

The Auditor-General
Audit Report No.49 2010–11
Performance Audit

Fuel Tax Credits Scheme

Australian Taxation Office

Australian National Audit Office

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Canberra ACT
21 June 2011

Dear Mr President
Dear Mr Speaker

The Australian National Audit Office has undertaken an independent performance audit in the Australian Taxation Office with the authority contained in the *Auditor-General Act 1997*. I present the report of this audit and the accompanying brochure to the Parliament. The report is titled *Fuel Tax Credits Scheme*.

Following its presentation and receipt, the report will be placed on the Australian National Audit Office's Homepage—<http://www.anao.gov.au>.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Ian McPhee', is positioned above the printed name.

Ian McPhee
Auditor-General

The Honourable the President of the Senate
The Honourable the Speaker of the House of Representatives
Parliament House
Canberra ACT

AUDITING FOR AUSTRALIA

The Auditor-General is head of the Australian National Audit Office (ANAO). The ANAO assists the Auditor-General to carry out his duties under the *Auditor-General Act 1997* to undertake performance audits and financial statement audits of Commonwealth public sector bodies and to provide independent reports and advice for the Parliament, the Australian Government and the community. The aim is to improve Commonwealth public sector administration and accountability.

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Abbreviations

ANAO	Australian National Audit Office
ATO	Australian Taxation Office
BAS	Business Activity Statement
DAFGS	Diesel and Alternative Fuel Grants Scheme
DFRS	Diesel Fuel Rebate Scheme
EGCS	Energy Grants Credits Scheme
FTCS	Fuel Tax Credits Scheme
GCPP	Greenhouse Challenge Plus Program
GPS	Generic Payment System
GVM	Gross Vehicle Mass
IQF	Integrated Quality Framework
RRE	Risk Rating Engine

Glossary

Audit	An examination by the ATO of a taxpayer's affairs involving contact with the taxpayer.
Active Compliance	Review and audit activity undertaken by the ATO to substantiate the claims made by a taxpayer.
Generic Payment System	A system that processes Fuel Tax Credits Scheme claims which are not made via the BAS.
Objection	A taxpayer may seek a formal, impartial review of a decision made by the ATO.
Post-issue payment	Refers to compliance activity undertaken after the release of payments claimed through a BAS.
Pre-issue payment	Refers to compliance activity undertaken prior to the release of payments claimed through a BAS.
Review	An examination by the ATO of a taxpayer's claims that typically is restricted to a review of supporting documentation.
Risk Rating Engine	A system that applies criteria to determine a risk rating for Fuel Tax claims submitted via a taxpayer's BAS.

Summary and Recommendations

Summary

Introduction

1. The Australian Taxation Office (ATO) is the Australian Government's principal revenue collection agency. The role of the ATO is to manage and shape taxation, excise and superannuation administrative systems that fund services for Australians, giving effect to social and economic policy.¹ In 2009–10, the ATO collected over \$253 billion in tax, superannuation and excise revenue and incurred expenses of some \$3 billion.
2. The ATO is also responsible for administering various grant and transfer payments, which give effect to a range of government policies. The Fuel Tax Credits Scheme (Fuel Scheme) is one such transfer payment program. Under transfer payment programs, the Government provides a financial benefit to an individual, corporation or other entity without requiring a good or service in return.
3. The Fuel Scheme commenced on 1 July 2006, replacing the Energy Grants Credits Scheme (EGCS). Both schemes were designed to provide eligible businesses, and limited categories of non-business users of fuel, with a means to recover the excise included in the cost of fuel, when that fuel is used for specific purposes, as defined by each scheme. When claiming a fuel tax credit for fuel intended to be used in a vehicle, the amount able to be claimed is dependent on the gross vehicle mass and whether the vehicle is used for travelling on a public road.
4. The new Fuel Scheme expanded the eligibility provisions that applied under the EGCS², and is currently the largest transfer payment program administered by the ATO. The cost of the Fuel Scheme in 2009–10 was some \$5 billion, a 14.5 per cent increase on the \$4.4 billion incurred in the

¹ Australian Taxation Office, *Australian Taxation Office Annual Report 2008-09*, 2009, p. iii.

² For example, on 1 July 2006, eligibility expanded to include agriculture, fishing, forestry and other activities. On 1 July 2008, the eligibility criteria of the Scheme was further expanded to include additional activities, and significantly, to include petrol as a fuel that could be claimed under the Scheme.

Fuel Scheme's initial year of operation in 2006–07.³ This increase, in part, stems from the growth in the number of active participants after the eligibility criteria under the Fuel Scheme were extended. The total number of active participants has also increased by 31 per cent since the Fuel Scheme's introduction, from 146 874 as at 1 July 2006 to 191 751 as at 30 June 2010. The mining industry was the main claimant group, by value, in 2009–10.

5. At present, the maximum fuel tax credit to eligible participants is 38.143 cents per litre of fuel. For business entities, a fuel tax credit is claimed and adjusted through their Business Activity Statement (BAS). Individuals and non-profit entities that are not registered for the Goods and Service Tax (GST) can only submit claims via a pre-populated paper form.

6. The ATO publishes a range of guidance material to assist claimants to comply with their obligations under the Fuel Scheme. The Department of Infrastructure and Transport is also responsible for publishing information outlining the environmental criteria for the Fuel Scheme.⁴

7. Administration of the Fuel Tax Credits Scheme within the ATO is undertaken by specialist staff in the Indirect Tax (ITX) business line.

Audit objective and scope

8. The objective of the audit was to assess the effectiveness of the ATO's administration of the Fuel Tax Credits Scheme. Particular emphasis was given to the Fuel Scheme's:

- governance and reporting arrangements;
- risk management strategies; and
- compliance management program.

