term, 'potential'. Another example is in the context of personal relationships where officers are asked to notify 'even if the conflict is only perceived', which could also result in officers forming the impression that this requirement indirectly excludes 'potential' conflicts of interest.

³³⁹ Above n 81, para [5].

3.177 Inconsistencies such as those above increase ambiguity and may result in an increased risk of non-compliance.

'Should' or 'must'?

3.178 Throughout the guidance document, the use of the word 'should' and 'must' introduces some uncertainty as to whether some actions are mandatory or an aspiration. For instance, example 1 in the guidance document states that if an officer, in the mining and energy segment of the PGI business line, has a shareholding in a mining company, they *should* report it via the ATO Integrity Register Form. Similarly, in example 8, it is stated that if an officer has a conflict of interest due to being on a procurement panel and is related to one of the tenderers before the panel, they *should* discuss the situation with their manager. By contrast, examples 3 and 4 state that officers *must* disclose their relationships via the ATO Integrity Register Form.

3.179 It should be noted that some guidance provided by other Commonwealth agencies do make a clear distinction between the use of such words. For example, the AGD's Protective Security 'Personnel Security Guidelines'³⁴⁰ makes a specific distinction between the use of the phrase 'need to' (as a mandatory requirement) and 'should' (as better practice).

The test to apply

3.180 As noted above, a key test for officers to determine the existence of a conflict of interest is 'whether an impartial observer would reasonably question if your financial or personal interests might influence the way you behave and the way you carry out your duties'. However, the guidance given to managers asks them to 'first establish whether or not a conflict of interest exists' with no reference to the impartial observer test. Such language may lead managers to regard themselves as the impartial observer in applying the test.

Personal interests arising from previous opinions

3.181 The guidance document does not refer to conflicts of interest which may arise where officers could be perceived to be prejudiced or biased because of their previous involvement or opinion.³⁴¹ For example, an officer may have conflicts of interest when they internally review a decision in which they had been previously involved.

Information other than that related to the taxpayer

3.182 The CEI/2014/06/10 and the accompanying guidance material alert officers to certain issues which, whilst not strictly amounting to conflicts of interest, are closely related integrity issues. These include issues that arise from contact with known criminals. However, other closely related issues, such as inadvertently disclosing sensitive ATO information in family or social settings, are not mentioned. For instance,

³⁴⁰ Above n 220, para [9].

³⁴¹ *Isbester v Knox City Council* [2015] HCA 20.

examples two, three and four discuss conflict of interest issues that may arise in family settings. However, no mention is made about the need to ensure sensitive ATO information, such as thresholds for compliance activities, are kept confidential at all times.

Movement of personnel between the ATO and the private sector

3.183 There are benefits in the recent increase in the movement of personnel between the ATO and the private sector as it has facilitated the sharing of skills, experience and information.³⁴² However, it has also resulted in greater risk of conflicts of interest arising from prior relationships and expressed views.

3.184 Once private sector personnel join the ATO, they are required to follow CEI 2014/06/10 and the accompanying guidance material to avoid or declare conflicts of interest – including conflicts which arise from previous employment or relationships. Officers who intend to leave the ATO and join the private sector are required to disclose any conflicts of interest that may arise in their new role as soon as they become aware of it. There are, however, no examples in the guidance to assist the reader. It is possible that this type of conflict of interest may not be well understood by all staff as an examination of the ATO's central conflicts of interest register reveals that no such disclosures have been made.³⁴³ Accordingly, the ATO should consider including examples of this type of conflict of interest.

3.185 Where officers disclose conflicts of interest in connection with starting a new role in the private sector, the guidance document sets out some of the possible treatment strategies available, including approval of leave until the new appointment commences or not working through the notice period. These strategies can be further bolstered by subjecting such officers to a period of 'gardening leave' or a 'cooling off period' before they commence their new employment. This approach is adopted by many overseas government agencies.³⁴⁴ The ATO does not currently include provisions in its standard employment contracts which could facilitate such an approach. The IGT believes that the ATO should explore whether these provisions could be practically enforced in the Australian context and, if so, include them in new employment contracts. Alternatively, legislation to impose post-employment conditions on ATO officers could be considered as is the case in the United States (US) with ex-IRS officers.³⁴⁵ However, the benefits of doing so should be balanced against the impact on flow of skills, experience and information between the APS and private sectors.³⁴⁶

3.186 Once an officer has left the ATO and began their new employment, they may seek to use prior relationships with ATO staff as a means of influencing ATO decision-making or obtaining information to assist them in their new employment. The guidance document makes it clear that former officers are prohibited from doing so.

³⁴² See also, APSC, *APS Values and Code of Conduct in practice: A guide to official conduct for APS employees and agency heads* (2015).

³⁴³ ATO communication to the IGT, 1 December 2017.

³⁴⁴ OECD, *CleanGovBiz Integrity in practice Public sector integrity: Providing services efficiently*, (2012) p 8.

³⁴⁵ United States 18 U.S.C § 207.

³⁴⁶ See above n 342.

However, it would be difficult to monitor and enforce as demonstrated by recent media coverage of CRA's experience in this area.³⁴⁷ It seems, therefore, that the enforcement of such prohibition relies on current ATO officers disclosing approaches made by their ex-colleagues. Currently, there is no requirement for officers to disclose these approaches unless, in their view, they amount to conflicts of interest. In the IGT's view, officers should be required to report any such approaches to improve the ATO's visibility of these risks.

3.187 Once approaches from ex-officers have been identified and their attempts to influence or obtain information have been prevented, the ATO may be able to refer them to professional bodies or industry associations to which they belong for any relevant disciplinary action.

3.188 Ex-ATO officers may also have had access to important information, for example, thresholds for commencing compliance activity which could be used to design undetectable non-compliant arrangements. In such a case, it could be argued that the ATO should 'change the locks' or regularly change the thresholds to address the risk of a former officer disclosing confidential information about how the ATO operates to their new employers. However, the ATO's internal thresholds are based on their analyses of risk and changing these thresholds may affect the ATO's compliance results and cause inconsistencies. It would be more appropriate to remind ATO officers that the ATO could take criminal action³⁴⁸ for any disclosure and/or civil action for use of its intellectual property.

Communication strategies

3.189 It is critical that the updated CEI/2014/06/10 and accompanying document are actively promoted and endorsed by the Commissioners and other senior executives. The ATO has already issued circulars and other existing materials such as a video on conflicts of interest. However, the IGT believes that more can be done to increase staff's awareness and compliance. For example, the video can be updated to begin with a message from the Commissioner on the importance of managing conflicts of interest and to promote an organisational culture that emphasises transparency and integrity.

Annual declarations

3.190 As noted above, SES officers and other officers in high risk roles are required to submit annual declarations detailing their personal and financial interests. They are also required to make these declarations even where there is no change or where there is nothing to declare (i.e. 'nil declarations'). Such regular disclosures would assist in increasing staff acceptance of the instructions by establishing a habit of positive disclosure.

³⁴⁷ Harvey Cashore, Kimberly Ivany and Katie Pedersen, 'Senior federal tax enforcer joined KPMG as its offshore 'sham' was under CRA probe', *CBC news Canada*, 12 April 2016.

³⁴⁸ *Crimes Act 1914* s 70(2) (Unauthorised disclosure of information by current and former Commonwealth officers).

3.191 Whilst it may be disproportionate to require all ATO officers to complete a form detailing their personal and financial interests, the ATO can use the Security Health Check. As mentioned earlier, it was piloted last year and is to be rolled out annually. During this process, officers could be asked by their managers to confirm that they have complied with CEI 2014/06/10 and that all required disclosures have been captured in lodged ATO Integrity Register Forms. It is acknowledged, however, that the Security Health Check currently only applies to officers who hold a security clearance. The ATO may consider using another existing annual process that applies to all officers, or using the annual process described in recommendation 3.1(d) in this report.

3.192 Such a process would also provide the FPII unit with intelligence concerning staff attitudes towards conflicts of interest that could be used in their broader work of detecting integrity issues.

Verifying ATO officers' compliance

3.193 Other than providing adequate guidance to ATO officers and raising awareness of their conflict of interest obligations, the IGT considers that a healthy conflict of interest system would also seek to regularly analyse the declared conflicts on the central register.

3.194 The ATO September 2017 Report indicates that 'timely periodic reviews to ensure ongoing completeness and accuracy of the register, and to identify broader themes for dissemination and response' would be undertaken.³⁴⁹ It is unclear as to whether these periodic reviews have commenced. The IGT is of the view that they should also examine the actions taken to address the declared conflicts and ensure that those actions were appropriate. For example, a decision maker may have come to the conclusion that it was not necessary to separate a husband and wife from working in the same team because they did not have any supervisory or line responsibility over each other. However, upon review, it may be discovered that due to the rankings of the officers involved, the closeness of their relationship and the nature of their work, the initial decision maker had not made the correct decision. By allowing a second pair of eyes to examine the conflict, the ATO gains the ability to rectify any errors that had been made as well as identifying trends.

3.195 The periodic review of the central register may also identify particular issues such as the underreporting of certain types of conflicts. For example, if the ATO had identified that there were zero instances of ATO officers reporting potential conflicts associated with exiting the organisation, they may have come to the conclusion that this type of conflict was not well understood by its officers and taken steps to address the issue.

3.196 The IGT believes that the periodic reviews could also verify the accuracy of conflicts of interest disclosed on the register. However, to do so, the ATO would need to acquire more information, personal and financial, about its officers. While it does not

³⁴⁹ Above n 11.

have the necessary information at present, as mentioned previously, there are opportunities to obtain it. For example, the recruitment process could be used to capture information from new employees about any pre-existing relationships that they may have with other ATO officers. There is also an opportunity for the ATO to acquire information from its HR area and its managers about officers who are leaving the organisation. The ATO could then use such information to verify if conflicts are being adequately disclosed and managed.

3.197 The ATO could consider the pilot being conducted by HMRC in the United Kingdom (UK) which is analysing the shareholdings and directorships of staff and their families as a means to detect conflicts of interest.

3.198 The IGT also considers that the periodic review of the register should be undertaken by officers in units such as FPII because they already have the expertise and deal with other related matters.

Conflicts of interest in recruitment

3.199 In relation to concerns that have been raised with the IGT concerning the potential for conflicts of interest in the SES recruitment processes, the APS Commissioner's Directions require the involvement of the APS Commissioner or his representative on the selection panel for any recruitment of SES officers. Such measures help to maintain a level of independence in the process, which would help address perceptions of favouritism in the recruitment of private sector practitioners to SES positions. In addition, the CEI provides a basis for the ATO to take disciplinary action if ATO officers who participate in such activities do not adequately disclose any conflicts of interest. The conflicts of interest guidance document also provides an illustrative example of how a selection panel member is expected to behave should they discover that they have a pre-existing relationship with an applicant.

3.200 Conflicts of interest may also arise where a person who is hired as a consultant has a relationship with those involved in the procurement process. As noted above, CEI 2014/06/10 continues to apply in such situations. Persons involved in a procurement process must disclose their conflict of interest through the ATO Integrity Register Form. In addition to the above controls, the procurement process also has similar controls.³⁵⁰

3.201 The above safeguards seem to adequately deal with the concerns about the potential for inappropriate recruitment practices as collusion amongst multiple personnel and members of the selection panel would be required in order to circumvent them. Nevertheless, such concerns persist as indicated by submissions to this review. The IGT is of the view that where any such allegations are raised they may be best addressed through specific complaints to the IGT or referrals to the FPII unit.

³⁵⁰ See, Department of Finance, *Commonwealth Procurement Rules* (2018); ATO, 'Chief Executive Instructions - Procurement (CEI 2014/03)' (Internal ATO document, 1 July 2014).

RECOMMENDATION 3.4

The IGT recommends that the ATO:

- a) update its conflict of interest guidance document to clarify ambiguities and provide further explanation, including practical examples, as well as require officers to register their conflicts of interest as soon as they become aware of them;*
- b) bolster its processes for ensuring that former colleagues of current ATO officers do not obtain information or exert influence by virtue of their previous associations;*
- c) improve awareness and compliance with its conflict of interest policies and guidance including through its active promotion by the Commissioners and other senior executives;*
- d) conduct periodic reviews on the central conflicts of interest register to identify trends, verify the accuracy of the declared information as well as ensure that the appropriate management actions have been taken to address the conflict; and*
- e) seek ways to capture and analyse information for detecting undeclared conflicts of interest as part of some its existing checks as well as from other sources.*

ATO RESPONSE

(a) Agree

Enhancements to the Conflict of Interest Chief Executive Instruction and guidance material have been completed. The ATO will consider the report's findings to determine if further enhancements are required.

(b) Implemented

(c) Implemented

(d) Agree

The central conflict of interest register is monitored and reviewed in line with the recommendation. However, further work will be undertaken to mature these processes.

(e) Agree

The ATO regularly analyses registers and declarations, and use data mining activities to detect undisclosed conflicts of interest. Further work will be undertaken to mature these processes.

CONTROLS IN RELATION TO SENIOR OFFICERS' INTERVENTION IN CASES

3.202 It is important for organisations to have clear and unambiguous lines of reporting which set out roles, responsibilities and lines of authority of all officers, including procedures for managing the escalation of concerns from those outside of the organisation. In this regard, the manner in which ATO senior officers intervene or become involved in operational matters upon the request of taxpayers or their representatives has to be clearly defined and transparent so as not to give rise to perceptions of undue influence, or at worse, suspicions of corruption.

Stakeholder concerns

3.203 Some stakeholders have raised concerns that certain taxpayers may have received favourable treatment in ATO audits, rulings or disputes after the taxpayer's representative had directly contacted a more senior officer with whom they had a pre-existing relationship. These concerns relate to current ATO officers being contacted by their former colleagues in the private sector particularly in the light of more recent recruitment of external candidates for senior ATO roles.

3.204 Whilst there is general agreement that the ability to escalate matters to senior officers is a valuable check on the work of more junior officers and for raising broader issues, there is concern about a lack of transparency in how those escalations are managed. In submissions to the review, some ATO officers have cited circumstances where failure to transparently record or communicate the nature of interactions between senior officers and taxpayers or their representatives have given rise to perceptions of inappropriate and undue influence.

Relevant materials

3.205 Whilst senior officers, such as SES officers, are involved in managing the strategic direction of the ATO, they may also become involved in operational matters.

3.206 SES officers may generally become involved in cases in one of three ways. First, they may have involvement at the outset in cases which involve taxpayers that are considered to be 'high impact' due to their volume of tax revenue or market influence. For example, if one of the top 30 largest Australian taxpayers is the subject of an ATO audit, an SES officer will attend the initial meeting with the taxpayer to discuss the audit management plan and attempt to obtain a mutual commitment to the timely completion of the audit.³⁵¹

3.207 Secondly, SES officers may become involved in cases as a result of internal processes which bring cases to their attention. For example, cases which reveal a heightened importance, sensitivity or complexity may be brought to the attention of senior officers for discussion in the ATO's internal forums and committees.³⁵²

3.208 Thirdly, SES officers may become involved in cases as a result of taxpayers or their representatives directly contacting them or seeking intervention. The Commissioner has indicated that such direct contact occurs frequently.³⁵³

3.209 The ATO has confirmed that it does not have specific guidance regarding senior officer intervention. They are expected to comply with the ATO's broader policies governing conduct, such as the *Taxpayers' Charter*, ATO CEIs and APS Code of

³⁵¹ ATO, 'Audit Products - Discussion of case plan with senior tax officer and taxpayer' (Internal ATO document, 7 September 2016).

³⁵² ATO communication to the IGT, 3 November 2017.

³⁵³ Commonwealth, Senate Economics Legislation Committee, *Proof Committee Hansard - Estimates*, 30 May 2017, p 23 (Commissioner of Taxation).

Conduct.³⁵⁴ As mentioned earlier, pursuant to CEI 2014/06/10, ATO officers are required to take reasonable steps to identify and disclose conflicts of interest so that they can be appropriately managed. For example, if a senior officer has a pre-existing relationship with the person who is seeking assistance, the senior officer would be expected to disclose the conflict of interest.

3.210 CEI 2014/01/01, on Records Management, requires ATO officers to also adhere to business processes and system instructions to create full and accurate digital records of their ATO activities, including decisions and actions.³⁵⁵ As part of the records management requirements, all ATO officers involved in active compliance cases, including SES officers³⁵⁶, are required to keep contemporaneous records on the relevant file in the ATO case management system ('Siebel notes').³⁵⁷ The ATO guidelines state that 'effective notes' are important as they support 'active case management', provide 'a sequence of events', can be 'relied upon in case review [... to] meet accountability requirements' and demonstrate transparency.³⁵⁸

3.211 Every time staff interact with a taxpayer, take action or make any decision, they are required to record such events in Siebel notes.³⁵⁹ If such contact is 'meaningful' and results in an outcome, the guidelines require ATO officers to make Siebel notes, at a minimum of, the following:

- the full name and title/relationship to the person spoken to;
- a concise record of any relevant discussions held;
- details of actions taken or proposed to be taken;
- clearly stated reasons for any decisions made;
- relevant due dates and review dates; and
- any warnings that may have been provided to the taxpayer.³⁶⁰

3.212 Similarly, Siebel notes are required to be kept for all internal communications and decisions made regarding the case.³⁶¹

3.213 The ATO has provided records which confirm that since January 2013, 341 Siebel notes have been recorded by six different SES officers in total, with 330 of these notes having been made by one particular SES officer. Only one of these Siebel notes documents communication with a taxpayer. All but one of the 341 Siebel notes was recorded in 2013 and 2014.³⁶²

³⁵⁴ ATO communication to the IGT, 20 November 2017.

³⁵⁵ ATO, 'Chief Executive Instruction 2014/01/01 Records Management' (Internal ATO document, 6 January 2014) p 1.

³⁵⁶ ATO, 'Guidelines for effective notes in compliance' (ATO Internal document, 2 August 2017).

³⁵⁷ ATO, 'Siebel Notes' (ATO Internal document, 13 September 2017) p 1.

³⁵⁸ Above n 356.

³⁵⁹ Above n 357, p 1. Note that the initial contact is recorded as a Siebel Activity.

³⁶⁰ Above n 356, p 4; Note that the initial contact is recorded as a Siebel Activity.

³⁶¹ Above n 357, pp 1-2 and 5.

³⁶² ATO communication to the IGT, 13 December 2017.

3.214 ATO senior management have advised that '[w]here an SES officer does not have access to the Siebel case management system, the case officer is responsible for ensuring that the relevant records are attached to the Seibel file". They have also advised that other SES officer interactions and decisions may have been recorded separately in forms other than Siebel notes, such as within e-mails sent to case officers. However, they acknowledged it would be impractical to assure that all externals' contact with the SES officers had been documented and attached to the case files.³⁶³

IGT observations

3.215 The IGT is of the view that taxpayers should have an avenue of escalation when they encounter difficulties in their dealings with the ATO. However, there is a need for transparency and appropriate controls for such escalation to prevent actual or perceived undue influence by relevant senior officers in individual matters.

3.216 There are a number of options to manage requests for escalation, including senior officer intervention. One option is to prohibit such officers from becoming involved in the matter at all, even if they are the responsible officer for the area. In the US, senior officers in the IRS are only privy to high level information and generally do not have any direct involvement in individual cases. When senior IRS officers are approached for their involvement, they encourage taxpayers to raise and resolve their concerns with the manager of the relevant case officers directly. The CRA in Canada has a similar approach. It is noted, however, that there are structural differences between the Australian and the US tax administration such as the separate appeals area in the US.³⁶⁴ Whilst prohibiting senior officer intervention in individual cases may reduce the risk of inappropriate interference, it may also prevent earlier resolution of disputes.

3.217 Another option is to allow senior officers who are responsible for the relevant area to intervene in cases, in a limited capacity, for example to address procedural fairness concerns, ensure staff conduct is appropriate and provide assurance that decisions have been made in accordance with the relevant policies. Importantly, substantive issues would be required to be resolved through a separate merits review or other dispute resolution process such internal review³⁶⁵. This approach would minimise perceptions that senior officers intervene in cases to influence decisions on substantive issues and may assist to empower more junior case officers to resolve the concerns raised.³⁶⁶

3.218 Currently, taxpayers may seek to resolve their difficulties with the ATO through the free service offered via the office of the IGT, as the taxation ombudsman, which is an important safety valve for the administration of the tax system, including

³⁶³ ATO communications to the IGT, 7 June 2018, 19 February 2018 and 24 May 2018.

³⁶⁴ See IGT, *The management of tax disputes* (2015) pp 27-29.

³⁶⁵ See, for example, ATO, 'Independent review of the Statement of Audit Position for groups with a turnover greater than \$250m' (23 January 2017) <www.ato.gov.au>.

³⁶⁶ See APSC, *Capability Review Australian Taxation Office* (2013) p 21.

the provision of a right of access for more vulnerable taxpayers such as small business and individuals.

3.219 A further alternative option may be to limit senior officer intervention to clearly defined situations, which are set out in written policy, and require the intervening officer to personally document all actions taken as well as explain any substantive changes to the original decision maker. Such an approach would promote full transparency and accountability of such interventions as well as operate as an integrity safeguard against actual or perceived undue influence being exerted by the relevant senior officer. Furthermore, disputes may be resolved more promptly through such an approach and promote more consistent decision-making as well as provide junior staff with valuable on-the-job training in a manner that reduces any sense of disempowerment.

3.220 Importantly, where senior officers receive requests for escalation or intervention in relation to areas outside of their responsibility, it would be mandatory to refer such matters to the responsible SES officer in the relevant area as well as personally document the initiating request that they had received and the subsequent referral.

3.221 The IGT believes that the last alternative canvassed above strikes an appropriate balance between resolving disputes at the earliest opportunity and ensuring the requisite degree of transparency and integrity safeguard. Should concerns persist after this option is implemented, it may be necessary to consider other alternatives such as those adopted by the IRS.

3.222 The ATO's general record keeping requirements outlined earlier are an important first step in the process. However, as mentioned earlier, the ATO's records show that these requirements are not being followed, i.e. SES officers' interaction are not documented in Siebel notes. The ATO has advised that such interactions may be documented in emails attached to the case file but it cannot provide assurance that all such interactions have been documented in this manner. Accordingly, the requisite degree of transparency, integrity and accessibility, as discussed above, requires improvement.

3.223 The IGT is of the view that the record keeping rules must ensure intervention by senior officers in cases is always recorded in a centralised case management system and personally documented in a form which is easily accessible for verification. Importantly, such documentation should include details of the senior officers' contact with the relevant taxpayers and ATO case officers as well as the details of the decisions made, supporting reasons, resulting outcomes and briefing provided to the relevant case officers by way of feedback loop.

RECOMMENDATION 3.5

The IGT recommends the ATO improve the policies regarding senior officer intervention by:

- a) specifying the circumstances in which senior officers are authorised to intervene in individual matters;*

RECOMMENDATION 3.5 (CONTINUED)

- b) where senior officers receives requests to intervene in matters outside their area of responsibility, requiring such requests to be transferred to their counterpart in the relevant area;*
- c) requiring intervening officers to document the initial request and all subsequent actions, including the details of decisions made, supporting reasons and resulting outcomes as well as briefings provided to the original decision maker on a single centralised system and in a form which is transparent and easily accessible; and*
- d) periodically reviewing senior officers' compliance with such policies.*

ATO RESPONSE

(a) Agree

(b) Agree

(c) Agree

The ATO agrees that changes can be made to our existing records management approaches to make the documenting and recording of intervention requests more transparent and easily accessible to all ATO stakeholders in a case. The ATO will do so in a way that seeks to prevent duplication of effort and the imposition of undue process. As a matter of principle, the ATO considers it is critical that its senior officers maintain an open and healthy engagement with our clients and other participants in the tax system. This is central to putting our clients at the centre of everything we do.

(d) Agree

CONTROLS IN RELATION TO SETTLEMENTS

3.224 The settlement process is a necessary and important feature of the Australian tax administration system, enabling taxpayers and the ATO to negotiate and resolve their disputes in a cost-effective manner without resorting to litigation. However, appropriate management, accountability and transparency of the settlement process are essential to preserve the integrity of the tax system and to maintain community confidence.³⁶⁷

3.225 It is acknowledged that, in some cases, it may be appropriate to proceed to litigation, particularly where there may be a public interest in clarifying uncertainties in the law.³⁶⁸

³⁶⁷ Above, n 364 p 80.

³⁶⁸ IGT, *Review into the Australian Taxation Office's use of early and alternative dispute resolution* (2010) p 51.

Stakeholder concerns

3.226 Stakeholders believe that as settlements involve the exercise of discretionary powers, it is important that there are clear guidelines to ensure ATO officers settle disputes on appropriate terms. They are particularly concerned that the current *Code of Settlement* is too brief and lacks some important guidance that was previously included.

3.227 Stakeholders were also of the view that the confidential nature of settlements could result in unreasonably favourable settlement terms being hidden from scrutiny. Some believed that more transparency was required as an integrity measure. Parallels were drawn with the private ruling system, where details about the ruling, redacted of identifying information, is published in the ATO's Register of Private Rulings (on its website).

Relevant materials

3.228 The ATO's guidance on settlements, *Code of Settlement Practice*, has been publicly available since 1999. Most recently, it was reviewed and updated in October 2014. It is much shorter and is only two pages in length now with an accompanying 16-page document, entitled *Practical Guidance to the ATO Code of Settlement* which includes examples of settlements and four model settlement deed templates.³⁶⁹

3.229 As part of the settlement assurance process, the ATO designed and trialed a process between July to October 2015 with the aim of providing the community with a level of confidence that its settlements with large and multinational taxpayers were a 'fair and reasonable outcome for the Australian community'. This process is referred to as the Independent Assurance of Settlements or 'IAS'.³⁷⁰

3.230 The above assurance process was piloted in consultation with The Honourable Justice Garry Downes who is a retired Federal Court judge and former President of the Administrative Appeals Tribunal (AAT). Following the pilot, the ATO amended its settlement documentation templates and implemented the IAS process from February 2017.³⁷¹ The IAS uses a panel of three retired Federal Court judges to annually review 10 to 12 settlement cases that have already been finalised. The assurers review separate cases independently of each other. Case officers are made available should the assurers have questions for them.

3.231 The ATO has published the outcomes of the IAS in its 2016–17 Annual Report:

In 2016–17, the assurers have completed reviews of five settlements as part of the independent assurance of settlements process. They concluded that the ATO's treatment of these were a fair and reasonable outcome for the Australian community.³⁷²

³⁶⁹ ATO, 'Code of settlement' (18 August 2015) <www.ato.gov.au>.

³⁷⁰ ATO, 'IAS Reports - ATO response' (Internal ATO document, 6 June 2016) p 4.

³⁷¹ Above n 14, para [3.32].

³⁷² Above n 7, p 68.

3.232 The reports issued by the IAS assurers are provided to the relevant Deputy Commissioners and Assistant Commissioners. The reports are also discussed at a fortnightly meeting of three Assistant Commissioners from the PGI, PGH and Review and Dispute Resolution (RDR) business lines, known as the Triumvirate meetings.³⁷³

3.233 The assurance reports for the first three cases were shared with settlement teams in debrief sessions in July 2017 and reports for the fourth to sixth assured cases were shared in October 2017. As at December 2017, the ATO is in the process of collating the learnings and feedback from the IAS and has not yet progressed to implementing the identified improvements.³⁷⁴

3.234 In addition to the recently implemented IAS process, the ATO has a range of measures to govern the use of settlements, which vary between business lines. For example, whilst all SES officers have a delegation to make a settlement decision, some business lines, such as PGH, Small Business (SB), Individuals, Indirect Taxes (ITX), Superannuation and RDR, also provide settlement authorisation to EL2 officers. In the PGI business line, only SES officers have the delegation to make a settlement decision.

3.235 Furthermore, with the exception of PGI³⁷⁵ and RDR, all business lines are required to refer settlement matters to a settlement panel. These panels may provide advice or parameters within which the settlement decision maker may settle.³⁷⁶

3.236 The ATO publishes high level details of its settlement activities in its Annual Reports. The ATO's 2016–17 Annual Report contains information about the numbers of settlements and the variances, both broken down by stage in the compliance activity and by market segment.

3.237 Table 3.5 below illustrates how the detail of settlement activities published by the ATO has changed in the last five financial years.

Table 3.5: Details of settlement activities reported by the ATO by financial year

Annual Report year	Details reported by the ATO
2016–17	Numbers of settlements and dollar variances broken down by stage at which settlement occurred (pre-audit, audit, objection, etc.), market segment and client group.
2015–16	Total number of settlements only.
2014–15	Numbers of settlements broken down by stage. Numbers of settlements and dollar variances broken down by market segment.
2013–14	Percentage of settlements (numbers can be inferred) broken down by stage. Numbers of settlements and dollar variance broken down by market segment.
2012–13	Numbers of settlements and dollar variance broken down by market segment.

Source: ATO Annual Reports

³⁷³ Above n 14, para [3.35].

³⁷⁴ *ibid.*, para [3.36].

³⁷⁵ Note: the ANAO audit found that the PGI business line provide 'adequate assurance on the integrity of settlement decision-making': above n 14, p 29.

³⁷⁶ Above n 14, paras [2.16] and [2.24]; ATO, 'Practical Guide to the ATO Code of settlement' (13 February 2017) example 5.2.

3.238 As indicated by Table 3.5 above, the most recent 2016–17 Annual Report contains more details about its settlement activities than it had in previous years.

International comparison

3.239 In his 2017 performance audit³⁷⁷ into the ATO’s use of settlements, the Auditor-General found that the ATO publishes more details of settlement activities than the revenue agencies of the UK, US and New Zealand – refer to Table 3.6 below.

Table 3.6: Extract from ANAO performance audit of ATO settlements

Reporting	Australia	United Kingdom	United States	New Zealand
Public reporting of settlement numbers	Yes	No	Yes	No
Public reporting of settlement amounts	Yes	No	Yes	No
Public reporting of settlements by market segment	Yes	No	No	No

Source: ANAO’s *Performance Audit on the Australian Taxation Office’s Use of Settlements* (2017–18)

3.240 In the UK, HMRC employees can only make decisions about settlements after they have considered the rules and policies outlined in HMRC’s litigation and settlement strategy – a detailed 41-page document that not only outlines the settlement principles but also clearly describes various scenarios where HMRC will not consider settlement as an option. For example, the document specifically states where ‘there are only two possible outcomes consistent with the law, HMRC will not accept any out of court resolution which splits the difference’.³⁷⁸

3.241 Further governance and assurance processes are in place to ensure that HMRC’s settlements comply with the litigation and settlement strategy. In addition to checks undertaken by the authorising officer, both HMRC’s central review teams and its internal audit area will review a sample of around 400 settlement cases annually and report their findings to the Tax Assurance Commissioner. The findings from these reviews are then published in HMRC’s Annual Report to ensure transparency.³⁷⁹ Through these controls, HMRC seeks to provide assurance that there is no element of favouritism in its settlement decisions and in doing so combats the perception of ‘sweetheart deals.’

3.242 In addition, HMRC’s Annual Report contains information about its internal annual review of governance in settlements. It details weaknesses discovered in the review (such as absence of audit trails, authorisations at the wrong level, incorrect figures entered into IT systems and delays) as well as improvements it is undertaking to address those weaknesses.³⁸⁰

³⁷⁷ Above n 14.

³⁷⁸ HMRC, *Litigation and Settlement Strategy* (30 October 2017) p 39.

³⁷⁹ HMRC, *HMRC Annual Report and Accounts 2016–17* (13 July 2017) p 106.

³⁸⁰ *ibid.*

Past reviews

3.243 The ATO's use of settlements has been the subject of prior scrutiny. In 2009, the IGT's *Review into aspects of the Tax Office's settlement of active compliance activities*³⁸¹ made recommendations to improve the administration of settlements including transparency and integrity aspects.

3.244 The IGT conducted two subsequent reviews, *Review into the Australian Taxation Office's use of early and alternative dispute resolution*³⁸² and *The Management of Tax Disputes*³⁸³ which examined aspects of settlements. In particular, in the latter review, the IGT recommended to Government that the ATO create a dedicated Appeals Group, separate from its compliance and legal advisory functions, to manage and resolve disputes. This sought to provide the highest level of independence and facilitate a fresh and impartial review of taxpayers' cases whilst ensuring that any settlements are adequately scrutinised and in the best interest of the community.

3.245 As mentioned earlier, the ANAO recently completed a performance audit into the ATO's use of settlements and found that the ATO effectively uses settlements to resolve disputes with taxpayers and that those settlements have generally been concluded in line with its policies and procedures. The ANAO made three recommendations to the ATO, with which the ATO agreed, in relation to a review of its 'pre-settlement assurance' mechanisms across business lines, incorporating future compliance obligations as part of settlement terms and for the recordkeeping obligations to be enforced.³⁸⁴

IGT observations

3.246 As noted earlier, the ANAO very recently conducted an audit of the ATO's settlement practices and found them to be effective with some recommendations for improvement with which the ATO has agreed. Given this ANAO report and time needed for the ATO to implement the resulting recommendations, the IGT is of the view that there is little utility in a re-examination at this time, particularly in the light of his own previous reviews and recommendations on this topic. However, the ATO could provide more public information about its IAS process such as improvement opportunities that have been identified and work undertaken to implement them.

RECOMMENDATION 3.6

The IGT recommends that the ATO publish more information about its Independent Assurance of Settlements process such as identified improvement opportunities and work undertaken to implement them.

³⁸¹ IGT, *Review into aspects of the Tax Office's settlement of active compliance activities* (October 2009).

³⁸² Above n 368.

³⁸³ Above n 364.

³⁸⁴ Above n 14, pp 8 and 10.

ATO RESPONSE

Agree

CONTROLS IN RELATION TO LETTERS OF COMFORT

3.247 In a self-assessment system, taxpayers are responsible for correctly applying the law to their circumstances.³⁸⁵ Due to complexity, however, taxpayers may seek advice from their own advisers or from the ATO. In its advisory role, the ATO may provide advice with different levels of protection for taxpayers including private rulings which are binding on the ATO. The ATO may also provide less formal non-binding advice about a range of matters. One example of such advice is a 'letter of comfort'.

Stakeholder concerns

3.248 Stakeholders have raised a number of concerns that when approaching the ATO to obtain private rulings, they have been offered letters of comfort instead. The reason provided by the ATO has been that, in the timeframe within which such advice was required, it was more feasible to issue letters of comfort as the private ruling process is more rigorous involving peer reviews and various approvals.

3.249 In addition to the concerns of a lack of certainty associated with letters of comfort, in the context of this review, stakeholders have questioned whether the less rigorous process for issuing these products exposes the ATO to integrity risks. In particular, they have mentioned that all private rulings appear on a public register and can be viewed by all whereas this is not the case with letters of comfort.

Relevant materials

3.250 The ATO issues a range of correspondence which may be considered as letters of comfort.

3.251 The first type of letter of comfort issued by the ATO is sent to large numbers of taxpayers to inform them that the ATO considers their tax position be 'low risk' according to its risk rating system as part of its 'Certainty Project'. This Project covers a range of specific business lines and its overall goal is to provide certainty to taxpayers that their income tax returns for a particular year would not be audited.

3.252 The ATO's Individuals business line issued 504,907 letters of comfort in the 2015-16 financial year and 500,582 in the 2016-17 financial year. However, this business line has decided to discontinue this practice and will not issue any such letters for the 2017-18 financial year.³⁸⁶

³⁸⁵ IGT, *Review into improving the self assessment system* (2013) para [2.1].

³⁸⁶ ATO communication to the IGT, 20 November 2017.

3.253 The PGH business line had been sending two different types of letters of comfort. The first type was the Income Tax Assurance Notification (ITAN) which are issued to taxpayers regarded as lower risk:

The ITAN is an acknowledgement (a 'thank you') for our lower risk clients for doing the right thing. It is also to provide encouragement to continue to engage early with the ATO and acknowledge that we appreciate their efforts in managing their tax affairs.³⁸⁷

3.254 The second type was the Income Tax Profile (ITP) which was issued to a range of taxpayers, who had been classified as medium risk, with the aim of encouraging them to address ATO concerns and engage early with the ATO or their tax agent.³⁸⁸

3.255 Over the 2014–15 and 2015–16 financial years, the PGH business line had issued more than 68,000 ITANs and 8,400 ITPs. It has since decided to stop issuing ITANs and ITP notices in bulk. However, PGH compliance officers may generate an ITP on demand as a tool to assist in their interactions with taxpayers.³⁸⁹

3.256 The ATO's ITX business line had also conducted a pilot in April 2016 involving the issuance of 2,090 Tax Assurance Notifications to PGH taxpayers that consisted of a consolidated certainty letter covering income tax and GST from the PGH and ITX business lines' perspectives respectively.

3.257 The ITX business line had also issued approximately 5,500 GST Assurance Notices which were notification letters providing comfort in relation to GST aspects of the March 2016 quarterly BAS. This has also been discontinued due to difficulties in accurately identifying the risk rating of taxpayers promptly.³⁹⁰

3.258 The ATO's internal research for all the projects had indicated that whilst certainty was a valuable objective for taxpayers and the provision of it desirable for the tax system, it was unclear whether issuing unsolicited notifications was the most effective way to provide certainty.³⁹¹

3.259 The second type of letter of comfort is issued in response to taxpayers' requests, seeking confirmation that their tax treatment of a particular transaction is compliant. Alternatively, the request may arise where the ATO has concluded compliance activity, for example a review or audit, and the ATO has not made an adjustment. In such cases, some taxpayers may seek more formal confirmation that the transaction need not be reviewed or audited in the future, especially where such transactions are ongoing.

³⁸⁷ ATO, 'Private groups client experience ITAN & ITP (Transparency) Strategy 2017/18' (Internal ATO document, 8 June 2017) p 1.

³⁸⁸ *ibid.*

³⁸⁹ *ibid.*

³⁹⁰ ATO, 'ATO Office Minute' (Internal ATO document, 20 September 2016); ATO, 'TES certainty project an organisational view of the efficacy of certainty and assurance notifications' (Internal ATO document, April 2017).

³⁹¹ ATO, 'TES Certainty Project An organisational view of the efficacy of certainty and assurance notifications' (Internal ATO document, April 2017).

3.260 ATO officers are required to follow certain procedures depending on the type of compliance activity, such as audits or reviews that they are conducting. At the conclusion of such activity, finalisation letters are generally approved by the case officer's manager. For example, procedures for PGH and PGI standard audits and standard risk reviews³⁹² make a distinction between a case owner (i.e. the case officer) and the case approver (i.e. the case officer's manager). Case officers must obtain the approval of the case approver before the case outcomes can be communicated to the taxpayer.

3.261 Taxpayers may also request letters of comfort unconnected with any compliance activity. In response, the PGI business line can use a product called a 'Tailored Compliance Engagement' (TCE) letter which:

...generally convey[s] our risk assessment [at a point in time] of the tax risks associated with a prospective or a recently implemented arrangement or transaction, and outlines our compliance approach. It [is] ... designed to provide taxpayers with the opportunity and incentive to seek early engagement on potential areas of compliance risk and attempts to balance the tension between timeliness vs absolute certainty.

While this approach does not have the legally binding effect of a ruling, the ATO will stand by the compliance assurance provided for the outlined arrangement as long as there are no changes in the law, client's circumstances [or] disclosed facts.³⁹³

3.262 Training material for the TCE letter indicates that the ATO should not use a TCE letter where the taxpayer has requested a private ruling even where the private ruling would take a long time.³⁹⁴ This TCE product is saved within the Siebel system. Since the introduction of TCE letters in early 2016, the ATO has received 95 requests from taxpayers.³⁹⁵

3.263 The procedures that case officers must follow when authoring a TCE letter are located in the same place as the procedures for more common ATO compliance products such as risk reviews and audits. The procedures for TCE letters indicate that, not only must the case be approved by a case approver (similar to the abovementioned products), but the case officer must also obtain SES officer sign-off before it can be sent to the case approver.³⁹⁶

IGT observations

3.264 Generally, taxpayers desire certainty and timeliness with respect to their tax affairs and interactions with the ATO. The ATO acknowledges such need but stresses that a balance has to be struck between timeliness and certainty. A number of previous IGT reviews have made recommendations aimed at improving taxpayer certainty in a

³⁹² ATO, 'Review standard - PGH' (Internal ATO document, 3 January 2018); ATO, 'Audit standard - PGH' (Internal ATO document, 1 December 2016); ATO, 'Review standard - PGI risk review' (Internal ATO document, 4 January 2018); ATO, 'Audit Complex' (Internal ATO document, 4 January 2018).

³⁹³ ATO, 'PG&I Tailored Compliance Engagement, version 1.1' (Internal ATO document, April 2016).

³⁹⁴ ATO, 'TCE Presentation Training Material' (Internal ATO document, June 2016).

³⁹⁵ ATO communication to the IGT, 1 February 2018.

³⁹⁶ ATO, 'TCE (Tailored Compliance Engagement)' (Internal ATO document, 9 November 2017).

range of specific circumstances³⁹⁷ as well as using pilots³⁹⁸, randomised controlled trials³⁹⁹ and other forms of testing to ensure ATO processes are effective.

3.265 The ATO has acknowledged that, whilst taxpayers desire certainty, the means by which it is delivered should be subject to a regular evaluation. Having evaluated the costs and benefits of letters of comfort, it has decided to discontinue them in most instances. They have been maintained in the form of TCE letters, in the PGI business line where there are defined procedures for their issuance, including manager and SES officer approval. Such letters are also saved within the Siebel system enabling the ATO or scrutineers, such as the IGT, to review them, however, they do not appear on a public register as edited private rulings do.

3.266 The IGT acknowledges that more transparency may be required with respect to letters of comfort. However, given their current low numbers, the ATO's existing processes in this regard and stakeholder concerns going beyond transparency issues, it may be appropriate to conduct a review covering all relevant issues at a later time if such concerns persist.

PREDICTIVE MODELS

3.267 Another fraud prevention strategy may be to detect early signs of staff behaviours that if left unchecked may lead to fraud.

Stakeholder concerns

3.268 Stakeholders believe that the ATO could better prevent fraud and misconduct by identifying behaviours or factors which are indicative precursors to fraudulent activity ('red flags') and taking targeted action to address them.

3.269 Stakeholders noted that the ATO's experience with officer misconduct would provide a guide in identifying red flags. They also suggested that the ATO should analyse information from a number of different sources within the organisation including its IT and HR areas, as well as all those who manage staff, to identify and address negative staff behaviour. Whilst such areas within the ATO would be aware of different aspects of officers' behaviours, the ATO could draw on these sources to

³⁹⁷ IGT, *Report into the Australian Taxation Office's large business risk review and audit policies, procedures and practices*, recommendation 8.1 para [8.37] – the IGT made recommendation to increase certainty for large business taxpayers at the conclusion of risk reviews by ensuring the ATO had made a decision to proceed to audit promptly and commence the audit as soon as possible; IGT, *Review into the Tax Office's administration of public binding advice*, recommendation 4 para [5.61] – the IGT made recommendation about the ATO's interpretation of 'general administrative practice'.

³⁹⁸ IGT, *Review into the Australian Taxation Office's use of early and alternative dispute resolution*, recommendation 6.1 (para 6.49) – the IGT recommended the ATO pilot a separate 'Appeals section' from the ATO's compliance functions; IGT, *Review into the Australian Taxation Office's use of benchmarking to target the cash economy*, see IGT observation at para [3.122] regarding the use of pilots before issuing bulk correspondence.

³⁹⁹ IGT, *Review into the Australian Taxation Office's compliance approach to individual taxpayers – income tax refund integrity program*, recommendation 5.1 para [5.23] – the IGT recommended the ATO use randomised controlled trials in correspondence design.

develop a more holistic picture of officer behaviour to proactively identify weaknesses in the ATO's fraud prevention systems.

3.270 Stakeholders have also suggested that some reliance can be made on broader Australian and international research to identify appropriate red flags. However, the most useful red flags are those that are drawn from the ATO's own experience.

Relevant materials

3.271 The ATO's Fraud and Corruption Control Plan lists a range of controls including the 'Organisational Behavioural Assessment' (OBA), which it describes as a key measure in identifying and responding to potential insider threats.⁴⁰⁰

3.272 Since 2014, the ATO has annually produced an internal report which analyses behavioural events with the aim of identifying indicative precursors of workplace behaviour of most serious concern, including misconduct, fraud or corruption (the OBA report).⁴⁰¹ The OBA report is primarily a report to the ATO's ARC and is used to identify high fraud risk areas or profiles for the FPII unit to target intelligence activities and/or fraud prevention and mitigation strategies.⁴⁰²

3.273 In developing the OBA report, the ATO identifies data which indicates 'intentional/volatile behaviours by employees and viewed by the organisation as contrary to its legitimate interests'. The ATO refers to these as Counterproductive Workplace Behaviours (CWBs). CWBs may affect the organisation when it takes such forms as misuse of information and resources, fraud and absenteeism, or it may be directed at individuals within the organisation, for example violence, harassment and bullying. The table below sets out examples of such behaviours.⁴⁰³

Table 3.7: Examples of Counterproductive Workplace Behaviours

Behaviours directed at the organisation	Behaviours directed at individuals
Misuse of information and resources	Violence
Destruction of property	Verbal abuse
Theft	Harassment
Fraud	Bullying
Sabotage	Disciplinary problems
Misuse of employee privileges	
Absenteeism and tardiness	

Source: ATO

⁴⁰⁰ Above n 86.

⁴⁰¹ ATO, 'Organisational Behavioural Assessment (OBA) 2017 report findings' (Internal ATO document, 2017).

⁴⁰² ATO, 'FPII Organisational Behavioural Assessment 2013, 11 July 2014 report submitted to the ARC' (Internal ATO document, 11 July 2014).

⁴⁰³ Above n 401.

3.274 The ATO identifies CWBs from information traditionally held in silos by fraud and integrity, HR, security areas⁴⁰⁴ and includes the following sources:

- FPII referrals, open FPII investigation cases and finalised cases in which allegations of fraud or serious misconduct have been substantiated;
- security incident referrals which are captured through the online security incident forms and may include allegations such as threats, loss or damage to ATO assets, theft and trespass; and
- health and people management cases including conduct and performance issues.⁴⁰⁵

3.275 The OBA report draws upon data from the previous calendar year and does not identify individual officers. Where specific FPII substantiated case files are examined for further detail to develop fraud profiles or typologies, these are only conducted by FPII Intelligence Analysts with a NV1 security clearance.⁴⁰⁶

3.276 Once the data has been collected, the ATO seeks to detect correlations between that data and conducts a statistical analysis⁴⁰⁷ to determine the strength of the relationship between different types of workplace behaviours. It is noted that such correlation does not, of itself, establish a causal relationship⁴⁰⁸ and must be considered in the light of other factors. For example, sites with fewer staff may have a lower rate of reporting types of CWB compared to larger sites. It does not necessarily follow that smaller offices are a means of reducing CWB.

3.277 Once a correlation is identified, the ATO may develop a hypothesis to explain the relationship. For example, with respect to the correlation between staff numbers and the rate of CWB reporting, the ATO hypothesises that larger sites grant more anonymity to staff who report misconduct, whereas in smaller sites there are likely to be relationships between the person suspected of misconduct and the potential reporter.⁴⁰⁹

3.278 The focus of the OBA report has been to analyse the incidence and prevalence of CWBs by ATO office location or 'site' and to identify clusters of CWBs ('hot spots').⁴¹⁰

3.279 Once the OBA report identifies a hot spot, the FPII unit conducts or recommends risk mitigation activity in that site. For example, where the analysis of survey data shows that staff in Site A are less likely to report fraud if they see it, the

⁴⁰⁴ ATO, 'Australian Taxation Office Organisational Behavioural Assessment Report on analysis of 2014 calendar year' (Internal ATO document, July 2015) p 3.

⁴⁰⁵ ATO 'Australian Taxation Office Organisational Behavioural Assessment - 2017 National Program Manager Information pack' (Internal ATO document, 2017) see 'Site based findings' section.

⁴⁰⁶ ATO communication to the IGT, 15 November 2017.

⁴⁰⁷ The Pearson Product Moment Correlation model.

⁴⁰⁸ Above n 402.

⁴⁰⁹ *ibid.*, p 9.

⁴¹⁰ ATO 'FPII Organisational Behavioural Assessment Inter-agency Workshop' (Internal ATO document, December 2014).

FPII unit may run face-to-face fraud awareness sessions in Site A, alerting people to the available channels for staff to refer matters to FPII and/or their obligations to do so.⁴¹¹

3.280 Where relevant, the FPII unit may also consult with the PST to assist in delivering risk mitigation strategies, or to better understand staff culture in these sites.⁴¹² One of the functions of the PST is to provide face-to-face support to managers in their relevant site. Their position would enable them to provide insight to the FPII unit about the trends or behaviours occurring.⁴¹³

3.281 Once risk mitigation activity has taken place, the ATO reviews the situation to see if there have been any changes. For example, where the FPII unit has delivered face-to-face awareness sessions on site to promote a positive reporting culture, it may refer to results of subsequent surveys (such as the ATO 'Pulse Survey') to see if staff sentiment has changed (i.e. an increase in staff indicating they would be more willing to report wrongdoing to the FPII unit) or if there has been an increase in referrals to the FPII unit subsequent to the session being delivered.⁴¹⁴

3.282 Since 2014, all OBA reports have provided a site-based analysis of hot spots. The 2015 OBA report included additional analysis by business line⁴¹⁵, however, the analysis has not been included in the 2016 or 2017 OBA report 'due to continued structural change and an inability to confidently match activity to the changing business lines'.⁴¹⁶

3.283 The 2017 OBA report provided a number of fraud risk profiles drawn from substantiated case data over the previous five years.⁴¹⁷

3.284 The OBA report has always been provided to the ARC⁴¹⁸, however, the manner in which information from the OBA report has been communicated and to whom has changed over time. In 2014, information from the OBA report was also informally communicated to the ATOP business line and members of the ATO Executive in identified sites.⁴¹⁹ OBA information was also provided in 2015 to business line Executives with a presence in identified sites⁴²⁰ and information from the 2016 OBA report was presented to Site Leaders of various ATO offices highlighted in that

⁴¹¹ Above n 405, see 'Burnie' as an example.

⁴¹² *ibid.*, see 'Chermside' as an example.

⁴¹³ Above n 404, p 8.

⁴¹⁴ Above n 401, see 'Parramatta' as an example.

⁴¹⁵ Above n 404.

⁴¹⁶ ATO, 'Australian Taxation Office Organisational Behavioural Assessment July 2016' (Internal ATO document, July 2016) p 2.

⁴¹⁷ ATO, 'Australian Taxation Office Organisational Behavioural Assessment - 2017' (Internal ATO document, 2017) p 2.

⁴¹⁸ For example, ATO, 'Minutes to the 28 August 2014 ATO ARC' (Internal ATO document, 9 September 2014), ATO, 'Minutes to the 29 August 2016 ATO ARC Meeting' (Internal ATO document, undated).

⁴¹⁹ ATO communication to the IGT, 15 November 2017.

⁴²⁰ For example, ATO, 'Office Minute FPII to Acting Deputy Commissioner CAS Service Delivery' (Internal ATO document, 30 July 2015).

report. Snapshots at the ATO Group level were also created and disseminated on request from Group Executives.⁴²¹

3.285 In 2017, the information from the OBA report was also provided to additional groups in the following manner:

- a 'National Program Manager Information Pack' was provided to all SES Band 2 officers;
- information was presented to all SES Band 1 and Band 2 officers in the Law Design and Practice Group; and
- a tailored snapshot of information relating to various business lines within the Service Delivery Group was provided to all SES Band 2 officers in that Group and the Chief Service Delivery Officer.⁴²²

IGT observations

3.286 The ATO's OBA is based on the premise that certain behavioural events can be used as a predictive indicator of more serious misconduct, fraud or corruption. The OBA's identification of such behavioural events is based on correlations of employee behaviours, at the group level (most commonly an ATO site).

3.287 By contrast, other organisations such as law enforcement agencies use 'early intervention' systems to identify individual officers whose performance exhibit concerns.⁴²³ There are a number of reasons why, in the current context, it is preferable for the ATO to adopt a site-based OBA approach rather than one focusing on individual officers.

3.288 First, the ATO does not collect the type of behavioural information at an employee level which would be useful in making accurate predictions. For example, studies by the Association of Certified Fraud Examiners (ACFE) have found that 'living beyond means' and 'financial difficulties' behaviours are exhibited by a significant percentage of perpetrators of occupational fraud.⁴²⁴ However, such information is not readily available from the ATO's electronic employee record system and if the ATO sought such information it may be perceived as a breach of trust which could undermine staff morale.⁴²⁵

3.289 Secondly, even if the ATO could collect the information needed, it would be difficult to design prevention strategies to target an individual without raising perceptions that the employee had been 'judged guilty' of conduct that they had not

⁴²¹ See, for example, Site Report for Chermside in ATO, 'Fraud Prevention and Internal Investigations Snapshot of Organisational Behavioural Assessment results, Chermside' (Internal ATO document, undated).

⁴²² See, ATO, 'Organisational Behavioural Assessment Snapshot for Service Delivery Group' (Internal ATO document, 2017).

⁴²³ See, for example, Office of Police Integrity Victoria, *OPI Research Paper No. 1, Early Intervention Systems for Police Agencies* (2007) p 2.

⁴²⁴ Association of Certified Fraud Examiners (ACFE), *Report of the Nations on Occupational Fraud and Abuse 2016 Global Fraud Study* (2016) p 68.

⁴²⁵ See, Cifas (UK Fraud Prevention Service), *Staff fraud and dishonesty: Managing and mitigating the risks* (2012) p 30.

yet engaged in. Such a prevention strategy removes the anonymity that is provided by current prevention strategies which are targeted at the group level. In any event, the ATO has a range of other prevention controls aimed at addressing unethical conduct at an individual level.⁴²⁶

3.290 Thirdly, any predictive models would also need to consider the influence that the officer's colleagues and workplace have on the officer's conduct. For example, case studies by ACLEI have shown that working in small teams can lead to the development of negative subcultures 'where loyalty to a friendship group rather than to a set of professional standards' prevails.⁴²⁷

3.291 In the IGT's view, the ATO's OBA is a positive initiative as it draws together information from different areas of the ATO to enable it to better understand employee behaviour at the site level. This focus on site level behaviour provides benefits over a focus at the individual level as it considers behavioural issues of groups of officers which inherently takes into account the influence of colleagues and culture at the workplace. Such a focus also appropriately allows the ATO to avoid using individual information and only relies on aggregated data.

3.292 It should be remembered, however, that any model's reliability depends on the data used, the analysis conducted and the accuracy of its results. In this respect, the ATO has used Pearson Product Moment Correlation modelling to measure the strength of certain red flags as predictors of misconduct in the context of its own organisation and has determined that certain correlations which are found in other organisations are not evident in the ATO context. For example, whilst the ATO acknowledges the connection between low levels of employee engagement and unplanned leave⁴²⁸, the ATO's OBA analysis has found little if any correlation between unplanned leave and substantiated fraud cases.⁴²⁹

3.293 As mentioned earlier, the OBA draws together and analyses data that has been previously isolated from each other, namely data sourced from its HR, security and internal investigation functions. Such analysis is important as the separation between information held by different areas within an organisation is considered to be one of the main organisational factors that enable insiders to act maliciously:

To fully understand the level of risk an employee poses, an organisation should be able to access information held by [HR] concerning performance and welfare issues, information held by IT about access to electronic data, and Security for physical breaches of security policies.⁴³⁰

3.294 For example, an employee who does not take leave or is protective of their work may simply be perceived as a performance management issue by one area within

⁴²⁶ For example, restricting access to information on a business needs basis and requiring officers to disclose conflicts of interest.

⁴²⁷ ACLEI, 'Vulnerabilities Brief, Integrity Risk Case Study' (March 2017) p 6 <www.aclei.gov.au>.

⁴²⁸ Commissioner of Taxation, *Annual Report 2012-13* (2013) p 82.

⁴²⁹ See, 'Behavioural connections - correlation analysis' in above n 401.