³ The cost of claims made in each year since 2006–07 includes costs associated with the Energy Grants Credits Scheme, as the ATO is unable to disaggregate payments made under each scheme. However, the quantum of Energy Grants Credits Scheme payments is relatively minor compared to the Fuel Tax Credits Scheme and is understood to have diminished significantly over time since the commencement of the Fuel Tax Credits Scheme.

⁴ Information that is made available on the Department's website includes the operation of the DT80 emissions test standard, the process for seeking accreditation for a vehicle maintenance program, appropriate record keeping, and representations regarding amendment or inclusions to the provisions specified in departmental vehicle maintenance schedules. The department publishes general guidance on these matters through the publication '*Guidelines for Environmental Criteria - Fuel Tax Credit for Heavy Diesel Vehicles*', supplemented by website material.

Overall conclusion

9. When the Fuel Tax Credits Scheme was introduced on 1 July 2006 as a replacement for the Energy Grants Credits Scheme (EGCS), it expanded eligibility provisions, refocused the fuel tax rebate system on the uses of fuel rather than on specific fuel types, and aimed to lower compliance costs for business.

10. In implementing the Fuel Scheme, the ATO was able to build on and refine the experience it had gained through administering the former EGCS. Existing administrative processes, such as claiming credits through the BAS, provided a generally effective basis for the ATO to collect and analyse most of the information required from participants to allow it to administer the Fuel Scheme, and to undertake risk analysis and compliance activity on a case by case basis, as required.

11. Overall, the ATO is effectively administering the Fuel Scheme. Governance, reporting and processing arrangements are generally sound. The Fuel Scheme's risk management strategies are appropriate and the compliance program addresses identified risks and non-compliant practices.

12. Governance arrangements support the administration of the Fuel Scheme at both the strategic and operational levels. At a strategic level, key governance bodies, including the Excise Product Committee and Excise Compliance Risk Forum, are well informed and provide appropriate direction, responding to identified risks and implementation issues over time. Operationally, effective governance is extended through decision making, review and quality assurance processes, which underpin, and provide assurance for, compliance decisions.

13. The ATO has in place various risk management strategies to address inappropriate or erroneous Fuel Scheme claims. Taxpayers are provided with guidance material to promote voluntary compliance, and claims are risk assessed at the pre-issue payment stage. The ATO also assesses all claims on a post-issue payment basis, including identifying claims which occur over multiple payment periods.

14. Over time, the ATO has modified its risk identification and management processes to better target known risks, and has sought to quantify new risks through adding, and altering, risk identification parameters—at both the pre-issue and post-issue payment stages. Overall, the application of the

various risk management strategies has been effective in identifying, responding to, and reducing Fuel Scheme risks.

15. The ATO supports the ongoing integrity of the Fuel Scheme by responding to identified risks through its compliance program, and undertaking reviews and audits of specifically identified taxpayers. As part of its active compliance program for the Fuel Scheme, the ATO undertook 15 053 reviews and 11 872 audits of fuel tax credit claims over the four year period commencing 1 July 2006. These reviews and audits resulted in adjustments to claims made of some \$124.5 million over the same period.

16. The ANAO has made one recommendation, directed at more closely aligning service standards for the timing of fuel tax credit reviews and audits with more realistic benchmarks. This would enable an improvement in compliance activity planning and communication with taxpayers regarding the proposed timeline for audit activity.

Key findings by chapter

Governance and performance reporting (Chapter 2)

17. The ATO has appropriate governance arrangements in place to support the operation of the Fuel Scheme. The key areas of focus for its governance bodies have been on the operation of the Fuel Scheme, the impacts of changing taxpayer eligibility, and the detection of, and response to, scheme risks.

18. Internal management committees, including the Excise Product Committee and the Excise Compliance Risk Forum meet on a regular basis to consider information about key risks and priorities for the administration of the Fuel Scheme. Relevant matters covered by these two committees include: work processes and allocations; objections and litigation; technical issues; and risk and intelligence.

19. Internally the ATO manages staff workloads through its operational plans, which are based on forecasting the time required to complete compliance reviews and audits. This measure, known as 'cycle time', is measured in days and recorded within the ATO's systems. Cycle time assists operational staff by providing guidance on the time a particular item of work should take to complete, and management to track performance against this expected timeframe. Cycle times are also used to inform taxpayers who are being audited of the proposed time to complete the audit.

20. The ATO is experiencing difficulty in meeting its own benchmarks on the time taken to complete some compliance activities, particularly where there is interaction with taxpayers. The benchmarks are used to advise taxpayers, inform the allocation of tasks to staff, monitor and manage staff performance and report internally on casework. Given their importance, the ANAO has recommended that the current benchmarks be reviewed to ensure they reflect more realistic timeframes.

21. To further strengthen its governance framework the ATO has applied two quality assurance processes over time. The first was the Technical Quality Review (TQR), which has been progressively replaced by the Integrated Quality Framework (IQF). The IQF applies to a broad range of administrative activities, examining procedures for soundness, integrity, correctness, appropriateness, effectiveness, transparency, consistency, timeliness and efficiency. The audit considered the application of the TQR and IQF processes only in relation to the scheme's compliance reviews and audits (discussed in Chapter 4).

Risk identification and management (Chapter 3)

22. The ATO seeks to minimise the risk of non-compliant claims and errors in two key ways: through educating taxpayers; and implementing a multi-layered risk assessment and compliance approach to identify and respond to Fuel Scheme risks.

23. Guidance material issued by the ATO is an effective way of educating claimants and supporting voluntary compliance. Legislative guidance, public rulings specific to certain industry groups, and general guidance material are all available on the ATO website.