⁴³⁰ United Kingdom Centre for the Protection of National Infrastructure, *CPNI Insider Data Collection Study Report of Main Findings April 2013* (2013) p 14 <www.cpni.gov.uk>.

the agency, but when viewed in the context of a known associate or unexplained wealth, it may be as an indicator of corrupt behaviour.⁴³¹

3.295 In the IGT's view, the OBA allows relationships between different sources of data to be made visible and, as a result, provides the ATO with a more holistic understanding of employee behaviours. It is, therefore, an opportunity to explore the relationship between less obvious variables. This is especially the case when one considers the fact that trusted insiders are likely to avoid triggering obvious indicators of fraud or misconduct. The ATO could test other data sets such as those related to employee technology usage. For example, the OBA could compare substantiated misconduct information against use of screen capture applications or the internet.⁴³²

3.296 The ATO should take a 'best fit' approach to its model as the focus is on addressing agency-specific risks⁴³³ and in doing so also consider the usefulness and relevance of other red flags identified in the literature and with the information holdings the ATO may use. For example, the ATO could consider the ACFE literature which indicates 'unusually close relationship with vendor/customer' as a significant red flag⁴³⁴ and, compare existing variables against data drawn from the conflicts of interest register and FPII investigation files.

RECOMMENDATION 3.7

The IGT recommends the ATO consider incorporating, into its Organisational Behavioural Assessment process, other data sets including employees' technology usage and conflicts of interest disclosures.

ATO RESPONSE

Implemented

⁴³¹ AGD, *Protective security better practice guide: Identifying and managing people of security concern – integrating security, integrity, fraud control and human resources* (2015) para [12].

⁴³² See, Raytheon, *Whitepaper - Best Practices for Mitigating and Investigating Insider Threats* (2009).

⁴³³ See, ACLEI, *Corruption and the changing opportunities for women in law enforcement* (2017) p 38.

⁴³⁴ Above n 424, p 68.

CHAPTER 4 – DETECTION OF AND RESPONSE TO INTERNAL FRAUD

DETECTION METHODS

4.1 No matter how effective a system of preventative controls and processes may be, it cannot provide absolute assurance against the risk of fraud and corruption. Therefore, it is imperative that adequate fraud and corruption detection mechanisms are in place.⁴³⁵

4.2 Detection measures work in tandem with preventative measures as the former informs the refinements required in the other. It is important to note that neither prevention nor detection measures can remain static if they are to be effective as those who seek to commit fraud and corruption will, in response to refinements, adapt their approach in an effort to remain unnoticed. Accordingly, identifying and addressing weaknesses in the fraud and corruption control environment is an ongoing task.

Stakeholder concerns

4.3 Many stakeholders sought assurance around the effectiveness of the ATO's processes to detect internal fraud and misconduct. Some have highlighted the changing workforce environment in the ATO and, in particular, the risks associated with the increase in the number of contractors and casual staff. Whilst some stakeholders were of the view that the ATO has processes in place for detecting unauthorised access to taxpayer information, the ability of the ATO to identify instances where an officer has inappropriately accessed taxpayer records at the request of another officer (by proxy) was questioned.

4.4 In submissions to the review, some ATO officers also indicated that the lack of anonymity in reporting inappropriate behaviour or misconduct, as well as fear of reprisal actions may discourage reporting of potential misconduct.

Relevant information

4.5 As mentioned earlier, the FPII unit is responsible for implementing measures which effectively prevent, detect and respond to internal fraud and corruption. It develops a biennial program of work, in consultation with the ARC and senior executives⁴³⁶, which includes fraud and corruption risk assessment reviews, awareness activities, intelligence work and analytics.

⁴³⁵ Above n 61, pp 53 and 57.

⁴³⁶ ATO, 'ATO Office Minute, FPII Risk Review Activity' (Internal ATO document, 6 June 2017) p 1.

4.6 The FPII unit's priorities for the 2016–18 period focuses on the following fraud and corruption risks:

- 'The information we hold' [and where that data is aggregated an additional risk regarding 'big data'⁴³⁷] – The ATO has a significant amount of sensitive and personal information. Unauthorised or inappropriate access to that information can compromise the integrity of the taxation and superannuation systems, and undermine public trust. The move to online access, as well as the capacity to aggregate and manipulate large amounts of data through system development, heightens the potential risks.
- 'Our changing workforce' – Our workforce mix is changing, with more externally engaged employees performing ATO functions. The need for specialist skills subject to labour market pressure, and the need to deploy additional resources quickly, can impact usual employment process. As well, employees are performing more work remotely, using a range of mobile technology to access ATO information systems, and there are fewer restrictions on things like wireless connectivity in the workplace. Employees also utilise cloud systems to share, store and transfer information.
- 'The integrity of our resources' – A cultural shift to a less rigid and defined rules based environment, with an associated focus on trust and empowerment, creates potential risks in how ATO assets and resources might be used. This includes both physical and financial assets.⁴³⁸

4.7 FPII fraud and corruption risk assessments and reviews seek to identify improvement opportunities or instances where the ATO's controls and processes may need to be reinforced. Over the 2016–18 period, the FPII unit had planned to conduct a total of 25 such risk assessment reviews.⁴³⁹

4.8 The FPII unit also works with the IA unit and relevant business lines in conducting risk assessment reviews and may seek assistance from external service providers if required.⁴⁴⁰ Upon the completion of these reviews, the FPII unit develops action plans with the relevant business lines to address and monitor risks that were identified.⁴⁴¹ The results of these reviews are provided to the ARC on a quarterly basis. Between 1 January 2014 and 31 March 2017, the FPII unit had provided the results of 38 such reviews to the ARC.⁴⁴²

4.9 The events connected to Operation Elbrus had required the FPII unit to reschedule parts of its program of reviews and a number of FPII staff were involved in responding to issues relating to those events. Furthermore, following investigations connected to those events, the FPII unit brought forward the commencement of its planned risk assessment review of conflicts of interest which had been scheduled for later. As mentioned earlier, the latter review resulted in the ATO September 2017 Report.

⁴³⁷ ATO, 'ATO Fraud and Corruption Control Forward Work Plan 2016–18' (Internal ATO document, 2017) p 2.

⁴³⁸ Above n 86, pp 4–5.

⁴³⁹ Above n 437, pp 2–3.

⁴⁴⁰ Above n 436, p 1.

⁴⁴¹ Above n 437, p 3.

⁴⁴² Above n 436, p 1.

4.10 In addition to the risk assessment reviews, the FPII unit works directly with other business lines in designing controls and detection processes to ensure that potentially fraudulent or inappropriate activities are addressed. For example, the FPII unit assisted the Service Delivery business line to test a business assurance process, the Post Event Control Framework which is designed to identify unusual or high risk transactions. This process identified 28 different scenarios and activities which would be unusual for an ATO officer to undertake. Analysis of the process, which is conducted by the business line on a monthly basis, was provided to the FPII unit who undertook social network data matching and data scans to identify potential relationships between ATO officers and identified taxpayer accounts that were involved in the unusual activity.⁴⁴³

4.11 The FPII unit also conducts regular data scans on ATO officer activities that leave electronic footprints on the ATO's systems. Scans can be used to detect inappropriate behaviours such as the misuse of fleet vehicles, time sheet fraud and unauthorised access to taxpayer information.⁴⁴⁴ The parameters of these scans may be adjusted to the identified level of risks and used to compare with other sources of information to identify trends or patterns for further review.⁴⁴⁵

4.12 Before examining FPII's unauthorised access scans, it is necessary to understand how employees leave an electronic footprint when accessing ATO systems and the restrictions placed on such employee access.

4.13 Access to the ATO's internal software platform is restricted to ATO employees who are allocated a unique User Identifier (User ID). The User ID together with a password provide access to ATO systems but also allow the ATO to track such access. For example, when officers are prosecuted for unlawful access to taxpayer records⁴⁴⁶, the audit logs of that User ID's access are relied upon in evidence.

4.14 The User ID is also used as a preventative measure and restricts employees' access to the applications and records that are needed by those employees to conduct their work. The applications and records that an ATO employee is authorised to access are recorded against the User ID as 'access attributes'. Approval to apply an access attribute to a User ID is given by the relevant manager in the business area, as they confirm that the employee with that User ID needs such access to perform their duties. The person who grants such access on the system is usually a person with a network assistance role (either in that business area or in the IT area) and, depending on the type of access attribute which is sought, may be restricted to a 'named' person.

4.15 The records of all ATO audit work as well as many other types of ATO work, such as advice work, are accessible via an application called Siebel. Siebel itself is integrated with other ATO systems to provide a 'whole of client view' for ATO employees, which they may use to search information and record activities. For

⁴⁴³ ATO, 'Fraud Detection' (Internal ATO document, undated) p 8.

⁴⁴⁴ ATO, 'Fraud Detection Strategy 2017-18' (Internal ATO document, undated).

⁴⁴⁵ ATO, 'ATO Office Minute - Unauthorised Access Data Probes Minute' (Internal ATO document, 4 November 2016).

⁴⁴⁶ *Taxation Administration Act 1953* s 8XA.

example, an officer may search for a taxpayer's case file and identify the range of interactions that the taxpayer has had with the ATO over the years, subject to any restrictions placed on the records and the employee's access attributes.

4.16 In certain circumstances, the ATO may restrict access to a particular taxpayer's identity and/or any ATO activity that is linked to a taxpayer (called a 'case'). For example, employees cannot access another ATO employee's tax records unless, they have a 'Restricted Access Client' attribute attached to their User ID.

4.17 Before February 2018, FPII unauthorised access scans were conducted on a quarterly basis by analysing audit logs of employees' accesses.⁴⁴⁷ For example, scans can be used to identify access to publicly known personalities or taxpayers who have a social or family connection with ATO officers. The FPII unit would examine these potential unauthorised accesses to determine appropriate treatment actions which would be discussed in the next section. Records of unauthorised accesses are also used to identify areas within the ATO where unethical behaviour may be more prevalent.⁴⁴⁸ The quarterly unauthorised access scans conducted over the period February - April 2017 identified 64 cases for potential investigation.⁴⁴⁹

4.18 In addition to the quarterly scan, the FPII unit ran a targeted scan on casual staff as the engagement of such staff had been identified as a potential risk area. The nature of their transient position raises a risk that they may be less likely to fully adopt the ATO's code of conduct and APS Values. This targeted scan was conducted over a period of 30 months. Casual staff accounted for approximately 12 per cent of the ATO's total workforce over the period of the scan. The scan identified 51 instances of potential unauthorised access which were investigated by the FPII unit, of which 19 were substantiated, five were unsubstantiated and 27 were still being investigated at the time the report was submitted to the ARC on 13 June 2017.⁴⁵⁰

4.19 The case study below demonstrates how the FPII unit utilises scans to detect unauthorised access to taxpayer information. Unauthorised access investigations account for approximately 65 per cent of the substantiated FPII investigations.⁴⁵¹

FPII CASE STUDY 1

The FPII unit conducted data scans to examine if any employees of a particular office had accessed the personal information of any taxpayers with whom they had a personal relationship. The scan identified an employee who had accessed the accounts of several taxpayers who had previously shared the same address as the employee. A separate scan identified the employee as also having accessed the taxation records of several high profile identities linked to Australian cricket.

⁴⁴⁷ Above n 444.

⁴⁴⁸ Above n 443, p 4.

⁴⁴⁹ Above n 444.

⁴⁵⁰ ATO, 'Fraud and Corruption Control Unauthorised Access Scan - Casual Staff' (Internal ATO document, submitted to ARC 13 June 2017).

⁴⁵¹ ATO, 'Internal Investigation Analysis 2009-2017' (Internal ATO document, undated).

FPII CASE STUDY 1 (CONTINUED)

The FPII unit conducted data scans to examine if any employees of a particular office had accessed the personal information of any taxpayers with whom they had a personal relationship. The scan identified an employee who had accessed the accounts of several taxpayers who had previously shared the same address as the employee. A separate scan identified the employee as also having accessed the taxation records of several high profile identities linked to Australian cricket.

Although the employee later admitted to the unauthorised accesses, they stated that they had not discussed the financial position of the accessed taxpayers with any other person and that they were sorry for their actions. However, the FPII unit had also detected over 700 additional unauthorised accesses that could be linked to the employee. Soon after, the employee resigned from the ATO.

Due to the number of accesses identified by the FPII unit, the matter was referred to the CDDP who proceeded with a prosecution. The employee entered a plea of guilty and was sentenced to a term of good behaviour for a period of two years.

Source: ATO

Referrals received by FPII

4.20 Allegations of fraud and serious misconduct ('referrals') are a key source of information for the FPII unit and serve as an important detection mechanism. Referrals may be made by members of the public, government and law enforcement agencies as well as ATO officers.⁴⁵² Referrals may also be received from other ATO business lines and other teams within the FPII unit.

4.21 Table 4.1 below sets out the different ways in which referrals were received in the 2015–16 and 2016–17 financial years respectively.⁴⁵³

Table 4.1: Number of referrals received by FPII, by channel and financial year

Year	Phone	E-mail	Anonymous fraud form	Letter	Public Interest Disclosure	Internally generated	TOTAL
2015–16	11	323	6	6	14	54	414
2016–17	13	266	11	1	19	156	466

Source: ATO

4.22 As indicated by Table 4.1 above, the FPII unit may receive referrals via the telephone, e-mail, via the ATO's anonymous form, by post, through the PID scheme and those which are internally generated by the FPII unit through its scans. The majority of the referrals made to the FPII unit were received by e-mail, which accounts

⁴⁵² ATO, 'Intelligence Team Manual' (Internal ATO document, undated).

⁴⁵³ Above n 285.

for 57 per cent of all referrals received in the 2016–17 financial year, compared with 78 per cent in the 2015–16 financial year.⁴⁵⁴

4.23 Since June 2008, ATO officers are able to lodge a referral to the FPII unit via the anonymous form that is located on the ATO intranet.⁴⁵⁵ In order to use the form, ATO officers must be logged onto the ATO's systems using their unique User ID. The ATO has advised that whilst ATO officers are required to be logged onto the ATO's systems to submit the form, the form has been designed such that the identity of the sender is not traceable. During the 2016–17 financial year, 11 of the 466 referrals received by FPII were made by ATO officers using the anonymous fraud form, compared to six out of 414 referrals in the 2015–16 financial year.⁴⁵⁶

4.24 In relation to referrals by ATO officers more generally, results from the ATO's Fraud and Corruption Control Survey in 2016 indicates that seven per cent of the 5,084 survey participants would not report fraud or corruption if they had witnessed it.⁴⁵⁷

4.25 As mentioned earlier, scans conducted by the FPII unit may also result in internal referrals for potential investigation. These scans have resulted in a marked increase in the number of reviews generated, from 54 in the 2015–16 financial year to 156 in the 2016–17 financial year.

4.26 FPII's Intelligence team is responsible for acknowledging and considering all referrals.⁴⁵⁸ This team also provides all referrals to FPII's Tasking and Coordination Committee (TACC) which comprises representatives from each of the areas within the FPII unit.⁴⁵⁹ The TACC meets daily to consider referrals received by FPII to determine what action will be taken in relation to the referral, including:

- taking no further action and allocating the matter to the Intelligence and Fraud Detection team to retain the referral for intelligence purposes and to manage closure of the matter;
- forwarding the referral to another ATO area for their action, for example, to the ATOP business line if the allegations concern a potential disciplinary issue;
- allocating the matter to a member of the Intelligence team to conduct a 'preliminary intelligence assessment' for further consideration; or
- commencing an investigation and allocating the matter to the FPII Investigations team, particularly for more serious allegations.⁴⁶⁰

⁴⁵⁴ *ibid.*

⁴⁵⁵ ATO, 'FPII Reference Manual' (Internal ATO document, undated).

⁴⁵⁶ Above n 285.

⁴⁵⁷ Above n 290.

⁴⁵⁸ Above n 452, p 3.

⁴⁵⁹ Above n 455, p 16.

⁴⁶⁰ Above n 452, pp 5–6.

2017 Corruption Risk Review

4.27 Following a Parliamentary Joint Committee's recommendation in 2016 for the ATO to assess its corruption risk profile⁴⁶¹ and the events connected with Operation Elbrus, the ATO contracted Professor David Lacey and Mrs Jane Bailey⁴⁶² (the reviewers) to evaluate the current areas of corruption risk for the ATO and to identify potential areas of emerging risk to inform future risk mitigation strategies (2017 Corruption Risk Review).⁴⁶³

4.28 The reviewers assessed that 'the focus on corruption prevention, detection and response is a high priority for the ATO' and that whilst the FPII unit is a 'key pillar within the ATO's corruption resistance framework', there was a tendency of business lines to defer ownership of the corruption risk to FPII or committees rather than take shared ownership of the active monitoring of controls and staff behaviours.⁴⁶⁴

4.29 It was noted that whilst the ATO placed the majority of its 'corruption risk efforts towards acts that involve the unauthorised access of taxation information', there are other risk areas, such as unauthorised access to non-tax related information, which require further attention.⁴⁶⁵

4.30 The reviewers observed that there was not strong evidence of a granular understanding of the corruption risks within each business line. In their view, such a granular understanding would improve the business line control environment and enhance broader business line ownership of corruption risks and their treatments. In order to obtain this granular understanding, they suggested that each business line, independent of each other, identify the decisions made and information held, within that business line, which would be of value to an external corrupting influence. With respect to those decisions and information, business lines were to determine the corrupt acts that had historically been detected and may be anticipated given the emerging areas of corruption risk.⁴⁶⁶

IGT observations

4.31 There are challenges in detecting internal fraud risks particularly as the perpetrators are likely to be well-acquainted with ATO processes and controls and make every effort to remain unnoticed.

4.32 There are also broader environmental factors and emerging trends which may impact on the ATO's efforts to detect internal fraud risks. Some of the emerging trends may not be tax-related or even confined to Australia, especially with the increasing interconnectivity in the digital environment. For example, technology now allows people to operate as anonymous vendors with little chance of detection when using

⁴⁶¹ Above n 17, paras [4.26]-[4.28].

⁴⁶² ATO, 'Dot point briefing on the Parliamentary Joint Committee Inquiry into the Jurisdiction of the Australian Commissioner for Law Enforcement Integrity' (Internal ATO document, July 2017).

⁴⁶³ Above n 10, pp 2-4.

⁴⁶⁴ *ibid.*, p 8.

⁴⁶⁵ *ibid.*, pp 4 and 10.

⁴⁶⁶ *ibid.*, p 5.

black hat software, the darknet⁴⁶⁷ and particular types of cryptocurrency⁴⁶⁸. If such anonymity was combined with knowledge of weaknesses in the ATO's system controls, fraud and corruption risks would be dramatically increased. External systems that are connected to ATO systems pose a particular risk of unauthorised access to taxpayer data.

4.33 The above issue may also intersect with national security risks if foreign state-sponsored actors attempt to scan the systems' environment of the ATO on whom the federal and state governments rely for funding in excess of \$420 billion.⁴⁶⁹ Such attempts appear more likely given recent events both in Australia and overseas.⁴⁷⁰ Accordingly, the ATO should liaise with the Australian intelligence community to anticipate such a risk and learn from countermeasures that revenue authorities in comparable jurisdictions may have taken against such threats.

Identifying fraud and corruption risk

4.34 The ATO has received advice in the 2017 Corruption Risk Review that, in the IGT's view, if followed, should improve its capability to systematically define its fraud and corruption risks in greater detail as well as encouraging shared ownership across the agency in detecting and treating those risks. As the ATO is in the process of developing its new Fraud and Corruption Control Plan for the next two years, there is opportunity for the ATO to apply such advice.

4.35 In the IGT's view, in identifying fraud and corruption, each business line should describe the details of each potential fraud and corruption event having regard to the following:

- data which has a corruption value⁴⁷¹ such as taxpayer and non-taxpayer (e.g. compliance thresholds) information and knowledge relating to discretionary decision-making authority;
- collusion of ATO officers with external parties such as criminal entrepreneurs, organised criminal networks and foreign state-sponsored influencers; and
- actions that may be part of a broader arrangement or series of events which may not be visible to the business line that is identifying the risks, for example, an action that appears to a business line to be an isolated event and may remain invisible unless viewed by the ATO, or relevant government agencies, as a series of actions collectively.

⁴⁶⁷ See, The Guardian, 'The Medicare machine: patient details of any Australian for sale on the darknet', *The Guardian* 4 July 2017, <www.theguardian.com>.

⁴⁶⁸ For example, cryptocurrency that obscures who sent or received the coins, such as those currencies using the CryptoNote application layer protocol.

⁴⁶⁹ See, Australian Cyber Security Centre, *2017 Threat Report* (2017) pp 16, 52 and 59.

⁴⁷⁰ See for example, US Department of Homeland Security, 'Joint Statement from the Department Of Homeland Security and Office of the Director of National Intelligence on Election Security', 7 October 2016, <www.dhs.gov>; ABC News (online), 'Government computer networks breached in cyber attacks as experts warn of espionage threat', 29 August 2016 <www.abc.net.au>.

⁴⁷¹ Corruption value refers to the value of decisions, information and services provided by an organisation which may be exploited: above n 10, p 6.

4.36 To carry out the above, informal and interactive discussions may need to be held with relevant staff to ensure that potential fraud and corruption events have been identified with full knowledge of business processes, information holdings and the broader range of methods that external corrupting influences may employ. Such a systematic approach should lead to questioning of existing safeguards and identifying areas requiring improvement.

4.37 The external reviewers had commented favourably on the ATO's identification of broader emerging themes that are set out in its Fraud and Corruption Control Plan. The ATO's detection activities were found to be strongly focused 'on the unauthorised access of tax information'.⁴⁷² Closer examination of the FPII unit's planned program of work supports this observation with both types of FPII's scans directed at the risk of unauthorised access. Furthermore, a greater proportion of FPII's planned reviews focus on unauthorised access, disclosure and misuse of taxpayer information⁴⁷³ rather than other risks including those relating to discretionary decision-making and disclosure of non-taxpayer sensitive information.

4.38 Whilst the emphasis on unauthorised access is expected due to the ATO's substantial taxpayer information holdings, detection activities may need a broader focus particularly in the light of emerging risks or threats. In the long term, the identification of risks through the systematic approach outlined above would help to create a stronger link between FPII's detection measures and the risks arising in each business line. In the interim, however, exploratory work could be conducted to determine if there would be benefit in strengthening the existing safeguards which are aimed at addressing the risk of ATO officers and externals working in concert to exploit the ATO's non-taxpayer information holdings and discretionary decision-making.

Analysing past events

4.39 Analysis of past events may assist in identifying opportunities to strengthen existing controls and processes. Such analysis may also identify perpetrator's motivating factors which could be useful in designing preventative strategies.

4.40 Following the events connected with Operation Elbrus, the ATO reflected on its overall corruption risk profile and conducted reviews of key controls regarding conflicts of interest and security clearance processes. Such work is to be commended and can be augmented by further analysis of events, recording all findings and resulting actions in one central library as a means of maintaining corporate history that may prove useful in the future.

⁴⁷² Above n 10, p 12.

⁴⁷³ Above n 437, p 2.

4.41 For example, following the events connected with Operation Elbrus, a retrospective analysis of the events leading up to and after the raids would have identified a number of key issues for further inquiry and analysis, including:

- what the alleged syndicate members knew of ATO and ASIC operations as well as liquidators and how that information had been obtained;
- how the alleged syndicate members exploited particular weaknesses arising from the interaction of tax, credit, corporation and insolvency laws⁴⁷⁴ and how they are administered; and
- whether loyalty to particular personalities override a culture that upholds integrity and professional standards.

4.42 Many of the above issues are not unique to the events connected with Operation Elbrus and some have persisted for many years and are common with those faced in the bottom of the harbour schemes of the 1970–80s.

4.43 The ATO already carries out some retrospective analysis of relevant events. For example, the FPII unit's work with the OBA report retrospectively analyses aggregated data from many cases to develop hypotheses which can then be tested.

4.44 In the IGT's view, the ATO should, as a routine business process, retrospectively analyse the facts and events surrounding any significant internal fraud case that may arise. Such analysis should consider why existing controls did not work and the nature of staff action or inaction as well as consideration of any relevant non-tax elements.

Unauthorised access by proxy

4.45 Detection activities do not operate in isolation. For example, the ATO's unauthorised access scans identify ATO officers who have inappropriately accessed taxpayer information for further investigation based on their User ID. It is more difficult to identify circumstances in which an authorised ATO officer accessed information at the request of another ATO officer who is not so authorised (unauthorised access by proxy). In these circumstances the only visible electronic footprint is that of the authorised officer and adherence to ATO's staff instructions is paramount. The instruction states that information should only be accessed on a strict 'need to know basis'.⁴⁷⁵ In the IGT's view the risks of unauthorised access by proxy may be addressed by requiring requests associated with such access to be made in writing outlining the justification for the request. These requests should be accessible to FPII investigators examining potential unauthorised access.

⁴⁷⁴ The Government's announcement regarding measures to address phoenix arrangements will change the control environment regarding these. See the Hon. Kelly O'Dwyer, MP, Minister for Revenue and Financial Services, *A comprehensive package of reforms to address illegal phoenixing* (Media Release, 12 September 2017).

⁴⁷⁵ Above n 82.

Referrals to the FPII unit

4.46 It is important that ATO officers are encouraged to report suspected misconduct, are taken seriously and are protected from reprisal action. Providing feedback to the person making the allegation and demonstrating that action was taken in response to allegations is crucial to ensure that staff appreciate that any allegation is taken seriously.⁴⁷⁶

4.47 During the review, some ATO officers had expressed concerns to the IGT that they may be discouraged from reporting suspicions of fraud or misconduct due to a lack of clarity about the relevant processes as well as concerns about confidentiality and fear of reprisal action. The number of referrals received by the FPII unit through the anonymous fraud alert form reflects such concerns. The total numbers of such referrals for the 2015–16 and 2016–17 financial years were six and 11 respectively. As mentioned earlier, officers must log on to the ATO system to make these referrals although the ATO has assured them that their identity would not be traceable.

4.48 The above concerns could be contrasted with the result of the 2016 ATO Fraud and Corruption Control Survey in which only seven per cent of the 5,084 survey participants said that they would not report fraud or corruption if they witnessed it.⁴⁷⁷ In any event, it is open to ATO officers to set up an external e-mail address and lodge an anonymous referral to FPII's e-mail address which is available externally.

4.49 It is noted, however, that FPII's acknowledgement of anonymous referrals does not include a reference number for subsequent contact with FPII investigators.⁴⁷⁸ The IGT considers that the FPII unit could consider providing such a reference number where acknowledging anonymous referrals as it may be difficult to link future communications to the same case.

RECOMMENDATION 4.1

The IGT recommends the ATO improve its ability to detect internal fraud and corruption by such means as:

- a) acting on the advice it received in its 2017 Corruption Risk Review, including requiring each business line to describe, in detail, potential fraud and corruption events in their area;*
- b) retrospectively analysing events surrounding any significant internal fraud case and recording all findings and resulting actions in one central library for future use; and*
- c) contemporaneous recording of officers' requests to access information about a particular taxpayer and ensuring availability of such records to its Fraud Prevention and Internal Investigations Unit.*

⁴⁷⁶ Audit Office of New South Wales, *Fraud Control Improvement Kit 2015* (2015) p 14.

⁴⁷⁷ Above n 290.

⁴⁷⁸ Above n 452.

ATO RESPONSE

(a) Agree

Work is already underway to implement a new enterprise fraud and corruption risk register and the ATO will continue to refine our fraud control strategies.

(b) Agree

Significant fraud event profiles, to an extent, are already provided in our Organisational Behavioural Assessment and annual reporting. The ATO will draw fraud event profiles from these reports and other intelligence to form a central register.

(c) Disagree

The ATO already requires our staff to use Siebel as a contemporaneous record of taxpayer requests, including action, interaction or decisions directed by ATO staff. An 'audit trail' captures such requests and Fraud Prevention and Internal Investigations interrogate this system as part of the investigation process. All ATO staff are required to make notes and follow the processes outlined in the Records Management Chief Executive Instruction and the 'Guidelines for effective notes in compliance' document.

FPII INVESTIGATIONS OF INTERNAL FRAUD

4.50 An organisation's fraud investigations and responses are key elements of the overall fraud control framework and 'provide Australian Government agencies and external stakeholders with reasonable assurance that perpetrators of fraud are identified and appropriate remedies are consistently applied'.⁴⁷⁹

Stakeholder concerns

4.51 Stakeholders have raised a number of concerns about the adequacy of the ATO's investigations and treatment of allegations of fraud, corruption and misconduct. They considered that there was a general reluctance by the ATO to investigate complaints about management and believed that referrals made to the FPII unit were either ignored or resulted in investigations being finalised without further action.

4.52 Stakeholders have also observed that the ATO may not take disciplinary action even when misconduct had been proven. Similarly, there were concerns that, where inappropriate behaviour was identified, the treatment action taken by the ATO was inadequate or disproportionate to the seriousness of the breach, signalling to the rest of the organisation that there are no consequences for misconduct.

4.53 The FPII unit's investigation methods were also questioned and it was queried whether investigations complied with the relevant government quality standards. In addition, there are concerns about whether the ATO has an effective complaints handling process for concerns raised in relation to the manner in which FPII conducts investigations.

⁴⁷⁹ Above n 61, p 63.

Relevant materials

Investigation

4.54 The Fraud Guidance states that in conducting investigations, Commonwealth agencies must comply with the *Prosecution Policy of the Commonwealth*, the *Freedom of Information Act 1982*, the *Privacy Act 1988*, Part 1C of the *Crimes Act 1914*, the Commonwealth Protective Security Policy Framework as well as other applicable laws.⁴⁸⁰ Under the Fraud Guidance, agencies are responsible for investigating routine or minor instances of fraud⁴⁸¹, that is, instances of fraud which on initial assessment by the agency would not be accepted by the AFP under its CCPM.⁴⁸² The conduct of a fraud investigation allows agencies to gather evidence in relation to specific fraud allegations to determine the relevant facts and to assist in deciding whether further action, if any, is required.⁴⁸³

4.55 Furthermore, the AGIS contains minimum standards for conducting investigations by Commonwealth agencies including a requirement for relevant investigators to have a Certificate IV in 'Government (investigation)' or equivalent qualification as a minimum, otherwise, they must be supervised by an appropriately qualified investigator.⁴⁸⁴ All members of the FPII Investigations team have completed the relevant Certificate IV as well as other relevant courses including those delivered by Commonwealth agencies such as the AFP.⁴⁸⁵

4.56 The responsibility for investigating allegations of fraud or misconduct within the ATO resides with the FPII Investigations team. FPII's roles and responsibilities in relation to the investigation of suspected internal fraud are set out in CEI 2014/05/08 'Internal Fraud'. This document also outlines the obligations for ATO officers in preventing, detecting and reporting fraud as well as assisting FPII investigators in preparing witness statements or attending court proceedings.⁴⁸⁶

4.57 The investigations undertaken by the FPII Investigations team, particularly the processes and actions taken in response to allegations of fraud or misconduct are based on the principles and requirements set out in the AGIS and the Fraud Policy, which were updated in August 2011 and August 2016 respectively.⁴⁸⁷

4.58 The ATO also recently updated its FPII Investigation Standards⁴⁸⁸ and FPII Investigations Reference Manual (FPII Reference Manual)⁴⁸⁹ which set out the manner in which investigations are expected to be conducted by its investigations team to ensure compliance with obligations and government standards.⁴⁹⁰ As part of their role,

⁴⁸⁰ Above n 21, p C18.

⁴⁸¹ *ibid.*, pp 16-17.

⁴⁸² AFP, *The Case Categorisation and Prioritisation Model* (2016) p 2.

⁴⁸³ Above n 61, p 63.

⁴⁸⁴ AGD, *Australian Government Investigation Standards* (2011) pp 1-2.

⁴⁸⁵ ATO, 'FPII Staff Qualifications as at October 2017' (Internal ATO document, October 2017).

⁴⁸⁶ Above n 455, p 13.

⁴⁸⁷ *ibid.*, p 6.

⁴⁸⁸ ATO, 'Investigation Standards' (Internal ATO document, undated).

⁴⁸⁹ Above n 455.

⁴⁹⁰ Above n 488, p 1.

the FPII Investigations team conducts investigations and prepares evidence briefs for criminal prosecution.

4.59 All allegations and relevant documentation about fraud or misconduct are recorded in the FPII case management systems. ATO officers and members of the public who lodge fraud or misconduct allegations can expect to receive acknowledgement within five business days of it being lodged with FPII and receive updates on the progress of their allegation at six week intervals, subject to secrecy and privacy law constraints.⁴⁹¹

4.60 The allegations of fraud and misconduct are reviewed in accordance with FPII's Case Evaluation Model to determine whether they will be accepted for further investigation. Generally, an allegation will not be accepted for further investigation if insufficient information has been provided, the matter raised in the allegation has previously been investigated or it is more appropriate for another area within the ATO or an external organisation to consider.⁴⁹²

4.61 When a case is referred to the Investigations team following the TACC, it is assessed to ensure that it is prioritised in accordance with a number of risk factors which include, the nature of the allegation, sensitivity, aggravating circumstances, the manner in which the person in question is employed as well as overall complexity of the matter. Other factors which may affect the level of priority for an investigation include the impact on resources, need for SES officer or external direction, materiality of the impact on both internal or external matters and any ongoing court proceedings.⁴⁹³ The FPII Investigations team undertakes further assessment of the allegations based on their potential impact on the ATO and its stakeholders to assist it in allocating its resources and determining investigation timeframes.

4.62 Allegations which have the potential to impact on the ATO's reputation, relate to the public interest or are expected to result in prosecution action, are reported to the FPII Director of Investigations and FPII Assistant Commissioner who may notify other relevant areas within the ATO, including the media relations team, if required.⁴⁹⁴

4.63 When an ATO officer is subject to an FPII investigation, they are required to be informed no later than 11 working days of an allegation being made about them, except where doing so may cause them undue distress or potentially compromise the investigation.⁴⁹⁵

4.64 During an FPII investigation, managers are required to allow officers who are subject to allegations to participate in interviews with FPII investigators or obtain other support services to assist them through the investigation.⁴⁹⁶ FPII investigators will also inform the officer's manager of the outcome of their investigation upon completion.

⁴⁹¹ Above n 455, pp 17 and 32.

⁴⁹² ATO, 'Case Evaluation Model' (Internal ATO document, undated) p 1.

⁴⁹³ *ibid.*, p 2.

⁴⁹⁴ Above n 455, p 29.

⁴⁹⁵ *ibid.*, p 20.

⁴⁹⁶ *ibid.*, p 21.

FPII investigators are also responsible for ensuring that the subject of an investigation is regularly informed about the general progress of an investigation.

4.65 In determining the manner in which an investigation is conducted, FPII investigators are expected to consider the nature of the allegation, the type of evidence which could be relevant and the appropriate means to obtain and test that evidence. They often make requests to the ATO's Forensics and Investigations team to obtain access to relevant electronic data on the ATO's systems, for example copies of e-mails and documents stored on ATO officers' personal drives and internet history use.

4.66 If more intrusive evidence gathering is required to be undertaken, FPII investigators must first obtain approval from the FPII Director of Investigations. The Director is responsible for maintaining records of such requests and FPII investigators are required to document the details of such activities. Indeed, all documents and evidence received by the FPII unit during an investigation are required to be recorded, labelled and uploaded to the FPII's electronic case management system pursuant to CEI 2014/01/01 Records Management.⁴⁹⁷ It should also be noted that any interviews should be recorded pursuant to section 23V of the *Crimes Act 1914*.

4.67 Documents obtained as part of an investigation are referred to as 'exhibits' which are required to be handled according to FPII evidence handling procedures as well as other law enforcement agency, CDDP and legislative requirements for the collection and securing of evidence. The responsibility for organising and regularly auditing the register resides with the FPII Director of Investigations.⁴⁹⁸

4.68 If evidence found during an investigation supports an allegation about an officer, the FPII investigator will inform the officer about the allegation in writing and provide them with the opportunity to respond. However, this opportunity will not be provided if the FPII investigator considers that prior notice may prejudice the investigation, for example, risk the destruction of evidence.⁴⁹⁹

4.69 All FPII investigators are required to discuss and obtain approval for all critical decisions which occur during an investigation and ensure that these interactions are recorded in the case file. The electronic case files and records of evidence obtained during an investigation will be reviewed by the FPII Director of Investigations as part of the quality assurance processes before finalising a case.⁵⁰⁰

4.70 An example of how the ATO gathers evidence and uses computer forensics data in its investigation of alleged fraud or misconduct is outlined in the case study below. It demonstrates how the investigation may identify further instances of inappropriate behaviour and how the FPII unit may refer matters to other areas or agencies to progress the matter further.

⁴⁹⁷ *ibid.*, pp 18 and 25–26.

⁴⁹⁸ *ibid.*, pp 28–29.

⁴⁹⁹ *ibid.*, p 20.

⁵⁰⁰ *ibid.*, p 19.

FPII CASE STUDY 2

In 2015, the ATO received an anonymous complaint about an ATO officer who was alleged to have engaged in long term fraud. The matter was referred to FPII investigators who requested and reviewed electronic data on the ATO's systems. Throughout the course of this review, a number of documents were discovered which raised concerns that the officer was potentially engaged in fraudulent activity. This in turn resulted in a further investigation of the matter.

Investigation

With assistance from the ATO's Forensics and Investigations team, FPII investigators were able to access all of the documents on the officer's personal drive, including those which were password protected. Evidence contained within these documents implied that the officer had fabricated the existence of a senior ATO officer and impersonated that officer for personal gain, using the alias to make several travel, luxury hire car and accommodation bookings. It also appeared that the officer had impersonated an operative from another Commonwealth agency.

Evidence contained in the officer's personal drive also indicated that the officer had engaged in other fraudulent conduct. This included the electronic modification of a legitimate medical certificate for the purpose of claiming sick leave for a period where the employee was travelling overseas as well as the creation of falsified ATO payslips.

After the evidence was presented to the employee, the officer did not respond to the allegation but instead elected to receive legal advice. While this occurred, the officer was suspended from ATO duties. The ATO officer, after receiving legal advice, declined to participate in a formal interview and did not otherwise respond to these allegations. The officer resigned from the ATO soon after.

Outcome

The ATO considered the behaviour to be sufficiently serious to warrant referring the case to the CDPP, however, the CDPP declined to prosecute on public interest grounds.

Source: ATO

4.71 In circumstances where allegations or complaints are raised about a member of the FPII unit or the manner in which they are conducting an investigation, the matter will be escalated to the FPII Assistant Commissioner for action. Similarly when an allegation is raised about an SES officer, it will be escalated by the FPII Assistant Commissioner who will subsequently notify the Second Commissioner of the Law Design and Practice Group.⁵⁰¹

⁵⁰¹ *ibid.*, p 29.

Statistical information on FPII investigations

4.72 In response to the IGT's request, the ATO has provided statistical information about FPII investigations. The tables below provide details about investigations conducted in the 2015–16 and 2016–17 financial years, focussing on the outcome of the investigations and the seniority of the officer investigated.

4.73 Table 4.2 provides details about the findings of FPII's investigations for the 2015–16 and 2016–17 financial years. The majority of referrals received by the FPII unit result in the commencement of an investigation with only five percent not proceeding due to insufficient information. Table 4.2 also shows that less than 50 per cent of completed investigations result in no findings due to insufficient evidence. In cases where the allegation is substantiated, the majority are referred to the ATOP business line for action. There are very few investigations (approximately one per cent) in which the FPII unit considers that the actions of an ATO officer warrant a referral to a law enforcement or other government agency for criminal proceedings.

Table 4.2: FPII investigations: outcomes

Outcome	Incapable of determination		No further action		Allegation unsubstantiated		Allegation substantiated	
	2015–16	2016–17	2015–16	2016–17	2015–16	2016–17	2015–16	2016–17
Insufficient evidence / No evidence to substantiate allegation	14	5	42	22	161	147		
Advice provided to informant			1	6				
ATOP Integrity Check			65	21		20		
Unauthorised access warning letter sent							9	38
Manager notified/taking action	1	2			2	14	17	13
Referred to other area for action (ATOP, IT security, TERC)			9	6	1		7	6
Referred to ATOP for potential action							64	54
Employee resigned before action taken	2				3		13	28
Referred to law enforcement agency/other agency							3	2
Uncategorised (a)								6
TOTAL	17	7	117	55	167	181	113	147

Source: ATO

Note (a): At the end of the 2016–17 financial year, there were also 76 open cases.

4.74 Historically, unauthorised access has been one of the key focus areas for the FPII unit. Table 4.3 shows a breakdown of all substantiated FPII cases. Unauthorised access is the largest category accounting for 53 per cent and 65 per cent of all cases in the 2015–16 and 2016–17 financial years respectively.⁵⁰² As a point of contrast,

⁵⁰² ATO, 'FPII Referrals IGT 2009–Current Data' (Internal ATO document, 2017).

substantiated cases primarily about conflicts of interest and abuse of position are very few in both financial years. The remainder of substantiated cases relate to departmental types of misconduct such as misuse of IT facilities and administrative issues which would be expected to be identified in other organisations.

Table 4.3: FPII investigations: substantiated allegations, by category

Category of allegation	2015–16	2016–17 (a)
Abuse of position	3	1
Conflict of interest	2	6
Corruption	0	0
Fraud - administration	5	7
Fraud - revenue	0	2
Misuse of ATO facilities	2	4
Misuse of IT facilities	11	9
Release of information	4	3
Unauthorised access	60	95
Other (b)	26	20
TOTAL	113	147

Source: ATO

Note (a): Figures provided for the 2016–17 financial year includes cases which were not finalised as at 30 June 2017 but were concluded before 31 July 2017.

Note (b): The category of 'Other' relates to cases that are difficult to define or fall outside the jurisdiction of FPII. For example, criminal activity outside the workplace, threatening behaviour or matters being dealt with by law enforcement. This also includes referrals for integrity checks.

4.75 Table 4.4 indicates that over 80 per cent of the substantiated cases relate to actions of ATO officers at APS levels 1 to 6. Contractors account for 13 per cent of substantiated cases and ATO officers holding EL positions account for five per cent of these cases.

Table 4.4: FPII investigations: substantiated allegations, by APS level

APS level	2015–16	2016–17 (a)
APS1	12	51
APS2	11	12
APS3	28	22
APS4	21	13
APS5	5	9
APS6	14	14
EL1	9	5
EL2	4	2
SES	0	0
EXT / CONTRACTOR	8	19
UNKNOWN (b)	1*	0
TOTAL	113	147

Source: ATO

Note (a): Figures provided for the 2016–17 financial year includes cases which were not finalised as at 30 June 2017 but were concluded before 31 July 2017.

Note (b): Unknown – referred to an impersonation of an ATO employee.

Sanctions

4.76 Once an FPII investigator has examined the allegation of fraud or misconduct, obtained the relevant supporting evidence and considered any response from the subject of an investigation, they are required to determine whether further action is required. Where the allegation is found to be unsubstantiated, they may consider that no further action is required. However, where the allegation is substantiated, they will recommend to the FPII Director to take one of the following three actions.

4.77 Firstly, where the misconduct is considered to be minor in nature, the matter may be referred to the manager of the officer who was the subject of the investigation or to other areas in the ATO for their information, for example IT Security to alert them to potential systems vulnerabilities that were uncovered in the investigation.

4.78 Secondly, where the conduct is suspected of breaching the APS Code of Conduct, FPII investigators may refer the matter to the Conduct Performance and Probationary Support (CPPS) area within the ATOP business line and provide them with a copy of the investigation report.⁵⁰³ The FPII investigator may also be tasked with providing a briefing, outlining the facts of the investigation to the CPPS area.

4.79 It is important to note that in such cases the FPII investigator only recommends that a matter should be referred to the CPPS area and does not comment on how the matter should proceed or what sanctions are to be applied. It is the CPPS area's role to determine whether a breach of the APS Code of Conduct has occurred and, if so, what disciplinary sanction should be imposed.⁵⁰⁴

4.80 In determining any misconduct sanctions that should be imposed, the CPPS area consults with the relevant business areas in the ATO⁵⁰⁵ including the director of the ATO officer in question. Sanctions may include reassigning duties or suspension from employment based on the procedures set out in the ATO's 'Practitioners guide to managing suspected misconduct in the ATO'.⁵⁰⁶ Table 4.5 below outlines the range of misconduct sanctions applied by the CPPS area on substantiated cases.

⁵⁰³ Above n 455, pp 31–32.

⁵⁰⁴ *ibid.*, p 32.

⁵⁰⁵ *ibid.*, p 22.

⁵⁰⁶ *ibid.*

Table 4.5: FPII investigations, by disciplinary sanction applied

Disciplinary sanction applied in case	2015–16	2016–17 (a)
Terminated	15	10
Resigned	12	11
Reprimand + reduction of APS level	1	0
Reprimand + 10% salary reduction	2	0
Reprimand + 5.0 – 9.9% salary reduction	10	0
Reprimand + 0.0 - 4.9% salary reduction	1	0
Reprimand + fine (<=2.0% of salary)	2	3
Formal counselling	3	9
Informal counselling	7	6
Reprimand only	1	0
No further action taken	9	9
Case ongoing	1	6
TOTAL	64	54

Source: ATO

Note (a): Figures provided for the 2016–17 financial year includes cases which were not finalised as at 30 June 2017 but were concluded before 31 July 2017.

4.81 Table 4.5 indicates that approximately 40 per cent of misconduct sanctions resulted in the termination or resignation of the ATO officer in question. There has been an increase in the use of formal counselling as one of the misconduct sanctions – from five per cent in the 2015–16 financial year to 17 per cent in 2016–17. Counselling, both formal and informal, accounts for less than 30 per cent of misconduct sanctions in the 2016–17 financial year. One of the other misconduct sanctions available is a reprimand and/or a fine. The fine can be a fixed sum, ranging from \$100–\$500, a percentage of the ATO officer’s salary, ranging from 0.5–10 per cent, or a reduction in APS level.

4.82 As noted in the above Table 4.5, in some instances the CPPS area may consider that no further action is necessary. Table 4.6 below provides a breakdown of the reasons for not taking further action.

Table 4.6: FPII investigations referred to CPPS: Reasons for no further action being taken by CPPS

Year	Subject unable to be identified	Subject left ATO	Breach not proven	Assessed by CPPS that no formal action needed	Refer back to manager for action	TOTAL
2015–16	0	2	1	6	0	9
2016–17	1	1	1	4	2	9

Source: ATO

4.83 Lastly, in some instances, FPII investigators may consider that the evidence and findings uncovered during an investigation may warrant referral to the AFP or another agency. Referrals to the AFP may become necessary where there are serious criminal allegations and the scope of investigation requires the exercise of the AFP’s legislative powers such as telephone interception and search warrants. FPII investigators may also seek AFP assistance to execute search warrants and obtain evidence which will involve collaborative operations during the course of an investigation. Referrals to the AFP occur through an agreement established between

the two agencies, with the decision to refer matters being based on discussions with the FPII Director of Investigations and the FPII Assistant Commissioner.⁵⁰⁷

4.84 Where FPII investigators consider that their findings and evidence suggest a potential breach of criminal law, they may be required to make a referral to the CDPP. As noted in Chapter 1, the CDPP is responsible for prosecuting offences against Commonwealth laws as well as recovering the proceeds of crime and enforcing civil remedies where appropriate. Depending on the nature of the issue and with prior approval from the FPII Director of Investigations, the FPII investigator may seek legal advice from the ATO General Counsel and the Australian Government Solicitor to refer the matter to the CDPP. Such referrals are documented under a memorandum of understanding.⁵⁰⁸

4.85 If it is determined that a referral to the CDPP is appropriate, the FPII investigator is responsible for the overall management and preparation of evidence for briefs in relation to criminal offences. All briefs for criminal prosecution and other referrals to the CDPP are prepared in accordance with the CDPP Guidelines and Directions⁵⁰⁹ manual and provided to the FPII Director of Investigations for approval.⁵¹⁰ It is important to note that the CDPP ultimately decides whether a matter will be prosecuted in accordance with the *Prosecution Policy of the Commonwealth*.⁵¹¹

4.86 When determining whether a matter will be prosecuted, the CDPP considers various factors⁵¹² with particular focus on the availability and effectiveness of any alternatives to prosecution, with the APS misconduct process being an example of an effective alternative. However, FPII investigators may consider that referral to the CDPP is not appropriate having regard to the circumstances of a case. In such cases, FPII investigators must prepare a written minute outlining the reasons for their decisions and provide it to the Director of Investigations for approval.⁵¹³

4.87 In addition to undertaking investigations in relation to specific allegations of fraud or misconduct, FPII investigators may identify deficiencies in controls and circumstances where management action or inaction is identified as contributing to the conduct of the officer under investigation. These matters are referred to the relevant business line within the ATO for their review and consideration.

4.88 In all of the above circumstances and in cases where it is determined that no further action is required due to an allegation being unsubstantiated, the FPII investigator will notify the person who raised the allegation and the officer, who is the subject of investigation, of the outcome within five business days of the matter being finalised.⁵¹⁴

⁵⁰⁷ *ibid.*, pp 10 and 14.

⁵⁰⁸ *ibid.*, p 10.

⁵⁰⁹ CDPP, *Guidelines and Directions Manual – Policy framework for the conduct of prosecutions* (2012).

⁵¹⁰ Above n 455, p 30.

⁵¹¹ Above n 70.

⁵¹² *ibid.*

⁵¹³ Above n 455, p 31.

⁵¹⁴ *ibid.*, p 32.

Quality assurance and reporting

4.89 In circumstances where an investigation exceeds 90 days, it will be subject to review by the FPII Director of Investigations to determine whether any action is required to facilitate a timely resolution. This would involve evaluating the merits of continuing or closing the investigation and ensuring that timely resolution has remained a priority.⁵¹⁵

4.90 At the end of all investigations, FPII investigators are required to prepare a 'Closure Report' minute for the FPII Director of Investigations' approval. The latter should explain the significant findings which resulted in their decision, including why certain lines of inquiry were not followed if they were reasonably obvious in the circumstances.⁵¹⁶

4.91 It is important to note that only the FPII Director of Investigations can approve the closure of a case on the FPII case management system.⁵¹⁷ Prior to closing a case, the FPII Director of Investigations must be satisfied that the investigation has met the AGIS and that any deficiencies which are identified are recorded and brought to the attention of the FPII Assistant Commissioner for appropriate action.⁵¹⁸ The FPII Director of Investigations must ensure that they maintain records about the closure of a case and document whether it was subject to quality assurance review by a peer. These records are maintained on the FPII share drive and may be subject to quality assurance review by external parties.⁵¹⁹

4.92 The FPII Reference Manual indicates that the accountability and quality assurance of its investigation practices should be based on AFP quality assurance reviews and feedback from the CDDP during prosecution referral processes as well as through FPII management and peer reviews.⁵²⁰ The FPII unit has also made preliminary enquiries to have the ATO's General Counsel or independently contracted private legal practitioners from a Commonwealth Government panel to conduct quality assurance reviews on its investigations.⁵²¹ The FPII Assistant Commissioner is expected to select a number of investigations each year and conduct quality assurance on them and report the outcomes to the ARC.⁵²²

4.93 In addition, the FPII Assistant Commissioner is also required to provide monthly reports to the Deputy Commissioner of ATOC and quarterly reports to the ARC about the ongoing progress of its investigations to provide insight into its management of the investigation function. The FPII Assistant Commissioner will also be provided with briefing reports which are likely to draw media attention, raise issues of public or political sensitivity or pose a reputational risk to the ATO prior to critical

⁵¹⁵ Above n 488, para [3.4].

⁵¹⁶ Above n 455, p 34.

⁵¹⁷ *ibid.*, p 33.

⁵¹⁸ Note that another FPII Director may do so in certain circumstances: above n 488, para [3.4].

⁵¹⁹ Above n 455, pp 34-35.

⁵²⁰ *ibid.*, p 20.

⁵²¹ Ashurst, 'Quality Assurance and Strategic Review Australian Taxation Office Fraud Prevention and Internal Investigations', report to the ATO (2017).

⁵²² Above n 488, para [3.4].

case milestones such as the execution of search warrants, court proceedings or media communication.⁵²³

IGT observations

4.94 The FPII Investigation Standards and Reference Manual, which are based on the AGIS, require the ATO processes for carrying out internal fraud investigations to be thorough and well-documented. Such processes aim to ensure allegations of internal fraud and misconduct are appropriately considered and investigated to a minimum standard. It should be noted that both documents have been recently updated and some of the processes and procedures are still to be fully put into practice.

4.95 In conducting this review, the IGT requested a list of all 2,829 allegations received by the FPII unit between 2009 and 2017. The IGT subsequently selected a sample of these cases and examined the relevant material. The cases were selected based on a combination of areas raised in stakeholder submissions to this review, for example, abuse of position, conflicts of interest and unauthorised access, as well as cases which were referred to the CDPP and those which resulted in fraud allegations being substantiated. The sample placed greater emphasis on more recent cases although some older cases were also selected to assist in comparing previous and current procedures and approaches.

4.96 The above sample cases were subsequently reviewed to assist the IGT to gain a greater understanding of FPII investigative practices and to determine the extent to which the procedures and guidelines in the FPII Investigation Standards and Reference Manual were applied. Consideration was also given to whether there was evidence of bias and the manner in which interviews were conducted and recorded. In addition, the IGT examined the overall level of supervision and guidance provided to FPII investigators, the application of quality assurance processes, whether officers, who were subject of an allegation, were afforded procedural fairness and whether the investigators had engaged law enforcement agencies appropriately.

4.97 Upon reviewing the sample of cases, the IGT found that almost half of the cases in the sample did not contain all relevant records on the case file. Apart from these record-keeping omissions, there was no evidence to suggest any further non-compliance with the FPII Investigations Standards and Reference Manual. For example, where allegations were raised, FPII investigators considered the allegations and in the majority of circumstances sought to obtain further information and conducted additional research before determining whether further action was required. Following this, the FPII investigators documented the facts of the case and provided their reasons for conducting a more comprehensive investigation. They then referred the matter to another area within the ATO or to another Commonwealth agency or took no further action as appropriate.

4.98 The IGT also found that, in cases involving more complex issues or requiring referral to other Commonwealth agencies, the FPII investigators had sought advice and

⁵²³ *ibid.*, para [3.5].

approval from the FPII Director of Investigations and the FPII Assistant Commissioner where appropriate. Throughout most of their investigations, the FPII investigators proactively communicated with the relevant parties where required, including contacting the person who had made the allegation to obtain further information, the officer who was the subject of the investigation, the latter's manager as well as potential witnesses.

4.99 It is important to note that while the FPII Investigations team is responsible for investigating the factual basis for any allegations, they do not recommend or impose any disciplinary actions. Such actions are determined by the relevant officer's manager where the conduct was minor in nature, by the CPPS area where the APS Code of Conduct is breached or by AFP or CDPP where more serious criminal allegations are at play.

4.100 Separating the investigation process from determining any resulting disciplinary action is consistent with the relevant Australian Standard.⁵²⁴ Accordingly, the IGT is of the view that it would be prudent to periodically check the appropriateness of disciplinary actions imposed particularly where they are determined within the officer's business line or the latter are involved in making such determinations.

4.101 It would also be prudent for the ATO to undertake periodic reviews of the quality of FPII investigations to assure itself and the community that it complies with the AGIS. In particular, requirement 3.7 of the AGIS specifies that the AFP is responsible for conducting quality assurance reviews of criminal investigations and that those relating to non-criminal investigations are to be conducted by another agency with the necessary skills and capacity. The AGIS also states that the outcomes of the quality assurance reviews are to be provided to the Chief Executive Officer (CEO) of the agency and the results, including an analysis of best practices and identified deficiencies are to be provided to the AIC.⁵²⁵

4.102 The FPII unit has outlined the manner in which it expects to provide internal and external quality assurance of its Investigation Standards in its Reference Manual. In conducting this review, the IGT review team requested that the ATO provide all examples of internal and external quality assurance activities which had been undertaken in relation to FPII investigations. As a result of this request, FPII provided copies of three external quality assurance reports which demonstrate that quality assurance reviews were conducted. Two of these reviews were conducted by the AFP for the 1998-99 financial year and Blackburn Chambers in the 2008-09 financial year respectively.

4.103 The IGT has also observed that the third external quality assurance review, conducted on FPII investigations after the introduction of requirement 3.7 of the AGIS, was undertaken by the Department of Foreign Affairs and Trade. There has not been such an external quality assurance review since 2012. However, the ATO has provided

⁵²⁴ Above n 84, para [5.5.3].

⁵²⁵ Above n 484, p 12.

evidence which indicates that it has recently made preliminary enquiries with an independent external law firm to conduct these reviews. Where the ATO commissions a private sector organisation to conduct such a review for a fee, perceptions of lack of independence may arise. Another government agency could undertake the task, however, there may still be perceptions of bias as both agencies are under the umbrella of the APS.

4.104 In the IGT's view, the ATO should engage externals to conduct an annual quality assurance review process for FPII investigations and publish the results of such reviews. Another option would be for the ATO to conduct such reviews more frequently. For example, selecting investigations for external quality assurance reviews on a monthly basis would provide the ATO with more timely feedback and allow refinements as required.

4.105 It should also be noted that the FPII unit has not yet implemented the annual quality assurance review process which is to be conducted by the FPII Assistant Commissioner. The IGT believes these reviews should commence as soon as practicable, particularly in the light of the current lack of external review. In this respect, it would be reasonable to expect that the FPII unit would engage with other Commonwealth agencies with similar experiences, challenges as well as fraud and corruption risk profiles.

4.106 It is also important to provide assurance about the conduct of FPII investigations particularly where they were initiated as a result of concerns raised by ATO officers or by the broader community. At present, only high-level information is provided on the ATO's intranet. Whilst it is understandable that it would be inappropriate to disclose investigation methodologies, other information, such as procedural safeguards and timeframes within which certain actions may be taken, could be shared. Provision of the latter information would engender confidence both for those raising concerns as well as ATO officers who are the subject of investigations.

4.107 ATO officers, who are the subject of FPII investigations and are dissatisfied with the manner in which it was conducted, can provide the FPII unit with valuable feedback. Procedures to handle complaints regarding the conduct of such investigations are required by the AGIS⁵²⁶, however, at present, the ATO does not have such procedures. Under the ATO's current procedures, if the subject of an FPII investigation wishes to lodge a complaint about the investigation process, the matter is referred directly to the FPII Assistant Commissioner in the first instance.

4.108 The absence of an independent formal complaints handling process may expose the FPII unit to perceptions of a general reluctance to investigate complaints about its own staff. Implementing a well-documented and transparent complaints handling process would assist the FPII unit in demonstrating that all complaints are treated seriously and are acted on in a comprehensive and timely manner in accordance with requirement 1.9 of the AGIS. Furthermore, such a process would provide timely insights into the broader issues which may not otherwise be identified

⁵²⁶ *ibid.*, p 3 requirement 1.9.

through internal or external quality assurance processes. Accordingly, the IGT is of the view that the ATO should implement such a complaints handling process and inform staff about their right to have their concerns considered by, for example, publishing information about how to lodge a complaint about an FPII investigation on its 'what you can expect from us' page on its intranet.

RECOMMENDATION 4.2

The IGT recommends that, with respect to its internal fraud investigations, the ATO:

- a) periodically review the appropriateness of sanctions imposed;*
- b) conduct appropriate and periodic external and internal quality assurance reviews and publish the results of such reviews;*
- c) provide more public information about the investigation process such as timeframes and procedural safeguards; and*
- d) develop a formal complaints handling process as well as inform its staff about the process and how such complaints may be lodged.*

ATO RESPONSE

(a) Agree

(b) Agree

Annual quality assurance has already been incorporated into the Fraud Prevention and Internal Investigations Standard. The ATO will publish results commensurate with the audience and balance transparency with investigative integrity and privacy.

(c) Agree

The ATO will include, in our internal communications, material which outlines the standards for internal investigations.

(d) Agree

CHAPTER 5 – GOVERNANCE, STRUCTURE AND OVERSIGHT FOR MANAGING INTERNAL FRAUD RISK

5.1 Pursuant to the PGPA Act, the Commissioner, as the CEO of a Commonwealth agency, is personally accountable for the exercise of his powers and those exercised by his staff by virtue of a series of cascading delegations and authorisations. The exercise of these powers is subject to governance arrangements which consist of a system of risk oversight and management as well as internal controls which include measures directed at ensuring compliance with relevant legislation and related policies, including the Fraud Rule and the Fraud Policy. Effective governance is vital in creating an environment of trust, transparency, integrity and accountability necessary for the administration of government programs as well as eliciting voluntary compliance from the community.

GOVERNANCE ARRANGEMENTS, INTEGRITY FRAMEWORK & REPORTING

Stakeholder concerns

5.2 In submissions to the review, stakeholders have raised concerns that the ATO's overall corporate governance framework and emphasis on ethical behaviour does not appear to be as robust as it was previously. They recalled, for example, the ATO's previous Integrity Reporting System which provided visibility to the Commissioner on the progress against each integrity indicator and allowed the Commissioner to directly query the responsible senior officer to discuss issues of concern.

5.3 Stakeholders were of the view that the ATO's performance against its integrity indicators should be more visible to the public as well as to the Commissioners and the ARC. In particular, some stakeholders believed that:

- the ARC should maintain focus on risks that have a high capacity to damage the reputation of the ATO, including the internal fraud risk;
- the FPII unit should be required to report directly to a Second Commissioner on fraud and misconduct issues;
- the ATO's performance against its integrity indicators should be made public; and
- the robustness of internal fraud controls should be proactively tested by the IA unit.

5.4 Stakeholders were also concerned about the removal of the ATO's Integrity Adviser who had played an important role by participating in key ATO Committee meetings and ensuring appropriate systems and controls were in place to alert the senior executive of acts of impropriety. Some have mentioned that even when the ATO had an Integrity Adviser, they were not always provided with sufficient independent support and experienced challenges where staff were not comfortable raising concerns

or where managers were not receptive to quantifying, reporting and addressing identified risks. For example, a stakeholder recounted an integrity advisor no longer being required to participate in an ATO committee after raising concerns about a number of unreported breaches.

5.5 Some stakeholders raised concerns with the increasing number of private sector candidates being appointed to ATO SES positions. In particular, they were of the view that they may not be as familiar with or appreciate the governance requirements in the public service, the value of these processes and the broader consequences of decisions made in the public administration context. For example, stakeholders were of the view that before reducing 'red tape', there must be an examination of the reasons for their existence and whether their reduction would expose the ATO to serious risks.

Relevant materials

Current governance arrangements

5.6 As mentioned in earlier chapters, the ATO's governance arrangements, includes:

- the Commonwealth Fraud Control Framework;
- the ATO Enterprise Risk Management Framework;
- the ATO Fraud and Corruption Control Plan; and
- the ATO CEIs.

5.7 The FPII unit, IA unit and ARC have key responsibilities in giving effect to the above governance arrangements. Unlike the FPII and IA units which consist solely of ATO officers, the ARC has five members, comprising of the Chair who is an ATO Second Commissioner, Deputy Chair who is an ATO Assistant Commissioner and three independent members.⁵²⁷ The ARC is also supported by ATO officers who provide advice on various matters and includes the ATO's Chief Financial Officer (CFO), Chief Internal Auditor and the FPII Assistant Commissioner. The ARC sub-committee's membership is the same as the ARC itself, with the exception of the Second Commissioner.

5.8 In addition to the above governance arrangements to manage internal fraud risks, the ATO applies the 'Three Lines of Defence' model for risk management and internal control:⁵²⁸

1. Senior managers of different business areas own and manage risks and are responsible for operationalising governance controls and implementing corrective actions to address process and control deficiencies.

⁵²⁷ Commissioner of Taxation, *Annual Report 2015-16* (2016); ATO, 'ARC and ARSC membership' (Internal ATO document, undated).

⁵²⁸ Above n 7, p 134.

2. Corporate functional areas, such as Risk and Assurance, facilitate, monitor and provide assurance on implementation of effective risk management practices by the business areas.

3. Internal audit, through a risk-based approach, provides independent assurance and advice to the ATOs Audit and Risk Committees and management, on how effectively the ATO assesses and manages its risks.

5.9 The above model corresponds with the guidance issued by the Department of Finance to assist agencies in implementing the Commonwealth Risk Management Policy.⁵²⁹ In accordance with this model, the ATO allocates responsibility to:

- the Deputy Commissioner of ATOC, for monitoring and providing assurance on the effectiveness of internal fraud controls as well as preparing conformance statements and integrity indicator reports⁵³⁰; and
- the FPII unit which supports the Commissioner with respect to obligations set out in the Commonwealth Fraud Control Framework and implements strategies to prevent, detect and deal with internal fraud and corruption.

5.10 As mentioned earlier, a significant part of the above governance arrangements is demonstrating conformance with legislative obligations and relevant policies through a number of reporting programs such as the conformance with obligations program and the corporate integrity indicators reports, both of which are provided to the ARC and the Deputy Commissioner of ATOC.

5.11 In Corporate Integrity Indicator reports to the ARC, the ATO uses four of the seven indicators for risks of internal fraud and corruption:⁵³¹

- mandatory training;
- unauthorised access to taxpayer records;
- conflicting access roles; and
- security incidents.

5.12 There is an indicator for unauthorised access to taxpayer records in these reports although the ATO considers it to be 'generally a lower level risk than fraud on the revenue or fraud administration'⁵³². The FPII unit is responsible for providing the measurement of this indicator. FPII provides the number of substantiated cases of unauthorised access, the trends, treatments and actions taken to address the risks such as targeted communication from FPII and regular integrity scans of ATO systems for access of high profile Tax File Numbers (TFNs) amongst other things.⁵³³

5.13 With respect to the other indicators, the ATO has advised that they are 'periodically reviewed by ATO Corporate to ensure integrity indicators focus on areas of high risk, priority or where the ATO needs to improve'. The relevant business lines

⁵²⁹ Department of Finance, *Resource Management Guide 211 - Implementing the Commonwealth Risk Management Policy - Guidance* (2016) p 27.

⁵³⁰ ATO, 'Risk Management CEI Guidelines' (Internal ATO document, 16 March 2015); Above n 105; Above n 101.

⁵³¹ See for example, above n 11, p 4.

⁵³² Above n 404.

⁵³³ ATO, 'Corporate Integrity Indicator Report - March Quarter 2017 results' (Internal ATO document, undated).

in the ATO are expected to 'monitor results, take action where improvement is needed, report any significant matters to the relevant executives and report any exceptions to the ATO Executive as required'.⁵³⁴

5.14 Reviews of the indicators may also be undertaken at the request of the ARC. For example, in 2015, the ATO reviewed them as part of its internal review of the integrity framework. At that time, there was an additional indicator for 'bullying, harassment and discrimination' which was discontinued soon after the internal review.⁵³⁵

5.15 The internal review had also observed that the integrity reporting was needed to be enhanced to include 'an annual snapshot summary of the health of the ATO's integrity arrangements' which would be provided to the ARC and senior management.⁵³⁶ Consequently, the ATO's 2015-16⁵³⁷ and 2016-17⁵³⁸ corporate integrity indicator reports included results of the previous quarters as well as the prior year. The ATO has advised that corporate integrity indicator reports are now incorporated into its 'ATO Executive report', which includes broader ATO measurements which are reported in its Annual Performance Statement, such as lodgments by taxpayers.⁵³⁹

ATO's Integrity Advisory Committee, Integrity Advisor and Integrity Framework

5.16 In 2000-01, the ATO established an Integrity Advisory Committee whose role was to advise the ATO Executive on how the ATO could remain, and be seen to remain, as an 'integrity based organisation'.⁵⁴⁰ In performing this role, the Committee had advised on issues such as:

...activities concerned with upholding and fostering APS values, promoting compliance with the Code of Conduct, preventing fraud, managing ethical challenges associated with relationships, and emerging issues relevant to sustaining an integrity based organisation...⁵⁴¹

5.17 The Committee's membership was comprised of senior officers from the APSC, Commonwealth Ombudsman and the AFP as well as the ATO's Integrity Advisor whose role was to act as:

...an independent adviser to the Commissioner.... The advisor provides high level support on integrity issues (such as the integrity of processes and systems), assists in promoting corporate values and appropriate standards of behaviour, coordinates processes to ensure that integrity

⁵³⁴ Above n 101.

⁵³⁵ ATO, 'Corporate Integrity Indicator Enhancements' (Internal ATO document submitted to the Audit and Risk Sub-Committee on 13 October 2015).

⁵³⁶ Above n 95, p 11.

⁵³⁷ ATO, 'Executive report, Quarter 3, 2015-16 - ATO Integrity Status Report' (Internal ATO document, 2016).

⁵³⁸ ATO, 'Executive report, Quarter 1, 2016-17 - ATO Integrity Status Report' (Internal ATO document, 2017).

⁵³⁹ ATO, 'Executive report, Quarter 3, 2016-17' (Internal ATO document, May 2017).

⁵⁴⁰ ATO 'Integrity Framework - how we ensure we are an integrity-based organisation' (Internal ATO document, January 2006) p 9; Commissioner of Taxation, *Annual Report 2000-01* (2001).

⁵⁴¹ ATO 'Integrity Framework - how we ensure we are an integrity-based organisation' (Internal ATO document, January 2006) p 9.

risks and issues are identified and/or resolved, and helps monitor the organisation's level of integrity.⁵⁴²

5.18 The ATO's inaugural Integrity Adviser was appointed in 2001. Since 2001, the ATO had engaged the following three Integrity Advisers:

- Dr Peter Kennedy (2001–2006);
- Professor Robyn Creyke (2006–2010); and
- Damien Bugg AM QC (2010–2015).⁵⁴³

5.19 The Integrity Advisory Committee was decommissioned in September 2008 and replaced with a future focused-strategy committee to oversee the development of the ATO's workplace 'People' strategy, namely the 'People Committee'.⁵⁴⁴ The ATO also formalised its integrity framework which identified issues to be addressed in the ATO's plans, specific measures to indicate whether the ATO was appropriately focused on integrity issues and associated governance arrangements to ensure conformance with the framework.⁵⁴⁵

5.20 In 2015, the ATO conducted an internal review into its integrity framework, (2015 Integrity Framework Review), including the role of the Integrity Adviser, the Integrity Advisory Committee and the other oversight arrangements, 'to determine an appropriate set of integrity arrangements for the ATO in the context of the ATO reinvention'.⁵⁴⁶

5.21 The 2015 Integrity Framework Review found that the Integrity Adviser had provided benefits such as provision of independent advice and perspective on specialist legal, integrity and reputation matters as well as an internal escalation point for internal integrity matters. However, due to the 'nature and pace' of the work environment, the view was formed that it was not feasible for one Integrity Adviser to provide the breadth and range of advice required and hence the role should be discontinued. It was considered that the ATO needed 'more flexible integrity arrangements' and a recommendation was made to establish an 'Integrity Panel', with members from differing backgrounds to provide integrity advice on an 'as-needed basis', and to be supported by 'regular monitoring and integrity reporting'.⁵⁴⁷

5.22 It was intended that the membership of the Integrity Panel would comprise of 'appropriately eminent and qualified people' such as 'ex-High Court judges, IT system experts and other specialists across a broader range of disciplines' to provide advice on the integrity of the taxation and superannuation systems, including IT and governance

⁵⁴² *ibid.*, p 7.

⁵⁴³ ATO, 'ATO Extra - The importance of openness and transparency' (Internal ATO document, 2006); Commissioner of Taxation communication to the Joint Committee of Public Accounts and Audit, 17 April 2007; Commissioner of Taxation, *Annual Report 2010–11* (2011) p 20.

⁵⁴⁴ ATO communication to the IGT, 8 December 2017; ATO, 'Integrity Adviser Report' (Internal ATO document, 1 September 2008).

⁵⁴⁵ Commissioner of Taxation, *Annual Report 2002–03*, pp 134 and 193–194.

⁵⁴⁶ Above n 95.

⁵⁴⁷ *ibid.*, pp 3, 5 and 8.

systems, taxpayer matters, cultural matters, emerging integrity issues including fraud and corruption, ethics and reputation.⁵⁴⁸

5.23 The 2015 Integrity Framework Review also recommended that the Integrity Framework be updated to provide clear advice on integrity arrangements and obtaining access and advice from the Integrity Panel. It was expected that requests for advice from the Integrity Panel would require sponsorship by the First Assistant Commissioner of ATOC and to be endorsed by the Chair of the ARC, a Second Commissioner. Administrative support for the Integrity Panel would be provided by the External Relations and Conformance Branch in ATOC.⁵⁴⁹

5.24 It was also proposed that the independent internal escalation channel to resolve internal integrity matters, that had been performed by the Integrity Adviser, be performed by a Deputy Commissioner for serious internal matters and that the Deputy Chair of the ARC be informed. It was considered that the new internal escalation channel would 'not need to be used very often' as the 'provision of this mechanism alone can be enough to ensure the right setting'.⁵⁵⁰

5.25 Later in 2015, the ATO engaged the services of RSM Bird Cameron to undertake Quality Assurance Reviews of the IA and FPII functions.⁵⁵¹ The RSM report found that:

FPII currently has a direct reporting line to the Deputy Commissioner ATO Corporate and a matrix of 'dotted line' reporting line to the Chair of the ATO Audit and Risk Committee. However, even though the Deputy Commissioner has FPII as a direct report, there is little direct oversight on FPII's operations with deferral to reporting to the Chair of the ATO Audit and Risk Committee who may not be aware that direct day-to-day oversight of FPII is being deferred to the Chair. For example, the Deputy Commissioner ATO Corporate stated that it is currently unclear who is accountable for the performance of the FPII, the reporting lines are undefined and appear to be decided on an ad hoc basis, and that this ambiguity creates a risk in the oversight of FPII and their functions where the risk of something improper within FPII may be overlooked...⁵⁵²

5.26 Accordingly it was recommended that:

...this dual reporting [to the Deputy Commissioner of ATO Corporate and the Chair of the ATO Audit and Risk Committee] continue but that there is a more transparent and formalised reporting of all strategic and operational matters to FPII's direct superior of the Deputy Commissioner ATO Corporate, as well as matrix or 'dotted line' reporting to the Chair of the ATO Audit and Risk Committee. On some highly confidential matters there may be a need to report only to the ATO Audit and Risk Committee but the majority of the strategic and

⁵⁴⁸ *ibid.*, pp 3 and 10.

⁵⁴⁹ *ibid.*, p 10.

⁵⁵⁰ *ibid.*, p 11.

⁵⁵¹ ATO, 'Minutes to the 30 July 2015 Audit and Risk Sub-Committee' (Internal ATO document, 30 July 2015) para [5].

⁵⁵² Above n 94, p 35.

operational reporting, management and supervision can be achieved, and is appropriate through, the Deputy Commissioner ATO Corporate...⁵⁵³

5.27 In response to the above recommendation, the ATO agreed to clearly set out responsibilities of the Deputy Commissioner of ATOC with respect to its oversight of FPII's strategic and operational matters and for FPII to provide regular reports to him or her.⁵⁵⁴

5.28 At the commencement of this IGT review, the ATO had no plans for any changes to its integrity framework including whether an Integrity Adviser would be reinstated or a new Integrity Panel would be established.⁵⁵⁵ However in December 2017, the ATO announced that it would appoint Dr Simon Longstaff AO as its new Integrity Adviser for a term of one year to:

...provide education, support and advise to leaders and staff across the ATO, and help to reinforce a culture that personifies and values integrity. Different to how the role roles has been done in the past (with a focus primarily on conformance and governance), Simon will focus on how we can embed integrity awareness in a practical way into the day-to-day decisions and operations of the ATO.⁵⁵⁶

Senior officers appointed from the private sector

5.29 The ATO has advised that since 2014, of the 85 new SES officers appointed, 35 have been external hires – 15 have directly come from the private sector, another 15 have public service backgrounds whilst the remainder were not employed at the time of recruitment.⁵⁵⁷

5.30 The ATO has also advised that, on commencement, the new SES officers attended a series of introductory meetings, over the course of a few weeks, with key senior ATO staff from relevant business lines to help them understand the different areas of the ATO.⁵⁵⁸ They also receive an induction pack which contains links to employment conditions, mandatory training programs, such as Security, Privacy and Fraud as well as the ATO's leadership and culture strategy to support the ATO's 'reinvention'. The SES officers are also enrolled in the APSC's SES Orientation Program for assisting new recruits 'understand Australian Government processes, standards and principles'.⁵⁵⁹

IGT observations

5.31 In earlier chapters, the Commonwealth Fraud Control Framework component of the ATO governance arrangement has been explored and scrutinised in detail. Its

⁵⁵³ *ibid.*

⁵⁵⁴ *ibid.*

⁵⁵⁵ ATO communication to the IGT, 29 September 2017.

⁵⁵⁶ ATO communication to the IGT, 11 December 2017.

⁵⁵⁷ ATO communication to the IGT, 13 November 2017.

⁵⁵⁸ *ibid.*; ATO, 'Example of on boarding program for external SES' (Internal ATO document, undated).

⁵⁵⁹ ATO, 'SES Induction' (Internal ATO document, undated); APSC, 'SES Orientation' (2 March 2018) <www.apsc.gov.au>.

broader governance arrangements have been described earlier in this chapter and appear appropriate, however, there is room for improvement.

5.32 First, there is scope to increase the independence of the ARC. Private sector entities as well as government bodies overseas have a requirement for the committee membership to be independent of the organisation.⁵⁶⁰ It is also generally accepted that whilst the CEO and CFO of the organisation and other experts are not members of the committee, it is helpful for them to attend the meetings from time to time.⁵⁶¹ Ensuring that no staff, including the CEO and CFO, are members of the ARC avoids any conflict of interest that may arise from the latter's oversight role and the functions performed by the staff by virtue of their employment.

5.33 It could be argued that the ATO is such a large and complex organisation that a truly independent chair may not have the requisite knowledge and understanding of the organisation.⁵⁶² However, such concern could be addressed by having specialist ATO officers attend ARC meetings and provide the relevant information, data and reports as required.

5.34 The IGT had previously outlined options for the ATO's governance arrangements, including the option to improve the independent operation of the ARC with members drawn exclusively from outside the ATO.⁵⁶³ The IGT remains of the view that the ATO's ARC should be comprised entirely of non-executive directors and draw on relevant ATO officers for information and advice.

5.35 Secondly, the IGT believes that the role of the Integrity Adviser should be maintained and its purpose and function better understood and promoted within the ATO. In doing so, consideration should be given to providing him or her with unfettered access to internal information and decision-making forums as well as appropriate support from the Commissioners and the ARC.

5.36 One of the key benefits that Integrity Advisers had previously provided was to assist in overcoming a culture of 'only good news going up the line'⁵⁶⁴ which increased the risk of ATO senior management not being made aware of integrity issues until it was too late to effectively address them.

5.37 The cumulative work of Integrity Advisers had also assisted the ATO in establishing an integrity framework which had identified the range of specific ATO legal obligations and publicly expected responsibilities as well as an assurance process which required operational staff to provide certificates of compliance with respect to identified risks. Through this process, operational staff were also required to take ownership in addressing the particular integrity risks which arose in their work area.

⁵⁶⁰ Governance Institute of Australia, *Good governance guide - issues to consider when constituting audit and risk committees* (2014).

⁵⁶¹ Australian Institute of Company Directors, *Role of the Audit Committee* (2016).

⁵⁶² ATO, 'Exit e-mail from the Integrity Adviser to the Commissioner of Taxation' (Internal ATO document, 3 July 2014).

⁵⁶³ IGT, Submission to the Treasury, *Tax Forum - next steps for Australia*, September 2011, p 15.

⁵⁶⁴ Above n 95, p 10.

5.38 Furthermore, it would be beneficial for ATO officers to have access to a source of advice and guidance on ethics and integrity, beyond their business line managers. In light of the recent events related to Operation Elbrus⁵⁶⁵, a function of the Integrity Adviser could also allow ATO officers to discuss fraud and corruption concerns if they do not feel comfortable with reporting the issue via other internal channels. The ATO is working towards this outcome. In February 2018, it had advised all SES officers that they could seek independent advice on workplace ethical issues from the current Integrity Adviser.⁵⁶⁶

5.39 Thirdly, the IGT believes that the Commissioners and the other ATO Executives would benefit from receiving periodic reports from the FPII Assistant Commissioner on internal fraud risks, trends and potential issues of concern. As previously mentioned, the FPII Assistant Commissioner is the responsible senior officer with the detail of all operational knowledge and is best placed to alert senior management to issues as soon as they arise. Such reporting also demonstrates the seriousness with which senior management consider such fraud risks.

5.40 Fourthly, the IGT is of the view that the ATO should formalise a regular review of its corporate integrity indicators in order to be responsive to emerging risks by ensuring that it continues to measure performance against the most appropriate indicators. The ATO has not conducted such reviews since 2015.

5.41 The above reviews may be informed by the findings of the OBA such that any relevant identified behaviours are addressed by a corresponding indicator or by other measures. The result of these reviews and actions arising from them should be made available to the Commissioners and the other ATO Executives.

5.42 Lastly, the IGT believes that induction for new SES officers, recruited from outside of the ATO, should be bolstered with specific training about APS standards as well as ATO policies, values and culture with a focus on the ethical standards and highest levels of integrity that an organisation such as the ATO must exemplify. Presentations from one or more of the Commissioners may be included to reinforce their expectations of senior officers in this regard. Such training may be supplemented by similar messaging in SES forums throughout each year.

RECOMMENDATION 5.1

The IGT recommends the ATO strengthen its oversight of internal fraud risks by:

- a) bolstering the independence of its Audit and Risk Committee by ensuring that, at the very least, the majority of its members, including the chair, are external to and independent of the ATO;*

⁵⁶⁵ See Appendix B para [A2.60]

⁵⁶⁶ ATO communication to the IGT, 20 February 2017.

RECOMMENDATION 5.1 (CONTINUED)

- b) maintaining the role of the Integrity Advisor and providing him or her with all necessary access and support as well as enabling ATO staff to discuss ethical or fraud related concerns with him or her;*
- c) requiring the Assistant Commissioner of Fraud Prevention and Internal Investigations to regularly report internal fraud risk trends and issues to the Commissioners and other ATO Executives;*
- d) conducting periodic reviews of the ATO's corporate integrity indicators and providing the results and actions arising from them to the Commissioners and other ATO Executives; and*
- e) augmenting the existing induction program for new SES officers, recruited from outside the ATO, with specific training on ethical standards and the highest level of integrity expected at such an organisation.*

ATO RESPONSE

(a) Implemented

(b) Agree

The ATO will periodically review the effectiveness of the role of Integrity Advisor as part of our ongoing integrity assurance activities.

(c) Agree

The ATO notes the Audit and Risk Committee already provides assurance to the Commissioner that the ATO has processes and systems in place to detect, capture and respond to fraud and corruption risk. The ATO will strengthen our current reporting processes for the Assistant Commissioner, Fraud Prevention and Internal Investigations to inform the ATO Executive of key fraud risk issues and insights.

(d) Agree

(e) Agree

EXPANSION OF THE PRIVATE GROUPS & HIGH WEALTH INDIVIDUALS BUSINESS LINE

Stakeholder concerns

5.43 Stakeholders have questioned the expansion of the PGH business line to include the SNC and Aggressive Tax Planning (ATP) business lines. In particular, stakeholders were concerned that having these three key areas report to a single Deputy Commissioner in PGH was 'too much to be led by one person,' noting that the expanded PGH business line has responsibilities such as the investigation and

prosecution of external fraud and tax crime, managing the ATO's participation in multi-agency taskforces as well as leading major programs such as the Project DO IT⁵⁶⁷ tax amnesty.

Relevant materials

5.44 The amalgamation of SNC, ATP and PGH into a single business line occurred on 1 July 2014 as part of the broader Compliance Group restructure. The intent of the amalgamation, which was designed in alignment with the Commissioner's Statement and the ATO's 2020 Vision, was to 'achieve efficiencies in areas where [the ATO's] collective work [was] duplicated or even triplicated'.⁵⁶⁸

5.45 Prior to the amalgamation, PGH⁵⁶⁹, SNC⁵⁷⁰ and ATP⁵⁷¹ were separate business lines led by different Deputy Commissioners. While the Deputy Commissioners of SNC and ATP maintained direct oversight over their respective areas after the amalgamation, they reported directly to the Deputy Commissioner of PGH, who became the head of the amalgamated business line.⁵⁷² By 2015, the amount of Deputy Commissioners within the amalgamated business line had reduced to two, as oversight for tax crime, which was previously under the purview of the Deputy Commissioner of SNC, was transferred to the Deputy Commissioner of PGH.⁵⁷³ The structure of the PGH business line as at July 2017 only contained one Deputy Commissioner. The areas of ATP and TEC (formerly SNC), as well as four other areas, are now headed by Assistant Commissioners who report directly to the Deputy Commissioner.⁵⁷⁴

5.46 In 2013-14, the financial year immediately prior to the amalgamation, the PGH, SNC and ATP business lines had average staffing levels equivalent to 1376, 528 and 223 full-time equivalent (FTE) employees respectively. The combined total for the three business lines was 2,127 FTE employees, of which 513 worked in a dedicated tax evasion and crime active compliance role. By comparison, in October 2017, the amalgamated PGH business line had the equivalent of 1,911 FTE employees, of which 541 worked in a dedicated tax evasion and crime active compliance role.⁵⁷⁵

5.47 A comparison of average staffing levels and deliverables for the 2013-14 and 2016-17 financial years is provided in the table below.

⁵⁶⁷ ATO, 'Project DO IT - the time to act is now' (Media Release, QC 42925, 23 October 2014).

⁵⁶⁸ ATO, 'PGH, ATP and SNC Amalgamation - High Level Implementation Plan' (Internal ATO document, undated).

⁵⁶⁹ ATO, 'PGH Organisational Chart Details' (Internal ATO document, 9 December 2013).

⁵⁷⁰ ATO, 'Serious Non-Compliance Organisational Chart' (Internal ATO document, January 2014).

⁵⁷¹ ATO, 'Aggressive Tax Planning Executive Organisational Chart' (Internal ATO document, August 2013).

⁵⁷² ATO, 'Private Groups and High Wealth Individuals' (Internal ATO document, June 2014).

⁵⁷³ ATO, 'PGH organisational structure' (Internal ATO document, 17 September 2015).

⁵⁷⁴ ATO, 'PGH organisational structure' (Internal ATO document, 19 July 2017).

⁵⁷⁵ ATO, 'PGH Senate Estimates Deputy Commissioner brief October 2017' (Internal ATO document, October 2017).

Table 5.1: Average PGH staff levels and deliverables, 2013–14 and 2016–17

	SNC/TEC active compliance staff numbers (in FTE)	ATP, SNC, PGH (incl. TEC active compliance) staff numbers (in FTE)	Audits and reviews completed	Investigations and prosecutions completed	Liabilities raised (\$billion)	Cash collected (\$billion)
2013–14	513	2,127	7,763	3,980	2.50	1.08
2016–17	506	1,827	6,440	3,863	3.04	1.46

Source: ATO ⁵⁷⁶

5.48 Decisions within the PGH business line are typically made collectively by groups of senior officers participating in panels and forums. There are separate panels to ‘determine case selection, allocation and progress, the resolution of complex technical issues, the issue of position papers, fraud or evasion determination and settlements, and escalation of matters to’ the Serious Financial Crime Taskforce (SFCT). In light of this governance structure, the ATO considers ‘that no individual, no matter how senior, can unduly or unilaterally influence the selection or outcome of a case’.⁵⁷⁷

5.49 Currently, the Deputy Commissioner of PGH is on several, but not all, of the internal PGH forums.⁵⁷⁸ For example, the Deputy Commissioner of PGH acts as the chair for the PGH Strategic Management Committee, which is responsible for strategy development, setting priorities and allocating resources.⁵⁷⁹ However, he does not participate in other forums such as the Tax Crime Referral Panel⁵⁸⁰, the Case Escalation Forum⁵⁸¹ or the Tax Crime Forum⁵⁸², which are the forums that have the primary responsibility for selecting and approving the commencement of audits, reviews and investigations within the business line.⁵⁸³ He does, however, represent the PGH business line in internal ATO forums, as well as the ATO in external forums. An example of the former would be the ATO’s Tax Crime and Account Integrity Steering Committee⁵⁸⁴ while an example of the latter would be the SFCT CEO Steering Group.⁵⁸⁵

IGT observations

5.50 A direct comparison between the position of the Deputy Commissioner of PGH before the amalgamation and the position after the amalgamation leads to the observation that whilst he may have more responsibility, there is also a corresponding increase in his accountability. Effectively, the Deputy Commissioner is currently

⁵⁷⁶ *ibid.*

⁵⁷⁷ *ibid.*

⁵⁷⁸ ATO, ‘PGH Forums Events and Meetings Register’ (Internal ATO document, undated).

⁵⁷⁹ ATO, ‘PGH Strategic Management Committee Charter’ (Internal ATO document, 1 July 2015).

⁵⁸⁰ ATO, ‘PGH Tax Crime Referral Panel Charter’ (Internal ATO document, undated).

⁵⁸¹ ATO, ‘Case Escalation Forum’ (Internal ATO document, undated).

⁵⁸² ATO, ‘Charter Tax Crime Forum 2017’ (Internal ATO document, July 2017).

⁵⁸³ Above n 578.

⁵⁸⁴ ATO, ‘Committee Charter Tax Crime and Account Integrity Steering Committee’ (Internal ATO document, November 2015); Note that in December 2017, the Tax Crime and Account Integrity Steering Committee was renamed to the ‘Crime and Account Integrity Steering Committee (CAISC)’.

⁵⁸⁵ ATO, ‘PGH TEC Governance Forums’ (Internal ATO document, undated).

accountable for how the ATO responds to three risk areas, as opposed to one, as well as being accountable for more than 500 additional FTE employees.

5.51 An examination of the panels in which the Deputy Commissioner participates shows that he is not involved in the making of any case specific decisions. For example, as mentioned above, the Deputy Commissioner does not participate in either the Tax Crime Referral Panel or the Case Escalation Forum. In addition, he is not a member of the Tax Crime Forum, which is the panel responsible for assessing and approving all ATO referrals to law enforcement agencies and joint agency taskforces.

5.52 Even where the Deputy Commissioner represents the ATO in external panels with other agencies, it is not for the purpose of making case specific decisions. For example, within the SFCT, the Deputy Commissioner is a member of the CEO Steering Group and the Senior Officer Group, which are responsible for providing executive oversight and setting the strategic direction of the SFCT. By contrast, the Deputy Commissioner does not participate in either the SFCT Joint Management Committee or the SFCT Treatment Forum, which are responsible for the approval and implementation of treatment strategies respectively.

5.53 Accordingly, while the Deputy Commissioner of PGH can exercise strategic decision-making powers, the ability to exert influence on individual cases or operational matters, through his involvement in the above forums, is minimal. Furthermore, where the Deputy Commissioner makes strategic decisions, they would be made after consultation and discussion in the relevant forums with input from other business lines or other agencies.

5.54 The Deputy Commissioner of PGH, however, may be tasked to become directly involved in making decisions in highly sensitive cases. In such circumstances, implementation of recommendation 3.5 of this report would provide transparency and integrity safeguard regarding any such involvement.

5.55 On the basis of the above information, the amalgamation of the SNC, ATP and PGH business lines has not resulted in less accountability. However, the role of the Deputy Commissioner of the expanded PGH business line is a high risk role and the IGT is of the view that the most appropriate way to address stakeholder concerns and the level of risk is by limiting the period of time within which any one person can occupy this role. The broader issue of staff rotation and associated recommendation is set out in Chapter 3.

EXTERNAL OVERSIGHT

Stakeholder concerns

5.56 Some stakeholders are of the view that the ATO should be subject to oversight by a specialist anti-corruption scrutineer, such as ACLEI. Their reasons are that the ATO is effectively a law enforcement agency by virtue of some of its high risk functions including those of the TEC area within its PGH business line as well as its active participation in joint operations such as the SFCT.

Relevant materials

5.57 The responsibility for preventing, detecting and investigating corruption in the public sector rests with ACLEI and the Fraud and Anti-Corruption Centre (FAC Centre) which comprise multiple Commonwealth agencies led by the AFP.⁵⁸⁶ In performing its role, ACLEI has strong investigatory powers, including:

- telecommunications interception and data access;
- compulsory information gathering hearings and related directions that prevent disclosure of the nature and existence of those hearings; and
- integrity testing which authorises ACLEI to test whether an officer of 'target agencies'⁵⁸⁷ will engage in illegal or unethical conduct in response to a controlled situation.⁵⁸⁸

5.58 Agencies under ACLEI's jurisdiction include the ACIC, AFP, Department of Home Affairs (including the Australian Border Force), AUSTRAC and prescribed aspects of the Department of Agriculture and Water Resources.⁵⁸⁹ Any member of the community or government agency, such as the ATO, may voluntarily refer matters to ACLEI for investigation.

5.59 In 2014, the Parliamentary Joint Committee on the ACLEI (the ACLEI Committee) initiated an inquiry (the ACLEI Inquiry) into the possible expansion of ACLEI's jurisdiction to other agencies, including the ATO. During the ACLEI Inquiry, ACLEI noted that there is a strong case for the ATO's inclusion under its jurisdiction due to the ATO being 'both a user and contributor of law enforcement related information, and a primary partner in joint law enforcement activities, such as Project Wickenby' and would 'add significantly to the law enforcement anti-corruption system'.⁵⁹⁰ Furthermore, the then Australian Crime Commission (ACC)⁵⁹¹ observed that the ATO 'contains high risk areas that would be susceptible to corruption'.⁵⁹²

5.60 The ATO, in its evidence to the ACLEI Committee, stated that whilst its FPII unit:

...has no statutory powers, it has the capability to conduct most facets of a criminal investigation, including the submission of briefs of evidence to the Commonwealth Director of Public Prosecutions. Several of these investigations have resulted in successful prosecutions and lengthy terms of imprisonment for those employees found to have acted corruptly.⁵⁹³

5.61 As an alternative to expanding ACLEI's jurisdiction to include the ATO, the ATO proposed a 'tier 2 arrangement' in which the ATO could 'call on ACLEI in certain

⁵⁸⁶ ACLEI, 'ACLEI's role' <www.aclei.gov.au>; AFP, 'Fraud and Anti-Corruption' <www.afp.gov.au>.

⁵⁸⁷ 'Target agencies' include the ACIC, AFP and the Department of Home Affairs: *Crimes Act 1914* s 15JC.

⁵⁸⁸ Explanatory Memorandum, House of Representatives, Law Enforcement Integrity Legislation Amendment Bill 2012.

⁵⁸⁹ *Law Enforcement Integrity Commissioner Act 2006* s 10.

⁵⁹⁰ Above n 17, paras [4.19] and [4.21].

⁵⁹¹ The then Australian Crime Commission merged with Crimtrac on 1 July 2016 to form the Australian Criminal Intelligence Commission.

⁵⁹² Above n 17, para [4.22].

⁵⁹³ *ibid.*, para [4.17] (Assistant Commissioner, ATO).

circumstances'. However, the ACLEI Committee noted that this model was not likely to be implemented in the near future⁵⁹⁴ and recommended that:

...the Government initiate an independent assessment of the Australian Taxation Office's corruption risk profile, together with an examination of the feasibility of including the Australian Taxation Office within ACLEI's jurisdiction.⁵⁹⁵

5.62 The ACLEI Committee was of the view that such an assessment should examine 'the likelihood of corrupt conduct within the ATO, its potential consequences for the organisation, the government and the economy, and the resourcing implications of inclusion'.⁵⁹⁶ The Government has not formally responded to the Committee's recommendation.

5.63 As noted earlier, following the events of Operation Elbrus, the ATO engaged an external contractor to conduct the 2017 Corruption Risk Review⁵⁹⁷ the main findings of which are discussed in Chapter 3.

5.64 It should also be noted that after the ACLEI Committee had made its recommendation, the Australian Government had become a member of the 'Open Government Partnership' which is a multilateral initiative which aims 'to secure concrete commitments from governments to promote transparency, empower citizens, fight corruption and harness new technologies to strengthen governance'.⁵⁹⁸ One of the commitments in this Partnership is for the co-creation of a National Action Plan every two years which outlines the steps it will take to improve and build confidence in Australian institutions.⁵⁹⁹

5.65 The first such Action Plan was issued by the Government in December 2016⁶⁰⁰ and had identified the integrity of the public sector as one of five important areas for improvement. Commitment 4.2 of this Action Plan aims to strengthen Australia's 'National Integrity Framework' through its ability to prevent, detect and respond to corruption in the public sector, including 'review [of] the jurisdiction and capabilities of ACLEI and [the FAC Centre] with the development of each National Action Plan to ensure they can focus on protecting Commonwealth agencies from risks of corruption'.⁶⁰¹ A review was scheduled to take place in the first half of 2018.⁶⁰²

⁵⁹⁴ *ibid.*, paras [4.23]-[4.24].

⁵⁹⁵ *ibid.*, para [4.28] rec 2.

⁵⁹⁶ *ibid.*, para [4.26].

⁵⁹⁷ ATO, 'Commonwealth Contract - consultancy services' (Internal ATO document, undated); Above n 10.

⁵⁹⁸ Australian Government, *Australia's First Open Government National Action Plan 2016-18* (2016) p 5; Note: the Australian Government joined the Open Government Partnership in November 2015.

⁵⁹⁹ *ibid.*, p 6.

⁶⁰⁰ Department of Prime Minister and Cabinet, 'Development of Australia's second Open Government National Action Plan' (8 February 2018) <www.pmc.gov.au>.

⁶⁰¹ Above n 598, pp 44 and 49.

⁶⁰² Department of Prime Minister and Cabinet, 'Open Government Partnership Australia' <<https://ogpau.pmc.gov.au>>.

IGT observations

5.66 As mentioned earlier, the ATO appears to have appropriate governance arrangements in place for managing risks of internal fraud and corruption although some improvements have been recommended. However, as indicated by the ACLEI Committee, the IGT is of the view that such governance arrangements and internal controls are not a substitute for a level of external scrutiny performed by an agency such as ACLEI.

5.67 The Government is currently considering its response to the recommendation of the ACLEI Committee and has other related processes in progress which would examine the broader issue of the extent of external scrutiny required.

CHAPTER 6 – THE ATO’S APPROACH TO EXTERNAL FRAUD

6.1 The first part of this report considers how the ATO prevents, detects and responds to internal fraud and other integrity-related issues. This chapter turns to how the ATO manages the risk of external fraud, that is, taxpayers and other external parties seeking to exploit the tax and superannuation system to commit fraud against the Commonwealth.

6.2 External fraud arises where taxpayers or their representatives dishonestly obtain a benefit from the ATO or cause a loss by deception.⁶⁰³ It is a broad term that may include small scale actions, the accumulation of which could result in a significant loss of revenue. However, the egregiousness of the actions is a major factor in how the ATO decides to treat the fraud. For example, knowingly claiming a \$5 gift donation as a deduction on an income tax return without having made the donation is a fraudulent act, but may be addressed through the ATO’s power to amend assessments and apply administrative penalties. However, the design of a complex phoenix arrangement with the intention of defrauding the Commonwealth and others of tens of millions of dollars or more without detection may require the application of criminal sanctions, such as prison sentences, as a form of punishment and deterrent to others.

6.3 The IGT has previously examined the ATO’s compliance approaches in applying administrative penalties.⁶⁰⁴ In this review, therefore, the focus is to examine the ATO’s approach to external fraud which involves criminal sanctions, namely ‘tax crimes’ or, where it involves other parties being defrauded, ‘financial crimes’.

6.4 The ATO has a specific framework, the ATO’s Tax Crime Framework, which outlines how its work in dealing with tax crime and external fraud fits within the Commonwealth Fraud Control Framework and the Commonwealth Risk Management Policy.⁶⁰⁵ The responsibility of addressing tax and financial crime lies with the PGH business line and the approach is captured in its ‘Tax Crime Strategic Intent 2015–18’.⁶⁰⁶ Within PGH there are different areas such as the Serious Financial Crime, Offshore Tax Evasion, Phoenix, and Refund Fraud units.⁶⁰⁷

PREVENTION

Stakeholder concerns

6.5 In submissions to this review and during interviews, stakeholders have suggested that success in addressing external fraud should be measured on whether

⁶⁰³ *Criminal Code Act 1995* s 134.2.

⁶⁰⁴ IGT, *Review into the ATO’s administration of penalties* (2014).

⁶⁰⁵ ATO, ‘Tax Crime Framework’ (Internal ATO document, 28 March 2018).

⁶⁰⁶ ATO, ‘Tax Crime Strategic Intent 2015–18’ (Internal ATO document, undated).

⁶⁰⁷ ATO, ‘PGH Enterprise Tax Crime Communication View’ (Internal ATO document, 16 November 2017).

the behaviour has been stopped rather than by the number of prosecutions and convictions. Accordingly, stakeholders are of the view that the ATO's main focus should be on preventing the fraudulent behaviour, with prosecution being considered as only one of a range of treatment options.

6.6 In addition, a number of former ATO officers have suggested that the ATO could do more to encourage its officers to identify weaknesses in the tax systems which are being exploited or could potentially be exploited. Where ATO officers proactively identify such weaknesses, the ATO should act promptly to address them.

6.7 Stakeholders have also raised concerns that the ATO has not made the most of publishing its successful investigations and prosecution action to deter others from engaging in such activities by demonstrating the severity of consequences. They note that there has been a significant reduction in ATO publications regarding fraud and tax crime. The ATO's former publications, such as the *Annual Compliance Program* and *Targeting Tax Crime*, were important tools that had assisted tax advisers to encourage their clients to adopt compliant behaviour. These former publications heightened public awareness about the ATO's approaches, which contributed to community perceptions that the ATO considered tax fraud as a priority and made visible the ATO's position on tax crime and fraud.

Relevant materials

ATO strategy to prevent tax crime

6.8 As described in Chapter 2, the Tax Crime Risk is part of the ATO's enterprise risk of Major Tax Integrity Threats. The Tax Crime Risk encompasses the risks associated with GST evasion, phoenix activities and refund fraud (the 'tax crime risk areas').⁶⁰⁸

6.9 The ATO's approach to addressing tax crime and external fraud is outlined in its 'Tax Crime Strategic Intent 2015-18' which states that 'tax crime prevention is an integral part of ATO business'.⁶⁰⁹

6.10 The ATO aims to reduce the risk of tax crime by making the 'tax and super systems secure and unattractive targets for crime'. It further states:

This means that we must focus our efforts on:

- systemic solutions that remove the opportunity for people to commit crime and avoid detection
- 'whole-of-crime' treatment approaches that provide long-term changes in participation by removing the opportunity to repeat an offence

⁶⁰⁸ ATO, 'Risk Register, Major tax integrity threats - tax crime' (Internal ATO document, ATO database, accessed January 2018).

⁶⁰⁹ Above n 606, p 3.

- taking firm action against people who are not doing the right thing and removing the profit from participating in tax crime.⁶¹⁰

6.11 The ATO's strategy outlines the five key principles that work together to achieve this aim. These principles are:

Secure systems and processes – Tax crime prevention measures are designed into the corporate, intermediary and trusted third party systems and processes we rely on.

Robust law and administration – Our legal and administrative framework has a focus on eliminating opportunities for tax crime.

Meaningful engagement – Innovative and contemporary engagement solutions are used, considering both content, channel and audience characteristics.

Intelligence-led detection – Our data and information sharing framework supports timely detection.

Sustainable compliance – Compliance strategies focus on achieving sustainable improvement in voluntary compliance.⁶¹¹

6.12 As part of the first principle of 'secure systems and processes', the ATO aims to incorporate 'effective authorisation controls' that 'work to prevent identity crime', 'tax crime minimisation concepts into system and process design,' and 'effective system security and controls as part of system design'.⁶¹²

6.13 The second principle of 'robust law and administration' refers to the prioritisation of reforms which 'remove key vulnerabilities' and the consideration of 'alternate reporting systems to reduce fraud' as well as 'effective sanctions that work to deter future participation'.⁶¹³

6.14 The principle of 'meaningful engagement' is where the ATO has a number of aims for its communication/engagement strategy, including 'consistent tax messages tailored' to its audiences, a 'simple channel for engagements/referrals', 'coherent and coordinated internal and external tax communications' as well as engaging 'key intermediaries' to 'harness their active involvement in tax crime approaches'.⁶¹⁴

6.15 The fourth principle of 'intelligence-led detection', by maximising data sharing and matching opportunities between internal and external treatment partners, seeks to meet compliance needs and prioritise a 'real time domestic and international data sharing capability'.⁶¹⁵

6.16 The final principle of 'sustainable compliance' is where the ATO seeks to remove 'the profit from tax crime activity' through 'effective recovery of tax liabilities and fraudulent profits', 'applying meaningful and targeted sanctions and

⁶¹⁰ *ibid.*, p 2.

⁶¹¹ *ibid.*, p 3.

⁶¹² *ibid.*, p 4.

⁶¹³ *ibid.*

⁶¹⁴ *ibid.*

⁶¹⁵ *ibid.*, p 5.

consequences for participation in tax crime’ and using a ‘whole-of-crime’ approach to ‘influence the environment so that the offence is harder to commit in the future’.⁶¹⁶

6.17 In addition to the ATO’s strategic intent, the ATO conducts Enterprise Tax Crime Risk Reviews that seek to evaluate the effectiveness of its risk controls and treatments and examine changes in the tax crime environment which may impact the risk ratings. The reports of these reviews contain some important information. For example, in the latest review, conducted in 2016, reference is made to the ‘Phoenix Risk Model’ which ‘provides a demographic and risk-based profile of the overall potential and confirmed phoenix population’ as well as characteristics of industries and business structures which may increase the risk of phoenix behaviour.⁶¹⁷

6.18 The Enterprise Tax Crime Risk Reviews also outline environmental factors that influence and facilitate ‘tax crime behaviours’ such as the participation of ‘opportunistic individuals,’ ‘sophisticated individuals,’ organised crime and professional facilitators, intermediaries and advisers who may ‘wittingly or unwittingly be used to facilitate financial crime’.⁶¹⁸

6.19 The five principles in the Tax Crime Strategic Intent mentioned above are referred to as ‘risk controls’ in the Enterprise Tax Crime Risk Reviews. In particular, the reviews outline aspects of the ATO’s work in contributing to the principles. For example, in discussing the principle of ‘robust law and administration’, the ATO states that ‘law reform activities undertaken by the ATO are focused on the introduction of legislation that better reflect modern business and enhances information sharing. This approach provides a platform for the ATO to be proactive and note any emerging risk areas, as well as innovative reforms occurring around the world’. The legislative reforms which the latest review notes as ‘being pursued by the ATO’ include reforms to ‘address fraudulent phoenix activity such as expanding the director penalty regime to cover GST and extending the promoter penalty regime’.⁶¹⁹

6.20 The PGH business line develops a ‘treatment strategy’ for each of the tax crime risk areas. This strategy provides a high level view of the key focus for that year, communication activities that will be undertaken, the effectiveness measures for the strategies as well as options for law simplification and reducing compliance cost. For example, the Phoenix risk and treatment strategy, states that PGH will ‘continue to lead the building of the Phoenix Taskforce brand, its key messages and initiatives, including systemic law reform’ and that under ‘law simplification and reducing compliance cost,’ it will be ‘integrally involved in all aspects of the implementation of Transparency of Tax Debt’ and contribute to a Phoenix Taskforce/whole-of-government law reform submission.⁶²⁰

⁶¹⁶ *ibid.*, p 4.

⁶¹⁷ ATO, ‘Tax Crime Risk Review’ (Internal ATO document, 14 May 2016) p 11.

⁶¹⁸ *ibid.*, pp 13–20.

⁶¹⁹ *ibid.*, pp 21, 23 and 31–32.

⁶²⁰ ATO, ‘Phoenix Risk and Treatment Strategy – planning 2017–18’ (Internal ATO document, 2 March 2017).

ATO officer insights

6.21 All ATO officers are, under CEI 2014/05/09, responsible for preventing, detecting and referring suspected tax crime committed by parties external to the ATO. The CEI outlines a number of responsibilities for officers, including referring suspected tax crime matters after consultation with their manager to the PGH business line and 'providing information into corporate processes designed to better understand Tax Crime behaviour, such as for reports and risk assessments'. In relation to the prevention of tax crime specifically, the CEI instructs officers to ensure that they consider tax crime prevention when developing or changing major tax or superannuation policy and to refer through their team and risk processes examples where the ATO's systems or processes 'enable tax crime' as 'fixing these locally can reduce tax crime opportunities'.⁶²¹

6.22 In addition to the above, the ATO also seeks to utilise the knowledge and insight of its officers by encouraging them to contribute ideas for innovations and improvement through a number of different channels. One such channel is the ATO 'Innovations SharePoint page', where ATO officers can submit their ideas, report concerns or issues regarding ATO systems, search for existing ideas and potentially collaborate with others to further develop existing ideas. When an ATO officer makes a suggestion on the ATO Innovations page, they will receive a confirmation with a reference number to allow them to track the progress of their submission. A member of the ATO Innovations Team will generally contact the ATO officer within 10 business days to discuss their idea and provide them with progress updates, or alternative channels to more effectively advance their suggestion, particularly where the idea relates to a specific ATO site or business unit.⁶²²

6.23 The PGH business line has also developed its own initiatives, under the oversight of the ATO Innovations team, to obtain staff insight and ideas to improve the way in which the business line undertakes its work of addressing fraud and tax crime. A key example of this is the 'Strategic Outcomes Initiative' which was commenced by the TEC area within PGH in October 2016. While suggestions raised by this initiative cover the entire spectrum of prevention, detection and response, the primary objective of the initiative is to gather ideas for 'shifting the behaviour of the 5%' who 'deliberately attack the tax and super systems or actively resist doing the right thing' by identifying gaps in 'law, policy, administrative and IT systems'.⁶²³ Accordingly, a large portion of the ideas raised were geared towards prevention, such as the suggestion for the ATO to publicise its 'successful and noteworthy prosecution outcomes' to 'demonstrate the ATO's approach to such matters' and 'assist with greater education in the community about obligations and possible repercussions for certain behaviours'.⁶²⁴

⁶²¹ Above n 89.

⁶²² ATO, 'External Fraud Detection Q 1-4' (Internal ATO document, 15 November 2017) p 1 paras [1] and [4].

⁶²³ ATO, 'TEC Strategic Outcomes Initiative' (Internal ATO document, undated).

⁶²⁴ ATO, 'TEC Staff Improvement Ideas Prioritised' (ATO database, accessed January 2018).

Communication as one of the strategies to prevent tax crime

6.24 Part of the ATO's strategy to prevent tax crime is through communication, which falls under the 'meaningful engagement' principle. The ATO has advised that its communication approach focuses on:

Prevention – making sure people know how to make the right choices;

Non-compliance – showing community we are not afraid to take firm action on those who don't comply; [and]

Victim support – helping innocent victims get the support they need.⁶²⁵

6.25 The ATO also has an Enterprise Tax Crime Communication View which outlines the process by which the PGH business line collates the necessary information to 'give the community evidence that shows the ATO to be both aware and capable of dealing with these perpetrators [of tax crime].' It also sets out key events which provide communication opportunities, such as court proceedings, execution of warrants, Parliamentary Committees and speaking opportunities. Part of this communication process involves the collation of materials from each of the tax crime risk areas.⁶²⁶

6.26 Within each risk area, there are specific communication strategies. For example, in the 2016–17 Phoenix communications strategy, it outlines the key outcomes of the strategy which includes highlighting the whole-of-government work of the Phoenix Taskforce and educating and informing the community on how to identify and report suspected phoenix activity as well as the range of target audiences and the different mediums through which the messages will be communicated, such as Facebook advertising, videos⁶²⁷ and newsletter articles.⁶²⁸

6.27 The ATO conducts evaluations of its communication strategies. At the conclusion of 30 June 2017, the ATO conducted an evaluation of its communication strategy for phoenix activities. As part of the evaluation, the access rate to the different channels were measured such as the number of times the ATO videos on 'Protect yourself from illegal phoenix activity' was viewed, the number of times the ATO's Phoenix and the Phoenix Taskforce webpages were viewed as well as the level of digital amplification via tweets and retweets. The ATO considered that there may have been a correlation between peak periods of communication activity and referrals made by community members about alleged tax evasion and fraud (tax evasion referrals, or 'TERs') to the Tax Evasion Referral Centre (TERC) hotline and that their peak advertising period commenced in April and ran until early June. The latter can be matched with the increasing TERs of 30 in April, 44 in May and 80 in June. The calls in late June may be the result of significant media coverage surrounding Operation

⁶²⁵ ATO, 'IGOT Information Pack - General Communications', embedded document entitled 'Tax Crime Overview for IGT Current Version' (Internal ATO document, November 2017).

⁶²⁶ Above n 607.

⁶²⁷ See, for example, ATO, 'The fight against tax crime' (21 May 2015) <www.ato.gov.au>.

⁶²⁸ ATO, 'IGOT Information Pack - General Communications', embedded document entitled 'A3 Communication Strategy Overview' (Internal ATO document, November 2017).

Elbrus.⁶²⁹ However, the evaluation did not provide details on the topics raised by the calls made to the TERC hotline and whether they related to phoenix activities or similar activities. The use of the TERC will be discussed later in this chapter.