24. The ATO has put in place effective strategies to identify potentially inappropriate claims or significant errors. At the pre-issue payment stage, the ATO's systems have various risk identification triggers to test all reimbursement claims for errors. Post-issue of the payment, all claims are assessed to identify higher risk claims for specific risks, over multiple claim periods. Regardless of whether a claim is selected on a pre-issue or post-issue payment basis, all claims may subsequently be selected for compliance review and audit. The ATO uses the experiences gained from risk identification and compliance outcomes to assist in informing its future risk identification approaches.

25. The ATO has recently reviewed its risk identification parameters, which has led to a reduction in the number of compliance review and audit activities undertaken in 2009–10. These reviews have resulted in:

- an adjustment of the risk identification parameters used to identify cases for compliance review and audit, in view of the maturity of the processes relating to the Fuel Scheme and the greater experience of taxpayers accessing the Fuel Scheme;
- revision of the dollar threshold level above which claims are selected for further examination. This level was increased because the ATO determined that the dollar threshold had previously been set too low, generating false positives, and creating work that had less risk mitigation value compared to other potential opportunities; and
- the introduction of higher claim averaging tolerances for businesses involved in certain activities that were, by their nature, impacted by cash flow variability.

26. The ATO, from time to time, also conducts general, whole-of-scheme risk analysis exercises to gain a better appreciation of Fuel Scheme risks. During July 2008, the ATO conducted a benchmarking exercise to assess the level of taxpayer compliance and to gain further insights into potential Fuel Scheme risks. Out of a potential population of 141 537 taxpayers at the time of the exercise, the claims of 171 taxpayers were examined. Through conducting audits on this sample, ATO analysis indicated that 33 per cent of those taxpayers made an error in preparing their fuel tax credit claims. However, it noted that the size of the errors was comparatively small — less than 1.2 per cent of the total value of fuel tax credits claimed by the sample group. By extrapolating the sample results back to the total population of claims, the ATO estimated the value attributable to errors from inappropriate claims to be approximately \$60 million, based on 2006–07 data.

27. A significant proportion of the errors detected in the benchmarking exercise resulted from the inappropriate application of environmental criteria when making a claim.⁵ In a targeted response to this exercise, the ATO undertook further educational activities, including the release of specific

⁵ The environmental criteria are outlined in the publication 'Fuel Tax Credit for Heavy Diesel Vehicles – guidelines for satisfying the Environmental Criteria', available online at http://www.infrastructure.gov.au/roads/environment/fuel_tax_credit/guidelines.aspx [accessed 13 April 2010]

pamphlets to promote a greater understanding of, and compliance with, the environmental criteria that were giving rise to the errors.

28. Overall, for most of the life of the Fuel Scheme, the ATO has considered it to be a 'moderate' risk, largely because it was a new scheme that included transitional provisions from the EGCS, and because eligibility would continue to alter over time. However, the ATO reduced the Fuel Scheme's risk rating to 'low' in November 2010. This lower rating recognises the recent stability in eligibility criteria and follows the assessment of a reduction in environmental risks, such as the impact of the global financial crisis on taxpayer behaviour. The ATO advised that Fuel Scheme risks would continue to be reviewed on an ongoing basis.

Compliance management (Chapter 4)

29. The ATO relies on its compliance activities, including reviews and audits, as the primary response to identified risks and non-compliant practices. It has in place generally effective and appropriate compliance strategies that support the integrity of the administration of the Fuel Scheme. High risk cases are identified on an ongoing basis and are subject to reviews and audits.

30. The ATO has undertaken, on average, 3763 reviews per year from 2006-07 to 2009-10. The majority of these reviews occurred within the micro enterprises and individuals and small and medium enterprises markets. Reviews generally do not involve taxpayer contact. Where a review is unable to substantiate a claim it is likely that the taxpayer will be audited. The ATO undertook more reviews in 2007-08 (3978) and 2008-09 (5821), in response to changes in eligibility criteria and general perceived risks.

31. Where, following a review, the ATO considers that a claim represents a higher risk, an audit is conducted. Audits typically consider a longer period of claims, involve direct taxpayer contact, and are likely to result in a revenue adjustment. Audits are more resource intensive than reviews and the ATO undertook, on average, 2968 audits per year over the four year period from 2006-07 to 2009-10. The liability adjustments for this period totalled some \$124.5 million.⁶

⁶ During 2006-07 the ATO raised \$12.2 million in adjustments, reflecting that the Fuel Scheme had just commenced. From 2007-08 through 2009-10 inclusive the ATO raised average adjustments of \$37.4 million each year.

32. To further underpin the integrity of its Fuel Scheme compliance reviews and audits, the ATO has used the TQR and IQF quality assurance frameworks to improve administration over time. For example, quality assurance processes may identify that, whilst technically correct, the clarity of documentation provided to taxpayers could be improved. The independent quality assurance processes also serve to verify the appropriateness of technical decisions made during review and audit processes, taxpayer liability adjustments and the technical accuracy of correspondence to taxpayers advising them of review/audit outcomes.

33. The Serious Non-Compliance (SNC) capability within the ATO assists in dealing with those taxpayers involved in fraud or more extreme cases of tax evasion, as well as taxpayers who have disengaged from the tax system, and those that have demonstrated a strong resistance to meeting their tax obligations. The process required to investigate, gather appropriate evidence and bring a case to court can be lengthy—particularly for complex matters. Currently, the SNC is investigating four fuel scheme cases. A fifth case has been finalised and required no further action. As of March 2011, one prosecution case was submitted to the Commonwealth Director of Public Prosecutions for consideration, resulting in a successful prosecution.

Summary of agency response

34. The ATO's summary response to the report is reproduced below. The full response is at Appendix 1 of the report.

The ATO notes the ANAO comment that '...The Fuel Scheme's risk management strategies are appropriate and the compliance program addresses identified risks and non-compliant practices.'