6.28 The ATO also publishes information on risks that it believes warrant attention as part of its tax crime communication strategy. Historically, the ATO's areas of compliance focus were published in the *Annual Compliance Program* which was superseded by *Compliance in Focus*. The latter outlined the ATO's focus for the different taxpayer groups, their risk areas as well as case studies and links to relevant taxpayer alerts about certain arrangements. It also contains a snapshot of preliminary results from the previous year (prior to being published in the Annual Report).⁶³⁰

6.29 In particular, in the first *Compliance in Focus* publication, the ATO stated that its four areas of focus in 2013–14 were data and information matching capability, tax crime, misuse of trusts and profit shifting. In addition, the ATO stated that it:

...will update the online version of the publication throughout the year to report on its progress and identify any emerging risks, including explaining what we are doing about them.⁶³¹

6.30 In March 2015, it was announced that a new publication, 'Building Confidence' would replace *Compliance in Focus*. It stated that:

In short, Building Confidence defines the outcomes we are trying to achieve - confidence in the ATO and the tax and super systems.

This online publication is about being transparent in our approach to fostering willing participation and dealing with non-compliance. It outlines how we are designing for the majority of the people who are trying to do the right thing while taking a determined and firmer stand with those who are not. It explains how we are achieving fairness - striking the balance between encouragement and enforcement based on risk, transparency and behaviour.⁶³²

6.31 The Building Confidence webpage outlines the ATO's expectation of the different groups of taxpayers as well as the areas that attract the ATO's attention. These areas can range from individuals who claim deductions for which they are not entitled to small businesses that do not meet their responsibilities as an employer. The webpage also contains results from the prior year's compliance activities as well as case studies ranging from research and development incentives to phoenix activities.⁶³³

6.32 The ATO also publishes its areas of focus in relation to tax crime on its 'The fight against tax crime' webpage, which states that the ATO focuses 'on key areas that present a high risk to the community and revenue, including international, trust and phoenix tax evasion and fraudulent behaviour, refund fraud, identity crime and

⁶²⁹ ATO, 'IGOT Information Pack - General Communications', embedded document entitled '2016–17 Phoenix Communications Evaluation' (Internal ATO document, November 2017).

⁶³⁰ ATO, *Compliance in Focus 2013–14* (2014) pp 2 and 26 <www.ato.gov.au>.

⁶³¹ *ibid.*, p 2.

⁶³² ATO, 'Reinventing the ATO - Commissioner's speech to the Tax Institute's 30th National Convention' (19 March 2015) <www.ato.gov.au>.

⁶³³ ATO, 'Building Confidence - case studies' (6 September 2017) <www.ato.gov.au>.

organised crime'.⁶³⁴ The webpage contains further links to some of these risks and how the ATO broadly manages these risks.⁶³⁵

6.33 The above publications and the periods of their operation are summarised in the table below.

Table 6.1: ATO publications on its compliance focus

ATO public communications	Years in operation
Compliance Program (paper)	2002–03 to 2012–13
Compliance in Focus (paper and online)	July 2013 – March 2015
Building Confidence (online)	March 2015 to present

Source: ATO⁶³⁶

6.34 Furthermore, the ATO publishes the outcomes of its activities and provides transparency on the actions it takes against those who deliberately avoid their tax. For example, 'The fight against tax crime' webpage contains results of 'serious tax crime joint investigations' which include the outcomes of joint investigations from July to December 2017. It also has a table which provides a summary of the offence, the result (prison sentence, arrest or fine imposed) and the names of those convicted.⁶³⁷ An extract of the table is below.

Table 6.2: Serious tax crime joint investigations, from July to December 2017

Result of investigations	Details	State
27 months jail – non-parole period 15 months	Anthony ROCK from Newcastle NSW lodged four income tax returns via his tax agent. The agent queried the excessive amounts of PAYGW. Refunds totalling \$555,924.80 for the four years were stopped prior to payment.	New South Wales
Arrest	A 56-year-old man from northern NSW was arrested when he surrendered himself to police. He was charged with attempted tax fraud to the value of \$10,229,360, but had failed to attend court resulting in the issue of a bench warrant.	New South Wales
3 years jail – no parole	Phillip LEACH was found guilty on 12 charges of lodging BAS across three entities claiming GST credits that were found to be false. He was sentenced to three years imprisonment without parole. A reparation order of \$134,011.99 has been made by the courts.	Queensland

Source: ATO

6.35 In addition to the outcomes of joint investigations, the ATO also publishes results of prosecutions for tax crime from the 2011–12 to 2016–17 financial years on its webpage as well as results from Project Wickenby which concluded on 30 June 2015.⁶³⁸

⁶³⁴ ATO, 'The fight against tax crime - Our focus' (25 July 2017) <www.ato.gov.au>.

⁶³⁵ ATO, 'The fight against tax crime - Our focus - Illegal phoenix activity' (16 March 2018) <www.ato.gov.au>.

⁶³⁶ Above n 632; Above n 630; ANAO, *The Australian Taxation Office's Management of Aggressive Tax Planning* (29 January 2004) p 53 <www.anao.gov.au>.

⁶³⁷ Above n 627.

⁶³⁸ ATO, 'The fight against tax crime - News and results - Tax crime prosecution results' (13 November 2017) www.ato.gov.au; ATO, 'The fight against tax crime - News and results - Project Wickenby has delivered' (16 November 2017) <www.ato.gov.au>.

It also publishes results of some of its actions in addressing tax crime in media releases⁶³⁹ and its Annual Reports.⁶⁴⁰

6.36 As public communications may be delivered to the taxpayer via an intermediary, these intermediaries also play an important role in the ATO's communication strategy. This was recognised by the ATO in its Phoenix Strategic Communication overview, where it stated that intermediaries, such as 'tax agents, accountants, financial planner/advisors, legal practitioners and advisors to high wealth individuals' are secondary audiences to its messaging as well as key influencers in the communication strategy. For example, with respect to Phoenix activities, one of the strategies was 'increased engagement with key industries and intermediaries with a focus on educating them about the warning signs of illegal phoenix activity'.⁶⁴¹

IGT observations

6.37 Perpetrators of fraud seek to conceal their unethical conduct from the authorities, for example by not registering or reporting tax obligations or otherwise giving the impression that their activities are legitimate, or a combination of both. For example, perpetrators may use nominee trustees in tax secrecy havens to hide beneficial ownership of trusts or false identities for accounts held with financial institutions.

6.38 Perpetrators of fraud actively seek weaknesses, which are little known or are not being addressed, the exploitation of which may be highly profitable. As fraud may be difficult to detect and often requires a significant amount of resources to investigate and address, effective preventative measures are paramount. Minimising weaknesses in the tax system or administrative arrangements is one such measure.

6.39 As mentioned earlier, the ATO currently has a number of measures to address potential weaknesses in the system. However, there have been occasions in the recent past where such weaknesses could have been addressed more promptly. For example, as illustrated in Appendix D of this report, in dealing with alleged fraud by some in the precious metal industry, the ATO should have addressed the weaknesses being exploited through earlier identification of the risks. Once the risk was identified, such weaknesses were ultimately addressed. However, a prompt whole of ATO approach was required to prevent the propagation of the alleged fraud at the same time as pursuing the perpetrators.

6.40 The IGT is of the view that the ATO should create an environment where its officers routinely consider whether risks encountered in their case work indicate a potential weakness in the system, ensure such weaknesses are promptly investigated and the necessary resources, from the requisite areas, are devoted to addressing them.

⁶³⁹ For example, ATO, 'Woman sentenced for \$960,000 tax fraud' (Media Release, QC 52103, 15 May 2017) <www.ato.gov.au>; ATO, 'Man arrested for fraud and identity crime' (Media Release, QC 53446, 5 October 2017) <www.ato.gov.au>.

⁶⁴⁰ For example, above n 7, pp 61–62.

⁶⁴¹ ATO, '2017–18 Phoenix Strategic Communications Overview' (Internal ATO document, undated).

6.41 ATO officers could be required to identify the typology of any potential fraud by reference to weaknesses in the system when actioning cases, estimate the potential impact of the weakness on the system and refer it to the relevant area for consideration and action. This requirement could be facilitated through an update of the existing CEI 2014/05/09 on Tax Crime and External Fraud by expanding the consideration of tax crime prevention to all case work and not only for changes to tax and superannuation policy and systems. The focus should be to identify potential weaknesses in the system rather than attempting to quantify the scope of the fraud before raising the weakness for consideration. This would allow the weakness in the system to be treated as a greater priority without needing to wait for the risk to manifest or propagate.

6.42 The proposed change to CEI 2014/05/09, may be underpinned by amending the ATO Corporate Plan to include targets for its prevention work as part of the existing performance targets. The ATO could also report on its performance against these targets in the Annual Performance Statement in its Annual Report. Such reporting would also reinforce with officers, as well as the community, the ATO's commitment to combatting external fraud. It would also shape the way business lines plan and undertake their operational activities.

6.43 Another way to reduce the opportunity for fraud is to recalibrate perceptions of the risk and reward associated with non-compliance or fraud. One option is communicating the risks to the community and the actions being taken to address those risks. In a general sense, the ATO has taken steps in this direction through its *Annual Compliance Program, Compliance in Focus* and more recently its Building Confidence online publication.

6.44 With respect to specific fraud risks, the ATO, for example, publishes information about the activities which it considers to be refund fraud and the actions it is taking both internally and with other agencies to detect it.⁶⁴² Such actions send a clear message that there is a greater risk of detection.⁶⁴³ It also reassures the community that the ATO is addressing fraudulent activities, builds their confidence in the system and improves voluntary compliance.⁶⁴⁴

6.45 The ATO has published the outcomes of the criminal investigations and prosecutions which may include, subject to confidentiality constraints, the perpetrators' names and actions. As discussed earlier, there are benefits to widely sharing such information as it can provide a more effective deterrent. However, the majority of serious tax crime joint investigations listed on the ATO webpage have not received the desired level of media coverage to adequately inform the public that the ATO does prosecute perpetrators of tax fraud.⁶⁴⁵ Accordingly, the ATO may need to employ a more effective media strategy.

⁶⁴² ATO, 'The fight against tax crime - Refund fraud' (25 July 2017) <www.ato.gov.au>.

⁶⁴³ Stuart Hamilton, 'New Dimensions in regulatory compliance - building the bridge to better compliance' (2012) 10(2) *E Journal of Tax research*, 483 p 506.

⁶⁴⁴ Above n 13, p 183.

⁶⁴⁵ See above n 13, p 178.

6.46 It would also be beneficial for the ATO to publicly report on its work with other agencies to disrupt broader criminal activities that have a tax element as it represents the broader scope of work that the ATO conducts in tackling fraud. For example, it may be possible in some situations for the ATO to work with other agencies to treat a tax crime risk through alternative means, which might not involve criminal prosecution. An example of the adoption of such alternative treatments has been provided in Appendix E in relation to illicit tobacco. Further discussion of the ATO's collaboration with other government agencies and its use of non-criminal treatments will occur in Chapter 7.

RECOMMENDATION 6.1

The IGT recommends that the ATO improve the prevention of external fraud by:

- a) requiring its officers to routinely consider whether risks encountered in their case work indicate a potential weakness in the system, ensure such risks are promptly prioritised and investigated as well as publicly reporting the outcomes where appropriate; and*
- b) improving its media strategy to increase the reporting of its tax crime investigations, prosecutions and recoveries of proceeds of crime.*

ATO RESPONSE

(a) Agree

As set out in the report, our existing *Tax Crime and External Fraud* Chief Executive Instruction (CEI) outlines the responsibility of staff to actively assist in preventing, detecting and reporting tax crime by referring suspected tax crime matters to the Private Groups & High Wealth Individuals (PGH) business line. We will consider how this policy might be enhanced to address the issue highlighted in this recommendation. The ATO already has initiatives in place to routinely keep ATO staff informed of the matters they identify and report. The ATO will seek to identify ways to publicise the outcomes where action is taken in these circumstances, which will include a consideration of the best channel through which this might occur.

(b) Agree

The ATO has a well-established integrated approach to communicating about tax crime matters, and specifically on the results of prosecutions and investigations. We continually review our communications approaches in order to ensure they remain current and contemporary.

DETECTION

6.47 Whilst perpetrators of small scale fraud may gamble on the ATO not selecting their claims for review, more sophisticated or larger scale fraud often relies on advice from professional advisers who have an in-depth knowledge and understanding of the ATO's thresholds and detection measures. Although these professionals may not knowingly facilitate tax crime, their specialist skills and expertise are often used by individuals and organised crime groups to gain unique industry insights, develop complex arrangements and establish strategies to conceal the proceeds of crime.

6.48 Perpetrators of fraud may further disguise the nature of their activities by using methods, such as dealing in cash, which are difficult to trace. While financial institutions are required to identify and report suspicious transactions or those which exceed a certain threshold to comply with anti-money laundering rules, smaller transactions which occur outside the banking system will often be invisible. These fundamental characteristics of cash currently make it a reliable and preferred means for criminals to facilitate illicit activities. There is also the potential for cash to be replaced by emerging cryptocurrencies particularly as they are currently unregulated.

6.49 Rapid advances in technology and the rise of digital transactions may also assist in the creation of complex arrangements, falsification of records and concealment of identities, resulting in an expansion of the tax crime landscape. There has been a corresponding increase in the volume of information which the ATO and its law enforcement partners must access to gain adequate visibility. For example, technological improvements now allow financial transactions to occur instantly⁶⁴⁶ which significantly speeds up the rate that the proceeds of tax fraud and crime can be moved offshore. Historically, the ATO would become aware of Australian taxpayers' involvement in transnational tax crimes through leaks of information, such as the Panama paper, or through leads in audits, such as the initial cases in Project Wickenby. In relation to the latter, it took many years before sufficient information was obtained to mount a prosecution.⁶⁴⁷

6.50 The ATO also faces difficulties in identifying the perpetrators of tax crime (the risk population)⁶⁴⁸ in a constantly changing environment that provides new opportunities to exploit weaknesses in the tax system and its administration.⁶⁴⁹ Accordingly, the ATO's fraud detection measures need to be agile, efficient and effective to ensure that the ATO is able to respond promptly and effectively. Such responses require regular evaluation to keep pace with the changing environment.⁶⁵⁰

6.51 The ATO receives information and intelligence from a variety of internal and external sources which contribute to the development of its fraud detection measures and strategies. The ATO's approach to fraud detection can be broken up into two main streams. The first stream is referrals, which can broadly be categorised as referrals from the broader community, referrals from its own staff and referrals from other government agencies. The second stream of the ATO's fraud detection mechanism is based on its intelligence, risk models and data analysis.⁶⁵¹

Referrals from the community

6.52 As discussed in Chapter 5, the Australian Government is committed to promoting transparency, empowering citizens and fighting corruption as part of its membership to the Open Government Partnership. The Government's National Action

⁶⁴⁶ Reserve Bank of Australia, 'New Payments Platform' <www.rba.gov.au>.

⁶⁴⁷ ANAO, *Administration of Project Wickenby* (2012) pp 65 and 152.

⁶⁴⁸ Above n 617, p 13 para [1].

⁶⁴⁹ ATO, 'Risk Assessment - Enterprise Tax Crime' (Internal ATO document, April 2014) p 36 para [7].

⁶⁵⁰ Above n 617, p 9 para [3].

⁶⁵¹ *ibid.*, p 41.

Plan has identified transparency and accountability in business as an important area for improvement, with the key objective being to ensure that there are appropriate protections in place for people who report fraud, corruption and misconduct within the corporate sector as well as tax evasion or avoidance.⁶⁵²

6.53 The Government aims to achieve this objective 'by improving whistleblower protections for people who disclose information about tax misconduct to the Australian Taxation Office' and through reforms to whistleblower protections in both the corporate and public sectors.⁶⁵³ This included an announcement in the 2016–17 Federal Budget by the Government to introduce whistleblower protections for those who disclose tax misconduct information to the ATO.⁶⁵⁴

6.54 The Black Economy Taskforce's Interim report also observed that:

various government agencies have whistleblower programs or reporting services in place where members of the public can report information on suspected fraud, tax evasion and other misconduct or breaches of relevant legislation. These have been effective to a degree, but should be better targeted, relaunched and rebranded to become more user friendly...If done well, this can play a role in changing wider social norms and behaviours.⁶⁵⁵

6.55 Members of the broader community can report alleged instances of tax fraud, or make TERs, to the ATO's TERC. It is expected that other coordinated Government initiatives, for example, the proposed Phoenix hotline⁶⁵⁶ and the proposed Black Economy hotline⁶⁵⁷ may impact the manner in which the ATO deals with TERs.

Stakeholder concerns

6.56 Stakeholders have expressed concern that the ATO does not demonstrate that it appropriately considers and investigates TERs made to its TERC by the community – a valuable resource for detecting fraudulent activity. The perceived lack of ATO action was said to discourage members of the community to make such reports.

6.57 The IGT has also received a number of complaints from taxpayers who were dissatisfied with the ATO's response to their TERs. They had sought independent assurance from the IGT that the ATO had appropriately considered their referral. In investigating many of these complaints, the IGT has been able to provide the required assurance that the ATO has considered the referral and had taken appropriate action. However, in a number of other cases, such assurance could not be provided. In one case, the ATO had internally allocated the TER to a team which had been disbanded due to an internal restructure and the referral had not been reallocated. In addition, the ATO had difficulty in confirming the processes for referrals which were sent to particular business lines. Accordingly, the IGT commenced an own initiative

⁶⁵² Above n 598, p 12.

⁶⁵³ *ibid.*

⁶⁵⁴ Treasury Laws Amendment (Enhancing Whistleblower Protections) Bill 2017.

⁶⁵⁵ The Treasury, *The Black Economy Taskforce – Interim Report* (March 2017) p 51 para [24] <www.treasury.gov.au>.

⁶⁵⁶ The Treasury, *Combatting Illegal Phoenixing (Consultation Paper)* (28 September 2017) p 7 <www.treasury.gov.au>.

⁶⁵⁷ Above n 13, p 339.

investigation⁶⁵⁸ to map the ATO's TERC process and to identify opportunities for improvement. The findings of this own initiative investigation have been incorporated into this review and discussed below.

Relevant materials

6.58 Taxpayers and members of the broader community can report alleged instances of tax evasion and external fraud to the ATO by lodging a TER with the TERC by telephone, by facsimile, through the tax evasion reporting form available on the ATO website and in writing by post.⁶⁵⁹ Such information may also be lodged through a variety of other channels such as by reporting⁶⁶⁰:

- potential scams via a hotline or to an e-mail inbox;
- potential identity theft or data breaches to the ATO's Client Identity Support Centre by phone or to an e-mail inbox;
- illegal superannuation schemes by phone; and
- potential tax planning schemes via a hotline or to an e-mail inbox.

6.59 All TERs received by the ATO are recorded and documented under an activity on its work management system, Siebel.⁶⁶¹ For example, when a community member provides information to the ATO via its online tax evasion report form, the form is initially managed through its Community Information Storage Communications and Observations (CISCO) system, ATO officers convert that information to a separate document which is attached to Siebel.⁶⁶² The ATO has indicated that it aims to incorporate the ability to automate the process of converting data on its CISCO form into a Siebel activity as part of an upgrade to the online tax evasion report form.⁶⁶³

6.60 ATO officers, who receive TERs by telephone, have scripting available to guide them in obtaining the relevant information. This scripting consists of 85 questions although not all of them are required to be asked as the answers will determine the further questions to be asked. ATO officers are also expected to use their judgement to tailor the questions based on the relevance to the specific TER being made. Under the ATO's current processes, TERs received by telephone are handled by specially trained officers, however, the ATO is seeking to ensure that all of its contact centre officers are appropriately trained to receive such calls in the future. The ATO has emphasised that it does not impose any time constraints nor does it assess calls based on the duration of the call.⁶⁶⁴

⁶⁵⁸ *Inspector-General of Taxation Act 2003* s 8; For a description of such investigations, see IGT, *Annual Report 2016–17* (2017) p 11.

⁶⁵⁹ ATO, 'Report a concern' (3 October 2017) <www.ato.gov.au>.

⁶⁶⁰ ATO, 'Avenues available to the community to report instances of suspected external fraudulent activities (excluding the TERC process)' (Internal ATO document, undated).

⁶⁶¹ ATO, 'TERC end-to-end process for staff dealing with TERC cases' (ATO intranet, undated).

⁶⁶² ATO, 'Journey maps -Final' (Internal ATO document, May 2017).

⁶⁶³ ATO TERC business area, IGT review team interview, 12 July 2017.

⁶⁶⁴ *ibid.*

6.61 All those who lodge a TER with the ATO using the online tax evasion reporting form or by telephone are provided with a reference number. These numbers differ depending on the channel through which they were lodged. For example, the reference number provided to taxpayers who lodged TERs by telephone can be searched on Siebel, however, reference numbers provided for online lodgments can only be searched through the CISCO system. The ATO expects to address this issue in the upgrade of its online tax evasion reporting form to ensure that a uniform approach is adopted.⁶⁶⁵

6.62 In the 2016–17 financial year, the ATO received 46,389 TERs of which 8,997 were by phone, 5,285 by mail and 32,107 online as outlined in the table below.⁶⁶⁶ The information in the table also demonstrates that since the 2013–14 financial year, the proportion of referrals lodged by web and e-mail has increased, accounting for over 65 per cent of total referrals for both the 2015–16 and 2016–17 financial years.

Table 6.3: The number of referrals from community by year and interaction

Interaction	2013-14	2014-15	2015-16	2016-17
Phone	12,460	10,706	9,347	8,997
Mail & Other	6,028	5,531	5,479	5,285
Web & E-mail	19,482	25,342	30,184	32,107
TOTAL	37,970	41,579	45,010	46,389

Source: ATO

6.63 It should be noted that 90 per cent of all TERs were lodged anonymously.⁶⁶⁷

6.64 The TERC is staffed by nine FTE officers who dedicate 13 hours per week to processing the TERs received. Upon receipt of a TER, the information provided is reviewed and the identity of the taxpayer, who is the subject of the allegation, is confirmed based on details such as name, address, date of birth, TFN, Australian Business Number or any other unique identifying information. In cases where there are insufficient details to identify the taxpayer, no further action is taken other than the records being stored on Siebel. Such records may be directed to the relevant business line in the future if additional information is subsequently provided which allows the ATO to take action.⁶⁶⁸

6.65 There may also be instances in which ATO officers identify that a TER has previously been made with the same information less than three months ago. These are treated as duplicates and are still recorded on Siebel but no further action taken. However, if new information is provided, the allegation would be treated as a new TER regardless of when the previous one was received.⁶⁶⁹

⁶⁶⁵ *ibid.*

⁶⁶⁶ ATO, 'Intermediaries and Lodgement - Tax Evasion Reporting Centre (TERC) - Handling Community information in the ATO' (Internal ATO document, October 2017).

⁶⁶⁷ *ibid.*

⁶⁶⁸ Above n 662.

⁶⁶⁹ Above n 663.

6.66 In reviewing a TER, ATO officers are required to determine whether the allegation indicates fraud or tax evasion. They must also review the lodgment history of the subject of the TER and confirm whether it is up-to-date. If it is confirmed that a taxpayer has outstanding lodgments, the TER is allocated to the Tax Practitioner and Lodgement Strategy team to pursue lodgment of any outstanding returns. If it is determined that the TER does not contain any allegation of tax evasion, it is finalised without any further action.⁶⁷⁰

6.67 In circumstances where it is identified that the TER contains sufficient information to indicate potential tax evasion or fraud, ATO officers are required to identify the issues, assess the level of priority and determine the relevant business line to which it can be referred for further action. This process is undertaken using the 'stakeholder reference tool' which is a matrix developed by the TERC in collaboration with the ATO's business lines. It contains 50 of the most common tax evasion behaviours reported to the ATO. The tool allows ATO officers to choose two of these tax evasion behaviours and the business lines to which the TERs may be referred.⁶⁷¹

6.68 In some cases, ATO officers may also be required to record the TER on the ATO Intelligence Discover database⁶⁷² which allows ATO staff to capture, store, retrieve, escalate and analyse information for intelligence purposes (this is discussed in more detail in the next section regarding referrals by ATO officers).

6.69 Once the ATO officer has recorded the relevant information about the TER in the Siebel activity, the latter is closed to ensure that the information received in the TER cannot be changed or altered.

6.70 At the end of each month, the TERC compiles a spreadsheet for each business line within the ATO. They contain details for all Siebel activities relating to finalised TERs and are sent to the relevant business line representative for their consideration.⁶⁷³ They include the taxpayer details, information about how the TER was received, the date the Siebel activity was closed and background data about the taxpayer such as the market segment to which they belong, whether they had a tax agent and their overall lodgment status.⁶⁷⁴

6.71 Table 6.4 below outlines the percentage of TERs allocated to each of the ATO's business lines for the last three financial years. The table demonstrates that almost a quarter of all TERs received by the ATO were allocated to the Individuals business line. The Cash and Hidden Economy (CHE) stream of the SB business line also received a significant proportion of referrals, averaging 19 per cent of all referrals over the past three years. In addition, the ATO's Lodgment and Employer Obligations (EO) business lines were allocated 16 per cent and 14 per cent respectively over the same period. A smaller proportion of the TERs were allocated to the Superannuation and PGH business lines, five per cent and three per cent of total referrals respectively.

⁶⁷⁰ *ibid.*

⁶⁷¹ *ibid.*

⁶⁷² *ibid.*

⁶⁷³ Above n 662.

⁶⁷⁴ Above n 663.

Table 6.4: Receipt of community referrals by business areas

Financial year	2014–15		2015–16		2016–17		Total for last 3 financial years	
Business Area	Total referrals	%	Total referrals	%	Total referrals	%	TOTAL	% of total
Individuals	11,289	23%	13,043	24%	14,099	24%	38,431	24%
CHE	10,616	22%	10,187	19%	10,377	18%	31,180	19%
SB (non-CHE)	8,217	17%	8,773	16%	9,483	16%	26,473	16%
Lodgment	6,717	14%	8,610	16%	10,700	18%	26,027	16%
EO	7,081	14%	7,582	14%	7,457	13%	22,120	14%
Superannuation	2,431	5%	2,974	5%	3,138	5%	8,543	5%
PGH	1,629	3%	1,346	2%	1,180	2%	4,155	3%
Other	1,038	2%	1,728	3%	2,004	3%	4,770	3%
TOTAL	49,018	100%	54,243	100%	58,438	100%	161,699	100%

Source: ATO

Note 1: The table above combines two ATO tables provided by the ATO to the IGT.⁶⁷⁵

Note 2: 'Other' includes referrals to PGI, ITX, Debt and other business lines within the ATO.

6.72 A breakdown of the types of tax evasion reported in the TERs for the 2016–17 financial year is provided in the table below. The table highlights that underreporting of income (41 per cent) and non-lodgment (19 per cent) account for the majority of the referrals. In addition, 15 per cent relate to cash-related payments with the remaining five per cent being related to non-payment of Superannuation Guarantee (SG).

Table 6.5: Type of tax evasion behaviour identified by community referrals

Tax evasion behaviour identified	No. of referrals	% of total
Under-reported / unreported income	24,605	41%
Non lodgment - income tax return or BAS	11,090	19%
Employers paying staff in cash	5,602	9%
Businesses demanding cash payment	3,647	6%
SG not paid	2,985	5%
Other	11,788	20%
TOTAL	59,717	100%

Source: ATO

6.73 Upon receipt of the monthly report from the TERC, each business line representative considers the information in the report in accordance with the relevant business line process. The processes between the business lines may vary due to the different risk assessment approaches that each business line may have adopted.⁶⁷⁶ Initially, the precise nature of these processes was not clear to the IGT. However, as the ATO further developed these processes, it was able to provide the following representations about the processes used by the six business lines that receive the majority of TERs.

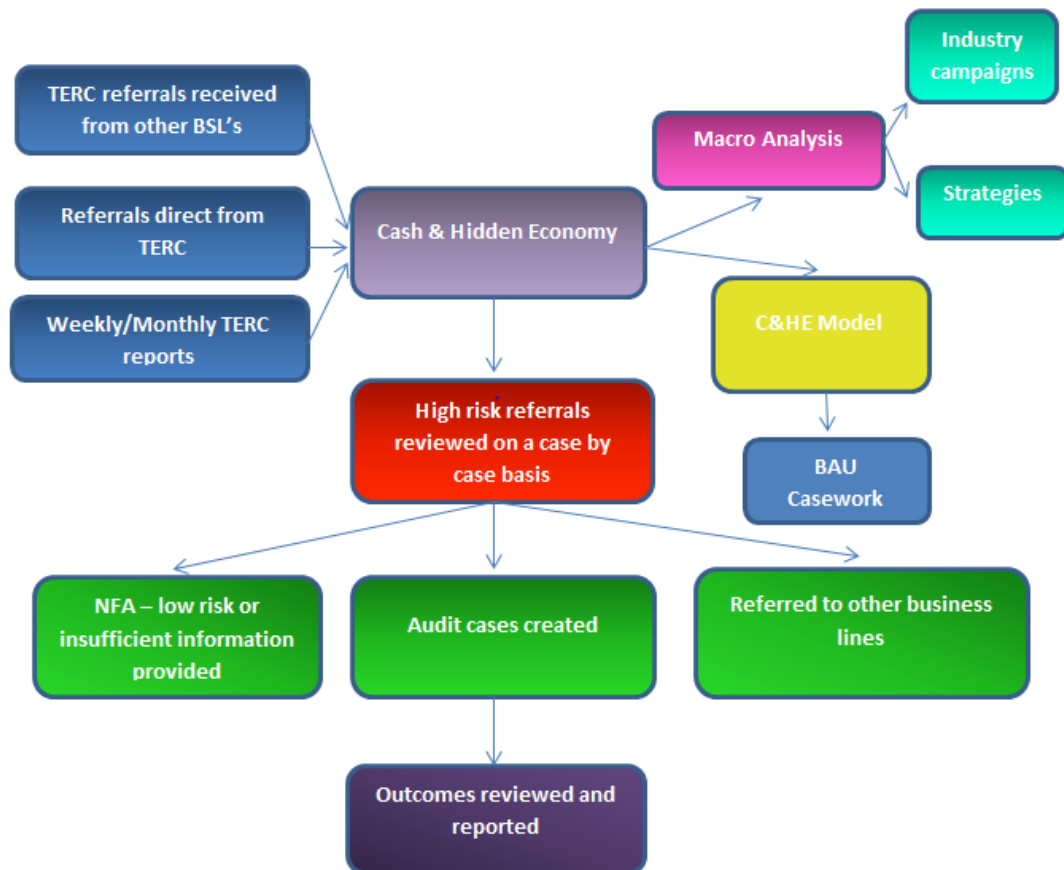
⁶⁷⁵ ATO, 'TERC SES Summary and overview -v3.1 July 2017' (Internal ATO document, undated); ATO, 'TERC - Overview of TERC processes v1.0 June 2017' (Internal ATO document, undated).

⁶⁷⁶ ATO, 'ATO Overview of TERC processes v1.0, June 2017' (Internal ATO document, June 2017).

Cash and Hidden Economy stream

6.74 The Risk & Strategy unit within the CHE stream receives TERCs from the TERC through its regular reports as well as referrals which may have been transferred to CHE from other business areas. Figure 6.1 below provides an overview of the CHE stream process for receiving and reviewing TERCs.

Figure 6.1: Cash and Hidden Economy stream's process for community referrals



Source: ATO

6.75 The above Figure shows that the CHE stream reviews TERCs in accordance with the following three methods:

- case-by-case assessment of high risk TERCs based on the nature of the allegation and reliability of information (high risk referral);
- broader review of a number of TERCs to identify behaviours and risks that may be relevant to CHE's current strategies or industry specific compliance campaigns (a macro analysis); and

- automated risk assessment by the CHE's risk rating model (the CHE Model) which uses TERs for the past three years as one of a number of inputs for case selection and risk analysis purposes.⁶⁷⁷

6.76 In their reviews of TERs, Risk and Strategy officers place emphasis on those which have been marked as high risk and may be relevant to any current or future CHE compliance projects. TERs which provide reliable information are sent to the relevant areas within the CHE stream or other areas in the ATO for action. TERs which do not provide such information are input into a database and no further action is taken unless the CHE Model selects the case for action.⁶⁷⁸

6.77 The CHE Model is a risk rating tool which analyses a range of taxpayer data to provide a risk score for each taxpayer. This risk score is added together with any score that the TERC may have attributed to the TER when it considered the prioritisation of the referral, as mentioned earlier. The combined score provides the CHE stream with an overall TERC-rated risk which is used when the CHE stream runs its risk models to select BAU cases. The BAU cases that are generated from the CHE Model take into consideration all of the information available to the CHE stream. As the TERC risk rating is one of many types of information input into the CHE Model to generate cases, it is difficult to identify whether the cases generated by the CHE Model were solely based on a TER as they would generally contain project codes relating to other risks.⁶⁷⁹ The CHE stream explained that it is currently considering undertaking compliance activity against taxpayers who have been subject to multiple TERs.⁶⁸⁰

6.78 The CHE stream provides reports on TERs and outcomes of cases which were created as a result of TERC referrals.⁶⁸¹ However, the outcomes are focused on the high risk referrals and TERC-related projects being conducted by the CHE stream.⁶⁸²

Individuals business line

6.79 Upon receiving the monthly report from the TERC, the Individuals business line identifies taxpayers for which treatment action is already being undertaken through its normal risk models. For example, six per cent of the TERs received by the Individuals business line over the July to September 2016 period included cases which had previously been identified by the business line through its usual detection processes and had become the subject of compliance action.⁶⁸³

6.80 It should be noted that 10 per cent of TERs received by the Individuals business line did not have sufficient information to identify the subject taxpayer. In addition, 95 per cent of the referrals were made anonymously.⁶⁸⁴

⁶⁷⁷ ATO CHE stream, IGT review team interview, 24 July 2017.

⁶⁷⁸ *ibid.*

⁶⁷⁹ *ibid.*

⁶⁸⁰ ATO Individuals business line, IGT review team interview, 26 July 2017.

⁶⁸¹ ATO, 'TERC to CE Process' (Internal ATO document, May 2017) p 5 para [1].

⁶⁸² Above n 677.

⁶⁸³ Above n 680.

⁶⁸⁴ *ibid.*

6.81 The remainder of the TERs received by the Individuals business line are assessed using its risk models in conjunction with other available information for the particular taxpayer including the identification of keywords, scams, specific agents or frauds. The use of the risk models generally results in a reduction of approximately 64 per cent of the referrals for further review.⁶⁸⁵ Officers' decisions are documented and inputted into a database for future intelligence purposes.

6.82 The Individuals business line stated that 51 per cent of the referrals it had received from the TERC, for the 2016–17 financial year, involved the non-payment of child support obligations and claimed that the relevant taxpayers had underreported their income or not lodged their income tax return. As a result of the TERs, the Individuals business line conducted a campaign which involved issuing letters to taxpayers who had a TER about non-lodgment raised against them. The letters to the taxpayers informed them that they had outstanding lodgments and that according to information available to the ATO, they were required to lodge them.⁶⁸⁶

6.83 The Individuals business line noted that it was in the process of determining whether it would be appropriate to place a TERC indicator on taxpayers' files to assist in its case selection process. The TERC indicator would form part of an overall risk rating for the taxpayer and assist in determining whether compliance action is required. It expects to review the TERC indicator to assess the likelihood of the risk occurring in the future and update taxpayers' risk profiles for the previous two years. It is also assessing the value of reporting revenue raised from compliance actions taken as a result of the TERs and also provides feedback to the TERC.⁶⁸⁷

Superannuation business line

6.84 The majority of TERs received by the Superannuation business line provide information regarding the non-payment of SG by employers. Accordingly, the initial review of these referrals focusses on determining whether sufficient identification information has been provided to commence an investigation of the employer through the Employee Notification (EN) process as the ATO has committed to investigate all ENs it receives.⁶⁸⁸

6.85 TERs which allege unpaid SG but do not adequately identify the employee, are assessed against the business line's risk models to determine whether further compliance activity against the employer would be appropriate.⁶⁸⁹

6.86 The Superannuation business line has advised that only 700 of the 3,138 TERs received from the TERC for the 2016–17 financial year had contained sufficient

⁶⁸⁵ *ibid.*

⁶⁸⁶ *ibid.*

⁶⁸⁷ *ibid.*

⁶⁸⁸ ATO Superannuation business line, IGT review team interview, 26 July 2017.

⁶⁸⁹ *ibid.*

information to be considered for further investigation. The remainder were, therefore, assessed in accordance with its risk filters.⁶⁹⁰

6.87 It also noted that 70 per cent of the allegations regarding unpaid SG are lodged via the online TER form and 15 per cent over the phone with contact centre scripting guiding staff to obtain sufficient information for lodging an EN. The online TER form does not inform users, that if their concerns relate to unpaid SG, relevant information is available on the ATO's website. Furthermore, it does not direct users to the online EN form in appropriate cases.⁶⁹¹

Small Business (SB) business line

6.88 TERs which are received by the SB business line are reviewed by an ATO officer in the SB Integrity team who determines whether there is sufficient basis for the TER to warrant further investigation. As part of this process, the ATO officer identifies the behaviour exhibited in the TER and the merits of the allegation. However, they must also consider any potential biases by the person making the TER. Once the TER has been assessed, the officer's decision is documented in Siebel. The SB Integrity team notes that due to the volume of referrals it receives, some of these decisions have limited detail, particularly those where no further action is taken.⁶⁹²

6.89 Of the TERs received by the SB business line in 2016–17, only 81 were considered suitable for further compliance action and only 40 per cent of these cases resulted in an audit outcome. Due to the small proportion of actionable cases, the SB business line is evaluating how it assesses TERs and whether it would be more practical to adopt a risk-based approach in considering them.⁶⁹³

Employer Obligations business area

6.90 The EO business area explained that the majority of TERs it had received in the 2016–17 financial year (approximately 73 per cent) involved employees receiving their wages in cash. The remaining TERs included concerns with employers not remitting PAYG tax to the ATO (8.3 per cent), the non-issuance of payment summaries (12.5 per cent) and the disputed status of the worker (6.9 per cent). The EO business area's current risk models aim to identify such concerns as part of its own processes. However, it is unclear whether these processes had already identified the concerns raised in the TERs.⁶⁹⁴

6.91 The EO business area has advised that it does not review each TER on a case-by-case basis, however, it does use the information reported in the TERs in developing future strategies for the business line.⁶⁹⁵

⁶⁹⁰ *ibid.*

⁶⁹¹ *ibid.*

⁶⁹² ATO Small Business business line, IGT review team interview, 18 July 2017.

⁶⁹³ *ibid.*

⁶⁹⁴ ATO Employer Obligations business area, IGT review team interview, 27 July 2017.

⁶⁹⁵ *ibid.*

PGH business line

6.92 TERs are sent to five different areas in the PGH business line. These are the Tax Crime, Phoenix, ATP, Fringe Benefits Tax (FBT) and National Case Selection (the BAU team) areas.⁶⁹⁶ In addition, PGH has a dedicated e-mail inbox for internal referrals made by ATO officers and other business lines within the ATO.

6.93 The Tax Crime area reviews TERs on a case-by-case basis to determine whether there are sufficient grounds for further investigation. The Tax Crime area provides confirmation to the TERC that it had received the TERs sent, however, it is unclear whether this communication includes details regarding the decision made as a result of that referral.⁶⁹⁷

6.94 The Tax Crime area received 140 TERs in the 2016–17 financial year. Of these, 129 were transferred to other areas of the ATO for their action and one was transferred to the TPB. No action was or could have been taken on the remainder. Table 6.6 below sets out the outcome of those referrals.

Table 6.6: Number of community referrals actioned by PGH’s Tax Crime area in 2016–17, by outcome

Type of outcome	Number
Transfer to other areas in PGH	84
Transfer to CHE	23
Transfer to SB (non-CHE)	14
Transfer to GST	4
Transfer to EO	2
Transfer to Superannuation	1
Transfer to Not-for-profit	1
Transfer to TPB	1
No further action – not a tax matter	3
No further action – general	1
Not able to determine	6
TOTAL	140

Source: ATO

6.95 The Phoenix area of PGH receives TERs through two main methods. The first method is through TERC staff who use the ATO Intelligence Discover database to report a potential phoenix arrangement in a TER. In this case, an e-mail is sent directly to the Phoenix area’s mailbox.

6.96 The second method is through referrals which are sent directly to the Phoenix mailbox by external parties such as liquidators, dissatisfied creditors and employees. In these cases, the information is entered into a TERC Siebel activity and added to the ATO Intelligence Discover database.

⁶⁹⁶ ATO PGH business line, IGT review team interview, 25 July 2017.

⁶⁹⁷ *ibid.*

6.97 The Phoenix area states that it treats all referrals as intelligence in the first instance and does not always commence an investigation. Upon receipt of the TER, the PGH officer reviews the relevant information and attachments in both ATO’s Risk Assessment Profiling Tool (RAPT) and Siebel. RAPT is used to determine whether the allegation is made in relation to an entity which is already considered to be part of the Phoenix population. After the initial assessment has been completed, the ATO inputs that data into a master reporting sheet which includes demographic details to assist in identifying industry trends and geographic locations.⁶⁹⁸

6.98 Once the TER has been considered for intelligence purposes, it is reviewed to determine whether a more detailed analysis is required. As part of this analysis, the Phoenix area seeks to determine information about the scope of the allegations, the potential impact and whether there is a reputational risk to the ATO if the matter is not investigated. Cases which are considered to be suitable for further action are placed on a checklist and presented to a case selection panel as a priority.⁶⁹⁹

6.99 The Phoenix area had received 456 TERs during the 2016–17 financial year of which 22 resulted in the outcomes set out in Table 6.7 below. Fifteen of these 22 TERs were subject to a current audit or were already identified as a risk by the PGH business line and the remaining two had initiated investigations.

Table 6.7: Number of community referrals actioned by PGH’s Phoenix area in 2016–17, by outcome

Outcome	Number of TERs
Subject to a current audit – information forwarded to auditor	6
In current Phoenix population	9
No further action due to insufficient risk or no evidence of phoenix activity	4
Referred to another area within the ATO	1
Phoenix case created	2
TOTAL	22

Source: ATO

6.100 The Phoenix team has stated that it is currently unable to determine whether action is taken or liabilities are raised specifically as a result of TERs as their treatment strategies are designed to address the behaviours of groups rather than those of individual entities.⁷⁰⁰

6.101 The Phoenix area prepares and provides reports about TERs and associated feedback on a quarterly basis to the TERC. Such reporting is one of the Phoenix area’s effectiveness measures that are reported to the PGH Executive annually.⁷⁰¹

6.102 The ATP area records all TERs assigned to it in the ATP Risk Management spreadsheet in the ATO Intelligence Discover database. The ATP area also forwards details about the referrals to the Smarter Data business line (responsible for all of the

⁶⁹⁸ ATO, ‘PGH report to the IGT on TERC referrals’ (Internal ATO document, 28 July 2017) p 3.

⁶⁹⁹ *ibid.*

⁷⁰⁰ *ibid.*, p 4.

⁷⁰¹ *ibid.*

ATO's risk assessment activities and described in detail in the section below on 'Risk Models and Data Analysis'). The TERs are reviewed by both ATP and Smarter Data to determine whether they have been appropriately assigned to the ATP area and whether there is sufficient information to take action. Where there is insufficient information, any resulting action may be deferred for six, nine or twelve months.⁷⁰²

6.103 The ATP area has expressed its concerns to the TERC that the majority of the TERs referred to it do not relate to its work. It explained that from 1 July 2016 to 31 March 2017, it received a total of 237 TERs which resulted in two being progressed for further analysis and another being placed on an ATP watch list. The remaining TERs were considered to be low risk or not associated with a risk managed by ATP. The ATP area stated that it is in the process of developing additional guidance, training and fact sheets for the TERC team in addition to the monthly feedback it already provides to them.⁷⁰³

6.104 The FBT team within the PGH business line allocates the TERs it receives from the TERC to its compliance staff to analyse and determine the appropriate response. Once an FBT officer has decided the appropriate action, their decision is required to be documented and recorded on Siebel and the ATO Intelligence Discover database.⁷⁰⁴ They also provide a response to the TERC's monthly report and inform the latter of the decisions they have made with respect to each TER.

6.105 The FBT area had received a total of 201 TERs during the 2016–17 financial year. Of these referrals, 71 were escalated as a potential risk for verification which in three cases resulted in an FBT amendment. Nil outcomes were recorded for 51 of the TERs with the remaining 17 cases still in progress.⁷⁰⁵

6.106 All TERs that are referred to the PGH business line but do not fall in any of the above four areas are sent to the BAU area. Each of these referrals is reviewed to identify those which relate to ongoing cases and those with respect to which compliance activity should be initiated. The resulting action may be referral to a risk manager, other areas of PGH or other business lines, or the case officer of an existing case. Analysis of the TERs include determining an appropriate risk rating based on whether documents have been provided, if the contact details of the person making the TER are available and how many previous TERs have been received from the same person.⁷⁰⁶

6.107 The BAU area also provides reports to the TERC about the actions it has taken with respect to each TER and whether they have been appropriately classified.⁷⁰⁷

6.108 For the 2016–17 financial year, the BAU area received 751 TERs. Of these referrals, 494 were considered to be of minimal risk or relevance to the PGH business

⁷⁰² *ibid.*, p 5.

⁷⁰³ *ibid.*

⁷⁰⁴ Above n 698, p 5.

⁷⁰⁵ *ibid.*

⁷⁰⁶ *ibid.*, p 6.

⁷⁰⁷ Above n 696.

line with no further action being taken. However, three were placed on the PGH Intelligence watch list. In addition, 235 TERs were referred to other areas within PGH or other business lines. The remaining 22 TERs were considered for further investigation with 20 investigations being commenced as a result.⁷⁰⁸

IGT observations

6.109 The general public including whistleblowers are a valuable resource to the ATO and can play a vital role in identifying and reporting instances of suspected fraud and tax crime. In this respect, they can supplement the ATO's resources by acting as a detection mechanism for no additional cost and provide real time insight about the tax environment, emerging trends and the effectiveness of the ATO's strategies to address tax crime. They may also be useful in ongoing cases and assist the ATO in gathering additional data to enhance its risk models and detection measures.

6.110 As a point of principle, the large number of TERs lodged with the ATO clearly reflects the community's desire to support the ATO in addressing fraud and tax crime although some TERs indicate that other motives may be at play and may be vexatious. Nevertheless, they all need to be reviewed diligently to ensure that important information is not overlooked. To maintain and develop this valuable source of information, the ATO has to demonstrate to the community that it values all TERs, scrutinises them closely and takes appropriate resulting action.

6.111 It is noted that the majority of TERs relate to small scale matters and may not be treated with the same priority as suspicions of major fraud which attracts the attention of multiple agencies and taskforces. However, if these smaller scale acts of fraudulent behaviour are not addressed, they may propagate, compound or lead to more serious fraudulent activities, adversely impacting the total revenue collected.⁷⁰⁹

6.112 Based on the reporting provided by the ATO, only a small percentage of TERs contain sufficient information to enable the ATO to take further action. This difficulty is further compounded by the majority of the community members lodging TERs anonymously without providing contact details (approximately 90 per cent). In the IGT's view, there are a number of steps the ATO could take to improve the quality of information it receives in TERs. These steps include widely publicising the availability of the TER process and specifying the types of information which would be most useful. In doing so, the ATO could specify the information needed to action the most common types of TERs. For example, the Individuals business line could specify the information needed to action a TER regarding the undeclared income of a person who has child support obligations.

6.113 The ATO could also provide greater confidence in the TER process by explaining how ATO officers seek to protect the identity of those who lodge TERs as they conduct their investigations. For people who still wish to lodge a TER

⁷⁰⁸ Above n 698, p 6.

⁷⁰⁹ See, for example, concerns expressed regarding work related expenses: Chris Jordan, 'Keynote address to the Tax Institute 33rd National Convention' (Speech delivered at the Tax Institute National Convention 2018, Cairns, 15 March 2018).

anonymously, the ATO could seek to establish a secure two-way information channel by, for example, suggesting they could set up a unique and anonymous e-mail address specifically for this purpose. They could also be assured that the law prohibits the ATO from accessing metadata to identify and track their Internet Protocol (IP) address, unless they are the subject of a criminal investigation. These types of information could be advertised widely as well as at the time TERs are being lodged online or by telephone.

6.114 Once TERs are provided to the ATO, the ATO's TERC processes for logging and referring them to the relevant business lines are detailed and robust. However, improvements are required to the processes that the business lines use to deal with TERs. These processes were being further developed during this review. The IGT believes that the ATO should ensure these processes are consistent across business lines, are formally documented and are available to all relevant staff.

6.115 Under the ATO's current approach, each of the ATO's business lines has different processes for considering TERs for intelligence and compliance purposes. Some of these differences are necessitated by the nature of work across multiple risk areas and taxpayer segments. However, in some business lines the risk rating scores only check to determine whether a TER has been lodged with no consideration given to the quality and reliability of information contained in the TERs. Accordingly, it is difficult to establish the priority which should be given to a TER investigation as compared to, for example, risks identified by the business line itself.

6.116 There may be many TERs that contain insufficient information or identify issues of low risks which may not warrant a detailed investigation or should not take priority over risks identified by other ATO processes. A consistent treatment of TERs across business lines is required which takes a whole of ATO view in determining the priority with which they should be investigated relative to each other as well as risks identified by other means. Relevantly, the ATO is considering developing an Enterprise View of Client Risk which would review the case selection systems across all of the ATO's business lines.

6.117 Furthermore, currently, the ATO is able to report on the number of TERs received each year, the business lines to which they have been allocated and the number of taxpayers that were the subject of TERs whilst an audit was conducted on their affairs. However, the ATO does not currently capture the extent to which the information provided in the TERs had contributed to its compliance activities, particularly whether they have resulted in the initiation of audits or have improved the outcomes of those audits. The IGT believes capturing such information would be useful in assessing the effectiveness of TERs and identifying further improvement. The publication of such aggregated data as well as information about identified trends and the most reported type of allegations would also enhance community confidence in the ATO's management of TERs and may increase their useful contribution.

RECOMMENDATION 6.2

The IGT recommends the ATO:

- a) better inform the public about making tax evasion referrals including by specifying the type of information required and assuring them of confidentiality;*
- b) formalise and document consistent processes, across all business lines, for dealing with tax evasion referrals; and*
- c) publically report aggregate data about the outcome of its investigations of tax evasion referrals including the extent to which they give rise to compliance activities, any identified trends and the most common types of referrals.*

ATO RESPONSE

(a) Agree

(b) Agree

The ATO will seek to formalise and document procedures for all business areas that receive and action tax evasion referrals from the Tax Evasion Reporting Centre, ensuring they are centrally recorded. The ATO notes that the detail of some processes may differ between business areas due to the volumes of referrals received and the nature of those referrals.

(c) Agree

Referrals from ATO officers and other agencies

Stakeholder concerns

6.118 Stakeholders, including some former ATO officers, have expressed concerns that when suspected tax frauds are reported within the organisation, the ATO is either slow to act or does not take action at all.

6.119 Stakeholders have also raised concerns about the ATO's processes for actioning referrals from other government agencies. In the past, they believe that ATO officers have not acted on documents received from other agencies for a significant period of time as they did not know which area of the ATO should be approached.

Relevant materials

ATO staff referrals

6.120 As mentioned earlier, pursuant to CEI 2014/05/09, all instances of suspected external fraud encountered by the ATO's other business lines must be referred to the

PGH business line⁷¹⁰ who assess the referral against tax crime priorities to determine whether the matter requires a criminal investigation.⁷¹¹

6.121 To make a referral, officers must complete a Tax Crime Referral Form and send it to their business line gatekeeper who checks the form for completeness, determines whether it aligns with the business line's risks and priorities as well as evaluates the strength of the evidence.⁷¹²

6.122 The business line gatekeeper is also required to provide the referral with a priority rating of between level one and four before uploading the details onto RAPT.⁷¹³ If the referral is considered to be of a low priority, the referral will be actioned through the 'BAU casework' process whereby the relevant data on RAPT will be routed to the PGH Director in the region where the alleged offence occurred.⁷¹⁴ A decision will then be made on whether a case is to be created for the PGH investigation team in the region after 'consideration of funding and resourcing requirements, case type and recommendations.'⁷¹⁵

6.123 Higher priority referrals, such as cases where the amount of revenue involved is in excess of \$1 million and cases where the specified risks are business line priorities, are actioned in accordance with a priority casework process. This involves a two-stage assessment by PGH's Criminal Law National Assessment Treatment. The first stage considers matters such as available evidence, the ATO's ability to commence a review, the strategic role of investigations, the risks and charges as well as engaging with the business line to understand matters of complexity. The second stage involves a 90-day review and is primarily concerned with establishing the grounds for issuing warrants. As with the BAU casework process, the end result will be a PGH investigation in the region where the offence was committed. If, due to the higher risk and complexity involved, the cycle times would be greater than 180 days, these cases also require approval by the PGH Case Escalation Forum before they are commenced.⁷¹⁶

6.124 If at any stage during the above process, PGH determines that the matter may need to be referred to the AFP for either investigation by the latter or a joint ATO/AFP investigation, the referral will be submitted to PGH's Tax Crime Forum for approval.⁷¹⁷

6.125 In addition to referring tax crime related matters to the PGH business line pursuant to CEI 2014/05/09, ATO officers are also required to comply with the CEI 2014/03/05 on Intelligence Management which states that they are responsible for

⁷¹⁰ Above n 89.

⁷¹¹ ATO, 'Referring suspected Tax Crime to PGH BSL Gatekeeper Expectations' (Internal ATO document, undated).

⁷¹² ATO, 'Introduction to the Tax Crime Business Line Partner Gatekeeper Role' (Internal ATO document, undated).

⁷¹³ *ibid.*, p 2.

⁷¹⁴ ATO, 'Criminal Investigations & CACT Referral Process' (Internal ATO document, undated).

⁷¹⁵ ATO, 'PGH Criminal Law Tax Crime Referral Guidelines' (Internal ATO document, undated); Above n 714.

⁷¹⁶ Above n 714.

⁷¹⁷ *ibid.*

recording in the ATO Intelligence Discover database any observations which have the potential to impact the ATO's business outcomes.⁷¹⁸

6.126 As mentioned earlier, the ATO Intelligence Discover database is a tool which allows ATO officers to share and analyse information throughout the organisation as well to monitor, detect and address compliance risks. It is most often used for referring concerns about taxpayers to other business units within the ATO.⁷¹⁹

6.127 Where an ATO officer identifies a case which involves a potential fraud or tax crime, they are encouraged to understand the key risks and determine whether they should deal with the risks in the current case or refer them onto another area through the ATO Intelligence Discover database. They may also consult with their team leader in this regard.⁷²⁰

6.128 All ATO officers who submit information through the ATO Intelligence Discover database will receive an automated acknowledgement e-mail and a reference number for their records. Once the referral has been received by a business unit, it will be assessed by intelligence analysts against risk rating models, business objectives and availability of resources to determine the level of priority for further action. The ATO has noted that since 'it is the responsibility of the risk management areas to review and assess the referral for the appropriate treatment, immediate treatment of the referral may not occur.'⁷²¹

6.129 Since 2011, a non-mandatory self-paced online training package has been made available to all officers to assist them fulfil their obligations of detecting and referring suspected tax crime.⁷²² However, a 2014 internal ATO review had found that there was significant underreporting and inaccurate reporting by ATO officers of fraudulent behaviour due to a lack of training amongst other things.

6.130 Following the above review, the training package was updated and now includes links to PGH's 'guide to a comprehensive referral' outlining the three key types of information required to improve the likelihood of a referral being considered suitable for investigation.⁷²³ This training package was also revamped in September 2017 with video scenarios used to illustrate examples of tax crime behaviour which were developed from real cases. It was released through a communications strategy that included the promotion of the package in ATO newsletters and e-mails to staff. A total of 2,090 ATO officers completed the revamped training package during the period September 2017 to January 2018, including 1,198 call centre staff.⁷²⁴

6.131 In the IGT's view, the above training package should be mandatory for all staff as it informs officers of the process for referring suspected tax crime. As

⁷¹⁸ ATO 'Chief Executive Instruction 2014/03/05 Intelligence Management' (Internal ATO document, 27 March 2014).

⁷¹⁹ ATO, 'ATOintelligence - Intelligence Centre' (Internal ATO document, 2 August 2017) p 1.

⁷²⁰ *ibid.*

⁷²¹ *ibid.*, p 2.

⁷²² ATO, 'Introduction to tax crime - an enterprise approach' (Internal ATO training module, undated).

⁷²³ *ibid.*, slides 8, 10 and 12.

⁷²⁴ ATO communication to the IGT, 5 March 2018.

mentioned earlier, such training should contain practical scenarios which assist officers to detect fraudulent behaviour.

Other agency referrals of suspected tax crime

6.132 Intelligence and referrals from law enforcement and other external agencies are received by the ATO through its 'Tax Crime Intelligence' mailbox. In situations where a referral is sent directly to an ATO officer, the ATO's procedures states that the officer should pass the referral on to the 'Tax Crime Intelligence' mailbox and 'advise the external agency that future referrals should be sent directly to the mailbox.'⁷²⁵

6.133 Information received via the Tax Crime Intelligence mailbox is reviewed, recorded and managed by the Intelligence Register Gatekeeper before it is uploaded on to the 'Tax Crime Strategy Management External Intelligence Product Register' (TCSM Intelligence Register). Information on the TCSM Intelligence Register is then reviewed fortnightly by the Tax Crime Referral Panel who may decide that the information received from the external agency warrants action. If so, an internal review will commence to profile the entity.⁷²⁶

6.134 If the profiler determines the entity to be high risk, the entity will be placed in a 'candidate pool' maintained in RAPT. There are currently seven candidate pools within the PGH Serious Organised Crime and Serious Financial Crime areas that correspond to each of the following: the National Anti-Gangs (Morpheus) Taskforce, the Criminal Asset Confiscation Taskforce (CACT), the National Criminal Target List, organised network refund fraud, illicit tobacco, serious financial crime and offshore tax evasion.⁷²⁷

6.135 Entities within each of the candidate pools may be selected for an ATO audit. Prior to commencement, audits with a cycle time of 180 days or less will need to be approved by the Tax Crime Referral Panel while audits with a cycle time of greater than 180 days will need to be approved by the PGH Case Escalation Forum.⁷²⁸

IGT observations

6.136 The ATO has a workforce of approximately 20,000⁷²⁹ officers who are responsible for carrying out activities which assist in the administration of the tax system. These officers, particularly those in client facing and compliance roles, are uniquely positioned to provide real time insights. Through audits, investigative work and interaction with taxpayers and their advisers, they are exposed to a variety of arrangements and are well placed to identify suspicious activities, patterns, or behaviours, which may appear to be abnormal for a given risk profile or taxpayer segment. These insights may be used to refine the ATO's risk models, detection mechanisms and strategies to address external fraud. Accordingly, all ATO officers are

⁷²⁵ ATO, 'Q-A intel register and candidate pools' (Internal ATO document, undated) p 3.

⁷²⁶ *ibid.*, pp 2-4.

⁷²⁷ *ibid.*, pp 4 and 7.

⁷²⁸ *ibid.*, p 6.

⁷²⁹ Above n 7.

required to refer intelligence and instances of suspected fraud to the PGH business line, whilst the latter has the primary responsibility for addressing external fraud.

6.137 The ATO's processes for referrals to the PGH business line aim to ensure that they are of sufficient quality to be useful for investigation and intelligence purposes. These processes also provide greater transparency and clarity regarding the assessment and prioritisation of the referrals and, as a result, enhance officers' confidence that their referrals will be appropriately considered. However, the IGT believes that the ATO could provide greater motivation to its officers, through appropriate incentives, to detect and report suspected fraud by reporting, at least internally, details of referrals which led to successful prosecution of the perpetrators.

6.138 Although ATO officers may be proficient in identifying compliance risks, they may be less familiar with the behaviours and events which may indicate fraudulent activities are at play. The ATO does provide information, in its non-mandatory training package, on the general types of behaviours which may indicate the existence of these activities as well as some interactive scenarios based on real cases.⁷³⁰ However, the training package places greater emphasis on the process for referring matters to the PGH business line than identification of the underlying suspicious behaviours.

6.139 In the IGT's view, the ATO could improve the assistance it provides to non-PGH officers to identify external fraud by providing them with more in-depth training about the range of behaviours and events which may be indicators of fraud being perpetrated. Such detail could be drawn from PGH's case work and provided in the form of typologies and case studies highlighting the type of behaviours and activities which should lead them to consider a referral to the PGH business line.

6.140 As mentioned above, there may have been instances in the past where former ATO officers had observed that referrals from external agencies, about suspected fraud, were not being appropriately addressed. The ATO's current processes for receiving and considering referrals from external agencies are the same as those made by ATO officers, which as stated earlier, provide confidence that the referrals will be appropriately considered.

RECOMMENDATION 6.3

The IGT recommends that the ATO consider:

- a) reporting ATO officer referrals, about potential fraud, which have led to successful prosecution along with appropriate recognition; and*
- b) requiring all its officers to complete more in-depth training about the range of behaviours and events which may be indicators of fraud being perpetrated.*

⁷³⁰ ATO, 'Tax crime: An enterprise approach' (Internal ATO document, ATO training package, accessed 5 May 2018).

ATO RESPONSE

(a) Agree

(b) Disagree

The wording of this element of the recommendation suggests that the 'in-depth training about the range of behaviours and events which may be indicators of fraud being perpetrated' will need to be managed through a mandatory training process. This requirement does not address the need for the training material to recognise the different roles and exposure to fraud matters faced by staff in order to ensure it is relevant and appropriate, and thereby properly supporting their ability to identify and report possible fraud matters. The 'Security, privacy and fraud' training package is a mandatory training requirement for all staff, which includes guidance and direction for staff in respect to their requirement to report matters of suspected external fraud. In support of this, the 'Introduction to tax crime' training package is available and promoted to all staff as a supplementary training package, providing greater detail and illustrative examples of external fraud matters.

Risk models and data analysis

Stakeholder concerns

6.141 Stakeholders are of the view that the ATO generally takes a long time to uncover fraudulent schemes and raised concerns regarding the effectiveness of the ATO's external fraud detection measures.

Relevant materials

6.142 The ATO uses automated tools and models to detect potential fraud or non-compliance before relevant assessments or refunds are issued to taxpayers⁷³¹ and to select cases for investigation (pre-issue detection processes). Examples of such processes include analytical models and business rules which are designed to recognise characteristics of potential non-compliance or fraudulent activity. There are also watch lists, based on experience from past fraud incidents, which aims to consolidate information about taxpayers who are most at risk.⁷³²

6.143 Pre-issue detection processes are often used where large volumes of data are being processed. For example, the SB business line's pre-issue compliance program employs a variety of automated tools to detect indicators of over-claimed deductions, understated income and identity fraud. It is important to note that these processes, generally, operate in isolation although the ATO is aware of the benefits that would be gained from integrating them to enhance overall effectiveness.⁷³³

⁷³¹ IGT, *Review into the Australian Taxation Office's compliance approach to individual taxpayers – income tax refund integrity program* (2013) p 4 para [1.19].

⁷³² Above n 649, p 25.

⁷³³ *ibid.*

6.144 The ATO also employs a variety of other detection measures across its business lines to complement its pre-issue detection processes. These detection processes apply after an assessment or refund has been issued (post-issue detection processes). The majority of investigations are based on post-issue detection processes which identify cases based on known attributes and characteristics.⁷³⁴

6.145 Post-issue detection processes rely heavily on the availability of appropriate information from internal sources including taxpayer-provided information (e.g. data in tax returns), ATO intelligence systems as well as external sources. It is critical that such information is reliable to ensure potential external fraud can be accurately detected. The outcomes of these processes are used to conduct investigations and disrupt criminal business models by such means as issuing default assessments and garnishee notices as well as commencing prosecution action.⁷³⁵

6.146 Prior to the introduction of the Smarter Data business line in 2014, each of the ATO's business lines were responsible for the development of their own risk models, analysis and detection methods. However, until recently, Smarter Data was responsible for assisting the ATO's business lines to develop and improve their pre-issue and post-issue detection processes.⁷³⁶ In addition, Smarter Data was responsible for all of the ATO's risk assessment activities, providing a centralised and coordinated approach to risk assessment strategies through a range of intelligence and data analysis services. These services included data collection, reporting, analysis and case selection models as well as consulting with business unit risk managers about risk and intelligence matters. In addition, Smarter Data also collaborated with the ATO's business lines to develop tailored project plans to undertake risk assessments which used various techniques and tools based on the complexity of the external fraud risks and the number of stakeholders involved.⁷³⁷

6.147 The 2016 Enterprise Tax Crime Risk Review (2016 ETCR Review) is an example of the risk assessment work that was undertaken by the ATO's Smarter Data business line. The 2016 ETCR Review focused on identifying changes in the external fraud environment and the potential impacts and risks they posed to the ATO as an organisation. It also sought to determine whether risk controls and treatments implemented by the ATO remained appropriate and effective in addressing fraud.⁷³⁸

6.148 It was found that whilst the controls and detection mechanisms in place appeared to be effective, there were a number of opportunities to improve their effectiveness and ability to adapt to the changing environment. These improvements included developing new analytical models to increase the detection rate for identity crime relating to refund fraud, refining and developing better GST refund fraud models to increase their accuracy and reducing the requirement for manual profiling.

⁷³⁴ *ibid.*, p 25 para [3].

⁷³⁵ *ibid.*, p 25 para [4] and p 26.

⁷³⁶ From 3 April 2018, the majority of the ATO's Risk Assessment and Intelligence competency was transferred from the Smarter Data business line to the Client Engagement Group's Strategy and Performance (CEG S&P) business line: ATO, 'A new home in Enterprise Analytics' (Internal ATO document, 3 April 2018).

⁷³⁷ ATO communication to the IGT, 4 August 2017.

⁷³⁸ Above n 617, p 8.

6.149 It was also noted that the majority of controls to detect and address external fraud were implemented at an operational level which made it difficult to measure their effectiveness individually and to consolidate them to form an overall view at the enterprise level to determine whether the ATO's strategic priorities are appropriate in the current fraud environment.⁷³⁹

6.150 Another finding of the 2016 ETCR Review was that the ATO's move to digital channels had caused difficulties in gathering data and information for compliance and fraud detection activities. In particular, the use of digital products meant that it was no longer able to obtain demographic details through myTax and shared government platforms have also resulted in difficulties in accessing data.⁷⁴⁰

6.151 The conclusion reached at the completion of the 2016 ETCR Review was that that the ATO's existing control and detection mechanisms were partially effective and that further mitigation strategies were required to be implemented. These mitigation strategies included conducting reviews of strategic priorities and controls implemented at the operational level every six months to evaluate their ongoing effectiveness and to identify potential new controls to further address fraud risks. It was also recommended that a further tax crime risk assessment be conducted within the next 12 months.⁷⁴¹

IGT observations

6.152 The effectiveness of the ATO's pre-issue and post-issue detection processes are critical elements of its overall strategy to detect fraud as they review large volumes of data. However, the effectiveness of these processes relies on the ATO's awareness of the types of fraudulent activities occurring in the current fraud environment. For example, these processes may detect unsophisticated fraudulent activity, such as not declaring income in form of cash, however, they may not detect more sophisticated arrangements which exploit weaknesses in the tax system until the ATO is specifically alerted to such behaviours. Where these fraudulent activities are allowed to flourish undetected and untreated, they may pose a risk that undermines the integrity of the tax system, as was the ATO's experience in the precious metals industry (more detail is given in Appendix D).⁷⁴²

6.153 As mentioned earlier, the ATO's risk detection processes are subject to periodic internal review and seek to ensure that they are responsive to emerging risks and the changing environment. The IGT is of the view that in doing so, the ATO should be particularly mindful of new technologies and how they may be employed to enhance their processes. First, new technologies such as biometric data and secure

⁷³⁹ *ibid.*, p 42.

⁷⁴⁰ *ibid.*, p 22.

⁷⁴¹ *ibid.*, p 42.

⁷⁴² See also Boucher, *Blatant, artificial and contrived – Tax schemes of the 70s and 80s*, ATO (June 2010), for example pp 73-177 and 386-388.

transaction processes, such as blockchain, can be used to strengthen the architecture of the tax administration system and prevent identity fraud.⁷⁴³

6.154 Secondly, the continued application of advanced data analytical techniques on the ATO's existing data holdings can better identify trends and connections. This analysis can be bolstered by additional data sources from third parties such as other government agencies and financial institutions to help deepen the ATO's understanding of taxpayer profiles and behaviours. For example, the expansion of the taxable payments reporting system to contractors in the courier and cleaning industry⁷⁴⁴ is one of the ways to increase the ATO's data holdings to improve the detection of fraud.⁷⁴⁵

6.155 Thirdly, the use of automated systems and artificial intelligence can increase the sophistication and speed at which data can be analysed to detect. These issues are explored in more detail in the IGT's *Review into the Future of the Tax Profession*.⁷⁴⁶

6.156 Finally, technological and societal changes may also provide alternative non-traditional sources of data, to help the ATO identify connections to tax crime which were previously hidden from detection. For example, social media data can be used to determine the various parties to a syndicate that are perpetrating fraudulent activities or the controlling minds behind sophisticated arrangements.

6.157 The IGT conducted a broad review into the ATO's risk assessment tools in 2013.⁷⁴⁷ Subsequent IGT reviews have considered more specific ATO risk analysis models such as those which relate to income tax refunds⁷⁴⁸ and the use of data matching⁷⁴⁹ in the individual taxpayer context. More recently, the IGT has also examined risk tools used in the GST refund verification process.⁷⁵⁰ As mentioned above, the ATO also plans to conduct further periodic reviews of its risk assessment processes. Accordingly, it is appropriate that further time be allowed for recommendations emerging from these reviews to be implemented and bear fruit before exploring them again.

STAFF CAPABILITY FOR CRIMINAL INVESTIGATION

Stakeholder concerns

6.158 Certain stakeholders have expressed concerns that the ATO's external fraud investigation teams do not possess the adequate skills and experience to conduct

⁷⁴³ Above n 655, p 53; ATO, 'Voice Authentication' (6 September 2017) <www.ato.gov.au>; OECD, *Shining the light on the shadow economy* (2017) p 48.

⁷⁴⁴ As was recommended in IGT, *Review into the ATO's employer obligations compliance activities* (2016) rec 3.4.

⁷⁴⁵ Australian Government, *Budget Paper No. 2* (May 2018) p 22.

⁷⁴⁶ IGT, *Review into the Future of the Tax Profession* (2018).

⁷⁴⁷ IGT, *Review into aspects of the Australian Taxation Office's use of compliance risk assessment tools* (2013).

⁷⁴⁸ Above n 731.

⁷⁴⁹ IGT, *Review into the Australian Taxation Office's compliance approach to individual taxpayers – use of data matching* (2013).

⁷⁵⁰ Above n 8.

criminal investigations. They have suggested that this may be remedied by recruiting staff from law enforcement agencies. They have also suggested that secondments to and from these agencies may also form part of the solution.

Relevant materials

6.159 Within the PGH business line, there are a number of teams responsible for ‘criminal law treatments’. These teams include the investigations, prosecutions, complex investigation, criminal law advice and digital forensics teams.⁷⁵¹ As at 19 October 2017, the PGH business line had a total of 154 officers in the criminal law treatment area.⁷⁵² The following table provides a breakdown of the staff numbers in this area by team for the last four financial years.

Table 6.8: Number of staff in PGH’s criminal law treatment area, by team

	Prosecutions	Criminal law advice	Investigations	Complex investigations (a)	Executive and support	TOTAL
2017–18 (b)	44	5	75	16	13	153
2016–17	44	5	78	12	13	152
2015–16	49	4	86		4	143
2014–15	51	4	100		2	157

(a): Complex investigations commenced part way through 2016–17, to be discussed in Chapter 7.

(b): 2017–18 figures as at 19 October 2017.

Source: ATO

6.160 As illustrated by Table 6.8, the total number of staff conducting investigations declined from 100 staff in the 2014–15 financial year to 86 staff in the following year. However, total numbers rose in 2016–17 to 90 staff, comprising 78 staff in the Investigations team and 12 in the Complex investigations team. The number of staff in prosecution roles has reduced from 51 in the 2014–15 financial year to 44 as at 19 October 2017.

6.161 Of the 112 officers who undertook ‘fraud-related duties’ in PGH’s criminal law treatment area for the 2016–17 financial year, approximately 54 per cent of officers held a Certificate IV in Government (Investigations) and approximately 32 per cent had attained the Diploma of Government (Investigations). The ATO, however, has advised that as at 8 May 2018, all officers conducting investigations hold the relevant Certificate IV/Diploma qualification, are supervised by an officer with such a qualification or are otherwise exempt as they hold an equivalent qualification.⁷⁵³

6.162 The ATO has also reported that over 40 per cent of its officers in the criminal treatment area have ‘fraud related law enforcement’ experience and 21 per cent have attended training in the AFP’s FAC Centre.⁷⁵⁴ Criminal law treatment staff have also

⁷⁵¹ ATO, ‘PGH Criminal Law Treatment Capability Planning 2017–18 DRAFT’ (Internal ATO document, 1 March 2017).

⁷⁵² ATO communication to the IGT, 27 November 2017.

⁷⁵³ ATO communication to the IGT, 8 May 2018.

⁷⁵⁴ ATO, ‘Response to AIC Commonwealth Fraud Census 2016–17’ (Internal ATO document, 2017).

attended specialist training at the AFP's Management of Serious Crime Program for Commonwealth Agencies⁷⁵⁵ and training presented by the IRS in 2017 on conducting criminal investigations on international tax evasion.⁷⁵⁶

6.163 Officers in the criminal law treatment area are also provided with a 'learning toolkit' which outlines the specific capabilities relevant to the role. Links are also provided to relevant online training packages on a number of areas such as information gathering, project management and tax technical topics.⁷⁵⁷

6.164 The ATO aims to improve the capability of officers in its criminal law treatment area so that it may be considered the 'tax crime investigative arm for the Commonwealth' in 18 months.⁷⁵⁸ To achieve this aim, the ATO plans to ensure that there is sufficient learning and development to provide an appropriate mix of core investigation and prosecution knowledge, skills and experience.⁷⁵⁹ Review of job design is also planned with the aim of providing opportunities for career advancement and succession management.⁷⁶⁰ To assist in developing such capability, the ATO also plans to improve its interactions with other agencies, for example, in working with the CDPP to improve the efficiency of the ATO's criminal investigations and prosecutions.⁷⁶¹

6.165 Furthermore, the ATO also seeks to further develop staff capability through secondments and specialist training with other agencies. In this respect, the ATO has advised that since 1 November 2013, it has hosted five staff from agencies such as ACIC, ASIC, CDPP and one financial restructuring firm as part of its secondment program. In that time, the ATO has also approved 54 secondments for ATO officers to work in a variety of institutions including eleven to the ACIC, 22 to the AFP, two to AUSTRAC and three to the CDPP.⁷⁶²

IGT observations

6.166 Based on the information above, the officers in the criminal law treatment area of the ATO possess relevant qualification and experience and there are plans to significantly improve the capability of this area. Accordingly, the IGT believes a review of the ATO's capability to conduct criminal investigation would be best conducted after some time has elapsed from the formal adoption and implementation of these plans.

⁷⁵⁵ ATO, 'Copy of e-mail outlining ATO attendance' (Internal ATO document, 13 February 2017); AFP, 'Management of Serious Crime Program' <www.afp.gov.au>.

⁷⁵⁶ ATO, 'Copy of IRS's presentation delivered to ATO staff in November 2017' (Internal ATO document, November 2017).

⁷⁵⁷ ATO, 'Learning Toolkit for Criminal Investigation' (Internal ATO document, November 2017).

⁷⁵⁸ Above n 751.

⁷⁵⁹ ATO, 'PGH CLT People Capability Plan Project Outline (draft version as at 7 July 2017)' (Internal ATO document, 7 July 2017).

⁷⁶⁰ Above n 751.

⁷⁶¹ ATO, 'ATO-CDPP Project Outline - Project Blossom' (Internal ATO document, 6 March 2017).

⁷⁶² ATO, 'PGH Secondments data as at 21 November 2017' (Internal ATO document, 21 November 2017).

6.167 The ability to adequately investigate external fraud is also dependent on the ATO's collaboration with law enforcement agencies. Such collaboration is examined in Chapter 7.

CHAPTER 7 – INTERAGENCY COLLABORATION

7.1 The ATO has a range of processes in place to prevent, detect and respond to external fraud, as noted in the previous chapter. The successful management of external fraud risks, however, is also dependent on the ATO's collaboration with external agencies, including law enforcement agencies. This chapter examines such collaboration in terms of information sharing, funding and the coordination of specialist skills and resources.

Stakeholder concerns

7.2 Stakeholders have suggested that there could be improvements in the level of cooperation between government agencies for the purpose of tackling external tax fraud. Although the ATO participates in a number of multi-agency taskforces, stakeholders have observed that the level of communication between the taskforce members is often lacking. While this may be due to the legislative limits imposed on the disclosure of information, the end result is one where 'no one is bringing data to the table that helps'. Furthermore, even if the issues surrounding information disclosure are resolved, the current taskforce approach of using information requests and responses is not well-suited to swiftly responding to tax crime.

7.3 Some stakeholders, including government agencies who receive referrals from the ATO, have also observed that the requests for assistance from the ATO arrive via a number of different channels. This has led to a perception that priorities in the ATO are not determined at an organisational level but by discrete areas within the organisation. Furthermore, stakeholders have observed that the lack of prioritisation at an organisational level has resulted in a large amount of referrals being rejected and returned to the ATO. They have also questioned whether the ATO takes any action with respect to these returned referrals.

7.4 More generally, stakeholders have observed that government agencies are overly conscious of each other's 'turf,' which results in a reluctance to deal with issues that may potentially cross over to another agency's jurisdiction. Certain stakeholders have also taken the issue of cooperation one step further and hold the view that the ATO should also engage the private sector to take advantage of the resources and opportunities they can provide.

7.5 Stakeholders have also observed that the ATO is very focused on prosecution as the primary means of dealing with external fraud, which may be problematic due to the higher standard of proof and the length of time that may elapse before a result is achieved. Even if prosecution is an appropriate channel to treat a particular behaviour, the ATO should be working with other agencies to concurrently implement shorter term action or consider taking the matter to prosecution themselves as a way of taking into account the competing priorities of the AFP.

Relevant materials

Private Groups and High Wealth Individuals business line

7.6 As mentioned previously, the TEC area in the PGH business line is responsible for the investigation and prosecution of all external fraud matters, ranging from less serious offences under the *Taxation Administration Act 1953* (TAA) to the more serious and complex offences under the *Criminal Code Act 1995*.

7.7 Where assistance is required from other agencies to investigate external fraud, the PGH business line is the gateway between the relevant ATO business lines and the other agencies. In doing so, PGH aims to ensure that the ATO takes a holistic and consistent approach to external fraud based on its understanding of the risks and priorities of each of the ATO's business lines as well as those of the Commonwealth.

7.8 The PGH business line also has responsibility for managing the ATO's participation in multi-agency taskforces such as the Phoenix Taskforce and the SFCT.⁷⁶³ These taskforces seek to provide a whole-of-government approach to preventing, detecting and addressing certain types of external fraud by cooperation amongst agencies including sharing of information, capabilities and potential solutions.

Information sharing

Information sharing regime under the TAA

7.9 Division 355 of Schedule 1 to the TAA prohibits ATO officers from disclosing taxpayer sensitive information to others (the 'tax secrecy provisions') unless one of the relevant exceptions applies. The exceptions that directly relate to the sharing of information to law enforcement are outlined in section 355-70. One exception permits the ATO to disclose protected taxpayer information to law enforcement agencies for the purpose of investigating or enforcing offences against Australian law punishable by more than 12 months imprisonment or for the purpose of making, supporting or enforcing a Proceeds of Crime order (the general law enforcement agency exception).⁷⁶⁴ Another exception permits the ATO to disclose protected taxpayer information if the disclosure was made to an officer of a prescribed taskforce (the prescribed taskforce exception).⁷⁶⁵

7.10 Of the above two exceptions, the former is more restrictive than the latter as it prevents the ATO from making a disclosure for criminal intelligence purposes or in situations where a specific offence has not been identified. Accordingly, designating a taskforce as a prescribed taskforce creates an environment where it is easier for the ATO to share information with law enforcement agencies. Regardless of which of the two exceptions, it must either be made or approved by the Commissioner, a Second Commissioner or an SES officer.⁷⁶⁶ Accordingly, these disclosures are forwarded to the

⁷⁶³ Above n 711.

⁷⁶⁴ *Taxation Administration Act 1953* sch 1 s 355-70(1) Item 1.

⁷⁶⁵ *Taxation Administration Act 1953* sch 1 s 355-70(1) Item 4; *Taxation Administration Regulations 2007* reg 67.

⁷⁶⁶ *Taxation Administration Act 1953* sch 1 s 355-70(1)(c).

PGH Information Disclosure Team who is responsible for checking the validity of disclosures, obtaining approval from relevant SES officers, disclosing the information to the authorised law enforcement officers and capturing the necessary data for reporting purposes. Information regarding these disclosures is included by the ATO in its Annual Report.

7.11 There is yet another exception where an ATO officer may disclose sensitive tax information to any entity, including law enforcement agencies, for the purpose of administering any taxation law (the performing duties exception).⁷⁶⁷ If a disclosure to a law enforcement agency can be made through both the law enforcement and the performing duties exceptions, generally, the disclosure would be made under the law enforcement exception. However, disclosures would be made under the performing duties exception if they are made to the CDPP, in support of a request for search warrant assistance, in response to an ACIC surveillance request or in relation to a joint agency investigation.⁷⁶⁸

7.12 Once a disclosure has been made to a law enforcement agency or taskforce member, the taxation laws limit the use and further disclosure ('on-disclosure') of that information by the recipient⁷⁶⁹ unless certain exceptions apply. One such exception is where the on-disclosure is made for the same purpose as for the original disclosure.⁷⁷⁰ For example, if the ATO discloses information to a law enforcement agency to enable that agency to investigate a potential serious offence, the latter would not be permitted to use that information for addressing other potential non-serious offences.

7.13 In addition to the tax secrecy provisions, prohibitions are placed on disclosures of TFNs unless such disclosures are made in connection with the exercise of powers or performance of functions under a taxation law (the TFN secrecy provision).⁷⁷¹ As the TFN secrecy provision operates independently from the tax secrecy provisions, the ATO redacts TFNs from its disclosures to law enforcement agencies.⁷⁷²

Limitations to effective information sharing under the TAA regime

7.14 Notwithstanding the above exceptions, the ATO considers that there are a number of barriers to effective information sharing with other agencies.

7.15 First, the ATO has observed that, in some circumstances, the general law enforcement agency exception does not allow disclosures to be made to non-law enforcement agencies who may be able to assist in addressing identified criminal behaviours. For example, in one case, the ATO detected large scale and ongoing fraud by prisoners but faced restrictions on the information that could be disclosed to the

⁷⁶⁷ *Taxation Administration Act 1953* sch 1 s 355-50(2) Item 1.

⁷⁶⁸ ATO, 'PGH Instruction 2015/08 - Information secrecy and disclosure' (Internal ATO document, 21 November 2016).

⁷⁶⁹ *Taxation Administration Act 1953* sch 1 s 355-155.

⁷⁷⁰ *Taxation Administration Act 1953* sch 1 s 355-175.

⁷⁷¹ *Taxation Administration Act 1953* s 8WB.

⁷⁷² Above n 768.

relevant state correctional institutions. As a result, the ATO could only make limited disclosures under the performing duties exception, which 'prevented a more holistic attempt to change the criminals' behaviour and prevent further, non-tax crime being committed in the future.'⁷⁷³

7.16 Secondly, the TFN secrecy provision prevents disclosure of TFNs to law enforcement agencies for non-tax purposes even where the TFNs themselves are critical to the prosecution of alleged offences. For example, in one case, fictitious TFNs and forged Notices of Assessment were used to create bank accounts in false names to perpetrate credit card fraud. The ATO was prevented from making disclosures to state police officers that a particular person was not linked to a particular TFN.⁷⁷⁴

7.17 Thirdly, the ATO has observed that the time taken to establish a prescribed taskforce, which can range from four to twelve months, does not always allow for rapid response to identified risks.⁷⁷⁵ Furthermore, delays are experienced in sharing information as every disclosure made under the law enforcement and prescribed taskforce exceptions require an SES officer to provide their approval.⁷⁷⁶

7.18 Fourthly, the exceptions to the tax secrecy provisions often prevent disclosing information to private sector entities even if such disclosures may protect the tax system from exploitation.

7.19 In addition to the limitation on the ATO's ability to make the above type of disclosures, other agencies may be limited in what they may disclose to the ATO. For example, telephone intercept information which is obtained pursuant to the *Telecommunications (Interception and Access) Act 1979* may only be shared with the ATO for the purpose of assisting the interception agency's investigations, such as those conducted by the AFP or ACIC. Accordingly, the raising of tax assessments, which is a tactic to disrupt criminal activities of organised crime, is not an available option. The Parliamentary Joint Committee on Law Enforcement had made recommendation that the ATO be allowed to use telephone intercept information for this purpose on the condition that the use be restricted to investigations conducted by prescribed taskforces.⁷⁷⁷

7.20 The ATO has indicated support for a project led by the Heads of Commonwealth Operational Law Enforcement Agencies (HOCOLEA) to propose a new stand-alone legislative scheme that would allow full information sharing by agencies tasked with combatting serious and organised crime.⁷⁷⁸ The ATO considers that having a stand-alone or singular regime would not only result in fewer legislative amendments, as only one Act would need to be amended, but the regime would also,

⁷⁷³ ATO, 'PGH Tax Crime Reform – Response to Productivity Commission inquiry into Data Availability and Use' (Internal ATO Document, undated) pp 1-2.

⁷⁷⁴ *ibid.*, p 2.

⁷⁷⁵ ATO, 'Operational Examples on Information Sharing For Serious & Organised Crime' (Internal ATO Document, 23 December 2014) p 7.

⁷⁷⁶ Above n 773, p 1.

⁷⁷⁷ Parliamentary Joint Committee on Law Enforcement, Parliament of Australia, *Inquiry into Commonwealth unexplained wealth legislation and arrangements* (March 2012) paras [3.116] and [3.118]-[3.121].

⁷⁷⁸ This project has been held in abeyance since 2016.

by focusing broadly on ‘serious and organised crime’ rather than specific sub-risks, lessen the need to constantly prescribe new taskforces as new risks emerge. The ATO is of the view that these efficiencies would have the additional benefit of reducing the risk of criminals being alerted to the direction of law enforcement activities due to the public nature of the legislative reform process.⁷⁷⁹

Information sharing with AUSTRAC

7.21 The ATO also receives information to assist in addressing external fraud from other agencies, such as AUSTRAC which operates as a specialist financial intelligence unit. During the 2013–14 financial year, it had provided information in about 20,931 ATO cases, resulting in \$358.3 million in additional tax raised.⁷⁸⁰

7.22 ATO officers are able to directly access the AUSTRAC database⁷⁸¹ which contains information about international funds transfer instructions, significant cash transactions, other suspicious transactions and cross border movements of physical currency. The insights drawn from the AUSTRAC data also identify money laundering and larger scale organised fraud.

7.23 AUSTRAC may also provide data relating to groups of individuals or entities linked by a particular industry, risk or region as well as intelligence reports upon request. Such requests are made by the ATO after consultation with AUSTRAC to ensure that duplicated requests are minimised.⁷⁸²

Information sharing with international entities

7.24 The ATO exchanges information with other countries that have entered into tax treaties or information exchange agreements with Australia and may use such information to prevent and detect fraudulent activities which have an offshore element. The response times for requests made under such agreements are typically provided within three to six months, however, timeframes may vary according to partner agency policies and relevant law. Australia has such agreements with over 100 jurisdictions.⁷⁸³ However, there are a few countries that Australia does not have a tax treaty with, including those in tax secrecy jurisdictions. Accordingly, the challenges with obtaining visibility over certain offshore information remains.

7.25 More broadly, the ATO’s work with the OECD to improve international information sharing include participating in forums such as the Joint International Taskforce on Shared Information and Collaboration (JITSIC) Network which has proven useful in addressing the invisibility of offshore information to local revenue authorities. For example, the release of the ‘Panama Papers’ has highlighted the importance of international collaboration between revenue authorities in order to

⁷⁷⁹ Above n 775, p 7.

⁷⁸⁰ AUSTRAC, ‘AUSTRAC: Australia’s financial intelligence unit’ (17 August 2015) <www.austrac.gov.au>.

⁷⁸¹ *Anti-Laundering and Counter-Terrorism Financing Act 2006* s 125.

⁷⁸² ATO communication to the IGT, 12 February 2018.

⁷⁸³ ATO, ‘Exchange of information under Australian tax treaties’ (Internal ATO document, 25 June 2014).

obtain relevant information for identification and investigation.⁷⁸⁴ Similarly, the release of the 'Paradise Papers' highlighted the 'commoditisation' of tax avoidance and the services offered by 'facilitators' and the need for international collaboration to analyse large data sets.⁷⁸⁵

7.26 Furthermore, the introduction of international transparency measures such as the Common Reporting Standard (CRS)⁷⁸⁶ and the US Foreign Account Tax Compliance Act⁷⁸⁷, where offshore account information is exchanged between jurisdictions, is expected to significantly reduce opportunities to evade tax. For example, the CRS is a global standard for the collection, reporting and exchange of financial account information on foreign residents for tax purposes. Under the CRS, banks and other financial institutions collect and report financial account information of non-residents to their revenue agencies. Such information may then be exchanged amongst these revenue agencies.

7.27 The ATO has also sought to identify alternative channels to share relevant information with international agencies. For example, in April 2018, the ATO had commenced a trial of its use of the Financial Criminal Investigation Network (FCINet) platform which allows international partner agencies to establish the existence of relevant information before formally requesting such information under an exchange agreement. The FCINet platform is a technology-based information sharing initiative led by the Belastingdienst (Dutch Taxation Office) and the HMRC and has been used in the European Union for over a decade. The ATO is also exploring the possibility of using the FCINet platform as a channel to facilitate information sharing with members of the SFCT, such as the ACIC and AUSTRAC, and their international counterparts.⁷⁸⁸

Working with law enforcement

Referrals to the AFP

7.28 There are three ways in which the PGH business line can refer a matter to the AFP for criminal investigation. First, a referral may be made to the ATO-led SFCT, which is the taskforce⁷⁸⁹ responsible for identifying and addressing the most serious and complex financial crimes. Formed on 1 July 2015, the SFCT comprises the AFP, ACIC, AGD, AUSTRAC, ASIC, CDPP and Australian Border Force (ABF) as well as the ATO. The Government has allocated \$127.6 million to the SFCT over four years to lead the Commonwealth's operational response to high-priority serious financial crimes which currently include phoenix fraud, trust fraud and international tax evasion fraud.⁷⁹⁰ Serious financial crimes that align with these priorities will be referred by the

⁷⁸⁴ See Appendix F.

⁷⁸⁵ See Appendix G.

⁷⁸⁶ *The Tax Laws Amendment (Implementation of the Common Reporting Standard) Act 2016*; ATO, 'Common Reporting Standard' (5 June 2017) <www.ato.gov.au>.

⁷⁸⁷ *The Tax Laws Amendment (Implementation of the FATCA Agreement) Act 2014*; ATO, 'Foreign Account Tax Compliance Act reporting' (6 February 2018) <www.ato.gov.au>.

⁷⁸⁸ ATO communication to the IGT, 5 March 2018.

⁷⁸⁹ Note: The SFCT sits within the FAC Centre which is a prescribed taskforce under *Taxation Administration Regulations 2007* reg 67.

⁷⁹⁰ AFP, 'Serious Financial Crime Taskforce' (August 2015) <www.afp.gov.au>.

PGH business line to the SFCT Treatment Forum which operates as the gateway into the SFCT. If the referral requires the AFP's investigative resources, it will be evaluated by the SFCT Treatment Forum. Through its representation on the Forum, the AFP will determine its capacity to accept the matter for criminal investigation. The AFP only accepts SFCT-related referrals through this process.

7.29 Secondly, the PGH business line may send a referral to the AFP-led Fraud and Anti-Corruption Centre (FAC Centre) where the referral relates to allegations of corruption by a Commonwealth official, the bribery of a foreign official by an Australian entity or a serious and complex fraud perpetrated against a Commonwealth system or program. In the case of fraud, ATO referrals to the FAC Centre may only be made where they do not fall within the remit of other taskforces, including the SFCT, or where the ATO does not have the capability to investigate the allegations.

7.30 Thirdly, PGH may refer a matter to the AFP-led CACT which is a prescribed taskforce that conducts investigations to trace, restrain and confiscate property in accordance with the *Proceeds of Crime Act 2002*, if all of the standard ATO debt recovery options have been exhausted and there is evidence that existing assets have been gained from fraudulent activity.⁷⁹¹

7.31 Since 1 July 2015, the Tax Crime Forum has approved a total of nine referrals to the SFCT Treatment Forum, CACT Case Management Forum or the FAC Centre and all such referrals were accepted.

7.32 In November 2017, the ATO introduced a Complex Investigations Model (CIM) which changed the ATO's internal process for making referrals to the AFP.⁷⁹² These changes were aimed at addressing some of the issues with the previous processes as well as feedback which had suggested that there were consistent weaknesses in ATO referrals to the AFP, often resulting in protracted assessment times and the need for the ATO to rework its referrals.⁷⁹³

7.33 Prior to the introduction of the CIM, all cases which potentially required the AFP's involvement were routed to the Tax Crime Forum within PGH. As previously mentioned, it is the forum's responsibility to assess and approve such referrals with the aim of ensuring that only matters of priority are referred to the AFP or the relevant taskforce. Once it has approved a referral, the relevant business line has the responsibility of preparing a referral package to the appropriate external forum which may be the SFCT Treatment Forum, the FAC Centre, or the CACT's Referral Forum.

7.34 Under the new CIM, if an approved referral is subsequently determined to require further work, it will be sent to the newly created ATO Case Development Team (CDT) within the PGH business line. The CDT includes ATO investigators, tax

⁷⁹¹ ATO, 'PGH Instruction 2015/03 - The Proceeds of Crime Act 2002: Guidance on policy and procedure' (Internal ATO Document, 24 August 2016).

⁷⁹² ATO, 'AC Message - Complex Investigation Unit operationalised' (Internal ATO document, 8 November 2017).

⁷⁹³ ATO, 'PGH CLT Complex Investigations Model Project Outline' (Internal ATO document, 28 October 2016) p 6.

technical specialists and a forensic accountant. It is responsible for assessing and developing complex tax crime referrals to the AFP and associated taskforces. Whilst the referring business line will engage with the CDT and provide assistance, the latter will 'build' the referral request and, with the authority of the Tax Crime Forum, present it to either the SFCT Treatment Forum or the CACT Referral Forum.⁷⁹⁴

7.35 Where the CDT is considering a request for referral to the SFCT Treatment Forum, the AFP will discuss and consult on the proposed referral with the CDT. The allocation of AFP resources to engage in this consultation will occur following negotiation with the AFP National Coordinator – Fraud. This early engagement is intended to allow prospective complex referrals to be more effectively triaged, encouraging subsequent efforts to be only directed to referrals with greater merit.⁷⁹⁵ The ATO envisions that this model will lead to more effective processing of complex crime type referrals.⁷⁹⁶

7.36 In situations where the FAC Centre, SFCT or CACT does not accept a referral that had been submitted by the Tax Crime Forum, the Chair of that Forum, who is also a senior director in PGH, will ensure that the feedback is provided to the Forum members and CDT as well as the original referring risk owner and case officer.⁷⁹⁷

Complex Investigation Teams

7.37 At the same time the CIM was implemented, three Complex Investigation Teams (CITs) were established, comprising ATO investigators and tax specialists. Two CITs are based in the ATO and either work on ATO-only complex matters or jointly with the AFP on SFCT matters.⁷⁹⁸ A third team is located within an AFP office.⁷⁹⁹ It is intended that forensic accountants will be recruited into the CITs in future.

7.38 The CITs were established as a result of an ATO-AFP agreement following a recent review of the ATO's investigative structure. It was intended that three joint investigation teams would collaborate on SFCT-accepted investigations with the aim of providing a more agile response whilst taking into account each agency's existing resources.⁸⁰⁰

7.39 One of the reasons for conducting the review of the ATO's investigative structure was to address potential impacts on the treatment of financial crime that were perceived to have arisen from the AFP's resources being devoted to a range of non-tax priorities, such as national security and counter terrorism. For example, whilst the ATO was concerned that the AFP may have previously committed additional resources

⁷⁹⁴ *ibid.*, pp 6 and 9.

⁷⁹⁵ AFP communication to the IGT, 27 April 2018.

⁷⁹⁶ Above n 793, p 7.

⁷⁹⁷ ATO, 'Tax Crime Forum Charter' (Internal ATO document, July 2017) p 2.

⁷⁹⁸ Above n 795.

⁷⁹⁹ ATO communication to the IGT, 8 May 2018.

⁸⁰⁰ SFCT CEO Steering Group, '2017 Impact Assessment' (Internal SFCT document, 22 September 2017) p 3.

over and above the SFCT funding, the ATO believed that the AFP's current capacity to continue to do so had been 'greatly diminished'.⁸⁰¹

7.40 Under the current arrangements, the AFP is funded to provide 20 FTE agents to the SFCT, including investigators, management and coordination staff, technical and specialist support. It should be noted that the AFP employs a strategy that ensures the allocation of resources is flexible enough to direct its resources to activities which are likely to have the greatest impact on criminal networks and security threats. For example, the AFP can redirect its resources to high priority matters when needed, such as by providing a 'surge capacity' when such matters move into significant overt phases and by providing specialist or technical capabilities when required. In 2016-17, however, this approach resulted in the AFP dedicating an average of 37 FTE agents to SFCT investigations. The AFP reports that it has maintained a similar average FTE contribution to SFCT investigations in 2017-18.⁸⁰²

7.41 It has also been noted that, in 2017, the SFCT had expanded its priorities beyond phoenix, offshore tax evasion and trusts risks to also include a focus on research and development fraud, precious metals and junket tour operators. However, due the competing demands on the AFP's investigative capability and the AFP's provision of more resources to SFCT investigations than that for which they are funded, 'only in exceptional circumstances is there likely to be criminal investigations progressed outside of phoenix and offshore tax evasion'.⁸⁰³

7.42 It is envisioned that the CIM model, including the CITs, will allow the ATO to play a larger role in assisting the AFP and result in more effective collaboration between the agencies. Furthermore, although agreement has not yet been reached with the AFP, the ATO aims to improve its capability to identify, assess and address complex fraud by, for example, CITs being led by AFP team leaders with direct access to the AFP's management systems and investigative tools.⁸⁰⁴

Evidence gathering for criminal matters

7.43 In addition to calling on the AFP's investigative capability, the ATO may also request the AFP's assistance to gather evidence for the ATO's own investigations. A common type of assistance requested by the ATO is for the execution of a search warrant by a police constable under section 3E of the *Crimes Act 1914*. Unlike referrals for criminal investigation, which must be routed through the Tax Crime Forum, PGH officers may apply directly to an AFP Operations Monitoring Centre for search warrants to assist with their investigations.

7.44 Approximately 85 per cent⁸⁰⁵ of search warrants applied for by the ATO are typically executed on disinterested third-party record holders, such as banks, who are willing to compile and provide the requested documents to the ATO investigator but have confidentiality constraints in making such disclosures without being compelled

⁸⁰¹ *ibid.*, p 2.

⁸⁰² Above n 795.

⁸⁰³ Above n 800, p 3.

⁸⁰⁴ Above n 793, pp 7 and 9.

⁸⁰⁵ ATO, 'Bank Warrant Project Table' (Internal ATO document, undated).

by law to do so (so-called 'friendly warrants').⁸⁰⁶ Although the ATO has compulsory information gathering powers under the TAA, they may not be exercised for criminal investigation purposes.⁸⁰⁷

7.45 The ATO's view is that the requirement to engage a police constable to execute a friendly warrant is disproportionate as it imposes an unnecessary drain on the AFP's resources. Each search warrant, on average, takes an AFP officer approximately 8 hours of work and, if there are competing AFP priorities, may also delay ATO investigations by one to four weeks. Accordingly, the ATO has suggested an alternative power could be provided which allows the ATO to compel a 'friendly' third party to provide documents for criminal investigation purposes, subject to review by a magistrate (proposed production order power).⁸⁰⁸

IGT observations

7.46 To effectively address external fraud, a well-coordinated whole-of-government response is required as no single agency has the requisite knowledge, skills, resources and powers to deal with the sophisticated arrangements that may be in place. As noted by the OECD, 'an effective framework for domestic interagency cooperation' is one of the ten principles that should be implemented to effectively address tax crime.⁸⁰⁹

7.47 Government agencies often operate discretely having designated legislative responsibilities as well as allocated budgets to fulfil those responsibilities. Such an approach to the organisation of the public service allows for the 'rational and efficient grouping of issues, clarity of focus to support a strong results orientation, and an effective basis for accountability and resource allocation'. However, it is not well-suited to handling problems that transcend the boundaries of each agency's responsibilities (so-called 'wicked problems').⁸¹⁰ For example, fraudulent activities in the perpetration of organised crime typically violate a number of different laws which are administered by a number of agencies. In these circumstances a whole-of-government approach is required which must be achieved through effective collaboration given the relative autonomy of the agencies.

⁸⁰⁶ ATO, 'Soft Warrants - ATO discussion paper' (Internal ATO document, 10 January 2014).

⁸⁰⁷ ATO communications to the IGT, 12 February 2018 and 3 May 2018.

⁸⁰⁸ Above n 806, pp 2 and 12.

⁸⁰⁹ OECD, *Fighting Tax Crime: The Ten Global Principles* (2017) p 57.

⁸¹⁰ Management Advisory Committee, *Connecting government: whole of government responses to Australia's priority challenges* (2004) pp 45 and 49.

Information sharing

7.48 An essential element for an effective whole-of-government approach is information sharing.⁸¹¹ It is one of the major strategies that government agencies can adopt to maintain a level playing field with those involved in external fraud which is inherently multi-faceted and difficult to detect. According to the OECD:

In the course of their activities, different government agencies collect and hold information on individuals, corporations and transactions which may be directly relevant to the activities of other agencies in combating financial crime. Mechanisms to enable this information to be shared improve the prevention and detection of financial offences, enable investigations to be conducted more effectively and efficiently, result in faster and more successful prosecutions, and increase the likelihood of the proceeds of crime being recovered.⁸¹²

7.49 Effective information sharing is essential to agencies' abilities to appropriately assess and manage their own risks as well as those of interagency taskforces. However, any such information exchange must be balanced against considerations of privacy and confidentiality.

7.50 Not only is there a general requirement to protect the privacy of individuals, which is a human right protected by the *Privacy Act 1988 (Cth)* and by Article 12 of the *Universal Declaration of Human Rights*, but government agencies also operate within the confidentiality constraints imposed by their respective secrecy provisions. For example, the tax law secrecy provisions aim to encourage taxpayers to provide fulsome and accurate information about their financial affairs to the ATO by restricting what information ATO officers may disclose and to whom.

Information sharing within a prescribed taskforce

7.51 As mentioned earlier, prescribed taskforces, such as the FAC Centre, are currently the most effective environment for the ATO to share information with other agencies as the latter may use such information for broader purposes.⁸¹³ However, there is still room for improvement even in this context. For example, the time taken to establish a prescribed taskforce may be too long and there are limitations on information that taskforce agencies may disclose to each other.

7.52 Timeframes for establishing a prescribed taskforce could be shortened by authorising a statutory office holder, such as the Commissioner of Taxation, to establish a prescribed taskforce by way of tabling a disallowable instrument in Parliament. However, such authorisation may operate to compromise the important Parliamentary oversight arrangements which operate as a safeguard against excessive executive power. Furthermore, any such process would require the relevant agencies to resource the taskforce out of their existing departmental expenditure as any additional appropriation from the Consolidated Revenue would require Parliamentary approval through the budget process.

⁸¹¹ *ibid.*, p 1.

⁸¹² OECD, *Effective inter-agency co-operation in fighting tax crimes and other financial crimes* (3rd ed, 2017) p 13 <www.oecd.org>.

⁸¹³ Explanatory Memorandum, House of Representatives, Tax Laws Amendments (2007 Measures No.1) Bill 2007 para [1.10].

7.53 Whilst the ATO is authorised to disclose more protected tax information to other agencies when it is for the purpose of a prescribed taskforce, these agencies are not similarly authorised to share any further information. As stated earlier, there is an exception to the tax law secrecy provisions, allowing the ATO to share more information but there are no corresponding provisions for the other agencies. All of the secrecy provisions of the legislation that apply to these other agencies would need to be amended to allow them to share correspondingly more information. However, such an approach may still not produce a consistent result given the varying legislative contexts. Furthermore, every time changes become necessary, all these pieces of legislation would have to be amended, potentially giving rise to more inconsistencies.

7.54 There are two other alternatives for improving information sharing within prescribed taskforces. One option is to consider introducing a stand-alone legislative regime that overrides the existing secrecy provisions and allows for full information sharing by agencies tasked with combatting serious and organised crime. While HOCOLEA has commenced a project that seeks to develop such an information framework, the project has been put on hold by the AGD since 2016. The ATO has been supportive of this proposed framework⁸¹⁴ and the IGT also believes that it has merit. However, such a stand-alone regime would be a significant undertaking, involving a large number of government agencies, and would need to be carefully balanced against the inherent potential for conflict with protecting citizens' privacy and right to confidentiality.

7.55 Another option for consideration would be to allow for real-time multi-lateral information sharing within designated information sharing centres or 'Fusion Cells.' A Fusion Cell builds on the idea of a prescribed taskforce but is distinguished from the taskforce in the sense that all members of the cell, as opposed to just the ATO, will be legislatively permitted to share information with other members for the purpose of the cell.

7.56 A Fusion Cell would differ from a prescribed taskforce in relation to the speed at which information is shared. Rather than relying on formal information requests, information sharing should instead occur at close to real-time speed so as to allow member agencies to quickly identify threats, predict targets' actions and develop response tactics. For example, the information sharing methodology that is currently used by AUSTRAC's Fintel Alliance allows for information sharing at a faster speed in the sense that each member has immediate access to their own agency's systems, can verbally request and divulge relevant information about entities of interest. Such an arrangement would allow conclusions to be drawn quickly, based on the totality of information that each member has contributed.⁸¹⁵ A similar information sharing methodology may be considered for adoption by the Fusion Cell.

7.57 While the Fusion Cell proposal is similar to that of the stand-alone regime in the sense that it may lead to a potential increase in exceptions to secrecy requirements,

⁸¹⁴ Above n 775, p 7.

⁸¹⁵ AUSTRAC, 'Fintel Alliance Launch' (8 March 2017) <www.austrac.gov.au>; The Fintel Alliance is a private-public partnership to combat money laundering and terrorism financing.

the key difference between the two is that the Fusion Cell is far less all-encompassing than a stand-alone information sharing regime. As the Fusion Cell concept would only permit information sharing within a specialised unit, the exceptions may be managed by limiting and naming the officers who participate in these cells. These officers could also be subject to additional reporting requirements so as to facilitate independent review by appropriate scrutineers.

7.58 Compared to the stand-alone legislative regime, it may be easier for the 'Fusion Cell' model to resolve the inherent conflicts with protecting confidentiality due to its more limited scale. However, the Fusion Cell model is faced with some of the same difficulties encountered by the current prescribed taskforce model. There may be a constant need to update or form new cells as new risks and sub-risks are identified. Accordingly, the potentially lengthy and public legislative and regulatory reform process to set up a new or expanded cell may not only restrict the ability to respond more rapidly to threats but may also alert target criminals to the areas where law enforcement agencies are focusing their attention. As both options present challenges, the IGT considers that the Government may wish to consider a broader review of the current interagency framework to determine the optimal model for information sharing between agencies.

Information sharing outside of a prescribed taskforce

7.59 Not all tax crime matters considered by the ATO will fit within the ambit of a prescribed taskforce or, if implemented, a Fusion Cell. Accordingly, it is also important to consider the disclosure of information to law enforcement agencies under the general law enforcement exception. As mentioned earlier, there are a number of limitations to making disclosures under this exception.

7.60 The IGT is of the view that, at least, some of the above limitations are necessary to prevent inappropriate disclosure of taxpayer information. For example, the limitation whereby disclosure can only be made to law enforcement agencies is an appropriate control as law enforcement officers belong to a specific class of personnel that possess the relevant security clearances and training as well as been found to be fit and proper persons. That is not to say that there would never be situations where disclosure to a non-law enforcement agency would be appropriate. However, this should be permitted on a case-by-case basis as opposed to a broad authority to making disclosure to a wide-range of agencies.

7.61 Given that disclosures are irreversible, the IGT also believes that the limitation requiring SES officer approval for certain disclosures is appropriate particularly in a non-prescribed taskforce environment.

7.62 A limitation which the IGT believes should be relaxed is one that has been identified by the Parliamentary Joint Committee on Law Enforcement regarding the ATO's use of telephone intercept information. The Committee has recommended that the ATO should be allowed to use such information where it was gained in the course of joint investigations by prescribed taskforces. The IGT agrees in principle with the Committee's recommendation and notes that it may not unduly infringe on civil liberties.

7.63 Currently, due to the intrusive nature of telephone intercepts, a high threshold must be met before a law enforcement agency can obtain an interception warrant. The above recommendation does not result in a relaxation of this threshold. It merely provides the opportunity for the ATO to potentially enforce taxation laws against individuals who are already the subject of a criminal investigation by a prescribed taskforce and where the threshold for an interception warrant has already been met. It is further observed that the issuing of tax assessments is both a timelier and less punitive treatment option compared to criminal prosecution.

Information sharing with AUSTRAC

7.64 The ATO has a memorandum of understanding and its own internal processes to prioritise and determine the appropriateness of the information it requests from AUSTRAC. The ATO could make greater use of AUSTRAC capabilities particularly its analytical expertise which it has been further developing more recently.⁸¹⁶

7.65 The ATO may also be able to more effectively exchange information with the private sector by engaging with AUSTRAC's Fintel Alliance. For example, the Fintel Alliance's work on the Panama Papers was critical to assisting the SFCT in identifying the flows of money and understanding how the offshore funds were repatriated into Australia. The distinguishing feature of the Fintel Alliance in this operation was the ability to engage the expertise and data of private sector financial institutions to provide a more holistic understanding of international and domestic flows of money.

Information sharing with international entities

7.66 As mentioned already, in recent years, there have been significant positive developments in terms of international collaboration to combat cross-border tax avoidance and fraud. In particular, the extent of information and intelligence sharing amongst revenue agencies has been encouraging following the revelations contained in the Panama Papers⁸¹⁷ and Paradise Papers⁸¹⁸. The next stage in the development of international collaboration should be for such matters to be uncovered by the revenue agencies rather than relying on whistleblowers and the media.

Agency risk management priorities, obligations and requirements

Shared purpose and funding

7.67 As mentioned earlier, the tension between the need for agencies to collaborate with each other and the need for each agency to manage their own risk priorities may result in an allocation of resources which is not optimal for achieving shared purposes, such as addressing sophisticated tax fraud. Experience has shown that such tension

⁸¹⁶ For example, AUSTRAC's improvements to its data lake and automated data integration: AUSTRAC, 'Submission to the Parliamentary Joint Committee on Law Enforcement', *Inquiry into the impact of new and emerging ICT*, January 2018, p. 9.

⁸¹⁷ See Appendix F.

⁸¹⁸ See Appendix G.

may be somewhat alleviated by providing agencies with funding that is separate from their usual budget appropriations to allow each agency to commit resources without being constrained by their existing risk management priorities. For example, the SFCT was funded by a budget measure which allocated funds to the ATO who then distributed agreed amounts to the members of the SFCT on an annual basis.⁸¹⁹

7.68 The provision of separate government funding for the SFCT, however, may not be sufficient to guarantee an appropriate allocation of resources to member agencies. First, there are risks with inaccurately predicting the resources needed, given the difficulty in identifying the extent of fraudulent activities and member agencies' competing priorities. For example, the AFP had been allocating resources to the SFCT beyond the funding provided to address 'a larger than anticipated volume of high priority tax crime risks' detected by the ATO. However, when the AFP was required to utilise those additional resources for its own priorities, the SFCT was forced to re-prioritise the types of cases it would investigate. As a result, alternative investigative models were explored.⁸²⁰

7.69 Secondly, where the budget appropriation is allocated to one agency and distributed to the member agencies, it is possible that the former unduly influences the focus of the taskforce's activities towards risks it considers to be the most important according to its own priorities. One option to mitigate the undue influence of one member agency is to adopt the SFCT approach where the key priorities of the latter were based upon the assessments conducted by the ACIC and the AFP authorisation of its investigatory resources.⁸²¹ Another option would be to appoint an independent leader, tasked with achieving a prescribed objective, similar to a Special Prosecutor used in the investigation of frauds and tax offences in the 1980s.⁸²² However, such an approach may compromise the independent statutory functions of the relevant agencies particularly if such a leader has a degree of control over the deployment of their resources. Accordingly, the level of power or control afforded to such a leader must be carefully considered. One option would be for the leader to have budgetary control and strategic design responsibilities whilst the relevant agencies retain control over their operational resources.