The ATO is also pleased with the audit finding that 'The Tax Office has put in place effective strategies to identify potentially inappropriate claims or significant errors.'

The ATO agrees with the ANAO recommendation to review cycle times of compliance reviews and audits for the Fuel Tax Credit Scheme.

Recommendations

Recommendation No.1

Para 2.33

To improve the basis for compliance activity planning, and associated communication with taxpayers, the ANAO recommends that the ATO reviews the cycle times of Fuel Tax Credit Scheme compliance reviews and audits so they reflect a more realistic benchmark of the time necessary to complete these tasks.

ATO Response: Agreed.

Audit Findings

1. Background and Context

Background

1.1 The Australian Taxation Office (ATO) is the Australian Government's principal revenue collection agency. The role of the ATO is to manage and shape taxation, excise and superannuation administrative systems that fund services for Australians, giving effect to social and economic policy.⁷ In 2009–10, the ATO collected over \$253 billion in tax, superannuation and excise revenue, incurred expenses of \$3.0 billion, and had a staffing level of 21 766.⁸

1.2 The ATO is also responsible for administering various grant and transfer payments, which give effect to a range of government policies. Under transfer payment programs, the Government provides a financial benefit to an individual, corporation or other entity without requiring a good or service in return. Several Commonwealth agencies are responsible for administering transfer payments, such as pensions and family support payments.⁹

1.3 During 2009–10, the ATO administered transfer payment programs and other benefits totalling \$8.7 billion, as outlined in Appendix 2.¹⁰ Of these, the energy/fuel schemes group is the most significant, and constitutes 58.6 per cent of the total payments administered by the ATO.

1.4 The Fuel Tax Credits Scheme (the Fuel Scheme) is the largest transfer payment program of the energy/fuel schemes, representing some 99 per cent of total funding. It provides claimants with a refund of the excise included in the cost of taxable fuel, when that fuel is used for the purposes defined by the Fuel Scheme.

1.5 Administration of the Fuel Scheme within the ATO is undertaken by specialist staff in the Indirect Tax (ITX) business line.

⁷ Australian Taxation Office, *Australian Taxation Office Annual Report 2008–09*, 2009, p. iii.

⁸ Australian Taxation Office, *Australian Taxation Office Annual Report 2009–10*, 2010, pp. iv–v, p. 259.

⁹ Transfer payments in the Australian context were examined as part of the Australia's Future Tax System Review (Henry Review) and reported in *Architecture of Australia's tax and transfer system* available online at <<http://taxreview.treasury.gov.au>> [accessed 29 October 2010].

¹⁰ Australian Taxation Office, *Australian Taxation Office Annual Report 2009–10*, 2010, p. 42.

The Fuel Tax Credits Scheme

1.6 In 2004, the Australian Government proposed, through the Energy White Paper, *Securing Australia's Energy Future*, the concept for a scheme to modify fuel taxation rebate arrangements.¹¹ This led to the new Fuel Scheme, which was designed to provide expanded relief from the excise levied on taxable fuels for businesses and households.

1.7 The Fuel Scheme aimed to improve administration, lower the costs of compliance by claimants, reduce taxation on business and reduce the burden of fuel taxation by expanding eligibility criteria to broaden the population of potential claimants. It also sought to address inconsistencies in the excise treatment of different types of fuel. The Energy White Paper stated that:

Australia's fuel excise system should be characterised by a system that is applied consistently across all relevant fuel and fuel usages and minimises taxation and administrative costs for businesses and government.¹²

1.8 The new Fuel Scheme commenced on 1 July 2006 and replaced the Energy Grants Credit Scheme (EGCS). It was established through the *Fuel Tax Act 2006* (the Act) and the *Fuel Tax (Consequential and Transitional Provisions) Act 2006*. Both schemes were designed to provide eligible businesses, and limited non-business users of fuel, with a means to recover the excise included in the cost of fuel, when that fuel is used for specific purposes, as defined by each scheme. When claiming a fuel tax credit for fuel, the amount able to be claimed is dependent on the gross vehicle mass and whether the vehicle is used on a public road.

1.9 The new scheme expanded the eligibility provisions that applied under the EGCS¹³, and is currently the largest transfer payment program administered by the ATO. A summary of the various activities and fuel types that are eligible for credit under the Fuel Scheme, and the amount of the

¹¹ Australian Government, 'Securing Australia's Energy Future', 2004, available online at <http://pandora.nla.gov.au/pan/79623/20071127-1411/www.dpmc.gov.au/publications/energy_future/index.html> [accessed 22 October 2010].

¹² *ibid.*

¹³ For example, on 1 July 2006, eligibility for agriculture, fishing, and forestry previously under the EGCS transitioned across under the new Fuel Scheme. Also, petrol was eligible under the new Fuel Scheme for use in eligible vehicles travelling on a public road from 1 July 2006. On 1 July 2008, the eligibility criteria of the Scheme was further expanded to include additional activities, and significantly, to include petrol as a fuel in mining and agriculture as eligible under the Scheme. On 21 January 2011 the Government released draft legislation seeking to change the taxation treatment of alternative fuels, such as liquid petroleum gas (LPG).

reimbursement per litre of fuel used, is included at Appendix 4. The cost of the Fuel Scheme in 2009–10 was \$5 billion, a 14.5 per cent increase on the \$4.4 billion incurred in 2006–07, its initial year of operation. This increase, in part, stems from the growth in the number of active participants after the eligibility criteria under the Fuel Scheme were extended.

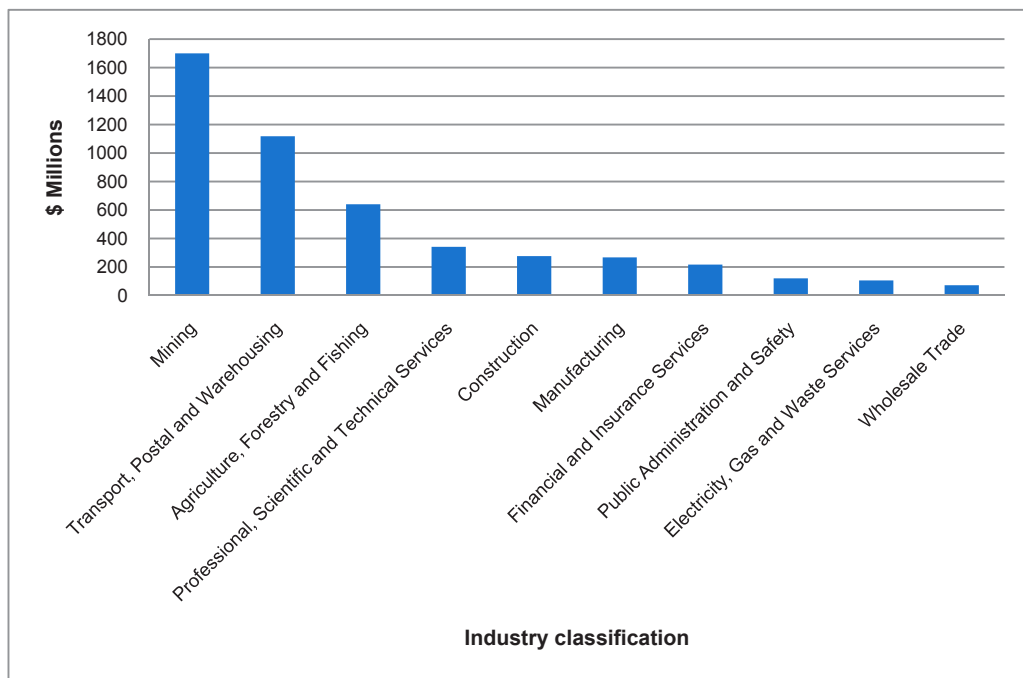
1.10 At present, the maximum fuel tax credit to eligible participants is 38.143 cents per litre of fuel. For business entities, a fuel tax credit is claimed and adjusted, through their business activity statement (BAS). Individuals and non-profit entities that are not registered for the Goods and Service Tax (GST) can only submit claims via a pre-populated paper form.

Fuel Scheme claimants

1.11 Over the four years since its introduction, the total number of active scheme claimants has increased from 146 874 on 1 July 2006 to 191 751 at 30 June 2010. The most significant scheme claimants by value and broad industry groupings, based on 2009–10 claims data, have been in the Mining (34 per cent), and Transport, Postal and Warehousing (22 per cent) categories. The concentration of claiming patterns, by broad industry group, has remained reasonably consistent since the inception of the current Fuel Scheme. For 2009–10, the broad industry breakdown of credit claims made by taxpayers is represented in Figure 1.1. More detailed long term industry trend data is presented at Appendix 3.

Figure 1.1

Fuel Scheme major industry claim groups (2009-10)



Source: ATO data

Note: The industry classification is supplied by the taxpayer based on Australian industry classification standards. The ANAO noted that one Australian mining company self-selected the 'Professional, Scientific and Technical Services' industry group. Because the taxpayer self-selects which industry classification group they belong to, there may be a degree of unquantified error in the data presented above.

1.12 Taxpayers self assess their eligibility to make claims under the scheme following consideration of a number of variables, including the:

- type of entity making the claim—businesses or individuals—which dictates the manner in which the claim is made;
- acquisition and use of taxable fuel for an eligible activity such as road transport, agriculture or mining, or electricity generation, which will dictate the eligible fuel that can be used and the rate that can be claimed for reimbursement; and
- location at which the activity is conducted—for example, on or off a public road.

1.13 For business claimants, fuel tax credits are claimed through their BAS, which is the same form used for a range of taxes, including the GST. To claim fuel tax credits, businesses must be registered for that purpose with the ATO in

order to have the appropriate labels included on their BAS. Taxpayers report their claim in dollar terms. This is a change from the EGCS, which required claims to be made in litres. The change in reporting units was a source of some initial confusion for taxpayers transitioning to the new scheme, and an initial focus for ATO compliance activity.

1.14 Individuals are typically not registered for the GST¹⁴, and hence do not complete a BAS, but may still claim fuel tax credits on a pre-populated paper form. Individuals are also eligible to claim for fuel used for domestic electricity generation. Not-for-profit organisations may also claim fuel tax credits related to the operation of emergency vehicles and/or vessels. While GST registered claimants use the BAS to lodge claims under the Fuel Scheme on a monthly, quarterly or annual basis, there are no established claiming cycles for non-GST registered claimants.

1.15 Claimants under the Fuel Scheme that operate heavy vehicles with a gross vehicle mass greater than 4.5 tonnes may have their entitlement offset by the road user charge.¹⁵ The road user charge is subtracted from the eligible fuel tax credit claim rate for fuel that is used in vehicles that travel on a public road.

1.16 The ATO website assists claimants by providing claim rates for certain activities that already incorporate the road user charge offset, simplifying the calculation required. The road user charge is subject to change, and one of the matters that the ATO examines during compliance reviews and audits is whether the appropriate rate for the relevant period has been used.

Interaction with the environmental initiatives

1.17 Under the *Fuel Tax Act*¹⁶, businesses claiming more than \$3 million in fuel tax credits in a financial year were not entitled to receive additional Fuel Scheme credits unless the business was a member of the Greenhouse Challenge Plus Program (GCPP). In addition, businesses operating eligible

¹⁴ Individuals that are conducting a business activity such as farming or transport services may be registered for GST and may use the BAS. However, the Fuel Tax Credit Scheme allows individuals to claim for electricity generation in certain circumstances that are not business related activity.