Specialist capability

7.70 As mentioned earlier, no single agency has the requisite knowledge, skills, resources and powers to address the sophisticated arrangements that may be employed by those perpetrating fraud. Collaboration is needed between the agencies rather than one agency attempting to perform tasks which another agency has the specialist capability to perform. The latter approach would give rise to significant risks.

⁸¹⁹ Australian Government, *Budget Paper No 2* (12 May 2015) p 30; ATO, 'Serious Financial Crime Taskforce annexure to the Fraud and Anti-Corruption Centre memorandum of understanding' (Internal ATO document, 1 July 2015) p 2.

⁸²⁰ Above n 800, pp 2-3.

⁸²¹ ATO, 'Serious Financial Crime Taskforce annexure to the Fraud and Anti-Corruption Centre memorandum of understanding' (Internal ATO document, 1 July 2015) p 4; ACIC, *Serious Financial Crime in Australia 2017* (2017) <www.acic.gov.au>.

⁸²² See, for example, *Special Prosecutors Act 1982* (Cth).

For example, although an ATO investigator may have significant law enforcement specialist capability, the absence of corresponding institutional safeguards may expose that officer and the ATO to a range of risks including corruption.⁸²³ Such risks may also include the investigator's brief of evidence, to the CDPP, being either incomplete or unwittingly tainted. To address the latter risk, the CDPP's expertise, in relation to which cases to prosecute and the type of evidence required, could be sought earlier in the process.

7.71 In collaborating with other agencies, requests from one agency to another for specialist work to be undertaken may compete with the latter's own priorities. Accordingly, the two agencies should consult and reach an agreement on the relative priorities and where certain work cannot be undertaken, alternatives should be identified. For example, the AFP has the 'primary law enforcement responsibility' to investigate serious or complex fraud⁸²⁴, whereas the ATO retains responsibility to investigate some tax fraud matters.⁸²⁵

7.72 For the most serious tax fraud matters, the SFCT referral process, described earlier, determines which matters should involve the use of the AFP's investigatory capability for identified high-priority areas. Although all ATO referrals to the SFCT have been accepted for investigation, the AFP has experienced demand for its capability beyond SFCT allocation. Recent efforts to reduce this demand on AFP resources have resulted in the ATO and AFP agreeing to implement the CIM model which is aimed at improving the quality of ATO referrals to the SFCT as well as the ATO's capability to conduct complex criminal investigations jointly with the AFP.

7.73 In the IGT's view, the above recent measures are positive steps which should be reviewed and evaluated in due course. However, further opportunities should also be sought to further improve interagency collaboration with enhancement to the taskforce model being one option.

Evidence gathering

7.74 There is opportunity to reduce the ATO's demand on the AFP's powers to execute search warrants under section 3E of the *Crimes Act 1914 (Cth)* as 85 per cent of the warrants sought by the ATO are so-called 'friendly warrants' which are served on third party record holders such as financial institutions.⁸²⁶ In the main, these types of warrants address the latter's concerns with confidentiality constraints⁸²⁷ and do not pose major safety risks. In the IGT's view, providing the ATO with the power to require such third parties to produce the required records for criminal investigation purposes would expedite matters and allow AFP resources to be directed to more specialist functions. Any concerns with the ATO's exercise of such a power could be appropriately addressed by requiring the approval of a magistrate.

⁸²³ See above n 10, p 15.

⁸²⁴ Above n 21, para [73].

⁸²⁵ Above n 18, para [71].

⁸²⁶ Above n 805.

⁸²⁷ Above n 806.

RECOMMENDATION 7.1

The IGT recommends that Government consider a broad review of the current arrangements for interagency collaboration for combating tax fraud including the following key issues:

- a) optimal models for information sharing between agencies;*
- b) the extent to which specialist capabilities should be shared amongst agencies and mechanisms to ensure that each agency has appropriate access to such capabilities;*
- c) structure and funding for interagency taskforces including whether they should be headed by an independent leader with appropriate powers and secretariat;*
- d) permitting the ATO to use telecommunication interception information obtained in joint investigations of prescribed taskforces in raising assessments for those who are subjects of such investigations; and*
- e) in appropriate circumstances, allowing the ATO to issue production orders to third parties such as financial institutions who hold relevant information about persons or transactions of interest.*

ATO RESPONSE

Matter for Government

APPENDIX A – TERMS OF REFERENCE

Background

On 20 June 2017, [the Committee] requested that the Inspector-General of Taxation (IGT) examine how the Australian Taxation Office (ATO) addresses the risk of fraud and associated issues. This request follows recent events including those relating to Operation Elbrus and allegations of tax fraud that may be linked to abuse of position by a public official.⁸²⁸ These events have attracted significant media attention and have led to calls for an independent review of the ATO's fraud control framework and, particularly, how it responds to inappropriate behaviours by its own staff.⁸²⁹

The IGT appreciates the Committee's concerns and the need to provide the community with independent assurance that the tax system is administered with high levels of integrity. Accordingly, on 27 June 2017, the IGT accepted the Committee's request and has commenced this review.⁸³⁰

Australia's democratic system of government consists of robust checks and balances which at the highest level includes the Parliament and its committees. Independent scrutineering agencies, such as the IGT, complement such Parliamentary oversight through in-depth investigation and public reporting providing greater transparency and increased community confidence in the integrity of the system. It is in this context that the IGT has accepted the Committee's request.

As a general rule, government regulators, including tax authorities, must operate, and be seen to operate, with the highest levels of integrity in order to legitimatise their authority, maintain the confidence and trust of those who they regulate and thereby elicit voluntary compliance.⁸³¹ The community rightly expects such authorities and their officials to fulfil their responsibilities as trusted stewards of public funds and make every effort to protect public resources.⁸³² There are also legal obligations that require them to take 'all reasonable measures to prevent, detect and deal with fraud'.⁸³³ Robust governance frameworks, regular risk assessment and fraud controls along with a culture that promotes ethical behaviour are necessary to appropriately address risks of fraud, corruption and abuse of power.⁸³⁴

⁸²⁸ AFP, 'AFP smashes \$165 million tax fraud syndicate' (Media release, 18 May 2017).

⁸²⁹ Jacob Greber, 'Too early for probe into ATO amid fraud fallout', *AFR*, 21 May 2017; Noel Towell, 'Favours granted': ATO's Michael Cranston let taxpayer off prosecution hook', *Canberra Times*, 30 May 2017; Rachel Olding, 'ATO deputy commissioner Michael Cranston suspended during criminal probe', *SMH*, 13 June 2017.

⁸³⁰ This review is conducted under paragraph 8(3)(d) of the *Inspector-General of Taxation Act 2003*.

⁸³¹ Eva Hofmann, Katharina Gangl, Erich Kirchler and Jennifer Stark, 'Enhancing tax compliance through coercive and legitimate power of tax authorities by concurrently diminishing or facilitating trust in tax authorities' (2014) 36(3) *Law and Policy* pp 290-313.

⁸³² AGD, *Resource Management Guide No. 201 – Preventing, detecting and dealing with fraud* (July 2014) p 5.

⁸³³ *Public Governance, Performance and Accountability Rule 2014* s 10.

⁸³⁴ OECD, *G20/OECD Principles of Corporate Governance* (2015) pp 13, 46-50; Colin Ferguson, 'Fraud in Australia' (2012) 12 *University of Melbourne Faculty of Business and Economics Insights* pp 47-51; Dr. Adam Graycar, AIC, 'Fraud prevention and control in Australia' (Paper presented at the Fraud Prevention and Control Conference), Surfers Paradise, (24-25 August 2000) p 4.

The Commonwealth Government's multi-layered fraud control framework involves a range of individual agencies being responsible for performing specific roles. The development of the fraud control framework is overseen by the Attorney-General's Department⁸³⁵, including the overarching Commonwealth Fraud Control Policy⁸³⁶, the Fraud Rule⁸³⁷ and related guidance.⁸³⁸ Individual agencies determine their own specific practices, plans and procedures to manage the prevention and detection of fraudulent activities.⁸³⁹ The interaction of these layers may also involve a range of legislative acts and government agencies such as the AFP (for investigation of serious and complex internal and external fraud) and the Commonwealth Director of Public Prosecutions (for prosecuting offences).⁸⁴⁰

As a key institution in the Australian economy, the ATO administers tax laws and other legislation which affects some 13.4 million individuals and 3.1 million businesses.⁸⁴¹ The ATO also administers a significant portion of the superannuation system, which impacts the Australian communities' retirement savings, as well as other non-tax regimes such as excise, numerous grant schemes, the Higher Education Loan Program and the Agricultural Land Register. These functions are performed by some 20,600 employees under the leadership of four statutorily appointed Commissioners.⁸⁴²

In addition to collecting approximately 80 per cent⁸⁴³ of total net revenue in Australia (\$342 billion in 2015-16)⁸⁴⁴, the ATO is one of the largest repositories of valuable, often sensitive, financial information which is also used by other government bodies to determine eligibility for social support services such as pensions and child support.

The magnitude and importance of the ATO's role, both economically and socially is unparalleled in the Australian context and hence, it is not surprising that the community expects very high standards of integrity from its staff and the organisation as a whole. The ATO itself has acknowledged that its 'integrity is fundamental to maintaining community trust and confidence in the tax and superannuation systems'.⁸⁴⁵

Accordingly, in this review, the IGT will examine the ATO's fraud prevention and detection policies and how they are practically applied to ensure that its practices reflect the standards befitting of such a key institution. In doing so, the IGT will seek to engage and consult with the relevant Commonwealth agencies involved in the fraud control framework to draw upon their insights as well as minimise any overlap. The IGT is also mindful of not prejudicing any relevant court proceedings.

The terms of reference of this review, as established by the Committee, are set out below followed by guidance on preparing and lodging submissions, together with assurance that such submissions would be maintained in strict confidence by the IGT.

⁸³⁵ The AGD is responsible for coordinating fraud control policy: AGD, 'Fraud Control' (28 June 2017).

⁸³⁶ AGD, *Commonwealth Fraud Control Policy* (30 August 2016).

⁸³⁷ *Public Governance, Performance and Accountability Rule 2014*, s 10.

⁸³⁸ Above n 836; above n 832.

⁸³⁹ Above n 836, p C6.

⁸⁴⁰ *ibid.*

⁸⁴¹ Commissioner of Taxation, *Annual Report 2015-16* (2016) p12.

⁸⁴² *ibid.*, p 86.

⁸⁴³ Australian Bureau of Statistics, '5506.0 - Taxation Revenue, Australia, 2015-16' (issued 27 April 2017).

⁸⁴⁴ Above n 841, p 38.

⁸⁴⁵ ATO, 'Integrity' (accessed 28 June 2017) <www.ato.gov.au>.

Terms of reference

The terms of reference from the Committee's request are reproduced below:

A review to examine how the Australian Taxation Office addresses the risk of fraud and associated issues, including:

- *the practices, procedures and structures to detect and act on fraudulent activity or potentially fraudulent activity, with a focus on staff conduct;*
- *whether risk assessment techniques for identifying fraudulent activity or potentially fraudulent activity are adequate, with a focus on staff conduct; and*
- *potential improvements to the practices, procedures and structures to detect and act on fraudulent activity or potentially fraudulent activity.*

The IGT may also examine other relevant concerns or potential improvements, including those that may be identified during the course of the review.

Submission guidelines

All IGT reviews seek input and views from a wide range of stakeholders and are conducted openly and independently. This approach is particularly important in this review given the serious nature of fraud and its impact on public confidence.

Fraud can be defined as 'dishonestly obtaining a benefit, or causing a loss, by deception or other means'.⁸⁴⁶ Fraudulent activities may include, but are not limited to, theft, misappropriation of funds, wrongfully using Commonwealth information (for example, taxpayer records) or unauthorised provision of access to or disclosure of sensitive information.⁸⁴⁷

The risk of fraud may arise from inside the agency (its officials or contractors) or outside of the agency (taxpayers or service providers)⁸⁴⁸ and may vary depending on their potential exposure to fraud.⁸⁴⁹ As this review has arisen largely because of fraud allegations that may have been linked to ATO officers, there would be a focus on fraudulent behaviour within the ATO. However, as internal fraud may involve or be part of a broader scheme involving external parties, the review may have to consider other forms of fraud such as phoenix activities and related director identity issues.

Those areas of the ATO which investigate fraudulent or potentially fraudulent activities of taxpayers, for example the PGH area⁸⁵⁰, may face higher risk of internal fraud and are likely to be an area of particular focus in this review. As noted earlier, those ATO personnel, who may be linked to Operation Elbrus, were high ranking officers within PGH.⁸⁵¹ PGH has also

⁸⁴⁶ AGD, *Commonwealth Fraud Control Framework* (2014) p C7.

⁸⁴⁷ Above n 832, p 8.

⁸⁴⁸ *ibid.*

⁸⁴⁹ Above n 846, p C10.

⁸⁵⁰ The ATO merged its ATP and SNC areas into the PGH area [which itself was operational by 7 July 2014].

⁸⁵¹ Above n 353, pp 9–17.

led major programs such as the Project DO IT tax amnesty⁸⁵² and has the carriage of the ATO's responsibility with respect to the Government's interagency Phoenix Taskforce.⁸⁵³

More broadly, this review will examine the ATO's practices, procedures and structures to prevent, detect and address fraudulent or potentially fraudulent activities including the use of diagnostic and mitigation tools and how risk management is embedded into its operations and business processes. The review will also consider the cultural or behavioural aspects within the ATO and how the policies are communicated and enforced within the organisation.

The IGT welcomes submissions from all interested members of the community, including tax and legal practitioners, fraud prevention specialists, current and former ATO officers as well as taxpayers. We envisage that your submission will outline your relevant experiences in dealing with the ATO, be it from an internal or external perspective. We would be particularly interested in any concerns you may have had about the conduct of ATO officers or contractors, its impact on you, whether you reported your concern to the ATO or any other body and the outcomes of such reporting. These experiences may include interactions in an audit or litigation setting.

In addition to international best practice standards, the IGT is also interested to hear about your expectations of the ATO fraud control framework and any opportunities for improvement, be they structural, procedural or behavioural.

Confidentiality

Submissions provided to the IGT are maintained in strict confidence (unless you specify otherwise). This means that the identity of the taxpayer and advisers as well as any information contained in submissions will not be made available to any other person, including the ATO. Section 37 of the *Inspector-General of Taxation Act 2003* safeguards the confidentiality and secrecy of such information provided to the IGT – for example, the IGT cannot disclose the information as a result of a Freedom of Information (FOI) request, or as a result of a court order generally. Furthermore, if such information is the subject of client legal privilege (also referred to as legal professional privilege), disclosing that information to the IGT will **not** result in a waiver of that privilege.

Lodgment

The closing date for submissions is 28 July 2017. Submissions can be sent by:

E-mail to: AFCM@igt.gov.au
Post to: Inspector-General of Taxation
 GPO Box 551
 SYDNEY NSW 2001
Fax: (02) 8239 2100

⁸⁵² ATO, 'Project DO IT - the deadline is fast approaching' (accessed 28 June 2017) <www.ato.gov.au>.

⁸⁵³ ATO, 'Phoenix Taskforce continues to put pressure on pre-insolvency industry' (accessed 28 June 2017); ATO, 'Inter-Agency Phoenix Forum minutes - 5 August 2015' (accessed 28 June 2017) <www.ato.gov.au>.

APPENDIX B – OPERATION ELBRUS

Introduction

A2.1 On 17 May 2017, the AFP publicly announced that over 290 AFP officers, assisted by ATO staff, had conducted a coordinated effort to execute 34 search warrants and seize approximately \$50 million of cash and assets from co-conspirators of an alleged ‘phoenix’ arrangement connected with a company, namely: Plutus Payroll Australia (Plutus). This action was the ultimate result of combining three independently commenced investigations by the ACIC, the AFP’s Operation Elbrus and the ATO’s Operation Crocodile into a single undertaking.

A2.2 On the same day, the ATO announced that disciplinary action had also been taken against ATO staff, including service of suspension orders on five officers and commenced investigations into potential breaches of the APS Code of Conduct by three officers.

A2.3 Following these events, the Senate Standing References Committee on Economics requested that the IGT undertake a review, the terms of reference for which are reproduced in Appendix A. The outcomes of the IGT review are outlined in the main body of this report.

A2.4 The issues covered in this review and the underlying nature of outworkings of Operation Elbrus is multi-faceted and complex. Therefore, in seeking to provide insight and facilitate understanding, the analysis that follows is not a simple chronology of events.

A2.5 Furthermore, the specifics of Operation Elbrus and the Plutus arrangements are being considered by the courts as part of criminal prosecutions. Therefore, a degree of generalisation has been necessary to ensure that the latter are not prejudiced in any way. There are also certain confidentiality constraints imposed by the relevant tax, law enforcement, privacy and employment laws that need to be considered regarding disclosures. Publicly available material is referenced where that is appropriate. In this regard, this appendix was provided to the AFP and CDPP for comment and confirmation that it could be made public.

Structure of the analysis

A2.6 The following analysis provides an initial overview of the Plutus arrangement in a more general sense along with the related themes, including the allegations and laying of charges. Thereafter, the individuals who are directly or indirectly linked or associated with the operation are noted. Finally, a chronology of events is provided through the prism of action taken by the relevant government agencies at a given point-in-time.

The 'Plutus' arrangement

A2.7 The Plutus syndicate arrangement provided for a 'zero-fee, fully automated, all-inclusive contractor payroll management service'⁸⁵⁴ for a large number of companies. The client companies had made regular payments to Plutus on the understanding that those funds, estimated by some to total \$1.3 billion⁸⁵⁵, would be used to pay the wages and superannuation of employees and also pay the ATO the required PAYG tax.⁸⁵⁶

A2.8 The syndicate arrangement had purportedly recruited 'straw directors' for a number of 'second-tier' or 'straw' companies whilst the management and operation of those companies was maintained by the syndicate members themselves. Plutus allegedly transferred payroll funds and a limited percentage of the PAYG tax to these second-tier companies. Accordingly, the PAYG commitments were only paid in part to the ATO.⁸⁵⁷ The AFP have alleged that the remaining funds had been transferred to the syndicate members through false invoices and the bank accounts of front companies. It was further claimed that the second-tier companies had kept records on the differences between the amount paid to the ATO and what the syndicate members received which, in May 2017, was thought to be \$165 million.⁸⁵⁸

A2.9 It is purported that the intention was to evade detection by the authorities and to dissipate the assets through use of a complex process under the insolvency laws if detected. These arrangements are commonly referred to as a type of 'phoenix' arrangement. It has been publicly commented that the fraud was not unusual in concept but was ambitious in scale:

Such advisors would have seen or advised on similar schemes and therefore gave it a go on a big scale, which was their mistake,' ... 'Too many people were involved with too big numbers and that is why they got caught this time.'⁸⁵⁹

A2.10 Clients were told that Plutus made money from the short term money market and not the payroll services. Accordingly, Plutus did not need to earn commission or fees on the work that was obtained from clients:

We are a financial services provider. Our biggest source of revenue is our outsourced payroll and payroll-funding options for dozens of businesses around the country. Also on the list of revenue contributors is mortgage brokerage. We source competitive mortgage rates (or car loans, personal loans etc) for our extensive customer base. 'There is no obligation to our contractors to take out any of these products, though they are all available to be used, if the

⁸⁵⁴ Chris Pash, 'What we know about Plutus Payroll, the company allegedly at the centre of Australia's biggest tax fraud', *Business Insider Australia* (online) 18 May 2017; See also archived website of Synep (2 November 2016) <<https://web.archive.org>>.

⁸⁵⁵ Fleur Anderson, Neil Chenoweth, Joanna Mather, and Geoff Winestock, 'The inside story of the \$165m scam on the ATO', *The Australian Financial Review* (online) 19 May 2017.

⁸⁵⁶ Nick Hansen, 'ATO scam: Tax boss Michael Cranston's alleged phone call to fraud accused son', *The Daily Telegraph* (online) 24 May 2017.

⁸⁵⁷ Daniel Peters, 'Tax Office boss Michael Cranston, 58, 'tried to cut a deal with senior colleagues to stop his son, 30, being investigated for his role in record \$165 MILLION fraud syndicate', *Daily Mail* (online) 18 May 2017.

⁸⁵⁸ Above n 856.

⁸⁵⁹ David Marin-Guzman, 'Plutus accused Simon Anquetil had phoenix activity form', *The Australian Financial Review* (online) 22 May 2017.

contractor so desires. It's a simple but effective business model that works for us, and for our contractors and clients.' The contractors' pay was supposedly invested on the overnight money market. The interest earned on the money market helped Plutus offer zero fees, the spiel went.⁸⁶⁰

A2.11 Furthermore, Plutus provided incentives to recruiters and contractors, including 'Plutus Points' – a monthly gift-card loyalty program equivalent to the amount contractors would have otherwise spent on other payroll agencies charging a two to three per cent fee.⁸⁶¹

A2.12 Recruitment companies were also reportedly paid amounts up to \$900 for each client they referred. Plutus was also reported to have wooed recruiters and government departments by inviting them to marketing events.⁸⁶²

A2.13 Plutus had offered contractors benefits as well, such as cheap mortgages, finance and insurance⁸⁶³ to persuade their recruiters to use Plutus' services.

A2.14 Where clients may have had doubts concerning the Plutus arrangements, they sought comfort from trusted third parties (well-meaning or otherwise) in assuaging their doubts. For example, contractors were assured by reputable third party recruitment firms that Plutus was part of the digital disruption in the contracting industry and could offer zero fees because the payroll business was just a very small part of a much larger business.

A2.15 Some of those with doubts had checked Plutus' credentials with peers on a chat forum which was frequented by IT contractors. Plutus was also reported to have engaged staff to assuage doubt.⁸⁶⁴

A2.16 It was not until the ATO began to garnish the bank accounts of some of the second-tier companies that doubts regarding Plutus' financial sustainability were publicly questioned. As this publicity threatened clients' confidence in Plutus, it was purported that the company took further measures to assuage the public and, behind the scenes, explore what they could do to avoid ATO action.

Overview of allegations

A2.17 During the investigations conducted by the agencies, it was revealed that two of the key participants in the syndicate were children of the ATO's Deputy Commissioner for the PGH business line who was also the Chair of the Government's Phoenix Taskforce⁸⁶⁵ and the public face of the 'crack down' on phoenix behaviour⁸⁶⁶.

⁸⁶⁰ Above n 855.

⁸⁶¹ *ibid.*

⁸⁶² *ibid.*

⁸⁶³ Geoff Winestock, 'Plutus Payroll's \$165m scam highlights risks of recruiter kickbacks', *The Australian Financial Review*, (online), 23 May 2017.

⁸⁶⁴ Above n 855.

⁸⁶⁵ Riley Stuart, 'ATO official Michael Cranston facing charges over son's alleged involvement in \$165m fraud', *Australian Broadcasting Corporation* (online) 18 May 2017.

A2.18 The PGH business line itself is the area in the ATO tasked with investigating 'those who criminally defraud the [tax] system or deliberately avoid their tax obligations' and, in doing so, collaborate with regulatory and law-enforcement agencies.⁸⁶⁷

A2.19 In Operation Elbrus, the AFP had also considered the potential involvement of an ATO Deputy Commissioner. However, immediately after the arrests, it was announced that, as a result of telephone intercepts, the AFP alleged that the Deputy Commissioner was not a party to the conspiracy and he 'was not suspected and is still not suspected of being involved in the syndicate and its activities of defrauding the Commonwealth'.⁸⁶⁸ The AFP further alleged, however, that the Deputy Commissioner's son had asked his father to make enquiries within the ATO regarding the status of ATO activities with respect to the Plutus arrangement and Mr Simon Anquetil.⁸⁶⁹

A2.20 The details of what actions were taken by the Deputy Commissioner are the subject of charges laid against him for two counts of 'abuse of public office' for allegedly obtaining information and exercising influence to obtain a benefit for his son. These charges are yet to be heard by the courts.

A2.21 Charges were also laid against eight other people on the basis that they were suspected of either participating as a 'controlling mind' or knowingly assisting the syndicate through the destruction of evidence and/or dealing with the proceeds of crime.⁸⁷⁰ The charges are outlined in more detail further below.⁸⁷¹

A2.22 The initial announcement by the AFP had quantified the potential fraud as being \$165 million in total. However, subsequent announcements reduced this figure to \$130 million. Others parties have claimed the amount to be higher as they believe that some members of the syndicate had been involved in previous phoenix arrangements which had, in total, allegedly defrauded the Commonwealth of \$191 million.⁸⁷² The latest figures provided by the ATO, state that the potential fraud approximates \$157 million in total.⁸⁷³

⁸⁶⁶ See, for example, ATO, 'Phoenix Taskforce cracking down on dodgy business behaviour', (Media Release, QC 49745, 29 July 2016); Simon Benson, 'ATO raids 12 major firms for fraud evidence', *The Daily Telegraph* (online) 10 June 2015.

⁸⁶⁷ Above n 7, p 59.

⁸⁶⁸ Above n 353, p 13 (Commissioner of Taxation).

⁸⁶⁹ AFP, Joint press conference with Acting ATO Commissioner of Taxation, AFP Headquarters, Canberra (17 May 2017); <www.Youtube.com>, 'AFP hold Press Conference to Discuss Bust of Tax Fraud Syndicate'.

⁸⁷⁰ Joanna Mather, 'The school buddies who became embroiled in \$165m ATO tax fraud', *The Australian Financial Review* (online) 24 May 2017.

⁸⁷¹ Paragraphs A2.88 and A2.99 in Appendix B outline the charges laid.

⁸⁷² Neil Chenoweth and David Marin-Guzman, 'Plutus payroll the \$191m Gen Y crime wave and the tax officer', *The Australian Financial Review*, 4 July 2017.

⁸⁷³ ATO communication to the IGT, 24 April 2018.

Main individuals of interest

A2.23 Having outlined the arrangements and the nature of the allegations raised, we now identify the main identities and how they are directly or indirectly linked with the arrangement or otherwise connected with each other as individuals.

Michael Cranston

A2.24 The Deputy Commissioner, Michael Cranston had started work for the ATO over 30 years prior and had risen through the ranks over that time. His first appearance in the senior management team occurred during 2005–06 when he had acted in the role of Deputy Commissioner, SME (Case Leadership) within the ATO's Compliance sub-plan and then permanently filled that position soon after.⁸⁷⁴

A2.25 In this role he had acquired considerable expertise in the practical and strategic application of deep technical knowledge to some of the more complex work in the ATO.⁸⁷⁵

A2.26 In the 2007–08 financial year, Michael Cranston was appointed as the Deputy Commissioner in charge of the SNC business line within the Compliance sub-plan.⁸⁷⁶ This followed publicity concerning a number of SNC officers who had allegedly engaged in corruption with one officer being suspected of having inappropriate links to the Melbourne underworld at the time.

A2.27 The SNC business line itself was formed several years earlier on 1 July 2003 by bringing together a number of different areas within the ATO that focused on tax audits involving an element of criminality, for example the 'Special Audit' unit which had focused on audits targeting organised crime. Through these early years each of the different areas were observed to have their own leaders and culture. During this period there had already been extensive efforts, including a number of internal reviews to address their structure, governance, management and culture as well as integrity standards. Notwithstanding those efforts, however, the prevention and detection of misconduct had remained incomplete.

A2.28 When Michael Cranston took charge of the SNC business line, he was met with substantial resistance from groups of disaffected staff who believed, for example, that the SNC Executive were incapable of understanding the work being conducted and were considered by them to lack understanding of the criminal environment. Officers of some of the other law enforcement agencies, at that time, had also expressed hesitation in sharing sensitive information with the ATO due to a number of events which had reflected poorly on the integrity of the ATO in dealing with the criminal element.

A2.29 In recent years, it has been said that Michael Cranston performed a key role in forging more cooperative relationships between the ATO and other law enforcement

⁸⁷⁴ Commissioner of Taxation, *Annual Report 2005–06* (2006) p 19; Commissioner of Taxation, *Annual Report 2006–07* (2007) p 167.

⁸⁷⁵ *ibid.*

⁸⁷⁶ Commissioner of Taxation, *Annual Report 2007–08* (2008) p 110.

agencies. For example, when the AFP would ask for ATO officer assistance in operations, Michael Cranston would hand pick whom he considered to be the most suitable ATO officer, given their skills and experience. He also played a key role in joint operations, most notably Project Wickenby and the Phoenix Taskforce of which he was Chair. Over the past few years, he had become the ATO's public face in relation to initiatives addressing tax crime.⁸⁷⁷

A2.30 Michael Cranston remained in his role as Deputy Commissioner of SNC until moving to the Deputy Commissioner role for the SME business line during 2011-12. The ATP, SNC and PGH (formerly SME and High Wealth Individuals) business lines were amalgamated in 2013-14 and Michael Cranston was appointed the head of the amalgamated business line—Deputy Commissioner of the PGH business line.⁸⁷⁸ In these roles, Michael Cranston had forged strong relationships with many staff, sometimes on a social level, and following the execution of the search warrants it was publicly stated that Michael Cranston had “quite an illustrious [career] up until this point”.⁸⁷⁹

A2.31 The suitability for, rotation of and concentration of responsibilities in senior roles, particularly those in high risk areas, are discussed in Chapters 3 and 5.

A2.32 As publicly reported, Michael Cranston has two children, Adam and Lauren, who are alleged members of the syndicate facing charges for conspiracy to defraud the Commonwealth.⁸⁸⁰

Adam Cranston

A2.33 Adam Cranston (Adam) obtained a Bachelor of Commerce at the University of Western Sydney and began his career at Rodgers Reidy Chartered Accountants as an insolvency accountant. There, he is reported to have worked in various fields of insolvency ranging from voluntary administrations, official liquidations, corporate voluntary liquidations and receiverships. Adam's online biography described his area of expertise whilst at Rodgers Reidy as forensic accounting. Adam also later worked in debtor finance sales with Fox Syme's 180 Corporate (180 Group) which specialised in business financing and short term loans for working capital requirements, including payments to meet statutory requirements.⁸⁸¹ At 180 Group he also performed a role as consultant to distressed businesses⁸⁸² which was a role that Mr Larcombe had also performed at the 180 Group.

⁸⁷⁷ ATO, 'Phoenix Taskforce continues to put pressure on pre-insolvency industry' (Media Release, QC 51654, 4 April 2017); Andrew White, 'Tax fraud scandal: Michael Cranston's 'illustrious career' shattered', *The Australian* (online) 19 May 2017.

⁸⁷⁸ See the annual reports of the Commissioner of Taxation for the 2006-07 to 2015-16 financial years.

⁸⁷⁹ Rachel Olding, 'Illustrious career on hold: Cranston suspended probe', *The Guardian* (online) (13 June 2017) <www.theguardian.com.au>

⁸⁸⁰ Paul Farrell, 'ATO fraud investigation: federal police freeze assets of 60 parties', *The Guardian* (online) 9 June 2017.

⁸⁸¹ Archived website of www.180businessloans.com.au (10 May 2006), <<https://web.archive.org>>.

⁸⁸² Aventis Capital website, <www.aventisgroup.com.au>.

Peter Larcombe

A2.34 Like Adam, Peter Larcombe had obtained a Bachelor of Commerce at the University of Western Sydney. Unlike Adam, however, Mr Larcombe began his career as a quantity surveyor for projects throughout Europe and as a residential and commercial real estate valuer for assets throughout the Sydney basin. He was an investment manager for Rubicon's Trusts and, in other roles, was responsible for Japanese real estate investment opportunities. For the 180 Group, he was the Group Business Development Manager, specialising in business turnarounds.⁸⁸³

A2.35 Mr Larcombe has also been reported to have entered into some business ventures with Adam. For example, in 2010, Adam and Mr Larcombe joined a property developer, Mr Daniel Hausman (Mr Hausman), in a property development and financing business that Mr Hausman had established, called Aventis Capital (Aventis). Aventis helped companies struggling with liquidation and the CFO position was filled by a friend of Adam's, Mr Chris Guillan, who had worked with Adam at the insolvency firm Rodgers Reidy earlier in his career.⁸⁸⁴

Jason Onley

A2.36 Mr Jason Onley (Mr Onley) also worked at the 180 Group, performing the roles of Head of Sales and later as Business Development Manager until July 2014, when he left to start Northstar, a business and turnaround advisory specialist, which professed to be 'experts when it comes to ATO negotiations, [having] successfully come to agreement on numerous payment plans'.⁸⁸⁵ Mr Onley was later to describe himself as a businessman who specialised in business turnarounds.⁸⁸⁶

A2.37 It has been reported that through his work at 180 Group, Mr Onley had provided advice to many during liquidation proceedings, including Mr Simon Anquetil, regarding companies that he had established.⁸⁸⁷

Simon Anquetil

A2.38 Mr Simon Anquetil (Mr Anquetil) had set up the EStrategy Group of companies which were placed into administration and then liquidation by a financial institution in 2012. It has been reported that ASIC files allegedly show that Mr Anquetil had backdated by 15 months the replacement of himself as director of one of his companies with a 21 year old female, who allegedly had a fake address and could not be located.⁸⁸⁸ The liquidator's preliminary report on the EStrategy Group, which was sent to ASIC, is reported to have said that the EStrategy Group had failed due to alleged:

⁸⁸³ *ibid.*

⁸⁸⁴ Rachel Olding, 'Australia's largest tax fraud syndicate had its origins in modest Menai', *Sydney Morning Herald* (online) 19 May 2017.

⁸⁸⁵ Archived website of www.180businessloans.com.au (13 October 2012) <<https://web.archive.org>>; Archived website of www.180businessloans.com.au (11 November 2013) <<https://web.archive.org>>; Peter Gosnell, 'Insolvency Referrer Charged in ATO Fraud Bust', *Sydney Insolvency News* (online) 19 May 2017.

⁸⁸⁶ Archived website of Synep (22 May 2017) <<https://web.archive.org>>.

⁸⁸⁷ Above n 872.

⁸⁸⁸ *ibid.*

...‘offences and frauds’ in part by former employee, [Mr Anquetil], insolvent trading, and the creation of ‘group enterprises’ concurrently operating ‘in order to defeat creditors and debtors and to make entities indistinguishable’; \$117,712 owed on corporate credit cards, and the ATO, which was owed \$101,752 from the company’s failure to contribute Pay As You Go tax and GST.⁸⁸⁹

Other individuals allegedly involved

A2.39 It has also been alleged that the following people were connected with Plutus:⁸⁹⁰

- Ms Lauren Cranston, who is Adam’s younger sister, together with her friend, Ms Devyn Hammond, allegedly controlled the accounts and e-mails for the second-tier companies and managed the payments for the companies;
- Mr Dev Menon, a tax lawyer, allegedly gave advice about how the Plutus arrangements should be managed;
- Mr Daniel Rostankovski was alleged to have managed the directors of the second-tier and other companies to ensure banking tokens were collected, mail redirected and handed to Ms Cranston and Ms Hammond. Mr Rostankovski is also facing blackmail charges for allegedly extorting money from other alleged co-conspirators with the help of Mr Hausman and another person (who has not been charged); and
- Mr Aaron Leo Paul, who allegedly helped to recruit people to act as directors for the second-tier and other companies.

Companies of interest are established

A2.40 It has been publicly reported that during April to August 2014, a number of companies were established which were later linked to Plutus. For example, in April 2014, Mr Anquetil was registered as director of a Hong Kong company, Solutions Mondiale Ltd, which was owned by an entity in the Seychelles. Mr Anquetil subsequently established Plutus Payroll Australia and another company which later traded as Zip Recruitment.⁸⁹¹ The ATO’s approach to transnational compliance is discussed in Chapter 7.

A2.41 During that same month, Mr Larcombe and Mr Willmott had established other companies which were later linked to Plutus, one of which later came to the attention of the ATO. The companies were involved in providing payroll services to IT and construction industry contractors. The directors of the companies were replaced and, in August 2015, two of the companies fell into liquidation.

A2.42 Plutus itself continued to trade. In June 2016, it was owned by a company called Synep Ltd who reportedly obtained a vendor financed loan of \$5 million for the

⁸⁸⁹ *ibid.*

⁸⁹⁰ Ava Benny-Morrison, Rachel Olding and Nick Ralston, ‘The close calls that almost derailed a \$165 million ‘tax fraud’ syndicate’, *Sydney Morning Herald* (online) 18 May 2017.

⁸⁹¹ Above n 872.

purchase. Mr Anquetil was replaced as Plutus' director.⁸⁹² Synep Ltd itself was a public company that was established in March 2016 by Adam Cranston, Mr Hausman and Mr Onley and with Mr Onley and Adam Cranston being listed as the directors.

How matters came to the attention of the ATO

A2.43 A number of contractors, who had not received their SG entitlements into their fund, approached the ATO in August 2015. At the time the two relevant contributing companies were in liquidation. However, no action was taken by the ATO due to the low prospects of recovering any money. For example, with respect to one of the companies, the liquidator had found few assets which it could recover, there were no records for the company and the directors did not or claimed not to know anything of the business of the company.

A2.44 It was later found, however, that the companies had also not paid PAYG tax to the ATO – the contractors had lodged income tax returns and there was no matching PAYG remittance to the ATO. The officers who identified this mismatch lodged intelligence reports for analysis. Following this analysis, it was considered that the similarities between two seemingly unrelated companies may signal a phoenix arrangement. The information was then brought to the attention of the employers' obligations unit. After some initial delay in commencing initial profiling work by that area, links were drawn between the companies and one of the prior directors who was known to law enforcement agencies. At this point the matter was referred to the ATO's TEC area for consideration in February 2016.

A2.45 Refer to Chapter 6 for prevention strategies against external fraud risks and TERs, Chapter 7 for interagency cooperation to address tax evasion and Chapter 4 for capturing retrospective analysis of past events surrounding any significant fraud cases.

The investigation by the ATO's Tax Evasion and Crime area

A2.46 In February 2016, the TEC area commenced the detailed work of profiling those people and companies connected with the two identified liquidated companies. Ultimately, the financial position, tax compliance history, known expenditure and relationships of over 200 companies with a multitude of directors were profiled and analysed in an effort to piece together nodes of intersection in relationships and transactions to identify the 'controlling minds' or 'targets'. In one sense, the pattern slowly emerged from the data mist:

Over the year, we progressively uncovered a complex web of suspected tax evasion involving a multitude of entities and individuals. The identities and details of those involved are not all apparent to start with. As with many of these kinds of syndicates, their identities, roles, activities and arrangements are deliberately opaque, deceptive and complicated, and they take

⁸⁹² Neil Chenoweth, 'Plutus ATO fraud Part 2: Part 2: Sex, tax and Instagram', *The Australian Financial Review* (online) 4 July 2017.

time to piece together. So far, over 200 entities in layered structures and complex transactional and business relationships have been identified.⁸⁹³

A2.47 One relatively minor part of this data mist concerned Adam Cranston, son of the Deputy Commissioner. Adam Cranston was identified as having a connection with a director of one of the liquidated companies – the latter’s directorship predated the non-payment of PAYG tax to the ATO.

A2.48 The team continued its work in profiling the numerous connected entities and had reached a conclusion by 4 April 2016 that no further action need be taken with respect to Adam Cranston as his involvement was ‘not considered significant’ based on the material that was available to the ATO at that time.

A2.49 By contrast, however, the profiling work on others indicated connections may exist regarding other companies that were suspected of being part of a broader phoenix arrangement. Although the connections between named individuals and entities as well as the related tax risks and opportunities for recovery were identified, there was still a need to understand the source of the funds and their final destination. Further information was needed to do so and it was decided that the profiling work warranted a proposal to conduct covert audit action. According to ATO procedure, such audits must be approved by the PGH Tax Crime Referral Panel.

A2.50 The Tax Crime Referral Panel approved the proposal to conduct a covert investigation ‘to target the key individuals and follow the money trail [and] also search for new start-up entities which may be carrying on this arrangement and attempt to disrupt [them].’ The code name for this operation was ‘Operation Crocodile’ and soon after a case number was allocated.

A2.51 For an audit conducted by the ATO’s Financial Crime unit, such as Operation Crocodile, access is restricted to the User IDs of the auditors in that case and their manager.

A2.52 Notwithstanding the ATO’s electronic controls, there are always weak points in security arrangement of any organisation – often it is the employees. For example, an employee who has the access may obtain the protected information and provide it to another as a result of a superior’s request. Also, an employee who has the access may allow another who does not have access to read the information on the screen. There are public examples of such occurrences such as the former Victorian Police Force’s Media manager who had allowed an Assistant Commissioner to read the terms of reference for a covert Operation regarding a murder which had then allowed the targets of that operation to be alerted to covert surveillance which was being conducted on them.⁸⁹⁴

A2.53 Mindful of the risks present in such tax crime audits, including unauthorised access or inadvertent disclosure, the members of the ATO’s Financial Crimes (FC)

⁸⁹³ Above n 353, p 12 (Commissioner of Taxation).

⁸⁹⁴ The Sydney Morning Herald, ‘Trial by media’, *The Sydney Morning Herald*, (online), 13 June 2010; Office of Police Integrity (Victoria), *Exposing corruption within senior levels of Victoria Police*, (February 2008) p 33.

audit team divided up the work between each other such that each one was working on discrete elements.

A2.54 From July 2016, the FC audit team commenced enquiries and obtained information on entities linked to the liquidated companies. From this information the FC audit team analysed the source and destination of money transactions, consolidated bank statement data and began to understand the relationship between connected parties.

A2.55 On 25 August 2016, the FC audit team's enquiries revealed that Adam Cranston was connected to a company of which he was neither a director nor shareholder. In the light of other information that the ATO had uncovered, there was nothing to indicate that Adam Cranston was anything more than a 'mere employee as opposed to a controlling individual'.

A2.56 Whilst the FC audit team was progressing enquiries for some of the 200 companies linked to the liquidated companies, they were also required to finalise covert audits of other related companies in a manner that would recover the liabilities raised. Accordingly, on 8 December 2016, the FC audit team had finalised the first eight audits of individuals who allegedly had peripheral links to the main entities of interest. Default notices of assessments were issued to those taxpayers and, as the ATO considered that there was a real risk of dissipation of assets, garnishee notices for the debts arising from those notices were issued at the same time.

A2.57 On 20 December 2016, as a result of the FC audit team's enquiries, information was received which indicated to the team that Adam Cranston had a significant role in the arrangements under investigation. He had now become a target and the FC audit team informed their manager.⁸⁹⁵

A2.58 Any information on the FC audit team's case file was restricted to the case team and their manager. If there was any disclosure whilst the audits were on foot, inquiries may be initiated with resultant delay which would heighten the risk of asset dissipation and destruction of evidence. Similar risks of delay may have arisen if the information was shared with other law enforcement agencies at that time.

A2.59 Accordingly, all communications about Operation Crocodile, outside of the FC audit team, did not contain any identifying information and work progressed with the aim of issuing assessments to the next round of entities in late January. As the covert audits were progressing, it was unlikely that the targets would seek to contact the ATO. Once these audits were almost finalised, the FC audit team notified the Assistant Commissioner of the FC unit of their findings on 31 January 2017. The Assistant Commissioner of FC, then, requested corroborative evidence so that complexities could be explained in a simple way.

A2.60 The Commissioner has subsequently made public comment in support of the ATO officers' decision:

⁸⁹⁵ ATO PGH business line, IGT review team interviews, 19 December 2017 and 19 January 2018.

When officers in the ATO working on the investigations were certain that one of the principals of the [Plutus] syndicate had a personal connection with Deputy Commissioner Michael Cranston, they took steps to further isolate and lock down the casework. This was in addition to the extra security and compartmentalisation already in place for such tax crime cases.⁸⁹⁶

... the criminal investigation was held very tight. As soon as Michael Cranston's son's name appeared, they overlaid that tightness with a very strong layer of strict need-to-know basis.' ... 'I found out through the (Australian) Federal Police,' he said. 'Not through my own people (but through) Andrew Colvin, the Commissioner of the AFP'.⁸⁹⁷

A2.61 Management of conflicts of interest is discussed in Chapter 3, the risk of possible convergence of internal and external fraud risks is in Chapter 4, governance of the fraud and corruption risk is in Chapter 5 and internal reporting of suspected external fraud is discussed in Chapter 6.

Commencement of the ACIC and AFP's investigations

A2.62 The ATO was unaware that the ACIC had commenced an investigation at the beginning of August 2016 into the same targets who were the subject of the ATO's investigation in Operation Crocodile. Unknown to the ATO and the ACIC, the AFP also had commenced an investigation, namely Operation Elbrus, into the same targets later that month. Shortly thereafter the ACIC became aware that the AFP was investigating the same targets. In coordinating their efforts the ACIC handed over the financial data and other intelligence they had gathered to the AFP.

A2.63 In October 2016, the AFP began intercepting telephone communications on identified targets (wiretaps). Excerpts from the transcripts of these telephone intercepts have since been reported publicly and have been used by many in the public to indicate the alleged co-conspirators' level of involvement and knowledge of the Plutus arrangements. This issue, however, is a matter for the Courts to determine. Accordingly, these publicly released excerpts have not been reproduced in this report.

A2.64 As a result of the above wiretaps, the AFP became aware of the garnishee notices that the ATO had issued on some of the entities peripherally associated with the targets. However, the AFP did not advise the ATO of these investigations at that time because of the familial relationship between Michael Cranston and Adam Cranston.

AFP discloses Operation Elbrus to the Commissioner

A2.65 On 11 January 2017, however, Commissioner Colvin of the AFP met the Commissioner of Taxation Chris Jordan to advise him of the subject matter of Operation Elbrus and of the link to Michael Cranston:

AFP Commissioner Colvin visited me ... to make me aware of their investigations and of the personal relationship between one of the principals they were interested in and [the Deputy

⁸⁹⁶ Above n 353, p 12 (Commissioner of Taxation).

⁸⁹⁷ Nick Tabakoff, 'Cranston scandal my most difficult case', *The Australian*, (online), 9 December 2017.

Commissioner]. Commissioner Colvin was clear to me that [the Deputy Commissioner] was not suspected ... of being involved in the syndicate and its activities of defrauding the Commonwealth.

... I was not asked by the AFP to intervene. In fact, the ATO was asked to leave things as they were, and to keep all existing arrangements in place ... while further information continued to be gathered about the syndicate and its operations.

A2.66 On 17 January 2017, two senior staff members from the FPII unit attended a briefing on Operation Elbrus at the AFP's headquarters. The FPII's investigative team was briefed, by senior FPII members, later on 20 January 2017 at which time roles were identified and tasks allocated. The ATO's IT forensics capability was also contacted to assist with the preservation of evidence. It was also agreed, as an added precaution, that all records of ATO assistance with Operation Elbrus were to be maintained offline from the ATO's integrated systems.

A2.67 FPII's role was to monitor ATO staff whilst the AFP continued their investigation and provided assistance where needed. Accordingly, FPII investigators began work in scanning the environment to determine whether there was a need to commence investigations. However, such preliminary inquiries did not reveal anything suspicious to warrant deeper analysis.

A2.68 The AFP also needed an ATO officer to assist them to understand the tax issues. AFP could not follow the usual channels to request such assistance without risk of compromising the operation as Michael Cranston may have become aware of the investigations. Accordingly, the AFP and FPII investigators selected a suitable tax officer with proven financial skills in an operational environment.

A2.69 On 24 January 2017, the FC audit team finished its third round of covert audits, including six of the second-tier companies. Notices of assessment and garnishee notices were issued. As a result of the garnishee notices, no wages could be paid to the contractors using Plutus' services as the FC audit team had targeted the second-tier companies, which were the companies that were subcontracted to manage the payroll of Plutus' clients.

A2.70 Once the AFP became aware of the garnishee notices, it caused concern that any further audit activity may interfere with Operation Elbrus. Accordingly, the AFP asked the FPII unit to find out what action the FC audit team was taking.

A2.71 The FPII investigators took covert measures to identify the FC audit team's activities as any enquiries may have signaled the existence of Operation Elbrus to PGH officers. The FPII investigators soon identified that the garnishee notices were part of a number of audits being undertaken by the PGH Financial Crime area under Operation Crocodile. By this time, however, the AFP had asked the FPII unit not to stop the tax audits as the garnishee notices allegedly prompted Adam Cranston to contact Michael Cranston. Accordingly, the AFP provided the FPII investigation team with information which assisted FPII in conducting an investigation into whether the relevant ATO systems and records had sought to be accessed and, if so, by whom and for what reasons.

A2.72 As a result of its investigations, the FPII unit is claimed to have identified two ATO officers who attempted to access records relating to the Plutus arrangements on the ATO's case management system.⁸⁹⁸ The attempts were unsuccessful due to the ATO's IT systems controls. In fact, the controls also operated to prevent the FPII investigators from accessing that file.

A2.73 FPII's initial inability to access the FC audit team's file was a challenge. Without such access, FPII investigators could not ascertain the FC audit team's knowledge of events and relationships given it was a protected case file. FPII could not ask the network administrator to provide them with access because it would identify their interest in Operation Crocodile. It took them until 14 February 2017 to obtain access to the protected case file.

A2.74 Once the FPII investigators had reviewed the records for Operation Crocodile, they identified the FC audit team's awareness of Adam Cranston's alleged role in the arrangements and that the FC audit team had taken steps to minimise risks of the disclosure of this information. The FPII investigation team commented favourably on the measures the FC audit team had taken.

A2.75 As a result, the FPII team engaged in discussions with the AFP as to whether the FC audit team should be briefed on Operation Elbrus. Subject to the Commissioner's approval, the AFP agreed to do so as it was considered there was little risk that the FC audit team would disclose the existence of the Operation to others within the PGH business line.

Commissioner agrees to coordinate investigation with AFP

A2.76 By 14 February 2017, the Commissioner was informed of the FC audit team's awareness of Adam Cranston's alleged role in the arrangements. On 16 February 2017, the Commissioner formally agreed to the AFP's request that the Assistant Commissioner of FC be made aware of the AFP operation. The Assistant Commissioner of FC was briefed by the AFP on 24 February 2017 and a coordinated investigation was negotiated, including information sharing arrangements.

A2.77 The coordinated investigation was proposed to operate under a tiered system, whereby the AFP worked with the FC audit team to understand the tax issues in pursuing their targets for any criminal liability, the FC audit team would separately conduct an administrative investigation focusing on compliance with the tax laws and FPII would oversee ATO officer involvement and investigate any staff issues.

A2.78 Following the briefing to the Assistant Commissioner of FC, it was agreed that he or his senior officers would discuss operational issues with the AFP on a weekly basis. As it was important that no suspicions be raised, such communications were to be limited to telephone and face-to-face meetings and any travel by these officers was

⁸⁹⁸ These allegations have been the subject of an ATO disciplinary investigation and are also likely to be an issue considered by the NSW Supreme Court in the upcoming hearings concerning the charges laid against the Deputy Commissioner.

kept to a minimum and not put on the system until after the search warrants were executed.

A2.79 Fortuitously, the FC audit team themselves were not located in the same office as Michael Cranston and the AFP briefed that team on 3 March 2017. Once again, the importance of confidentiality was impressed.

A2.80 Towards the middle of April 2017, the FC audit team was ready for the next round of assessments and garnishee notices to issue. The AFP was alerted, given they had previously raised concerns regarding the issue of such notices on subjects of their investigations. The FPII team was also put on alert to monitor any staff issues.⁸⁹⁹

A2.81 On 26 April 2017, the FC audit team had finalised their fourth round of covert audits which involved five entities including Plutus. When the ATO had garnished funds from the company's bank accounts (reportedly for \$46.6million⁹⁰⁰), payments of wages to 2,000 of Plutus' clients were stopped.⁹⁰¹

A2.82 The above garnishee notices prompted contact with Michael Cranston that resulted in actions being taken by other ATO staff. This contact and the actions of six ATO officers has been the subject of ATO disciplinary investigations and is the subject of pending legal proceedings. It should be noted that no information held on the Operation Crocodile case file was accessed by these officers. However, it has been reported that some of these officers had been requested to make internal inquiries.⁹⁰² As a result, they had found out that the garnishee notices issued were the result of a covert investigation by the PGH Financial Crimes Unit.

A2.83 On 27 April 2017, the AFP signaled to the FPII team that it intended to execute search warrants on 17 and 18 May 2017. Importantly, the AFP required assistance of the ATO's FC audit team and FPII unit as well as IT forensics officers to preserve data from devices which were to be seized. The Commissioner was briefed and the arrangements included the following:

- confirming the locations where the 34 search warrants were to be executed on 17 and 18 May 2017, the numbers of personnel needed to assist and their roles as well as coordinating actions with the AFP's CACT so that identified funds and assets can be seized;
- confirming the charges that the AFP intended to lay, suspension notices that will be issued to ATO officers as well as the location of the targets and interview strategy;
- developing the strategy to manage staff with close ties to Michael Cranston, secure staff access to buildings and systems as well as more broadly informing staff of events;

⁸⁹⁹ ATO PGH business line, IGT review team interview, 18 January 2018.

⁹⁰⁰ Rachel Olding, 'Michael Cranston captured in phone taps on '\$144m ATO tax fraud'', *The Sydney Morning Herald*, 21 June 2017.

⁹⁰¹ Rachel Baxendale, 'ATO tax fraud: IT link prompts review of records', *The Australian*, 24 May 2017.

⁹⁰² Neil Chenoweth, 'Plutus ATO fraud Part 3: Michael Cranston and the AFP bug that caught him', *The Australian Financial Review* (online) 5 July 2017.

- briefing the ATO's media area to prepare a media strategy in consultation with the AFP and resolving the question of whether transcripts of the telephone intercepts may be used;
- engagement of an external party to investigate the 'administrative actions' of identified ATO officers for the purposes of determining whether ATO employees had breached the APS Code of Conduct and the imposition of sanctions (Code of Conduct investigator); and
- finalising the fifth round of covert audits which involved 14 entities, including those who were alleged to have conspired to defraud the Commonwealth.⁹⁰³

AFP's searches and seizures actioned

A2.84 On the morning of 17 May 2017, search warrants were executed by 290 AFP officers, assets were seized and within the hour nine targets were reported to be in custody. Work property that Michael Cranston was carrying at the time was also seized. Following this, FPII investigators began interviews with him and other ATO staff.

A2.85 The ATO also served five ATO officers with suspension notices pending further investigation and revoked building access. Those with close ties to Michael Cranston were told not to go to work or access ATO systems.

A2.86 The AFP also released information to the media. Operation Elbrus had now become public and the AFP confirmed that Michael Cranston was not party to the alleged conspiracy to defraud the Commonwealth.⁹⁰⁴

A2.87 Since that time senior ATO officers have made public comment on the events.⁹⁰⁵ The Code of Conduct investigations have also been finalised. As a result, sanctions were imposed on two officers.⁹⁰⁶

Charges laid

A2.88 As a result of Operation Elbrus, six people were charged with conspiracy to defraud the Commonwealth, one person was charged with conspiracy to defraud the Commonwealth and blackmail, two people were charged with dealing with proceeds of crime, one person was charged with blackmail and Michael Cranston, the Deputy Commissioner, was charged with abuse of public position. Civil proceedings to recover the proceeds of crime were also commenced against nine people.

A2.89 The charges laid against the ten defendants in this matter were originally adjourned to 29 August 2017⁹⁰⁷ and the brief of evidence was expected to be delivered

⁹⁰³ ATO FPII business area, IGT review team interviews, 19 December 2017 and 18 January 2018.

⁹⁰⁴ Above n 353, p 13 (Commissioner of Taxation).

⁹⁰⁵ Fergus Hunter, 'Tax commissioner Chris Jordan says 'staggering' \$165m Plutus scandal tarnished ATO reputation', *The Sydney Morning Herald* (online) 5 July 2017; Above n 897.