¹⁵ Current claim rate as of 20 October 2010, latest rates are available online at <http://www.ato.gov.au/businesses/content.asp?doc=/content/00174722.htm> [accessed 20 October 2010].

¹⁶ *Fuel Tax Act 2006*, Division 45.

vehicles that were manufactured prior to January 1996 must meet certain environmental criteria to be eligible to claim the credit.¹⁷

Greenhouse Challenge Plus Program

1.18 The GCPP was administered by the then Department of the Environment, Water, Heritage and the Arts through the Australian Greenhouse Office. It was launched in 2005, and ceased on 1 July 2009. The program aimed to:

- reduce greenhouse gas emissions;
- accelerate the uptake of energy efficient practices;
- integrate greenhouse issues into business decision-making; and
- provide more consistent reporting of greenhouse gas emissions levels.

1.19 The impact of the program, in terms of taxpayers accessing the Fuel Scheme was minimal. For example, in 2007–08, 14 companies had scheme claims denied or reduced as a result of not being a member of the GCPP. However, by August 2008, nine of these companies had become members. As a result, approximately only 0.3 per cent of the total scheme funding pool was denied to taxpayers in 2007–08, a very small amount of overall Fuel Scheme funds.

Environmental criteria

1.20 To support the effective operation of the Fuel Scheme and the related operation of the GCPP, the ATO and the then Department of Transport and Regional Services (DOTARS)¹⁸ exchanged letters of understanding in October 2006 to establish their respective Fuel Scheme responsibilities. Whilst the ATO acknowledged that it would be the ‘first point of contact’, DOTARS accepted responsibility to publish information regarding environmental criteria, including:

- the operation of the DT80 emissions test standard¹⁹;

¹⁷ Australian Taxation Office <<http://www.ato.gov.au/print.asp?doc=/content/76476.htm>> [accessed 1 November 2010].

¹⁸ Now the Department of Infrastructure and Transport.

¹⁹ Additional information on the DT80 test can be found on the Department of Infrastructure and Transport website at <http://www.infrastructure.gov.au/roads/environment/fuel_tax_credit/pdf/Requirements_for_DT80_Facilities.pdf> [accessed 6 January 2010].

- the process for seeking accreditation for a vehicle maintenance program;
- appropriate record keeping; and
- interacting with taxpayers regarding amendment or inclusions to the provisions specified in vehicle maintenance schedules.

Guidance on these matters is accessible through the publication *Guidelines for Environmental Criteria - Fuel Tax Credit for Heavy Diesel Vehicles*²⁰, supplemented by material published on the department's website.

Fuel Scheme early payments facility

1.21 To assist the transition from the EGCS to the new Fuel Scheme, an early payments facility was established for businesses from 1 July 2006 until 30 June 2008. The facility provided a mechanism for those claimants transferring from the EGCS to receive their fuel tax credits for eligible fuel early, providing cash flow relief, and time to align their reporting practices to the requirements of the new scheme. To be eligible to claim early payments, businesses had to meet only one of the following criteria:

- be entitled to an energy grant under the EGCS;
- use burner fuels;
- supply burner fuels to private consumers for domestic heating; or
- package and sell fuels, such as kerosene, in small containers for use other than in an internal combustion engine.

Audit approach

Audit Objective and Scope

1.22 The objective of the audit was to assess the effectiveness of the ATO's administration of the Fuel Tax Credits Scheme. Particular emphasis was given to the Fuel Scheme's:

- governance and reporting arrangements;
- risk management strategies; and

²⁰ Department of Infrastructure, Transport, Regional Development and Local Government, available online at <http://www.infrastructure.gov.au/roads/environment/fuel_tax_credit/index.aspx> [accessed 30 August 2010]

- compliance management program.

Audit Methodology

1.23 The ANAO conducted fieldwork and interviewed ATO staff from relevant Excise and Finance business areas. The ANAO also examined relevant ATO documents including business plans and analysed a sample of 44 reviews and audits.

1.24 The audit was conducted in accordance with ANAO auditing standards at a cost to the ANAO of approximately \$497 000.

Previous ANAO audits

1.25 The ANAO has undertaken a number of previous audits that relate to fuel taxation. These include:

- Australian Customs Service—*Diesel Fuel Rebate Scheme*, Audit Report No.27 1990–91.
- Australian Customs Service—*The Diesel Fuel Rebate Scheme*, Audit Report No.20 1995–96;
- Australian Taxation Office—*The Australian Taxation Office's Management of the Energy Grants (Credits) Scheme*, Audit Report No.20 2004–05; and
- Australian Taxation Office—*The ATO's administration of the Petroleum Resource Rent Tax*, Audit Report No.33 2008–09.

Report Structure

1.26 The audit report structure reflects the audit criteria outlined in paragraph 1.22. Accordingly, the chapters examine the ATO's approach to:

- Governance and performance reporting (Chapter 2);
- Risk identification and management (Chapter 3); and
- Compliance management (Chapter 4).

2. Governance arrangements

This chapter examines the governance arrangements that support the administration of the Fuel Tax Credits Scheme.

Introduction

2.1 The ATO has adopted a matrix approach in developing its corporate governance framework. This framework combines key elements of the organisation's management, planning and reporting processes.

2.2 High-level management is provided by a senior leadership group and through the ATO's senior executive reporting structure. Collectively, they have responsibility for managing a number of business and service lines designed to deliver the ATO's outcome and program commitments to government.²¹ Planning, performance measures and reporting are linked through the development of a suite of corporate documents, which include the ATO plan²², Annual Report, and various branch and line sub-plans.²³

2.3 The ATO also has in place a quality assurance framework. The current Integrated Quality Framework (IQF) has progressively replaced the original Technical Quality Review (TQR) process. The IQF applies to a broad range of administrative activities, examining procedures for soundness, integrity, correctness, appropriateness, effectiveness, transparency, consistency, timeliness and efficiency. The application of the IQF and TQR processes in relation to the Fuel Scheme is considered in this audit only in relation to compliance activities and is discussed in Chapter 4.

2.4 To assess the effectiveness of the ATO's administration of the Fuel Scheme, the ANAO examined the following key aspects of the governance arrangements supporting the Fuel Scheme:

- organisational administrative arrangements and planning processes;

²¹ ATO, 2009–10 *Commissioner of Taxation Annual Report*, p. 119.

²² ATO plan 2010–11, provides a high-level outline of all the work the ATO intends to undertake in the financial year, and includes performance measures against deliverables. The strategies outlined in the plan cascade down into the sub-plans and ultimately to tasks at the individual level for ATO staff.

²³ Australian ATO management arrangements, file ref:05/8799, April 2010, available from <www.ato.gov.au> [accessed 23 February 2011].

- staff skilling and support;
- performance reporting; and
- managing complaints and claim objections.

2.5 Risk identification and management as a component of the governance framework supporting the administration of the Fuel Scheme is discussed separately in Chapter 3.

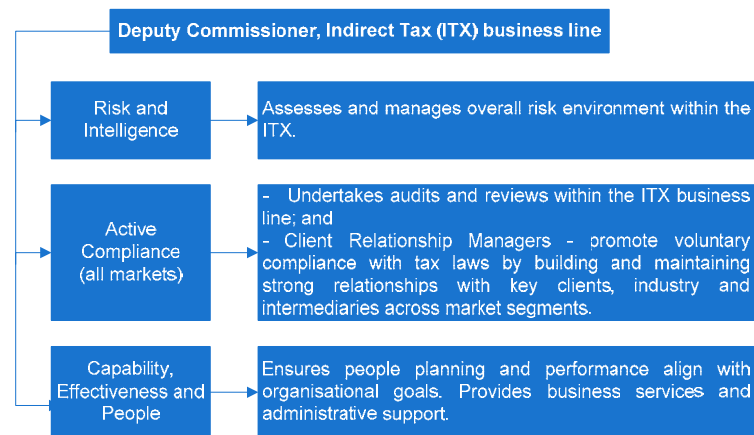
Organisational administrative arrangements and planning processes

2.6 As previously noted, administration of the Fuel Scheme is currently managed through the Indirect Tax (ITX) business line, although certain support functions such as Marketing and Communications are undertaken on a corporate basis in other areas of the ATO.

2.7 The management structure and planning processes in the ITX business line, insofar as they apply to administration of the Fuel Scheme, combine specialist services and market segments, as shown in Figure 2.1. Under these arrangements, administration of the Fuel Scheme is spread across functional branches and teams. Whilst there is some concentration of support functions in Perth, capabilities are nationally distributed.

Figure 2.1

Structure of the Indirect Tax (ITX) business line in relation to the Fuel Scheme.



Source: ANAO analysis of ATO information.

Note: Marketing and Communications are undertaken on a corporate basis in other areas of the ATO.

2.8 The ATO has put in place internal and external arrangements to assist in managing the Fuel Scheme that include:

- internal committees, such as the Excise Product Committee and Excise Compliance Risk Forum within the ITX business line, that provide strategic direction for the Fuel Scheme, and act as a focal point in the formal identification, assessment and treatment of Fuel Scheme risks at a strategic level; and
- external forums that provide a mechanism for consultation between the ATO and stakeholders on matters of scheme administration, including the Fuel Schemes Advisory Forum that facilitates consultation with key industry bodies; and the Fuel Schemes Intermediary Forum that promotes discussion with tax agent representatives and accounting bodies.

2.9 An examination of committee minutes for key governance bodies over the period 2006–07 to 2009–10 demonstrated that they were well informed about the operation of the scheme. For example:

- the Excise Product Committee, which advises the ITX business line executive, was provided with comprehensive documentation that addressed a broad range of Fuel Scheme issues including: taxpayer awareness; work processes and allocation; objections and litigation; technical issues; risk and intelligence; and taxpayer behaviours. In addition, the committee was well informed on an ongoing basis, of more operational matters, including the number of claimant registrations, industry access, compliance activity, and volume and amount of Fuel Scheme payments.
- the Excise Compliance Risk Forum, which advises the Excise Product Committee and meets approximately twice per year, identifies, analyses, assesses and reviews specific compliance risks that relate to the Fuel Scheme. This committee also monitors the development and implementation of risk treatment strategies to address identified and emerging risks, such as changing eligibility criteria.

Planning processes

2.10 The ATO produces a hierarchy of planning documents that link the corporate plan with business line plans, through to individual performance and development agreements for staff. Staff are able to see how the work they

do contributes to the delivery of high level strategies identified in the ATO's corporate plan.

2.11 The ITX business line plan incorporates aspects of Fuel Scheme management and operational planning. The Fuel Scheme has also been specifically considered as part of the ATO's annual compliance planning process since its introduction in 2006. Compliance activities that have had a particular focus on the Fuel Scheme include sending letters to registered claimants (2008–09) to explain expanded eligibility criteria, and targeting contractor claims (2010–11).

Staff skilling and support

2.12 Having a skilled and experienced workforce that understands the application of legislative and regulatory requirements is an integral element of a sound governance framework for the Fuel Scheme. The ATO provides staff with training and support opportunities through self-paced online i-learn training modules, which cover a broad range of tax administration issues. The following i-learn modules are specific to the Fuel Scheme:

- legislation and eligibility;
- general overview of the Fuel Tax Credits Scheme;
- Generic Payment System clients for fuel tax credits;
- record keeping requirements for the Fuel Tax Credits Scheme;
- early payments; and
- introduction to penalties.