⁹⁰⁶ Doug Dingwall, 'ATO assistant commissioner returns after being stood down', *Canberra Times* (online) 28 July 2017.

by 8 August 2017.⁹⁰⁸ However, extensions to file the brief of evidence were provided to the prosecution until 13 July 2018.⁹⁰⁹ Additionally, on 9 March 2018, the Magistrate set the trial date of the charges against Michael Cranston for 21 January 2019.⁹¹⁰

Follow-up ATO initiatives

A2.90 The above events led to a number of ATO initiatives. As mentioned in the body of this report, on 8 June 2017, the Chief Internal Auditor and the Assistant Commissioner of the FPII unit commenced a joint review into the ATO's conflicts of interest and security clearance policies and processes.⁹¹¹

A2.91 The ATO also engaged two contractors who specialised in corruption resistance and integrity framework design to evaluate the ATO's areas of corruption risk.⁹¹² This evaluation is discussed in more detail in Chapter 4.

A2.92 Substantial developments also took place during insolvency action regarding the entities connected with Plutus. These events are ongoing and include ATO efforts to address concerns with relevant creditors and liquidators.⁹¹³

⁹⁰⁷ Nick Hansen, 'Michael Cranston reveals fears for heavily pregnant daughter as she faces jail term for alleged tax scam', *The Daily Telegraph*, 14 June 2017.

⁹⁰⁸ Rachel Olding, 'ATO Deputy Commissioner Michael Cranston suspended during criminal probe', *The Sydney Morning Herald* (online) 13 June 2017.

⁹⁰⁹ Nine news, 'Cranston doesn't appear in NSW court', *Nine News* (online) 29 August 2017; Kelly Fedor, 'Former tax chief's lawyer says case is 'a disgrace'', *Nine News* (online) 19 December 2017.

⁹¹⁰ Anthony Klan, 'Former ATO deputy commissioner Michael Cranston's trial date set', *The Australian* (online) 9 March 2018.

⁹¹¹ Above n 304.

⁹¹² Above n 10, p 4.

⁹¹³ Noel Chenoweth, 'ATO overturns 'last minute' bid to control tax fraud company Plutus Payroll', *The Australian Financial Review* (online) 9 June 2017; Peter Gosnell, 'Liquidator Facing 10 Year Ban', *Sydney Insolvency News* (online) 18 October 2017; Peter Gosnell, 'Tax Boss v Liquidator - where's ASIC', *Sydney Insolvency News* (online) 20 October 2017 and Peter Gosnell 'PPB Preparing To Tread on Deloitte's Plutus Patch', *Sydney Insolvency News* (online) 15 November 2017.

APPENDIX C – OTHER RELEVANT REVIEWS

A3.1 The IGT has considered the findings of other reviews to better understand the fraud and corruption control landscape both within the ATO as well as more broadly amongst Commonwealth agencies. These reviews include the following:

ANAO performance audit of ATO's use of settlements (2017)

A3.2 The ANAO conducted a performance audit to examine the effectiveness of the ATO's use of settlements to resolve taxpayer disputes. The audit made a number of recommendations including improvements to pre-settlement assurance mechanisms and record keeping.⁹¹⁴

ANAO performance audit of ATO's internal fraud control arrangements (2000)

A3.3 The ANAO conducted a performance audit into the ATO's internal fraud control arrangements⁹¹⁵ and had identified areas for further improvements to ensure that the ATO's internal fraud control framework becomes an integral part of the ATO's corporate governance framework and would be consistent with best practice. The audit made a number of recommendations. Those relevant to this review include:

- adopting a more holistic approach to risk management and planning processes by incorporating relevant aspects of its fraud risk assessment process as explicit elements of the broader ATO risk management processes;
- further refining the performance assessment framework to enable quantitative and qualitative assessment of the internal fraud control function;
- as part of fraud education processes, making greater use of internal publications and other awareness raising techniques to share case studies and results of internal fraud investigations;
- the ATO IT Security Section and, where necessary the Fraud Prevention and Control section (the precursor to the FPII unit), undertaking regular targeted reviews of the ATO IT systems logs to detect and deter unauthorised access to taxpayer data;
- improving the efficiency and effectiveness of internal fraud detection strategies; and
- strengthening the coordination between the IA unit and the Fraud Prevention and Control Section to improve the development of risk mitigation strategies.

⁹¹⁴ Above n 14.

⁹¹⁵ ANAO, *Australian Taxation Office Internal Fraud Control Arrangements* (2000).

Black Economy Taskforce (2017)

A3.4 The black economy refers to people who operate entirely outside the tax and regulatory system or who are known to the authorities but do not correctly report their tax obligations. The Treasury's Black Economy Taskforce⁹¹⁶ was established to develop a forward looking whole-of-government policy response to combat the black economy in Australia, recognising that these issues cannot be tackled by traditional tax enforcement measures alone. The taskforce's final report was publicly released in May 2018⁹¹⁷ along with the Government response which indicated that a number of the report's recommendations would be implemented. These recommendations include the removal of the tax deductibility of employees' wages for employers who have not withheld the requisite PAYG⁹¹⁸ and the establishment of a taskforce to combat the trade in illicit tobacco.⁹¹⁹

Phoenix Taskforce

A3.5 Illegal phoenix activity refers to the stripping and transfer of assets from one company to another by individuals or entities to avoid paying liabilities. This issue was the subject of an interagency government taskforce with a range of proposed measures being announced by the Government in September 2017.⁹²⁰ Further measures were more recently announced, including the introduction of new phoenix offences to target those who conduct or facilitate illegal phoenixing.⁹²¹

Fraud within the Commonwealth Census

A3.6 The AIC conducts a periodic 'Fraud within the Commonwealth' census on the Commonwealth's most costly fraud incidents. These studies analysed the information about the most costly incidents each agency experienced each year and those who perpetrated them. A summary of the findings of these censuses is outlined below:

- 2014 census⁹²², identified that the majority of the 166 frauds related to employee entitlements or financial benefits and were committed through misuse of documents or technology;
- 2010–11 and 2012–13 censuses⁹²³ revealed that 137 Commonwealth agencies reported 7,809 incidents of internal fraud; and
- 2010–11 and 2012–13 censuses of the most costly incidents⁹²⁴, discovered that across 154 agencies, 60 per cent did not detect or experience any instance of fraud

⁹¹⁶ Treasury, 'Black Economy Taskforce', (2017) <www.treasury.gov.au>.

⁹¹⁷ See, above n 13.

⁹¹⁸ Above n 745, pp 22–24.

⁹¹⁹ See, Appendix E.

⁹²⁰ Above n 474.

⁹²¹ *ibid.*; Above n 745, p 37.

⁹²² AIC, *Statistical Bulletin no. 2 – Fraud within the Commonwealth: A census of the most costly incidents 2013–14*, (3 March 2017) <www.aic.gov.au>.

⁹²³ AIC, *Research in practice no. 41 – Fraud within the Commonwealth: A Census of the most costly incidents, 2010–11 to 2012–13* (9 March 2016) <www.aic.gov.au>.

⁹²⁴ AIC, *Fraud against the Commonwealth Report to Government 2010–11 to 2012–13* (2015).

however, there were a total of 265,886 incidents of suspected internal and external fraud with an estimate of over \$530m in losses.

Misuse of information and communications technology within the public sector (2015)

A3.7 In 2015, the AIC drew on its findings from the 'Fraud against the Commonwealth Surveys' and presented data regarding the misuse of Information and Communication Technology (ICT) within the Commonwealth Government over the three year period between 1 July 2008 and 30 June 2011.⁹²⁵ It was concluded that although the ICT environment is rapidly changing, fraud control plans, organisational policies, and technical standards for data security minimise the risk of ICT misuse and identify intervention points at which prevention and detection methods may be focused.

Review of anti-corruption strategies (2006)

A3.8 In 2006, the AIC released a report on its 'Review of anti-corruption strategies'⁹²⁶ which outlined what experts consider to be the three most significant causes of corruption:

- norms and values of politicians and public servants;
- lack of control, supervision, auditing; and
- interrelationships.

A3.9 Similarly, the AIC attributed the size and incidence of corruption to four key factors:

- the level of public benefits available;
- the discretionary power of officials;
- the level of risk associated with corrupt deals; and
- the relative bargaining power of the corruptor and corrupted.

Parliamentary Joint Committee on Corporations and Financial Services' inquiry into whistleblower protections (2017)

A3.10 The Parliamentary Joint Committee on Corporations and Financial Services in its report on its Whistleblower protections inquiry⁹²⁷ recommended the establishment of a Whistleblower Protection Authority (to be housed within a single body or an existing body) that can support whistleblowers, assess and prioritise the treatment of whistleblowing allegations, conduct investigations of reprisals, and oversee the implementation of the whistleblower regime for both the public and private sectors.

⁹²⁵ AIC, *Trends & issues in crime and criminal justice no. 470 - Misuse of information and communications technology within the public sector* (31 July 2015) <www.aic.gov.au>.

⁹²⁶ AIC, *Technical and background paper series no. 23 - Review of anti-corruption strategies* (2006).

⁹²⁷ Joint Committee on Corporations and Financial Services, Parliament of Australia, *Whistleblower protections* (13 September 2017).

Parliamentary Joint Committee on ACLEI (2016)

A3.11 The Parliamentary Joint Committee's inquiry into the jurisdiction of the ACLEI⁹²⁸, recommended an independent assessment of the ATO's corruption risk profile, together with an examination of the feasibility of including the ATO within ACLEI's jurisdiction.

The Department of the Prime Minister and Cabinet's Review of the PID Act (2016)

A3.12 The Department of the Prime Minister and Cabinet's Review of the PID Act⁹²⁹ gathered information and views on whether the PID Act was operating as intended and whether it could be improved. It found that whistleblowers did not have a positive experience after making a disclosure and that the PID Act was difficult to apply by the agencies.

⁹²⁸ Above n 17.

⁹²⁹ Above n 16.

APPENDIX D – PRECIOUS METALS

Introduction

A4.1 Since 2012, the ATO has been considering the risk of exploitation of the GST rules as they apply to the precious metals industry and in particular gold. The ATO believes it to be the 'largest risk to the GST system.'⁹³⁰

A4.2 The underlying nature of outworkings of the ATO's response is multi-faceted and complex. Therefore, in seeking to provide insight and facilitate understanding, the analysis that follows is not a simple chronology of events. A degree of generalisation is also needed in certain instances, as due regard must be given to the ongoing investigations and litigation to ensure they are not prejudiced in any way. There are also certain confidentiality constraints imposed by the relevant tax, law enforcement, privacy and employment laws that need to be considered regarding disclosures.

Gold and the gold industry

A4.3 Gold is used in the manufacture of collectable goods and industrial processes⁹³¹ as well as a financial investment in itself, for example, as a hedge against inflation or uncertainty.⁹³² One of the main benchmarks for the price of gold as an investment product⁹³³, namely the gold spot price⁹³⁴, had dramatically increased following the global financial crisis in 2009. In 2008, the gold spot price increased from approximately AUD\$500 to a peak of over AUD\$1,700 in August 2011. Since that peak, the gold spot price has remained in the range of AUD\$1,300 to AUD\$1,800.⁹³⁵

A4.4 It has suggested that the increase in the gold spot price had attracted many more participants to the gold industry and the current total population is estimated to total between 350-500 entities⁹³⁶, including the following types of businesses:

- refineries that acquire products containing gold from a number of sources, such as doré⁹³⁷, jewellery and industrial by-products, from which they produce gold for investment purposes or for manufacturing jewellery or industrial use;

⁹³⁰ ATO, 'Criminal Law Investigations Gold Briefing' (Internal ATO document, 27 May 2016) cited in ATO, 'Executive Summary SFCT Evaluation Intel Bulletin Precious Metals' (Internal ATO document, 2017) p 3.

⁹³¹ World Gold Council, 'Global gold demand' <www.gold.org>.

⁹³² London Bullion Market Association (LBMA), *The Guide - An Introduction to the Global Precious Metals OTC Market*, (2017) p 9.

⁹³³ The other is the LBMA Gold price, also known as the London gold fixing: above n 932, p 50.

⁹³⁴ The gold spot price is derived from the intra-day trade in the commodity markets: <<https://goldprice.org>>.

⁹³⁵ Gold Price, 'Gold Price Australia' (2018) <<https://goldprice.org>>.

⁹³⁶ ATO, 'Precious Metals Industry - Improving industry compliance - GST Options Paper' (Internal ATO document, April 2016) p 4.

⁹³⁷ Ore or other material, containing gold, which is extracted by miners.

- traders who generally deal in gold markets, including banks and commodity brokers;
- bullion dealers who typically trade in physical bullion both domestically and internationally; and
- gold buyers, for example gold kiosks and pawn shops, who obtain gold from public sources such as unwanted jewellery – state based legislation governing dealers of second hand goods require such buyers to obtain a dealer’s license.

A4.5 Anyone may buy what is purported to be gold, however, they must rely on others’ representations regarding the content and quality of the metal unless they have equipment and expertise to carry out the testing (assay) themselves. Accordingly, the reputation of the gold refiners is an important factor in maintaining investor confidence in the trade of gold.

A4.6 The ‘only globally accepted accreditation for the [gold] bullion market’ is the accreditation that the London Bullion Market Association (LBMA) may give to refineries that have proven to produce gold bars to a minimum standard.⁹³⁸ Refiners mark gold bars with their distinctive hallmark and investors may confirm whether a refiner has been accredited by the LBMA by consulting the ‘London Good Delivery List’ that is published on the LBMA’s website.⁹³⁹

A4.7 Currently, there are 69 refiners in the world who have LBMA accreditation⁹⁴⁰ and only two of these are located in Australia.⁹⁴¹ It should be noted that from time to time there have been a number of other gold refiners in Australia, however, they have not been LBMA accredited.⁹⁴²

GST treatment of gold transactions

A4.8 Gold in non-investment form, for example jewellery⁹⁴³, is treated according to the basic rules of the GST law. These basic rules classify supplies of such gold as taxable supplies⁹⁴⁴ which would require GST registered suppliers to charge GST on these supplies. As a result, GST registered entities who acquire the gold would be entitled to claim input tax credits (ITCs) for the embedded GST where they hold a valid tax invoice⁹⁴⁵ and the acquisition was for a creditable purpose⁹⁴⁶.

A4.9 There are special rules for the GST treatment of gold in investment form. The term, ‘investment form’, is not defined in the GST legislation, however, the explanatory memorandum to the bill that introduced that term states:

⁹³⁸ LBMA, *Precious Metals Integrity - Responsible Sourcing* (2018) pp 5 and 7.

⁹³⁹ LBMA, ‘Good Delivery List’ (2018) <<http://www.lbma.org.uk>>.

⁹⁴⁰ Above n 938, p 6.

⁹⁴¹ LBMA, ‘Refiners Search’ (2018) <<http://www.lbma.org.uk>>.

⁹⁴² Above n 936, p 4.

⁹⁴³ ATO, ‘Goods and Services Tax: What is ‘precious metal’ for the purposes of GST?, GSTR 2003/10’, 18 June 2003, paras [11] and [18].

⁹⁴⁴ *A New Tax System (Goods and Services Tax) Act 1999* s 9-5.

⁹⁴⁵ *A New Tax System (Goods and Services Tax) Act 1999* s 29-10(3).

⁹⁴⁶ *A New Tax System (Goods and Services Tax) Act 1999* s 11-15.

...investment form means precious metal sold in a wafer, bar or other tradable form (i.e. bullion) which has an internationally accepted hallmark. In the case of gold, this means a hallmark that has been approved by the London Bullion market and means that the gold can be traded on the international Bullion market.⁹⁴⁷

A4.10 The price of gold itself is effectively fixed by the gold spot price which would prevent dealers from passing on the GST in their sales. For this reason, there are special GST rules for gold, in an investment form, to ensure that there is no GST embedded in the price of gold supplies. Accordingly, the GST laws will treat a supply of gold as GST-free if:

- the gold is a 'precious metal', which is defined as including gold with a fineness of at least 99.95 per cent and 'in an investment form'⁹⁴⁸;
- it is the first supply after refinement; and
- the recipient is a dealer of precious metals.

A4.11 Subsequent supplies of gold are input taxed as they are a form of investment similar to shares and are treated as a form of financial supply.⁹⁴⁹ As a result, no GST is to be remitted to the ATO and no ITCs may be claimed with respect to the acquisition of gold in 'investment form'.⁹⁵⁰

A4.12 ITCs may be claimed on the acquisition of second hand goods from non-GST registered entities where the goods were purchased for resale.⁹⁵¹ The entitlement to claim these ITCs avoids any double-taxing of GST that is already embedded in the goods. The definition of second hand goods, however, explicitly excludes precious metals or goods to the extent that they would be precious metals if they had been of the required fineness. As the definition of precious metals is that the metal be in investment form, resold gold which is not in investment form could be considered as a second hand good. Accordingly a second hand goods dealer who had acquired gold which was not in investment form could claim ITCs on the purchase of that gold.

A4.13 The above mentioned GST provisions are referred to as the GST rules for gold in the discussions below. A summary of these provisions is provided in Figure D1 below.

⁹⁴⁷ Explanatory Memorandum to the A New Tax System (Indirect Tax and Consequential Amendments) Bill (No. 2) 1999 para [1.11].

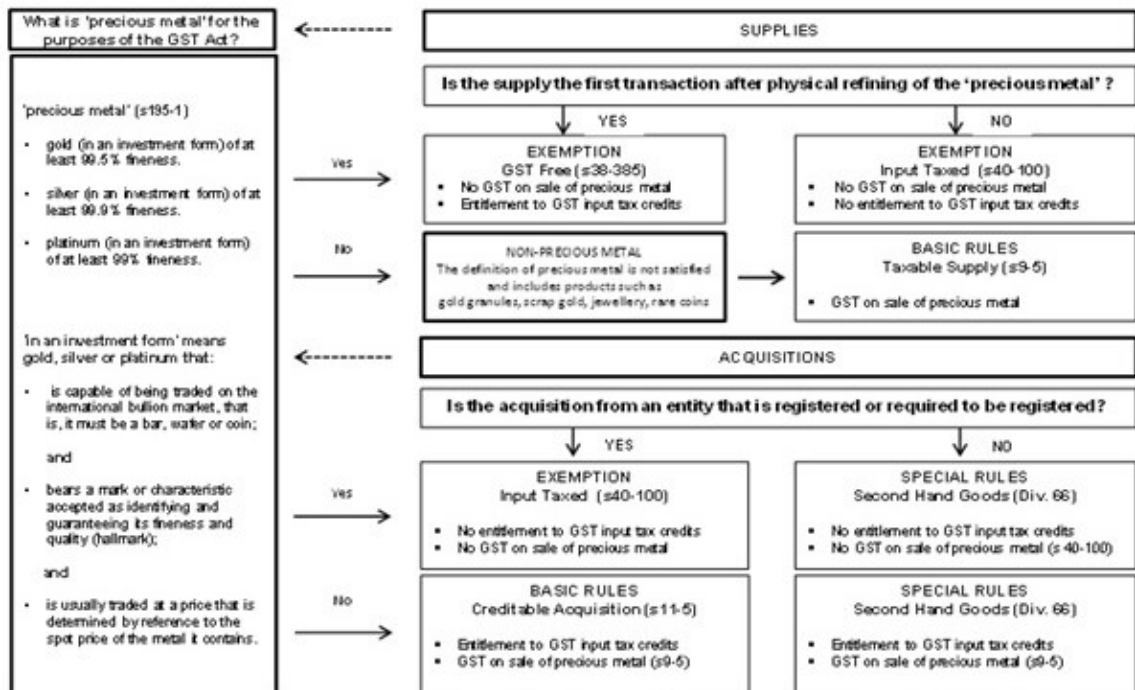
⁹⁴⁸ *A New Tax System (Goods and Services Tax) Act 1999* s 38-385.

⁹⁴⁹ *A New Tax System (Goods and Services Tax) Act 1999* s 40-100.

⁹⁵⁰ Above n 936, p 7.

⁹⁵¹ *A New Tax System (Goods and Services Tax) Act 1999* Div 66.

Figure D1: GST rules for gold



Source: ATO

Prior international experience with exploitation of value added tax rules for gold (1954–1998)

A4.14 Arrangements which seek to exploit the different taxation treatment of gold in value added tax (VAT) systems, such as the GST, are not new. For example, the European Commission proposed an anti-fraud measure in 1992 that would allow Member States to require purchasers of investment gold to pay relevant VAT (a 'reverse charge' which is explained in detail further below).⁹⁵² This proposal was subsequently adopted by the European Union Council as a Directive to Member States in 1998.⁹⁵³

A4.15 New Zealand was also alive to risks, of the exploitation mentioned above, when it implemented the GST in 1986 which had addressed the risks by preventing input tax deductions being claimed for gold, including the gold component in second hand goods⁹⁵⁴ by defining it according to the metal's purity.⁹⁵⁵ Other countries with a VAT system, have also sought to address such risks.⁹⁵⁶ A summary table showing the comparative approaches adopted by the UK, Canada, New Zealand, Singapore,

⁹⁵² Prof Dr Ben JM Terra, 'New VAT rules on investment gold' (1999) 10(1) *VAT Monitor*, p 16.

⁹⁵³ Directive 98/80/EU, art 26F.

⁹⁵⁴ New Zealand Policy and Strategy, Inland Revenue and the Treasury, *GST Current Issues – An Official's issues paper* (2015) pp 15–17.

⁹⁵⁵ The relevant purity for gold is defined as having at least 99.5 per cent fineness.

⁹⁵⁶ Michael Walpole, 'Tackling VAT Fraud', *International VAT Monitor* (September/October 2014) pp 258–263.

Malaysia, Germany and South Africa jurisdictions is reproduced in Appendix 4 of the IGT's review into *GST Refunds*.⁹⁵⁷

Law design and initial interpretation of GST rules for gold (1999–2012)

A4.16 At the time of developing the GST regime in Australia⁹⁵⁸, the ATO had the benefit of observing the experience in other jurisdictions, most notably the UK and New Zealand. The proposed GST law which was originally introduced into Parliament had adopted a similar approach to that of New Zealand by preventing ITCs from being claimed for precious metals based on the purity of the metal. For example, the proposed definition of 'precious metals' included 'gold (in any form) of at least 99.5% fineness.'

A4.17 At the time the GST law was drafted, there was pressure to draft the volume of the GST law within short timeframes.⁹⁵⁹ Government had sequestered the drafters and required authorisation to be obtained for any consultation with industry.⁹⁶⁰ When the relevant proposed legislation was tabled in Parliament, Government authorised consultation with industry as concerns were raised with the proposed law as it applied to precious metals.⁹⁶¹ As a result, amendments were introduced into the House of Representatives to replace the term '(in any form)' with '(in an investment form)'.⁹⁶² The basis for this change was that the originally proposed definition 'did not reflect the way precious metals is mined and supplied in Australia'. In particular, it was considered that the original proposal would unnecessarily limit a GST-free supply to transactions in which dealers had acquired the precious metal for investment purposes.⁹⁶³ The Explanatory Memorandum which accompanied the amended definition stated that:

... investment form means precious metal sold in ... tradeable form which has an internationally accepted hallmark. In the case of gold, this means a hallmark that has been approved by the LBMA and means that the gold can be traded on the international bullion market.⁹⁶⁴

A4.18 According to some of the participants who worked on the design of the GST law at the time, the frauds that other jurisdictions had experienced had arisen from factors which were idiosyncratic to their jurisdiction.⁹⁶⁵ The drafters also considered that a GST general anti-avoidance rule (GAAR)⁹⁶⁶ would operate to address such frauds, unlike other overseas jurisdictions which did not have such a rule.

⁹⁵⁷ Above n 8.

⁹⁵⁸ The implementation and operation of the GST system is discussed at length in the IGT's *Review into GST Refunds* (2018).

⁹⁵⁹ ATO, 'Office Minute' (Internal ATO document, 19 September 2013).

⁹⁶⁰ ATO communication to the IGT, 27 February 2018.

⁹⁶¹ Above n 947, para [1.11].

⁹⁶² *A New Tax System (Goods and Services Tax) Act 1999* s 195-1.

⁹⁶³ Above n 947, para [1.11].

⁹⁶⁴ *ibid*.

⁹⁶⁵ ATO, 'Intelligence Assessment – Carouselling and Missing Trader Fraud - Overview' (Internal ATO document, 24 August 2006).

⁹⁶⁶ *A New Tax System (Goods and Services) Act 1999* Div 165.

Accordingly, the proposed amendments were adopted and became law, effective from 1 June 2000.

A4.19 Later, in November 2002, a case arose in which the ATO was of the view that gold in investment form has a GST-free status after each refinement of the metal as the word 'refinement' in the law was not limited to the first refinement which had transformed ore into gold.⁹⁶⁷ In addition, the ATO responded to calls to provide a public view on the terms, precious metals and investment form.⁹⁶⁸ As a result, the ATO issued a public ruling, Goods and Services Tax Ruling 2003/10 (GSTR 2003/10), which provided a more expansive application than that indicated by the Explanatory Memorandum – the public ruling allowed 'in investment form' to include gold with an accredited hallmark that was accepted in the Australian market.⁹⁶⁹ Over 2011 and 2012, the ATO also issued approximately 12 private rulings on the application of definition of 'second hand goods' as it applied to jewellery. The ATO issued these private rulings on the basis that 'it was not Parliament's intent to allow jewellery to fall within the definition of second hand goods for the purposes of Division 66'.⁹⁷⁰

Opportunities to exploit the GST rules for gold

A4.20 More recently, the ATO has identified that the GST rules for gold has created significant exploitation opportunities as gold is a high value asset and its form may be easily altered.⁹⁷¹

The high value of gold provides significant opportunity for exploitation, particularly in organised networks, both registered and unregistered. The behaviour ranges from simple and opportunistic (individuals and entities operating independently) to elaborate schemes, principally carousel type arrangements, whereby established syndicates acquire bullion and alter the form (melting or defacing) and resupply the altered precious metals for refining.⁹⁷²

A4.21 An example of the above exploitation opportunity is 'asset flipping' in which participants obtain profit from the difference in GST rates and without any fluctuation in the gold spot price. In an asset flipping arrangement, the GST treatment of gold is 'flipped' from an input taxed supply to a taxable supply and then to a GST-free supply when it is refined back into investment form and sold. The gold is then flipped back to an input taxed supply in subsequent sales and the circular series of actions involving refiners, dealers and suppliers starts again (a 'carousel'). In such carousel arrangements, however, there may be innocent and unwitting participants in the circular supply chain. A taxpayer may have no knowledge of the source from which another entity had acquired the gold, may have undertaken enquiries of the other entity in accordance with industry practice and may have conducted dealings at arm's-length.

⁹⁶⁷ ATO, 'TCN paper' (Internal ATO document, 27 November 2013) p 4 citing ATO, 'Interpretative Advice Report No. 3328808' (Internal ATO document, undated).

⁹⁶⁸ ATO, 'TCN Discussion Paper' (Internal ATO document, 24 July 2014).

⁹⁶⁹ Above n 943, para [34].

⁹⁷⁰ ATO, 'Law Advocacy Working Group' (Internal ATO document, 25 May 2016) p 4.

⁹⁷¹ Gold is a soft metal, little harder than a finger nail: Moh's scale of hardness.

⁹⁷² ATO, 'Indirect Tax SES Brief' (Internal ATO document, 1 December 2015).

A4.22 In a more egregious form, asset flipping may involve traders in the supply chain who charge GST on the supply but do not remit it or report it to the ATO (missing traders), whereas the purchaser may claim the corresponding ITCs from the ATO. A more fulsome description of carousel and missing trader fraud is provided in the IGT's report, *GST Refunds*.⁹⁷³

A4.23 Another opportunity to exploit the GST rules for gold does not need complex arrangements and may be conducted by using recipient created tax invoices which misrepresent the nature of the goods as second hand and the timing of the transfer of the title to the gold. For example, an entity may claim that before they purchased gold in investment form, they had conducted an internal composition test, such as drilling through the gold, to check the metal's quality before agreeing to the purchase. Entities may explain repeated instances of such transactions due to the comparatively higher margins they have offered to attract business.

A4.24 A further exploitation opportunity arises when GST refunds may be claimed on the export of gold which has in fact been diluted, for example, by adding inferior alloys. This allows some of the gold to be extracted and recirculated into the domestic market. To detect such arrangements and to identify artificial assay results and transaction splitting, forensic analysis and industry expertise is required.

A4.25 It should also be noted that it is well known in law enforcement circles that gold is a form of currency amongst organised crime syndicates and that unexplained trade in large amounts of gold bullion or granules may indicate an organised crime syndicate's efforts to launder money.⁹⁷⁴ Furthermore, they may be attracted by the profits from exploiting weaknesses in the GST rules for gold as there is a known low risk of detection and weak enforcement measures to deal with non-compliance.⁹⁷⁵

Signals of exploitation of GST rules for gold (2000–2012)

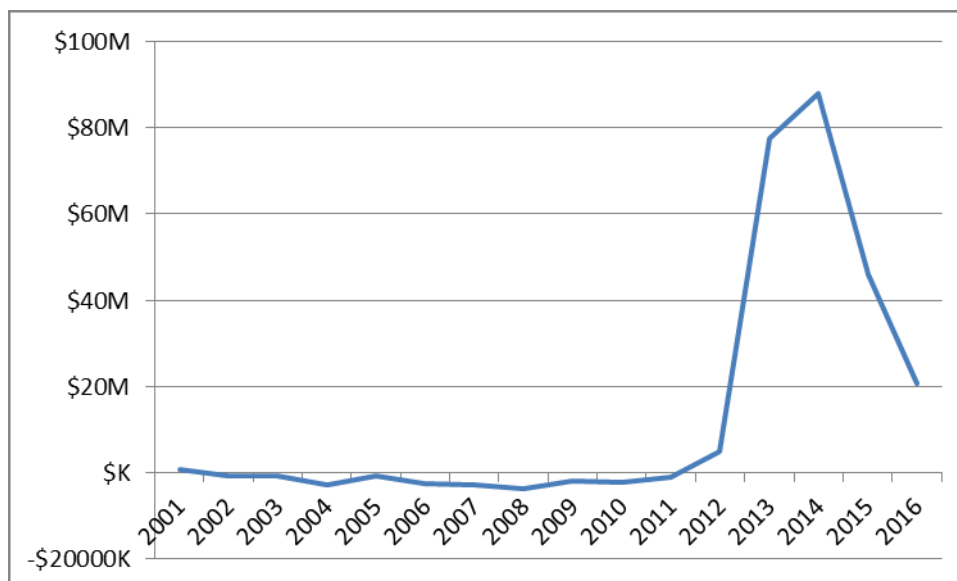
A4.26 The ATO first became aware of the exploitation of the GST rules for gold in May 2012. It is difficult to determine the exact time when a significant risk to revenue arose due to the total population of the gold industry not being known by the ATO. However, the data reported to the ATO by recognised gold refiners in their BASs can provide an indication as refiners perform a role in refining scrap gold into investment form. Figure D2 below represents a retrospective analysis of the total annual net GST refunds paid to eight refiners from 2000–01 to 2015–16.

⁹⁷³ Above n 8, pp 73–74.

⁹⁷⁴ ATO communication to the IGT, 20 July 2017; AUSTRAC, *Typologies and Case Studies Report 2013* (2013) p 13.

⁹⁷⁵ Above n 936, p 21.

Figure D2 – Total net GST paid to eight refiners, by financial year



Source: IGT, based on ATO data

A4.27 As Figure D2 shows, prior to 2011–12, the refiners were, on aggregate, net payers of GST and after that financial year the refiners became net receivers of GST refunds. Also, the total amount of net GST that was paid to refiners rose significantly in the 2012–13 year and peaked in 2013–14. After this peak, the total amount of net GST paid decreased substantially over the 2014–15 and 2015–16 financial years.

A4.28 From 2000 to 2013, the ATO had processes to detect broader risks in GST refund claims but did not have a specific process to risk-assess or monitor claims in the gold industry:

...no specific refund integrity processes targeting the precious metals industry were employed by the ATO, as refund claims by industry participants would have been risk assessed by the General GST refund risk models in operation at the time. These models included the Risk Rating Engine (RRE), which incorporates a number of business rules that it high-risk refunds such as low value claims, unusual refunds, and claims from new businesses.

In addition to the RRE, suspect refund models (post-2009) specifically targeted fraudulent refunds, as such, high risk refund claims for the precious metals industry would have been subject to business as usual (BAU) verification checks by these processes at that time...⁹⁷⁶

A4.29 However, in 2013, the ATO became aware that, since 2010, its RRE and suspect refund models had not detected some large claims made by entities in the gold industry.

A4.30 There were also external signals, such as a media article published on 10 June 2011 which reported an alleged CAD\$150 million asset flipping fraud in the Canadian gold industry.⁹⁷⁷

⁹⁷⁶ ATO communication to the IGT, 19 December 2017.

ATO's gold bullion project (May 2012 – May 2013)

A4.31 In May 2012, the CACT⁹⁷⁸ had identified information which indicated that two companies in the gold industry had been party to suspicious purchases and sales of gold over an eight month period. These transactions involved approximately \$18.7 million of GST which had not been remitted to the ATO.⁹⁷⁹

A4.32 The CACT referred this information to the ATO's ITX business line who immediately commenced analysis of that information and conducted initial enquiries regarding the activities of the relevant taxpayers with a view to commencing audits.⁹⁸⁰ However, shortly after the start of ITX's enquiries, the two companies were put into liquidation and the director left the country permanently.⁹⁸¹ The ATO was also not made aware of creditors' meetings for these two companies before they were put into liquidation. The ATO later discovered that any dividend was unlikely to be forthcoming.⁹⁸² Accordingly, the ITX business line cancelled its plans to commence audits⁹⁸³ and engaged its profilers to deepen their understanding of the risks.

A4.33 The analysis soon identified a third company which was continuing to conduct business in the gold industry. The ITX business line commenced an audit into this company in July 2012. The audit was finalised in December 2012, however, the audit had uncovered little evidence of how the transactions were carried out. As a result, the ITX business line focused on technical arguments regarding the GST refund claims, namely that the company had misclassified taxable supplies as GST-free, claimed input tax credits on input taxed supplies and claimed ITCs on second hand goods which did not meet the statutory definition.⁹⁸⁴ On this basis, the ATO had issued GST assessments to the company, including penalties for recklessness.⁹⁸⁵

A4.34 During the period over which the above audit was conducted, there were a number of relevant developments. First, the ITX business line had become aware of a CRA newsletter which had reported a typology of asset flipping. The typology was that of a scheme which had recently been detected in Canada and the identified behaviours appeared similar to those observed by the ITX business line in their profiling and audit work.⁹⁸⁶

A4.35 Second, the ITX profilers had commenced more detailed and wide-ranging profiling and analysis to understand the scope of the arrangement and links to other taxpayers. When the ITX profilers had concluded their analysis in December 2012, they

⁹⁷⁷ Nicholas Van Praet, 'Revenue Quebec investigates widespread gold fraud', *Financial Post* (online) 10 June 2011 <<http://business.financialpost.com>>.

⁹⁷⁸ An explanation of this taskforce is provided in Chapter 7 of this report.

⁹⁷⁹ ATO communication to the IGT, 20 July 2017.

⁹⁸⁰ *ibid.*

⁹⁸¹ ATO, 'Operational Intelligence Assessment' (Internal ATO document, March 2015) p 6.

⁹⁸² ATO communication to the IGT, 20 July 2017.

⁹⁸³ Above n 981, p 6.

⁹⁸⁴ ATO communication to the IGT, 20 July 2017.

⁹⁸⁵ ATO, 'Operational Intelligence Alert' (Internal ATO document, 20 June 2013).

⁹⁸⁶ ATO communication to the IGT, 20 July 2017.

had identified that the two liquidated companies had made a profit by not remitting the charged GST to the ATO. The ITCs which had corresponded to the GST charged by the two liquidated companies, however, was not claimed by the purchasers. The profilers had also identified that, with the benefit of hindsight, an additional \$59.85 million of GST refunds had been paid by the ATO for GST that had not been remitted to the ATO by five other companies over the 2010–2012 period. The ATO's suspect refund models had not stopped these refunds before they were paid.⁹⁸⁷

A4.36 The ITX profilers believed that some of the companies and related individuals were connected and acting together in the arrangement, either in full knowledge that the missing trader would not remit the GST to the ATO or by willfully ignoring suspicious transactions. The profiling work had also uncovered that one of the people connected to this suspected syndicate was known to law enforcement agencies.⁹⁸⁸

A4.37 The information and behaviours which had been identified by the profilers and audit teams prompted the ITX business line to conduct a broader scan of information in March 2013 as it was 'unknown how prevalent this type of behaviour [was] within the gold trading industry and what ... risks were involved.'⁹⁸⁹

ATO's Operation Nosean (May 2013 – June 2015)

A4.38 On 2 May 2013, the CACT made another referral to the ATO – this time to the former SNC business line⁹⁹⁰ (hereinafter referred to as the PGH business line⁹⁹¹) suggesting four groups that may be exploiting the GST rules for gold.⁹⁹² As a result, the ATO started Operation Nosean.⁹⁹³

Compliance strategy (May 2013 – October 2013)

A4.39 Soon after the above referral⁹⁹⁴, the ITX and PGH business lines agreed on a strategy to address the identified risks with respect to four potential syndicates.⁹⁹⁵ This strategy involved a combination of audits as well as the development of technical arguments.⁹⁹⁶ If such audits surfaced criminal conduct, the matters would be referred to PGH investigators who would commence criminal investigations. However, any cross-agency support would only be sought after the ATO's technical position had been developed and sufficient evidence obtained. This strategy appeared to be based on a view that the risk was localised to the identified transactions and activities of the

⁹⁸⁷ *ibid.*

⁹⁸⁸ *ibid.*

⁹⁸⁹ ATO, 'Operational Intelligence Alert' (Internal ATO document, 19 March 2013).

⁹⁹⁰ ATO, 'IGT Review Information Request - Precious Metals Timeline' (Internal ATO document, undated) p 1, which refers to CACT/SNC Meeting regarding specific activities undertaken by Indirect Taxes and further instructions.

⁹⁹¹ The SNC business line was incorporated within the PGH business line in July 2014.

⁹⁹² ATO, 'SNC/ITX cross BSL Risk strategy' (Internal ATO document, 15 May 2013).

⁹⁹³ ATO communication to the IGT, 'IGT-PM_REQ1' (undated) p 1.

⁹⁹⁴ Above n 990, p 3, refers to ATO, 'PGH Exec AC briefing – Gold Bullion Treatment Strategy' (Internal ATO document, 28 May 2013).

⁹⁹⁵ Inferred from ATO, 'Project Outline - Gold bullion' (Internal ATO document, 21 August 2013) p 7.

⁹⁹⁶ ATO, 'Precious metals Governance Chronology' (Internal ATO document, 28 February 2018) pp 1–2; *A New Tax System (Goods and Services) Act 1999* Div 165; Above n 995, p 5.

four suspected syndicates.⁹⁹⁷ The PGH and ITX Executives were briefed, activities were commenced and the two business lines met twice during June 2013 regarding the progress of the activities.⁹⁹⁸

A4.40 During ITX's intelligence gathering activities⁹⁹⁹, however, it was observed that there were numerous entities operating in 'gold supply chains' with missing traders. These entities had also experienced significant recent growth in turnover and a rapid increase in GST refund claims. For example, in one business there was a ten-fold increase in turnover in one financial year. The ITX business line had also observed different arrangements which exploited the GST rules for gold, including a missing trader typology with gold passing through four to five layers of entities, asset flipping, significant discrepancies between BAS and Customs forms regarding gold quantities and misclassification of supplies.¹⁰⁰⁰

A4.41 Accordingly, the ITX business line started to monitor the data reported by gold industry entities in their BASs. The ITX business line also requested other ATO teams to provide information and insights regarding the gold bullion and precious metal trading industries. In this request, the ITX business line noted that it was possible that others in the gold industry may be 'complicit by conspiring or choosing to ignore the fraudulent actions of others' and that this possibility appeared to be supported by some of the TERs that the ATO had received from the community.¹⁰⁰¹ Importantly, this ITX request appears to have been prompted by a concern that the risk was increasing significantly:

The observations ... indicate that significant revenue is potentially risk with tax evasion in the gold bullion and precious metal sectors. Recent open source reporting indicates an increased trend in the volumes and value of gold bullion trading from 2012. The operation of a number of [Groups] carrying out serious evasion in this sector could, if untreated, resulting in a rapid growth in serious evasion behaviour and subsequent increase risk to GST revenue.¹⁰⁰²

⁹⁹⁷ Above n 995, p 7.

⁹⁹⁸ Above n 990, pp 1 and 3; ATO, 'PGH Exec AC briefing - Gold Bullion Treatment Strategy' (Internal ATO document, 28 May 2013); Above n 992; ATO, 'PGH Exec briefing on ongoing risk for gold bullion industry' (Internal ATO document, 21 October 2013).

⁹⁹⁹ ATO 'Precious Metals Governance Chronology' (Internal ATO document, 28 February 2018) p 1.

¹⁰⁰⁰ Above n 985, pp 4-5.

¹⁰⁰¹ *ibid.*

¹⁰⁰² *ibid.*, p 5.

A4.42 The ATO commenced a risk assessment of the gold bullion industry in July 2013.¹⁰⁰³ One of the issues considered was whether the increase in turnover was due to commercial factors, such as increased demand in gold following the global financial crisis.¹⁰⁰⁴ However, the ATO's enquiries suggested that such an explanation did not explain the total increase. Furthermore, the public opinions of some gold industry participants cast doubt concerning the commercial explanation for the increased turnover:

One industry source said there simply isn't enough privately held gold in Australia to account for the volumes being traded, suggesting the same gold was being sold over and over again. Even if you melted down all the jewellery and fillings in the country there wouldn't be enough to cover the quantities involved...¹⁰⁰⁵

A4.43 By September 2013, concerns were raised within the ATO regarding the effectiveness of its strategy to appropriately protect the revenue from risk.¹⁰⁰⁶ It was considered that the ambiguity of the relevant GST laws had allowed suspicious arrangements to be structured in a way that gave them an appearance of authenticity.¹⁰⁰⁷ As a result, it was recommended that a change in approach was needed including:

- seeking assistance from law enforcement agencies;
- conducting data matching to better identify the risk population; and
- addressing the weaknesses in the law that were being exploited.¹⁰⁰⁸

A4.44 As a result, a criminal investigation was commenced and cross-agency support was sought.¹⁰⁰⁹

Search warrants executed (October 2013)

A4.45 On 29 October 2013, Operation Nosean became publicly known when the AFP executed 16 search warrants on gold industry entities that were thought to be connected with two of the four groups. At the same time, the ATO had issued amended GST assessments of approximately \$130.7 million including penalties and interest.¹⁰¹⁰

¹⁰⁰³ Above n 990, p 3, refers to 16 July 2013 Risk Assessment; ATO, 'Operational Intelligence Product Tasking Plan-GST Risk and Intelligence Precious Metals Project 2013-2014' (Internal ATO document, 25 October 2013).

¹⁰⁰⁴ Above n 936.

¹⁰⁰⁵ Chris Vedelago, Cameron Houston, 'Rivers of gold: Raids take shine off alleged scam that has cost taxpayers an estimated \$200m', *Sydney Morning Herald*, 13 July 2014.

¹⁰⁰⁶ Above n 995, p 5.

¹⁰⁰⁷ ATO, 'Operational Intelligence Product Tasking Plan-GST Risk and Intelligence Precious Metals Project 2013-2014' (Internal ATO document, 25 October 2013).

¹⁰⁰⁸ Above n 995, pp 7-10.

¹⁰⁰⁹ Above n 990, pp 1 and 3; ATO, 'Cross agency meeting - gold bullion project - Agenda' (Internal ATO document, 17 September 2013); Above n 990, p 1, which refers to 14/10 Cross Agency Meeting SNC/ATP/ITX (Agenda/Minutes/Presentation Gold Bullion); AFP, *Annual Report 2013-14* (2014) p 55.

¹⁰¹⁰ Above n 981, p 6. It was later reported that the amount collected was \$22 million: AFP, *Annual Report 2013-14* (2014) p 55.

A4.46 The ATO observed that the search warrants had an immediate impact on the behaviour of some gold industry entities as there was a substantial decrease in the amount of ITCs that were claimed in BASs lodged.¹⁰¹¹ For some entities in the gold industry, GST refund claims had decreased more than 90 per cent from that claimed in September 2013. Also, the total amount of GST refunds claimed by recognised refiners' in this period had halved.¹⁰¹²

A4.47 The above decreases, however, do not, of themselves, indicate that these entities had engaged in any illegal activity as they may have been an innocent and unwitting party to subsequent transactions in the broader chain of transactions. In any event, the impact of the search warrants was short lived as the total amount of GST refund claims began to increase again from January 2014.¹⁰¹³

Criminal investigations (from November 2013)

A4.48 In November 2013, the PGH business line also commenced a criminal investigation into entities in one of the groups¹⁰¹⁴ with a view to referring briefs of evidence to the CDPP for prosecution.¹⁰¹⁵ On 1 April 2015, a cross agency workshop¹⁰¹⁶ was held following which the brief of evidence was referred to the CDPP¹⁰¹⁷ recommending charges be brought against the entities for conspiracy to defraud the Commonwealth and dealing with the proceeds of crime. The CDPP accepted the brief. However, fifteen months later in July 2016, the CDPP asked the ATO to undertake additional work, including forensic accounting analysis.¹⁰¹⁸ This work continued until early 2018 when two people were charged and they are due to appear in court on 4 September 2018.¹⁰¹⁹

A4.49 Due to resource constraints¹⁰²⁰, the ATO delayed the commencement of a further criminal investigation until January 2015.¹⁰²¹ On 10 May 2016, a cross-agency Gold Bullion Prosecution Workshop was held to discuss the investigation's progress on this group¹⁰²² and six months later the ATO made a formal referral to the SFCT to investigate the gold fraud which was later accepted for investigation and treatment.¹⁰²³ It was agreed that PGH investigators would conduct the investigation together with seconded AFP officers.¹⁰²⁴ In February 2017, the ATO hosted an intra-agency workshop with representatives from the ATO's ITX and PGH business lines, AFP, AUSTRAC,

¹⁰¹¹ Above n 981, p 6.

¹⁰¹² ATO, communication to the IGT, 8 January 2018.

¹⁰¹³ *ibid.*

¹⁰¹⁴ ATO, 'Minutes of meeting, Cross Agency Workshop - Operation Nosean' (Internal ATO document, 24 June 2014) p 2.

¹⁰¹⁵ ATO, 'Commissioner Briefing Minute' (Internal ATO document, 25 October 2016) p 2.

¹⁰¹⁶ Above n 990, p 1.

¹⁰¹⁷ Above n 981, p 6.

¹⁰¹⁸ ATO communication to the IGT, 12 July 2017.

¹⁰¹⁹ Commonwealth, Senate Economics Legislation Committee, *Proof Committee Hansard - Estimates*, 28 February 2018, p 69 (Deputy Commissioner of the PGH business line).

¹⁰²⁰ Above n 1014, p 7.

¹⁰²¹ *ibid.*, p 6; Above n 1015, pp 1-2.

¹⁰²² ATO communication to the IGT, 6 June 2018.

¹⁰²³ ATO, 'Project Status Report (1 November 2016 - 28 February 2017)' (Internal ATO document, undated) p 6.

¹⁰²⁴ ATO communication to the IGT, 12 July 2017.

ASIC, ACIC and the CDPP to consider and discuss a draft investigation plan for the referral.¹⁰²⁵ Importantly, this meeting involved the CDPP which would assist in addressing issues early in the investigatory process rather than addressing the issues after the brief of evidence had been prepared and sent to the CDPP. The SFCT Treatment forum reviewed this investigation in October 2017 and endorsed a recommendation to close this operation.¹⁰²⁶

A4.50 No criminal investigation has been commenced with respect to the other two groups.

Cross-agency work (May 2013 – March 2015)

A4.51 Meetings between the ATO, CACT, AFP and ACC have been held on a periodic basis. It has been an important forum to discuss operational issues. In mid-June 2014, a third cross-agency workshop was held between the relevant areas of agencies involved, including AFP investigatory staff, CACT staff, ACC investigators as well as relevant ATO officers including ITX objections officers, ITX auditors, PGH auditors, PGH investigators and Tax Counsel Network (TCN) officers.¹⁰²⁷ At this workshop, progress on the ITX audit, PGH prosecution and CACT's Proceeds of Crime work on three Groups were discussed.

A4.52 Cross-agency cooperation and contribution was seen as important to Operation Nosean's success and the identified treatment strategies were seen as 'a model for the future'. For example, the search warrants that had been executed in October 2013 had effectively shut down two of the groups' GST refund claims. Notwithstanding these observations, however, there were emerging groups that appeared to be 'moving large sums of cash'. The strategies remained the same as before, i.e. the ITX business line's audits and PGH's criminal investigation continued.¹⁰²⁸

A4.53 The interagency meetings also provided opportunity for participants to discuss how each agency's contribution could be utilised and coordinated. Also, discussed were how delays and difficulties experienced by one party was affecting others.¹⁰²⁹

Interpretative issues (January 2013 – January 2015)

A4.54 Interpretative issues had begun to surface soon after the conclusion of the initial audit in December 2012. For example, in that audit the taxpayer's representative subsequently pointed out to the ATO that the auditor's view on the second hand goods issue was contrary to that which had been provided in previous private rulings issued to other entities. Accordingly, in June 2013, the ITX business line had engaged its technical area, Central Technical Support, to obtain the ATO view on two main

¹⁰²⁵ Above n 1023, p 10.

¹⁰²⁶ ATO communication to the IGT, 23 April 2018.

¹⁰²⁷ Above n 1014, p 9.

¹⁰²⁸ *ibid.*, pp 2, 6 and 9.

¹⁰²⁹ *ibid.*, p 4.

interpretative issues of concern.¹⁰³⁰ The first issue concerned the tax treatment of gold in investment form which had been refined from scrap gold. The issue was whether the sale of that gold was the first sale and if so, was it a GST-free supply. The second issue was whether entities were entitled to claim ITCs for the gold component of second hand jewellery¹⁰³¹ that was acquired.¹⁰³²

A4.55 The views taken on the above two issues were important to resolve as they were intended to form the technical basis for an ITX compliance strategy which would retain GST refunds due to gold refiners. Previously, there were no specific internal controls to address the exploitation of the GST rules for gold, apart from the ATO's usual compliance activities¹⁰³³ and retention of refunds appeared to be more appropriate than targeting missing traders after refunds had been issued.

A4.56 In October 2013, there was an escalation to the Special Tech Projects (STP) unit in the ITX business line to confirm the ATO view on the above issues. The STP unit confirmed that the view would support the refund retention strategy. As a result, the ITX business line began retaining refiners' GST refunds in November 2013.¹⁰³⁴

A4.57 The ITX's retention strategy, however, was stopped by TCN's November 2013 advice, overturning the advice of STP.¹⁰³⁵ The ITX business line understood that TCN would review GSTR 2003/10.¹⁰³⁶ However, later events indicated that this understanding was not shared by TCN.

A4.58 Notwithstanding the above TCN action, the ITX business line continued to identify and assess the system's vulnerabilities. It progressed work to clarify the technical issues by researching the application of the legislative framework. New Zealand's jurisdictional framework was also compared to that of Australia's, with a focus on assessing the impact that the term 'in an investment form' had on the definition of precious metals.

A4.59 A number of ITX audits had raised additional technical issues.¹⁰³⁷ As a result, the ITX business line approached TCN on 24 February 2014 for clarification of TCN's November 2013 advice.¹⁰³⁸ This clarification was provided seven months later in September 2014.¹⁰³⁹

A4.60 In the meantime, during May 2014, TCN released a discussion paper which considered the potential law reform options to mitigate the identified risks¹⁰⁴⁰,

¹⁰³⁰ Above n 985, p 4.

¹⁰³¹ *A New Tax System (Goods and Services) Act 1999* Div 66.

¹⁰³² Above n 985.

¹⁰³³ Above n 1007.

¹⁰³⁴ ATO, '...Application of s 38-385 to 'precious metal' refined from scrap' (Internal ATO document, 27 November 2013) pp 1 and 5-6; Above n 999, p 4.

¹⁰³⁵ Above n 1034, p 1.

¹⁰³⁶ Above n 999, p 4.

¹⁰³⁷ *A New Tax System (Goods and Services) Act 1999* s 66-5(1).

¹⁰³⁸ Above n 990, p 4; Above n 999, p 2.

¹⁰³⁹ Above n 999, p 2.

¹⁰⁴⁰ *ibid.*, p 3; Above n 936; Above n 1014, p 9.

including amendment of the definitions of 'refining'¹⁰⁴¹ and 'second hand goods'¹⁰⁴². These options were intended to be canvassed with Department of Treasury and, to do so, the support of an ATO internal Law Advisory Working Group (LAWG) was needed.¹⁰⁴³ The ITX business line had begun to seek such support on 30 May 2014, however, it was decided that any such work should await TCN's agreement to review GSTR 2003/10.¹⁰⁴⁴

A4.61 TCN provided advice to the ITX business line on some issues on 24 July 2014. The ITX business line, then, requested advice on the other issues and TCN provided such advice on February 2015.

A4.62 In reflecting on the events, the ITX business line observed that the inability to quickly resolve the technical ambiguities limited the ATO's ability to progress audits and address the identified behaviours of concern:

At this stage, the ATO view remained unclear with preliminary audits and further compliance activities deemed to be on hold until an ATO view could be established, particularly for cases impacted by Div 66 Second Hand Goods provisions. Additionally, it was evident that the risk was systemic across the industry (sample of [ITX] initiated test cases e.g. exporters, buyers and second hand goods were progressed through audit). ITX ... had progressed the targeted compliance activities which demonstrated that the core provisions limited the Commissioner's ability to treat the behaviour.¹⁰⁴⁵

A4.63 During the last half of 2014, the ITX business line informally approached Treasury with its concerns. However, it was understood that a request for law change may not be supported at that time. The ITX business line then considered alternatives to law reform, for example an industry voluntary code of compliance¹⁰⁴⁶ and decided that a streamlined audit strategy would be the most effective alternative. However, greater clarity on the scope and types of non-compliance was needed.

Risk assessment of industry population (March 2013 – March 2015)

A4.64 As mentioned earlier, the ITX business line had commenced an information scan in March 2013. By November 2013, the key intelligence needs were specified which included determining the total number of gold industry entities, the portion involved in identified behaviours of concern and quantifying the potential revenue loss.¹⁰⁴⁷ Based on the information available to them at this time, the risk in the gold industry was estimated to total approximately \$300 million.¹⁰⁴⁸

A4.65 In mid-June 2014, the ITX business line initiated steps to acquire a dataset which could assist in obtaining the above information.¹⁰⁴⁹ By January 2015, the ATO

¹⁰⁴¹ *A New Tax System (Goods and Services Tax) Act 1999* s 38-385.

¹⁰⁴² *A New Tax System (Goods and Services Tax) Act 1999* Div 66; Above n 990, p 2.

¹⁰⁴³ Above n 936.

¹⁰⁴⁴ Above n 990, p 4, refers to contact established with Integrated Tax Design (ITD).

¹⁰⁴⁵ Above n 999, p 3.

¹⁰⁴⁶ *ibid.*; Above n 990, p 3.

¹⁰⁴⁷ Above n 1007, pp 2-3.

¹⁰⁴⁸ AFP, *Annual Report 2013-14* (2014) p 55.

¹⁰⁴⁹ Above n 990, p 3; Above n 999, p 3.

had obtained the first half of such a dataset.¹⁰⁵⁰ It revealed that the number of entities suspected of exploiting the GST rules for gold was ‘larger than first expected’.¹⁰⁵¹ This had indicated a ‘need to ensure an industry response ... to prevent proliferation in real time...’¹⁰⁵² In March 2015, the second half of the dataset was received.

A4.66 Based on the above full datasets as well as the ATO’s understanding of the risks and observations of the behaviours of concern, the ITX business line had estimated that the total amount of GST at risk could be more than \$2.45 billion – a total which was made up of an estimated \$850 million which had not been remitted to the ATO and an estimated additional \$1.609 billion of GST over the next three and a quarter years.¹⁰⁵³

A4.67 Based on the above information, the ITX business line formed the view that taking compliance action against the suspected entities would be ineffective in addressing the risks:

Compliance activity, including cross agency investigations and proceeds of crime action can only treat the symptoms and not the cause. Consequently priority focus needs to be applied to addressing the underlying legislative provisions.

...GST refund fraud associated with precious metal trading remains an ongoing problem as the inherent vulnerability with the GST system in this gold market means that compliance activity cannot effectively treat the risk [, and due to the] relative ease at which the fraud can be undertaken may make it an increasingly attractive proposition for organised crime and other fraudsters.¹⁰⁵⁴

A4.68 The Commissioner was briefed¹⁰⁵⁵ and the ATO later referred Operation Nosean to the AFP in June 2015 for further consideration.¹⁰⁵⁶

ATO’s Gold Project (March 2015 – August 2016)

A4.69 In July 2015, the ITX business line commenced the Gold Project with a ‘more holistic approach to the risk treatment and reduced audit timeframes’.¹⁰⁵⁷

Audit case work

A4.70 The Gold Project was subject to the direct oversight of an ITX Assistant Commissioner and involved key stakeholders from other business lines including

¹⁰⁵⁰ Above n 990, p 2; ATO, ‘Precious Metals (Gold Project) an Indirect Tax Executive Submission Paper’ (Internal ATO document, 27 March 2015).

¹⁰⁵¹ ATO, ‘Precious Metals (Gold Project) an Indirect Tax Executive Submission Paper’ (Internal ATO document, 27 March 2015) p 2.

¹⁰⁵² *ibid.*

¹⁰⁵³ Note, the total estimate of total future revenue leakage was based on a three and a quarter year horizon and only half of the dataset which had been received at that time: Above n 1051, p 2.

¹⁰⁵⁴ Above n 981, pp 4 and 13.

¹⁰⁵⁵ Above n 990, p 4.

¹⁰⁵⁶ ATO communication to the IGT, (undated) ‘IGT-PM-REQ3’ p 3.

¹⁰⁵⁷ Above n 999, p 3; Above n 990, p 2.

RDR, TCN, Debt and PGH.¹⁰⁵⁸ In addition to the ITX business line's usual audit case call-overs, other case discussions were held particularly where refunds were retained or understanding of supply chain topologies would have benefited from input from other auditors and technical experts, for example, those in the TCN, Case and Technical Leadership, and Debt areas.¹⁰⁵⁹

A4.71 The Gold Project required more resources. It was estimated that, without increased resources, only \$147 million in revenue would be recovered and \$314 million in revenue leakage would be prevented. With additional resources it was expected that a further \$700 million in GST would be recovered and \$1.295 billion in revenue leakage would be prevented.¹⁰⁶⁰

A4.72 The ITX business line reassigned officers to the Gold Project from other areas of the ATO and aimed to increase personnel from 33 officers in March 2015 to 48 officers in the 2014-15 financial year and to 57 in the 2015-16 financial year. The largest intended increases in personnel were directed towards the review and audit functions. However, it was forecast that ITX staff would reduce to 10 FTE in the 2016-17 year.¹⁰⁶¹

A4.73 During these ATO audits, it was discovered that a number of entities had links to suspected organised crime groups.¹⁰⁶²

Using the GAAR (June 2014 – August 2016)

A4.74 The GAAR was initially applied to an entity in June 2014¹⁰⁶³ after the ATO was unable to obtain evidence to support its view that ITCs were not allowed to be claimed as the gold was input taxed.¹⁰⁶⁴ However, it was noted that there were difficulties in applying the GAAR due to insufficient information on how the arrangements were carried out.

A4.75 Following a concerted ATO information gathering effort, preliminary advice was obtained from the Chair of the GAAR Panel¹⁰⁶⁵ which had provided further clarification to the ATO team as to the arguments that were to be put to the entities.¹⁰⁶⁶ Advice was also obtained from TCN in September 2014¹⁰⁶⁷ on the GAAR in this case¹⁰⁶⁸ and the case was presented to the GAAR Panel in February 2016.¹⁰⁶⁹ After considering the entities' views, the GAAR Panel concluded that it was reasonable to apply the

¹⁰⁵⁸ ATO, 'ITX Precious Metals Project' (Internal ATO document, undated).

¹⁰⁵⁹ Above n 999, p 3.

¹⁰⁶⁰ Above n 1051.

¹⁰⁶¹ *ibid.*

¹⁰⁶² Above n 1023, p 17.

¹⁰⁶³ Above n 1014, pp 2 and 9.

¹⁰⁶⁴ ATO communication to the IGT, 19 December 2017; Above n 990, p 2.

¹⁰⁶⁵ Above n 990, p 3.

¹⁰⁶⁶ ATO, 'GST and precious metals - Senate Estimates' (Internal ATO document, March 2017) p 3.

¹⁰⁶⁷ Above n 999, p 2.

¹⁰⁶⁸ ATO, 'Note: Application of the *A New Tax System (Goods and Services) Act 1999* (GST Act) to gold schemes' (Internal ATO document, 13 February 2015) pp 9-11.

¹⁰⁶⁹ Above n 1058.

GAAR¹⁰⁷⁰ and assessments were issued to the relevant entities in April 2016.¹⁰⁷¹ In response, the relevant entities lodged objections. A different ATO technical team considered the objections and, in September 2016, the ATO disallowed them.¹⁰⁷² Some entities went into liquidation and some sought further review including review of the GAAR assessments.¹⁰⁷³

A4.76 The GAAR was applied in another case in August 2016 and the relevant entity also went into liquidation. A third case was identified in February 2017 and the ATO considered the application of the GAAR in other cases in 2018.¹⁰⁷⁴

A4.77 On reflection, the ATO observed:

The anti-avoidance provisions may prove effective [to prevent revenue leakage] in some instances; however, this requires significant investment of time to address the complexities of Division 165, with unknown prospects of success in potential litigation, after the fact.¹⁰⁷⁵

Focus on law reform (March 2015 – August 2016)

A4.78 The need to address the weakness in the law became a priority focus from March 2015 and the ITX business line resubmitted their request to TCN to clarify their advice.¹⁰⁷⁶ The LAWG was also reconvened for the purpose of seeking policy advice from Treasury and the focus became seeking law reform.¹⁰⁷⁷

A4.79 Treasury were informally advised of the ATO's concerns.¹⁰⁷⁸ A briefing was also provided to representatives from the States and Territories as they are the recipients of GST revenue¹⁰⁷⁹ even though it is collected by the Commonwealth.¹⁰⁸⁰

A4.80 In preparation for the ATO's formal approach to Treasury¹⁰⁸¹, TCN provided clarification of the ATO's view¹⁰⁸² and the ATO's Revenue Analysis Branch was also asked 'to provide the most accurate population and potential figure including providing consideration of potential proliferation if risk is left untreated'.¹⁰⁸³ The

¹⁰⁷⁰ *ibid.*; Above n 1015, p 2.

¹⁰⁷¹ Above n 1015, p 1; see Above n 1023, p 8.

¹⁰⁷² Above n 1066, p 3.

¹⁰⁷³ Above n 1023, p 8.

¹⁰⁷⁴ *ibid.*; ATO, 'GST Product Committee' (Internal ATO document, 21 April 2017) p 2.

¹⁰⁷⁵ ATO, 'Action Brief GST Treatment of Precious Metals' (Internal ATO document, 26 August 2016) pp 5–6.

¹⁰⁷⁶ Above n 990, p 4.

¹⁰⁷⁷ Above n 999, p 5.

¹⁰⁷⁸ Above n 981, p 5.

¹⁰⁷⁹ Above n 990, p 3.

¹⁰⁸⁰ Council of Australian Governments, *Intergovernmental Agreement on Federal Financial Relations* (2011) cl 25.

¹⁰⁸¹ Above n 990, p 4; Above n 981, p 5.

¹⁰⁸² TCN responded to the ITX business line's March 2015 request for clarification that gold need not have LBMA accredited hallmarks to be in 'investment form' and confirmed its early advice on the second hand good issue: Above n 999, p 3; ATO, 'TCN advice' (Internal ATO document, 25 March 2015).

¹⁰⁸³ ATO, 'Precious Metals – Law Advocacy Action Items' (Internal ATO document, 20 October 2015) p 5.

LAWG was also tasked with developing a response to Treasury's request for advice regarding a related matter.¹⁰⁸⁴ This response was provided on 18 November 2015.

A4.81 The ATO had also consulted with their counterparts in selected overseas jurisdictions, namely the UK's HMRC, the CRA, New Zealand's IRD and the Inland Revenue Authority of Singapore on the options for legislative and administrative reform to improve compliance.¹⁰⁸⁵

A4.82 In addition to the earlier request for advice, on 20 January 2016, the ATO formally alerted Treasury¹⁰⁸⁶ to its concerns with the exploitation it had observed regarding the GST rules for gold, the ineffectiveness of compliance actions and that it was considering options to reduce the prevalence of non-compliance.¹⁰⁸⁷

A4.83 The ATO then developed options to address the issues and by April 2016, it had produced an Options Paper (April 2016 Options Paper) which identified 12 options. One of the options was to implement a 'recipient GST remittance' system which would require a purchaser to remit any GST on an acquisition of any good containing precious metals and allow those recipients to claim input tax credits (a reverse charge). As these two amounts would generally offset one another, requiring a purchaser to retain the GST would reduce the risk of unremitted GST and missing trader fraud. However, such a requirement would also increase compliance costs for some in the industry and would not address the issues arising from the misrepresentation of second hand goods.¹⁰⁸⁸ It should be noted that a reverse charge had been suggested by an external representative in January 2014 and again in December 2014.

A4.84 One of the other options proposed was to change the law to limit the 'in an investment form' requirement to GST-free supplies and input tax all supplies of precious metal 'in any form'. Such a change would still allow ITCs to be claimed on lower grade precious metals in second hand goods, such as jewellery.¹⁰⁸⁹

A4.85 In August 2016, the ATO provided its formal advice on the issues and the options for Government's consideration.¹⁰⁹⁰

ATO's Precious Metals Project (September 2016 – April 2017)

A4.86 The total GST refund claims by the seven main gold refiners rose from \$3 million per month in January 2016¹⁰⁹¹ to \$14 million per month in August 2016.¹⁰⁹² As a result, the ATO refocused its streamlined audit strategy to 'holistically mitigate

¹⁰⁸⁴ *ibid.*, p 2; see also, ATO, 'Precious Metals - Law Advocacy Action Items' (Internal ATO document, 10 November 2015) p 3.

¹⁰⁸⁵ Above n 990, p 4.

¹⁰⁸⁶ ATO, 'Advocacy Alert - GST on precious metals', 20 January 2016, pp 1-2.

¹⁰⁸⁷ ATO, 'ITX Executive Briefing Minute' (Internal ATO document, 6 May 2016).

¹⁰⁸⁸ Above n 936, pp 25-26.

¹⁰⁸⁹ *ibid.*, p 22.

¹⁰⁹⁰ Above n 1075, pp 1-2.

¹⁰⁹¹ ATO, 'Indirect Tax SES Brief-Big four Meetings' (Internal ATO document, 27 October 2017).

¹⁰⁹² Above n 1058.

the ATO's revenue risk and seek to change the behaviour identified within the precious metals risk population.¹⁰⁹³ This new phase was called the Precious Metals Project (PMP).

A4.87 The PMP was led by the ITX business line and aimed to integrate compliance activity, debt action, advice to industry, reform to the *A New Tax System (Goods and Services Tax) Act 1999* (GST Act), engagement with the SFCT and referrals for prosecution.¹⁰⁹⁴

A4.88 The PMP was directly overseen by an SES Band 2 officer Steering Committee which had enabled the ATO to marshal resources across the agency, initiate interagency assistance and respond quickly to non-routine issues.¹⁰⁹⁵ For example, the Steering Committee assisted by allowing ATO officers to quickly engage and brief external Counsel on the retention strategy and allocated resources to issue a draft GST determination in February 2017. In monitoring progress on criminal investigations, it approved the scope of briefs of evidence and interagency workshops on investigatory matters as well as ensured that debt action activity was monitored.¹⁰⁹⁶

Refiner retention strategy

A4.89 A key strategy of the PMP was to review and, where applicable, retain the monthly GST refunds¹⁰⁹⁷ of gold refiners¹⁰⁹⁸, subject to verification.¹⁰⁹⁹ This strategy was implemented in September 2016¹¹⁰⁰ and led to considerable litigation, including objections to the retention decisions. Such litigation was conducted in addition to appeals to the AAT and Federal Court regarding ATO assessments of tax and judicial review of ATO decisions.¹¹⁰¹

A4.90 In February 2017, the AAT upheld the Commissioner's assessment, in one of the above cases, to disallow claimed ITCs as, amongst other grounds, the entity did not adduce sufficient evidence to support its contentions regarding the transactions.¹¹⁰²

A4.91 According to a media article, the above refund retention strategy had significant impact on the working capital of the refiners and some retrenched staff.¹¹⁰³ Parallels were also drawn with a 2006 European Court of Justice decision which reversed HMRC's decision to retain VAT refunds of taxpayers who were unknowingly part of a supply chain in which transactions were vitiated by VAT fraud.¹¹⁰⁴ The ATO's

¹⁰⁹³ Above n 1074, p 1.

¹⁰⁹⁴ *ibid.*

¹⁰⁹⁵ ATO, 'PMP Steering Committee Minutes of Meeting' (Internal ATO document, 13 October 2016).

¹⁰⁹⁶ ATO, 'PMP Band 2 Steering Committee - Action Item register' (Internal ATO document, 10 March 2017).

¹⁰⁹⁷ *Taxation Administration Act 1953* s 8AAZLGA.

¹⁰⁹⁸ Above n 1058.

¹⁰⁹⁹ Above n 1074, p 2.

¹¹⁰⁰ Above n 990, p 2.

¹¹⁰¹ *Judiciary Act 1903* s 39B; ATO, 'Commissioner Briefing' (Internal ATO document, 17 May 2017).

¹¹⁰² *Eastwin Trade Pty Ltd v Commissioner of Taxation* [2017] AATA 140.

¹¹⁰³ Robert Gottliebson, 'Tax office in stunning U-turn on gold tax fraud', *The Australian*, 11 January 2017.

¹¹⁰⁴ *Optigen Ltd (C-354/03), Fulcrum Electronics Ltd (C-355/03) and Bond House Systems Ltd (C-484/03) v Commissioners of Customs & Excise*, Judgment of the European Court (Third Chamber), 12 January 2006, 62003CJ0354.

GST refunds verification processes are explored in more detail in the IGT's *GST Refunds* review.¹¹⁰⁵

A4.92 In the first month of the PMP, the ATO observed that the aggregate GST refunds for the refiners had dropped from \$14 million in August 2016 to \$3.5 million in September 2016. By December 2016, the aggregated refund amount had dropped further to \$332,000.¹¹⁰⁶ The ATO observed that the strategy appeared to reduce the volume of scrap gold to that which was transacted in 2011¹¹⁰⁷ and believed that this reduction 'directly supported the ATO's assertion that the scheme perpetuated by the risk population has created an artificial and contrived scrap gold market'.¹¹⁰⁸

A4.93 The ITX business line, however, continued to monitor the relevant supply chains to identify whether they would extract GST refunds through other means. As a result, the ATO identified that they may have been exporting scrap gold to obtain GST refunds as well as selling the gold offshore. It was suspected that, in the latter case, the gold was then repatriated to Australia as GST-free investment form gold, which was then recirculated through the supply chains.¹¹⁰⁹

Voluntary reverse charge

A4.94 In December 2016, the ATO sent a letter to 60 of the entities under ATO review¹¹¹⁰ to make an offer regarding future GST refunds. The letter explained that by adopting a voluntary reverse charge approach, their GST refund claims would be processed faster as it would lessen the chance of ATO enquiries and they would not need to collect the GST on the sale.¹¹¹¹ The letter was sent to the remaining entities in the risk population in January 2017.¹¹¹² The ATO knew, however, that the voluntary reverse charge would only be effective if every entity in a supply chain adopted this approach.¹¹¹³

A4.95 The voluntary charge was implemented in January 2017 following industry consultation.¹¹¹⁴ However, only a small proportion of the gold industry participated in the voluntary reverse charge initiative.¹¹¹⁵ The ATO was still of the view that legislative change was needed to overcome this issue.¹¹¹⁶

¹¹⁰⁵ Above n 8.

¹¹⁰⁶ ATO communication to the IGT, 12 July 2017.

¹¹⁰⁷ Above n 1023, p 10.

¹¹⁰⁸ Above n 1074, p 2.

¹¹⁰⁹ ATO communication to the IGT, 12 July 2017.

¹¹¹⁰ *ibid.*

¹¹¹¹ ATO communication to the IGT, 6 December 2017.

¹¹¹² ATO, 'Project Status Report' (Internal ATO document, 28 February 2017) p 3.

¹¹¹³ ATO communication to the IGT, 12 July 2017.

¹¹¹⁴ ATO, 'Ministerial Briefing' (Internal ATO document, 13 January 2017).

¹¹¹⁵ Above n 1091.

¹¹¹⁶ Above n 1114, p 3.

Legislative amendments (March 2017)

A4.96 On 31 March 2017, the Assistant Treasurer publicly announced the Government's intention to enact law to address the exploitation of the GST rules for gold. Broadly, a mandatory reverse charge for business to business purchases of precious metals would be introduced and the definition of 'second hand goods' would be amended to exclude any goods containing precious metals unless they were jewellery or a collectable. These amendments would be intended to apply from 1 April 2017.¹¹¹⁷

A4.97 On 1 June 2017, the proposed legislative amendments were introduced into Parliament.¹¹¹⁸ They received Royal Assent on 26 June 2017 with legal effect from 1 April 2017.

A4.98 In the most recent information available, the turnover of gold within the risk population in June 2017 had reduced to \$141 million as a result of the refund retention strategy and the legislative reverse charge. The ATO had also conducted a total of 221 cases resulting in GST and income tax assessments totaling \$879 million of which \$55 million was collected. As at October 2017, there were 87 cases on hand which were estimated to involve a further \$50 million in liabilities and eight cases were awaiting hearing in the AAT.¹¹¹⁹

Observation on the ATO undertakings

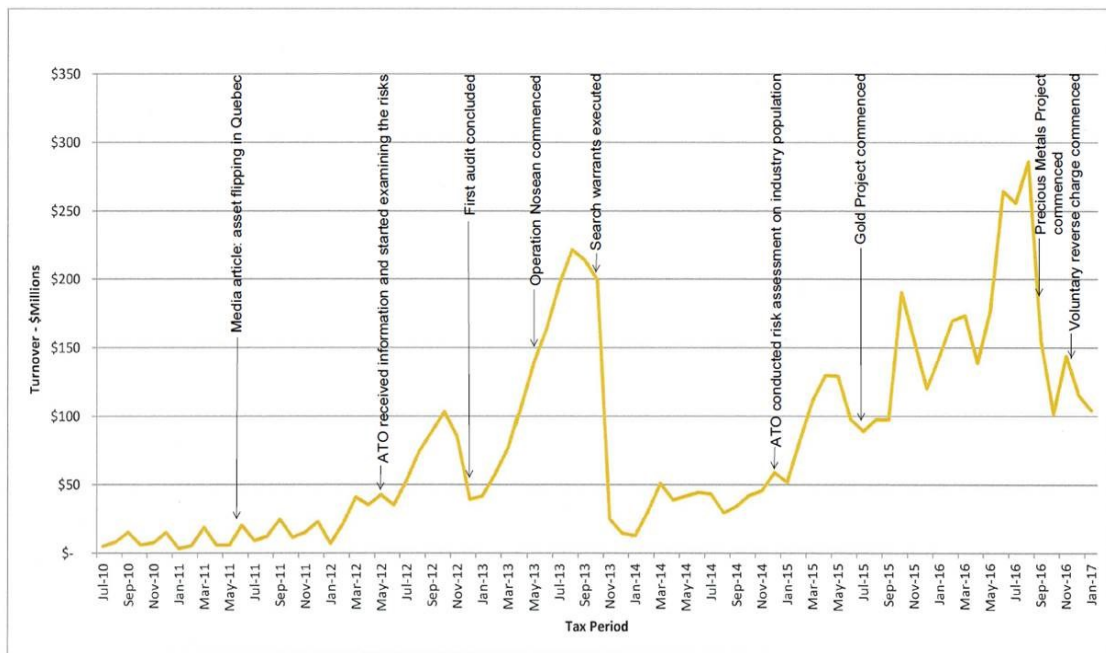
A4.99 Figure D3 below tracks the gold turnover for the risk population between July 2010 and January 2017. Key events are also identified.

¹¹¹⁷ The Hon. Kelly O'Dwyer, MP, Minister for Revenue and Financial Services, 'Combatting fraud in the precious metals industry' (Media Release, 31 March 2017).

¹¹¹⁸ Explanatory Memorandum to the Treasury Laws Amendment (GST Integrity) Bill 2017, p 3.

¹¹¹⁹ ATO, 'GST and precious metals - Senate Estimates' (Internal ATO document, October 2017).

Figure D3: Gold turnover within the risk population



Sources: ATO and other¹¹²⁰

A4.100 As illustrated in Figure D3, the gold turnover of the risk population did not total more than \$50 million before July 2012. The amount increased to more than \$200 million in July 2013, before dipping in November 2013 to less than \$30 million. From January 2014, the amount increased progressively and reached the peak in August 2016 of more than \$275 million before dipping once more to below \$150 million over the September 2016 to January 2017 period inclusive.

A4.101 In reflecting on the difficulties that were faced in addressing the risk presented by the exploitation of the GST rules for gold, the ATO has observed that a significant number of resources is needed to conduct enquiries to ascertain the true nature of transactions, map the supply networks, identify suspicious entities and determine the point in the supply chain where the gold had been altered.¹¹²¹ In addition, ATO auditors require a high degree of industry knowledge to determine the legitimacy of transactions.

A4.102 The ATO has also observed that when entities, involved in fraudulent activities, become aware of ATO enquiries, they may implement more complex supplier networks which in turn requires more ATO activities. Furthermore, even where suspicious entities and transactions are identified, recovery opportunities may be limited or unsuccessful as the entities may have dissipated assets or funds or left Australia permanently. As a result real-time responses are required to address phoenix type activities, new supply chain entrance and proliferation of suspicious arrangements.¹¹²²

¹¹²⁰ ATO communication to the IGT, 8 January 2018; Above n 977.

¹¹²¹ ATO, 'Precious Metals Industry Workshop' (Internal ATO document, 10 May 2016) pp 9-10.

¹¹²² *ibid.*, p 9.

APPENDIX E – ILLICIT TOBACCO TRADE

Introduction

A5.1 The manufacture and distribution of illicit tobacco (illicit tobacco trade) has been a long standing public policy issue for Australia and globally. For example, in 2015–16, almost \$600 million in tobacco duty was foregone as a result of such tobacco trade.¹¹²³ In addition to revenue forgone, the illicit tobacco trade has health policy, law enforcement, border control¹¹²⁴ and consumer protection implications.

A5.2 Those responsible for the smuggling or domestic cultivation of illicit tobacco are often linked to serious and organised crime syndicates who import other illicit drugs and seek to corrupt public officials¹¹²⁵ in an attempt to avoid payment of any excise or customs duty that may arise.¹¹²⁶

A5.3 The illicit tobacco trade can be defined as ‘any practice or conduct prohibited by law and which relates to production, shipment, receipt, possession, distribution, sale or purchase [of tobacco], including any practice or conduct intended to facilitate such activity’.¹¹²⁷ As the trade in illicit tobacco touches a number of laws and regulatory regimes, different agencies are involved in law enforcement efforts and different policy agencies are responsible for different aspects of the applicable legislative framework.

The regulation of tobacco

A5.4 Domestically produced tobacco products are subject to excise, pursuant to the *Excise Act 1901*, and imported tobacco products are subject to customs duties, under the *Customs Act 1901*. For some imported goods, the applicable rate of customs duty is the rate of excise duty that would apply if the goods were domestically produced.¹¹²⁸ These imported goods are known as ‘excise-equivalent goods’ (EEGs).

¹¹²³ The Hon. Kelly O’Dwyer, MP, Minister for Revenue and Financial Services, and the Hon. Peter Dutton, MP, Minister for Home Affairs, Immigration and Border Protection, ‘New illicit tobacco taskforce and tobacco duty measures to fight organised crime’ (Media Release, 6 May 2018).

¹¹²⁴ Parliamentary Joint Committee on Law Enforcement, ‘Terms of Reference’ (2016) *Inquiry into Illicit Tobacco* <www.aph.gov.au>.

¹¹²⁵ Australian Criminal Intelligence Commission (ACIC), *Organised Crime in Australia 2017* (2017) p 23; AFP, ‘Multi-agency operation destroys global criminal syndicate’ (Media Release, 10 August 2017); ACLEI, ‘ACLEI Operation Zeus’ (Media Statement, 10 August 2017).

¹¹²⁶ Department of Immigration and Border Protection (DIBP), Submission 77 to the Parliamentary Joint Committee on Law Enforcement, *Inquiry into Illicit Tobacco*, undated, p 3.

¹¹²⁷ World Health Organization (WHO) Framework Convention on Tobacco Control, WHO, *Protocol to Eliminate Illicit Trade in Tobacco Products* (2013) p 6.

¹¹²⁸ Explanatory Memorandum, House of Representatives, Excise Tariff Amendment (Tobacco Duty Harmonisation) Bill 2017, p 5 para [1.3].

A5.5 In 1999, administration of the *Excise Act 1901* was transferred from the then Australian Customs Service to the ATO. The *Customs Act 1901* is administered by the Department of Home Affairs, which was previously known as the Department of Immigration and Border Protection (DIBP). However, in 2010, the then DIBP delegated to the ATO authority to issue licenses for warehousing¹¹²⁹ EEGs upon which customs duty had not been paid¹¹³⁰ as well as the responsibility for controlling the movement of such EEGs.¹¹³¹ This delegation was designed to streamline services to taxpayers.

A5.6 Health-related regulation of tobacco is the responsibility of the Department of Health who investigates and enforces legislation which imposes restrictions on the presentation and appearance of tobacco packaging that is offered for sale or otherwise supplied.¹¹³² Violation of the relevant law carries heavy penalties.¹¹³³

A5.7 More broadly, the Department of Health has primary responsibility for developing the Government's public health policies, including those with respect to legally produced and marketed tobacco products¹¹³⁴, and administers the National Tobacco Strategy 2012–2018¹¹³⁵ which is part of the broader National Drug Strategy 2017–26, administered by the Ministerial Drug and Alcohol Forum.¹¹³⁶

A5.8 In addition to plain packaging requirements, it is an offence to offer tobacco products for sale if their packaging does not have health warning labels applied, including graphics.¹¹³⁷ Substantial financial penalties may be applied if such offences are committed. The relevant legislation is administered by the Australian Competition and Consumer Commission (ACCC).

Approaches and challenges to combatting the illicit tobacco trade

A5.9 There are dedicated areas within the above agencies which seek to address aspects of the illicit tobacco trade. For example, the ATO's ITX business line has dedicated areas to assessing and investigating fraud risks associated with non-payment of excise.¹¹³⁸ The ATO's approach in this area has previously included a 'disruption' strategy to make the practice of cultivating and distributing illicit tobacco

¹¹²⁹ *Customs Act 1901* s 79.

¹¹³⁰ DIBP, *Licencing – Warehouses, Depots and Brokers, Practice Statement PS2011/43* (29 September 2011) p 2.

¹¹³¹ ANAO, *ANAO Report No.34 2015–16 Performance Audit Administration of Tobacco Excise Equivalent Goods* (2016) p 17 para [1.8].

¹¹³² *Tobacco Plain Packaging Act 2011*.

¹¹³³ AFP, Submission 161 to the Parliamentary Joint Committee on Law Enforcement, *Inquiry into Illicit Tobacco*, February 2016, para [e].

¹¹³⁴ Department of Health, Submission 157 to the Parliamentary Joint Committee on Law Enforcement, *Inquiry into Illicit Tobacco*, February 2016, p 2.

¹¹³⁵ Australian Government, *National Tobacco Strategy 2012–18* (December 2012) <www.nationaldrugstrategy.gov.au>.

¹¹³⁶ Department of Health, Ministerial Drug and Alcohol Forum (21 February 2018) <www.health.gov.au>.

¹¹³⁷ See, Competition and Consumer (Tobacco) Information Standard 2011 which has the force of law by virtue of the *Competition and Consumer Act 2010* sch 2 s 134.

¹¹³⁸ The Excise Product Leadership in the ITX business line is responsible for the non-payment of excise risk.

less attractive to perpetrators of fraud by making such activities less profitable such as by destroying illicit tobacco crops.¹¹³⁹

A5.10 The ABF's Tobacco Strike Team¹¹⁴⁰ targets serious organised crime syndicates and other commercial enterprises that seek to make significant profits from illicit goods including the smuggling of tobacco across the border¹¹⁴¹ whilst the National Measurement Institute, pursuant to the delegated authority of the Department of Health, investigates potential contraventions of the plain packaging legislation and reports to the Department of Health's Tobacco Plain Packaging Enforcement Committee. The latter considers recommending enforcement action against any identified contraventions, including the commencement of administrative, civil or criminal proceedings.¹¹⁴²

A5.11 There are also a number of interagency forums aimed at addressing the illicit tobacco trade. For example, the Department of Health's Tobacco Control Interdepartmental Committee provides an interagency forum to discuss issues arising from tobacco control generally.¹¹⁴³ It has replaced the Illicit Tobacco Committee which had been focused on the illicit tobacco trade and was chaired by the then DIBP. The Department of Home Affairs chairs the Illicit Tobacco Industry Advisory Group which allows representatives from industry and government agencies to share information and discuss the illicit tobacco environment, including the illicit tobacco market.¹¹⁴⁴ It is usually attended by representatives from the Treasury, ATO, ACIC, ACCC, AFP, Department of Health and the tobacco industry.

A5.12 The ATO leads the Tobacco Stakeholder Group which is a forum for industry representatives, the ATO and the Department of Home Affairs to focus on improving the ATO's administration of the EEG regime. Representatives from the Treasury, ACCC and Department of Health may also attend meetings of this group.¹¹⁴⁵

A5.13 More recently, the Government has announced that a new multi-agency Illicit Tobacco Taskforce will be formed in July 2018, comprising members from a number of law enforcement and border security agencies, to combat illicit tobacco smuggling. This new taskforce is intended to build on the approach of the ABF's Tobacco Strike Team and have additional powers to enhance intelligence gathering and proactively target, disrupt and prosecute serious and organised crime groups at the centre of the illicit tobacco trade.¹¹⁴⁶

A5.14 The main challenges faced by the above agencies in combatting the illicit tobacco trade include the following:

¹¹³⁹ ATO, Submission 16 to the Parliamentary Joint Committee on Law Enforcement, *Inquiry into Illicit Tobacco*, undated, p 5.

¹¹⁴⁰ The Australian Border Force's Tobacco Strike Team was established in October 2015. See, above n 1126, p 6.

¹¹⁴¹ Above n 1126, p 6.

¹¹⁴² Department of Health, *Tobacco Plain Packaging Enforcement Policy* February 2013 (9 July 2014) para [5] <www.health.gov.au>.

¹¹⁴³ Answers to Questions on Notice to the Parliamentary Joint Committee on Law Enforcement, *Inquiry into Illicit Tobacco*, Canberra, 22 March 2017, Question 19 (Department of Health).

¹¹⁴⁴ Department of Home Affairs, *Illicit Tobacco Advisory Group* <www.homeaffairs.gov.au>.

¹¹⁴⁵ ATO, *Tobacco Stakeholder Group* (23 February 2018) <www.ato.gov.au>.

¹¹⁴⁶ Above n 745, p 12.

- obtaining the necessary assistance from overseas law enforcement agencies to intercept tobacco being illegally imported into Australia¹¹⁴⁷;
- penalties for cultivation of illicit tobacco not being aligned with those for smuggling illicit tobacco¹¹⁴⁸ – the Treasury Laws Amendment (Illicit Tobacco Offences) Bill 2018 (the 2018 Tobacco Bill), seeks to address this issue¹¹⁴⁹;
- satisfying the element of intent which is required for prosecution of importation, conveyance or possession of tobacco products with the intention of defrauding the Commonwealth¹¹⁵⁰ – enactment of the 2018 Tobacco Bill is aimed at addressing this issue with respect to certain offences¹¹⁵¹;
- proving the origin of illicit tobacco which may not be possible once the tobacco has been cut out of the ground,¹¹⁵² leading to regulators resorting to less punitive treatments, such as tax assessments for underreported income¹¹⁵³ – the 2018 Tobacco Bill is aimed at addressing this difficulty¹¹⁵⁴;
- aligning the public health policy objective¹¹⁵⁵ of the plain packaging legislation with the law enforcement use of that legislation to disrupt the efforts of organised crime¹¹⁵⁶ – proposed offences in the 2018 Tobacco Bill are aimed at addressing this difficulty¹¹⁵⁷;
- ensuring relevant agencies obtain the specialist capabilities of other agencies required to enforce certain laws¹¹⁵⁸; and
- accurately estimating the tax gap from the illicit tobacco trade or more specifically the customs duty gap and excise gap.¹¹⁵⁹

A5.15 In addition to the 2018 Tobacco Bill mentioned above, amendments to the *Customs Act 1901* have been introduced into Parliament which, amongst other changes, are intended to align the offences for illegally importing and domestically cultivating tobacco.¹¹⁶⁰ The Government has also recently announced a number of further measures to target the three main sources of illicit tobacco, namely: smuggling, leakage from licensed warehouses and domestic production. From 1 July 2019 importers will be required to hold a permit and pay all relevant duty and tax liabilities

¹¹⁴⁷ AFP, 'Multi-agency operation destroys global criminal syndicate' (Media release, 10 August 2017).

¹¹⁴⁸ ACLEI, 'Operation Zeus' (Media Statement, 10 August 2017).

¹¹⁴⁹ Explanatory Memorandum, House of Representatives, Treasury Laws Amendment (Illicit Tobacco Offences) Bill 2018 p 34 para [1.146].

¹¹⁵⁰ *Customs Act 1901* s 233BABAD.

¹¹⁵¹ Above n 1149, p 16 para [1.45].

¹¹⁵² Above n 1139, p 6 para [19].

¹¹⁵³ Evidence to the Parliamentary Joint Committee on Law Enforcement, Parliament of Australia, Canberra, 23 November 2016, p 8 (Assistant Commissioner, ATO).

¹¹⁵⁴ Above n 1149, p 16 para [1.47].

¹¹⁵⁵ Department of Health, Supplementary submission 157.1 to the Parliamentary Joint Committee on Law Enforcement, *Inquiry into Illicit Tobacco*, April 2016, p 4.

¹¹⁵⁶ Above n 1133, para [e].

¹¹⁵⁷ Above n 1149, p 18 para [1.55].

¹¹⁵⁸ Above n 1155, p 4.

¹¹⁵⁹ Evidence to the Parliamentary Joint Committee on Law Enforcement, Parliament of Australia, Canberra, 4 March 2016, p 23 (Assistant Commissioner, ATO).

¹¹⁶⁰ Customs Amendment (Illicit Tobacco Offences) Bill 2018.

upon importation. The ATO will also be provided further funding to combat the production of illicit domestic tobacco crop.¹¹⁶¹

¹¹⁶¹ Above n 745, p 12.

APPENDIX F – PANAMA PAPERS

Background

A6.1 In April 2016, the International Consortium of Investigative Journalists (ICIJ) coordinated the release of data leaked from the Panamanian law firm Mossack Fonseca, also known as the 'Panama Papers'. In May 2016, the ICIJ published the additional information containing details of entities implicated in the Panama Papers, including office holders and intermediaries connected to those entities.¹¹⁶²

A6.2 There were 200,000 entities mentioned in the Panama Papers which consisted of 11 million documents covering a period of almost 40 years from 1977 to 2015. The entities were tax resident in a wide range of countries including Australia.¹¹⁶³

Global regulatory and market response

A6.3 Two days after the Panama Papers were first publically reported, the OECD called an emergency meeting in Paris. In the months following this meeting, 150 major inquiries, audits and investigations were commenced by 79 countries involving more than 6,500 entities and individuals. For example, the European Parliament agreed to establish a 65-member committee to investigate potential money laundering and tax fraud, the authorities in Iceland referred 46 cases of potential tax evasion to prosecutors and Europol, Europe's law enforcement agency, reported that 3,469 of the individuals revealed by the Panama Papers had known links to organised crime, tax fraud and terrorism. India had commenced the country's largest-ever tax inquiry by establishing a special taskforce to investigate the offshore affairs of 415 Indians and France's Ministry of Finance commenced audits of 560 taxpayers. Announcements were also made by the CRA regarding the commencement of investigations into 85 individuals for tax evasion. Similarly, HMRC commenced 66 criminal and civil investigations that were expected to raise an additional £100m in tax revenue.¹¹⁶⁴

A6.4 The largest loss in the financial markets, as a result of data leaks or corporate scandals, was also experienced with approximately \$135 billion of the value for 400 publicly traded companies being lost. According to some academics, the drop in value reflected a belief by investors that the companies were exposed to potential fines for tax evasion and would find it more difficult to avoid paying tax in future.¹¹⁶⁵ Accordingly, some of the world's largest financial institutions were reported to have

¹¹⁶² ATO, 'PGI Panama Papers Project Communication Strategy 2017' (Internal ATO document, 2017).

¹¹⁶³ Above n 575; Elise Worthington, 'Panama Papers: Vladimir Putin associates, Jackie Chan identified in unprecedented leak of offshore financial records', *Australian Broadcasting Corporation* (online) 5 April 2016.

¹¹⁶⁴ Will Fitzgibbon and Emilia Díaz-Struck, 'Panama Papers Have Had Historic Global Effects – and the Impacts Keep Coming', ICIJ, 1 December 2016; Rajeev Syal, 'HMRC's struggling to deal with fallout of Paradise Papers leak', *The Guardian* (online) 12 January 2018.

¹¹⁶⁵ James O'Donovan, Hannes F. Wagner and Stefan Zeume, 'The Value of Offshore Secrets - Evidence from the Panama Papers' (Paper presented at the HKUST Finance Symposium 2017, Hong Kong, 19 April 2016) p 5.

formed response teams to identify suspicious accounts and customers of higher risk in an effort to minimise their exposure to potential criminal offences such as those involving money laundering and assisting clients to evade tax.¹¹⁶⁶

ATO and other agency responses to the Panama Papers

A6.5 On 4 April 2016, the ATO published a statement indicating that it had identified more than 800 individual taxpayers and had linked 120 of them to an offshore service provider located in Hong Kong. It advised that the data included taxpayers who were previously investigated by the ATO, including a small number who had previously made voluntary disclosures. However, the data also included a large number of taxpayers who had not disclosed their arrangements to the ATO including a number of high wealth individuals.¹¹⁶⁷

A6.6 Through the SFCT, a range of agencies conducted activities during a 'week of action' in September 2016. This included the ATO conducting '15 unannounced access visits in Victoria and Queensland and executed search warrants following analysis of the leaked information'. The AFP and ACIC executed these search warrants as part of two criminal investigations into a number of individuals linked to the Panama Papers. AUSTRAC and ACIC both issued media releases indicating their involvement and support for the operations.¹¹⁶⁸

A6.7 Specifically, as part of the SFCT's response, AUSTRAC engaged with domestic and international banks to build a picture of offshore service providers as they relate to Australian individuals and entities and identified professional facilitators, including accountants and lawyers, who had facilitated the creation of offshore structures and vehicles to conceal and move illicit wealth.¹¹⁶⁹

The ATO's work on the Panama Papers

A6.8 Within the ATO, the oversight of Panama Paper related activities was managed under the Offshore Tax Evasion Steering Committee, the SFCT Treatment Forum and operational interagency meetings. In addition, the ATO had a Data Steering Group to prioritise analytical needs.¹¹⁷⁰

¹¹⁶⁶ Will Fitzgibbon and Emilia Díaz-Struck, 'Panama Papers Have Had Historic Global Effects – and the Impacts Keep Coming', *ICIJ*, 1 December 2016, <<https://panamapapers.icij.org>>.

¹¹⁶⁷ ATO, 'ATO statement regarding release of taxpayer data' (Media Release, 4 April 2016).

¹¹⁶⁸ The Hon. Kelly O'Dwyer, MP, Minister for Revenue and Financial Services, 'No one hides from the tax system' (Media Release, 6 September 2016); Commonwealth, Senate Economics Legislation Committee, *Proof Committee Hansard - Estimates*, 25 October 2017, p 74 (Deputy Commissioner of the PGH business line); AUSTRAC, 'AUSTRAC follows the Panama Papers' money train' (Media Release, 6 September 2016); ACIC, 'ACIC response to Panama papers' (Media Release, 6 September 2016).

¹¹⁶⁹ The Hon. Kelly O'Dwyer MP, Minister for Revenue and Financial Services, 'No one hides from the tax system' (Media Release, 6 September 2016).

¹¹⁷⁰ ATO communication to the IGT, 12 February 2018; ATO, 'Smarter Data Edition 18' (Internal ATO document, undated).

A6.9 The ATO analysed ten data sets associated with the Panama Papers leak and obtained an additional seven data sets which were sourced through cooperation with revenue agencies in other jurisdictions and law enforcement authorities.¹¹⁷¹

A6.10 The ATO commenced a program of work to confirm the identity of names listed in the Panama Papers against taxpayer records in its possession. For example, as at 31 August 2017, the ATO's Smarter Data business line identified the TFNs of 1,184 of the 1,400 names published in the ICIJ Panama Papers and completed a preliminary risk assessment in relation to those taxpayers. Of these, 572 taxpayers were assessed as requiring further review and of those, 244 were identified as PGI taxpayers.¹¹⁷²

A6.11 The ATO has advised that 83 of the identified taxpayers were involved in previous compliance activities and nine taxpayers were linked to Project DO IT. In addition, 244 public corporate taxpayers were also profiled to determine whether they had links to Panama Papers' entities involved in cross-border arrangements.¹¹⁷³

A6.12 The PGI business line commenced a project to confirm whether identified taxpayers had connections to Mossack Fonseca and, if so, verify whether there was an indication of tax mischief or non-compliance. If necessary, the ATO would engage with the taxpayer to gain voluntary disclosure or begin compliance action.¹¹⁷⁴

A6.13 The above ATO compliance actions to date have determined that the majority of the taxpayers had 'met their obligations, as they were non-residents, had not derived any income or were operating legitimate businesses'.¹¹⁷⁵

A6.14 In a statement made on 13 November 2017, the ATO advised that their work on the Panama Papers had raised more than \$50 million in liabilities and uncovered an additional \$40 million of omitted income. The ATO's achievements in relation to the Panama Papers are summarised in the table below.¹¹⁷⁶

Table F.1: Results of ATO's activities on Panama Papers, as at 31 December 2017

Periods	ATO activity	Total cases	Cases in progress	Cases completed	Liabilities raised	Cash collected
2015-16	Reviews	34	27	7		
2016-17	Audits	88	138	207	\$3,002,810	\$4,552,742
	Reviews	257				
1 Jul 2017- 31 Dec 2017	Watching brief	9	104	74	\$50,556,560	\$3,789,128
	Audit	27				
	Voluntary disclosure	4				
	Reviews	138				
TOTAL		557	269	288	\$53,559,370	\$8,341,870

¹¹⁷¹ ATO, 'International tax evasion, including Panama Papers, Swiss bank matter and other data sets Senate Estimates Deputy Commissioner brief October 2017' (Internal ATO document, October 2017) p 3.

¹¹⁷² *ibid.*; ATO, 'Case Context Document Panama Papers Part 1' (Internal ATO document, 31 July 2017).

¹¹⁷³ *ibid.*; ATO communication to the IGT, 12 February 2018.

¹¹⁷⁴ ATO, 'Case Context Document Panama Papers Part 1' (Internal ATO document, 31 July 2017).

¹¹⁷⁵ Above n 1171.

¹¹⁷⁶ ATO, 'Paradise Papers and the ATO' (Media Release, QC 53909, 13 November 2017); ATO communication to the IGT, 12 February 2018.

7.75 As indicated by the table above, as at 31 December 2017, the ATO has completed 288 cases, with 269 cases in progress, and collected cash of \$8.3 million.

The ATO's model for future analysis of data sets

A6.15 Following its response to the Panama Papers, the ATO developed a strategy, namely: the Offshore Tax Evasion system, which aims to analyse future data received from partner agencies. The Offshore Tax Evasion system has 12 steps including cleansing data received from partner agencies and matching them against existing data sets before conducting compliance activities into those assessed to be high risk.¹¹⁷⁷

International collaboration

A6.16 The Panama Papers highlight the importance of international cooperation amongst revenue authorities to obtain relevant information about taxpayers and transactions. The OECD has noted that the use of cross-agency networks in the Panama Papers has 'resulted in a better understanding of evasion and avoidance arrangements, especially the role of intermediaries in these arrangements, improved exchange of information practices and an agreed collaborative approach to future data leaks'.¹¹⁷⁸

A6.17 Furthermore, incidents such as the Panama Papers provide a stimulus for revenue authorities to share information with one another in line with their information sharing agreements¹¹⁷⁹ and establishes methods of working collaboratively to process and analyse large data sets.

International response

A6.18 Legislatures in many countries have proposed to enact regulations and laws to address weaknesses pinpointed by the Panama Papers. These include requiring companies, who wish to set up in the US, to report their real owners to appropriate agencies.¹¹⁸⁰ The European Union, as well as a number of other countries such as New Zealand¹¹⁸¹ have also introduced similar measures.

¹¹⁷⁷ *ibid.*; ATO, 'Offshore Tax Evasion Strategy System Map - DRAFT' (Internal ATO document, undated).

¹¹⁷⁸ OECD, Forum on Tax Administration, 'Communique of the 11th Meeting of the OECD Forum on Tax Administration', Oslo, Norway (29 September 2017) <www.oecd.org>.

¹¹⁷⁹ OECD, 'Tax administrations meet on 'Panama Papers'' (13 April 2016) <www.oecd.org>.

¹¹⁸⁰ Michael Hudson, 'US Officials react to Panama Papers disclosures with get-tough proposals', *International Consortium of Investigative Journalists*, 6 May 2016 <<https://panamapapers.icij.org>>.

¹¹⁸¹ David Pegg and Hilary Osborne, 'EU to force companies to disclose owners with directive prompted by Panama Papers', *The Guardian* (online) 15 December 2017; ABC News, 'Panama Papers: New Zealand to tighten trust laws after being named in leaks', *Australian Broadcasting Corporation* (online) 13 July 2016.

APPENDIX G – PARADISE PAPERS

A7.1 In November 2017, the ICIJ co-ordinated the release of another leaked data set dubbed the 'Paradise Papers'. This leak comprises of 13.4 million documents dating from 1950 to 2016. Many of these documents originated from a Bermuda-based law firm, Appleby.¹¹⁸²

A7.2 It has been reported that the Paradise Papers revealed the expanded involvement of offshore tax providers and the 'extent to which intermediaries such as banks, law firms and accountants have commoditised tax avoidance' as well as how they may be 'encouraging this type of behaviour'.¹¹⁸³

A7.3 On 6 November 2017, the ATO announced that, as a result of working with overseas agencies, it would analyse the information contained in the Paradise Papers to identify possible Australian links. The ATO also indicated that it would work with the ACIC, AFP and AUSTRAC to build an intelligence base, undertake audits and, where appropriate, refer cases to the SFCT for criminal investigation.¹¹⁸⁴

A7.4 As at January 2018, the ATO has identified 344 entities and 731 individuals with possible links to the Paradise Papers.¹¹⁸⁵ The ATO has stated that it was too early to say if individuals identified were already known to the ATO. It will be 'looking closely at all [identified] taxpayers and take firm and decisive action' against those who have been found to 'be doing the wrong thing'.¹¹⁸⁶

A7.5 The OECD announced on 9 November 2017 that JITSIC was already working collaboratively on the issues raised by the Paradise Papers following the model adopted for the Panama Papers. The OECD also noted that increasing work on tax transparency such as the automatic exchange of offshore financial account information under the CRS was 'already having significant impacts'.¹¹⁸⁷

¹¹⁸² Four Corners and the International Consortium of Investigative Journalists, 'Paradise Papers, What is the leak and who is behind the firm Appleby?', *Australian Broadcasting Corporation* (online) 6 November 2017.

¹¹⁸³ Gareth Hutchens, 'Paradise Papers revealed commoditisation of tax avoidance', *The Guardian* (online) 16 January 2018.

¹¹⁸⁴ ATO, 'ATO statement regarding the 'Paradise Papers' (Media Release, QC 53852, 6 November 2017).

¹¹⁸⁵ ATO, 'Senate Estimates Brief' (Internal ATO document, February 2018).

¹¹⁸⁶ ATO, Submission to the Senate Economics References Committee, *Inquiry into Corporate Tax Avoidance*, 30 March 2017, p 16.

¹¹⁸⁷ OECD, 'Paradise Papers' leaks: Statement by Hans Christian Holte, Chair of the OECD's Forum on Tax Administration (9 November 2017) <www.oecd.org>.

APPENDIX H – ATO RESPONSE



Second Commissioner of Taxation

Mr Ali Noroozi
Inspector-General of Taxation
GPO Box 551
SYDNEY ACT 2001

Dear Ali

Review into the ATO's Fraud Control Management

Thank you for the opportunity to comment on the final draft of your report on the review into the *ATO's Fraud Control Management*.

The ATO recognises that this report thoroughly examines a challenging area in light of the revelations associated with Operation Elbrus and notes the overall IGT findings that:

- there is no evidence of actual internal fraud or corruption of a systemic nature within the ATO
- the ATO generally has sound systems in place for managing risks of internal fraud.

At the outset, the ATO highlights that we already have an extensive range of strategies, processes and procedures in place to address the underlying issues considered in the this review.

As you have reflected in your report, the examination of ATO practices, procedures and structures, and how they are enforced, is detailed. As the report also recognises, the ATO has undertaken reviews since Operation Elbrus and work following on from these reviews address a significant number of matters dealt with in the recommendations to this report. Where the ATO has agreed with the review's recommendations, we see this as supplementing the already solid foundations the ATO has in place to address the risk of internal and external fraud and associated issues.

The ATO agrees, has implemented, or agrees in part with the 13 recommendations in the report that are not a matter for government. We note within those 13 recommendations there are 41 elements – we agree with 32 of those elements, have already fully implemented five elements and disagree with the remaining four elements.

In this regard, you should note that where our response indicates that a recommendation has already been fully implemented, we will provide evidence of this to our Audit and Risk Committee who will, as per our normal processes, assure the implementation.

In relation to those elements of the recommendations with which we disagree, our position has been informed by the scope of the recommendation and the risk that is being addressed by it. In particular, in a number of these cases, our view is that our

existing strategies, process or procedures are a proportionate response to the risks presented, and accordingly no further action is warranted.

Our detailed response to the review is attached at Annexure 1.

We wish to take this opportunity to reiterate the ATO view that some details in Appendix B are not necessary in light of the purpose of the review. The review's terms of reference focuses on how the ATO addresses the risk of internal and external fraud and associated issues. It is appropriate for Appendix B to consider how ATO practices, procedures, structures and risk assessment techniques were applied in relation to the Plutus arrangements, and there is material appearing in Appendix B which does go to this end.

However, the ATO considers the material dealing with information on the periphery of the arrangements or some of the history associated with key alleged participants, all of which was sourced from media reports, to be in a different category. This material is presented in such a way that a reader may elevate these to matters of fact, when this cannot be verified at this point. In any case we consider the material is not required to sustain the IGT's findings and recommendations.

We also wish to offer our view on the issues dealt with in Appendix D, which is about external fraud risks in the precious metals industry. The ATO view is that these risks reflect significant complexity in the arrangements that are in place in some parts of this industry. The compliance risks have evolved as has the approach taken by the ATO to address them. Our view is that a number of entities operating within the precious metals industry have engaged in a significant fraud on the Australian community with many schemes utilising missing traders/carousel fraud and liquidation or phoenix of entities (bullion dealers, intermediaries and refiners). We undertook extensive compliance activity to identify the schemes with many of those entities involved now in litigation with the Commissioner. The law has now been amended to address the fraudulent activity in the precious metals industry.

The ATO is of the view that the response to this risk was appropriate having regard to the complexity of the issues and the evolution of the risk. Notwithstanding this, the ATO acknowledges improvements can be made in respect to how it identifies and addresses compliance risks and will endeavour to implement those improvements as noted in our response to the recommendations made in Chapter 6 of the report.

Finally, I would like to acknowledge the efforts of all involved in undertaking this review.

If you require further information on our response, please contact [REDACTED] on [REDACTED].

Yours sincerely



Neil Olesen
Second Commissioner
Australian Taxation Office



Jacqui Curtis
Chief Operating Officer
Australian Taxation Office

Date: 7 June 2018

SHORTENED FORMS

AAT	Administrative Appeals Tribunal
ABF	Australian Border Force
ACC	Australian Crime Commission
ACFE	Association of Certified Fraud Examiners
ACIC	Australian Criminal Intelligence Commission
ACLEI	Australian Commission for Law Enforcement Integrity
ACLEI Committee	Parliamentary Joint Committee on the ACLEI
ACNC	Australian Charities and Not-for-profits Commission
AFP	Australian Federal Police
AGD	Attorney-General's Department
AGIS	Australian Government Investigation Standards
AGSVA	Australian Government Security Vetting Agency
AIC	Australian Institute of Criminology
ANAO	Australian National Audit Office
APS	Australian Public Service
APS Commissioner's Directions	<i>Australian Public Service Commissioner's Directions 2016</i>
APSC	Australian Public Service Commission
ARC	Audit and Risk Committee
ASIC	Australian Securities and Investments Commission
ATO	Australian Taxation Office
ATOC	Australian Taxation Office Corporate
ATOP	Australian Taxation Office People
ATP	Aggressive Tax Planning
AUSTRAC	Australian Transaction Reports and Analysis Centre
BAS	business activity statements
BAU	business-as-usual
CACT	Criminal Assets Confiscation Taskforce
CDPP	Commonwealth Director of Public Prosecutions
CEI	Chief Executive Instruction
CEO	Chief Executive Officer

CFO	Chief Financial Officer
CHE	Cash and Hidden Economy
CIM	Complex Investigations Model
the Committee	Senate Standing References Committee on Economics
CPPS	Conduct Performance and Probationary Support
CRA	Canada Revenue Agency
CRS	Common Reporting Standard
CWB	counterproductive workplace behaviour
DSAP	designated security assessed position
EL	executive level
EO	Employer Obligations
EST	Enterprise Solutions & Technology
FAC Centre	the AFP's Fraud and Anti-Corruption Centre
FC	Financial Crimes
FCINet	Financial Criminal Investigation Network
FPII	Fraud Prevention and Internal Investigations
FTE	full-time equivalent
GAAR	general anti-avoidance rule
GST	Goods and Services Tax
GST Act	<i>A New Tax System (Goods and Services Tax) Act 1999</i>
HMRC	United Kingdom's Her Majesty's Revenue and Customs
HOCOLEA	Heads of Commonwealth Operational Law Enforcement Agencies
HR	human resources
IA	Internal Audit
IAS	Independent Assurance of Settlements
ICAC	NSW's Independent Commission Against Corruption
IGT	Inspector-General of Taxation
IRD	New Zealand's Inland Revenue Department
IRS	United States' Internal Revenue Service
IT	information technology
ITC	input tax credits
ITX	Indirect Taxes
JITSIC	Joint International Taskforce on Shared Information and Collaboration

NV1	Negative Vetting Level 1
NV2	Negative Vetting Level 2
OBA	Organisational Behavioural Assessment
OECD	Organisation for Economic Co-operation and Development
PAYG	Pay As You Go
PEIC	Pre-Engagement Integrity Check
PGH	Private Groups and High Wealth Individuals
PGI	Public Groups and International
PGPA Act	<i>Public Governance, Performance and Accountability Act 2013</i>
PGPA Rule	<i>Public Governance, Performance and Accountability Rule 2014</i>
PID	Public Interest Disclosure
PID Act	<i>Public Interest Disclosure Act 2013</i>
PST	People Support Team
RAPT	Risk Assessment Profiling Tool
RDR	Review and Dispute Resolution
SB	Small Business
SES	Senior Executive Service
SFCT	Serious Financial Crime Taskforce
SG	Superannuation Guarantee
Siebel	Australian Taxation Office's case management system
SME	Small and Medium Enterprises
SNC	Serious Non-Compliance
SPF training	security, privacy and fraud training
TAA	<i>Taxation Administration Act 1953</i>
TACC	Tasking and Coordination Committee
TCN	Tax Counsel Network
TEC	Tax Evasion and Crime
TER	tax evasion referral
TERC	Tax Evasion Referral Centre
TFN	tax file number
TIGTA	United States' Treasury Inspector General for Tax Administration
TPB	Tax Practitioners Board
User ID	User Identifier