2.13 Some of these modules have an assessment capability to track staff completion, but like most other ATO i-learn modules, completion is optional for staff development purposes. Rather than relying on the i-learn packages, some teams have developed a program that is targeted at providing training specific to team duties.

2.14 Regardless of whether staff rely on i-learn or specific team based learning approaches, learning opportunities are available within the ATO to support the skilling of its staff involved in administration of the Fuel Scheme.

Performance reporting

Reporting against management benchmarks

2.15 Internally, the ATO manages staff workloads by benchmarking and then tracking the timing for various activities, including compliance review and audit tasks. The measure, known as 'cycle time', is recorded in days within the ATO's systems. Cycle times for compliance reviews and audits vary between 10 and 183 days and assist operational staff by providing guidance on how long it should take to complete the particular item of work. Management are able to track performance against the expected cycle times. Cycle times are also used to inform taxpayers who are being audited of the anticipated duration of the audit.

2.16 The ATO closely manages work allocation. The Excise workflow management (active compliance) team in Perth allocates proposed compliance reviews and audits to specific teams and monitors the amount of work that they have on hand to ensure that there is adequate work always available. Within compliance teams, directors and team leaders are responsible for monitoring this work and assisting staff conducting the work to progress audit and review cases in an appropriate timeframe. Where timely progress is not made a management intervention known as 'call-over', outlined in paragraph 4.27, occurs.

2.17 The ATO determines cycle times for tasks at a granular level, having regard to whether the task requires contact with the taxpayer, the inherent complexity of the task and the general level of work that is involved. The cycle time may be a matter of negotiation between work units before the work is commenced.

2.18 A review of ATO statistics on the results of actual times taken for completing work on specific products reflected two trends in relation to the benchmarked cycle times:

- when work is more complex, reflected in planned longer cycle times that recognise inherent task complexity, it is less likely that the ATO will be able to complete the task within the benchmark cycle time; and
- tasks that involve contacting the taxpayer are significantly less likely to be completed within the benchmark cycle time.

2.19 Given the difficulty the ATO is experiencing in meeting the expected cycle times in some categories of task, a review of scheme cycle time benchmarks for compliance work would be beneficial. Revised benchmarks,

that more closely reflect the actual time required to complete the task would better position the ATO to:

- use more accurate performance information to better manage taxpayer expectations of the time an audit will take;
- plan and manage resources, given that the ability to plan resources is linked to knowledge of the average time to complete a task; and
- manage staff performance using cycle times that more accurately reflect the time taken to complete tasks.

2.20 The ATO advised that the analysis of actual work times is constrained by the inability of its main case management system to ‘stop the clock’ whilst the matter is being dealt with by the taxpayer. Taxpayers may take considerable time to gather evidence requested by the ATO, and this time is not accommodated by the cycle time benchmark.

External Fuel Scheme reporting

2.21 Agency level program outcomes and performance indicators are set out in Portfolio Budget Statements (PBS). The PBS set out the key performance measures for individual programs, and the agency reports its performance as well as more general reporting of the activities of individual programs in its annual report.

2.22 Since the Fuel Scheme has been in operation, the performance reporting regime has evolved into a more detailed and transparent program based reporting approach. Because the EGCS overlapped with the implementation of the Fuel Scheme, the ATO did not adjust its existing data structures to enable separate program based reporting of the Fuel Scheme. This resulted in an inability to identify specific program-based performance information relating to the Fuel Scheme from 2006.²⁴ As the Fuel Scheme is a multi-billion dollar program, it would have been desirable, from a transparency perspective, to specifically monitor and report on its activities.

2.23 Prior to the 2009–10 PBS, the Fuel Scheme was not featured prominently. Following the implementation of the Outcome—Program

²⁴ During the complete phasing in of the new Fuel Scheme (1 July 2006 until completion on 1 July 2012), the ATO determined that a high proportion of the available program based information was pertaining to the new Fuel Scheme, however, a small proportion was still relating to the previous EGCS. The proportion relating to the previous EGCS is expected to continue to fall as time restraints are reached on amendments that can be made to previous EGCS cases.

Framework from 1 July 2009, the Fuel Scheme was specified as one of the programs under Outcome 1.

2.24 The program's deliverables are the dollar value of the claims, and the number of registered participants. The key performance indicator is that 'the ATO's role in successfully delivering this program is demonstrated by the payments being made in accordance with the law.'²⁵

2.25 The results of the key deliverables are outlined in Table 2.1. The extent to which payments meet the key performance indicator, of being paid in accordance with the law, is considered in Chapter 3 (Risk Identification and Management) and Chapter 4 (Compliance management).

Table 2.1

Fuel Scheme key performance indicators

Financial Year	Delivery of Fuel Tax Credits Scheme		
	Cash Claims (\$ millions)	Registered participants	Active participants ¹
2006–07	4379 ²	169 529	146 874 (86.6%)
2007–08	4648	195 155	171 398 (87.8%)
2008–09	5014	231 537	191 870 (82.8%)
2009–10	5016	234 672	191 751 (81.7%)

Source: ATO data.

Note 1: This column is not an Australian Taxation Office key performance indicator for the Fuel Tax Credits Scheme. The information is presented for illustrative purposes, and may be a more representative reflection of 'Fuel Scheme access/work effort', compared with statistics on registered participants, given that approximately 20 per cent of those registered in 2009–10 were not actively accessing the Fuel Scheme.

Note 2: The 2006–07 figure reflects the Energy Grants Credit Scheme and Fuel Tax Credits Scheme combined.

2.26 The ATO has historically reported on administration of the Fuel Scheme in its annual reports, including the compliance activity undertaken and areas of particular importance, such as eligibility changes.

²⁵ Australian Government, 2010–11 Treasury Portfolio Budget Statements, p. 214.

Complaints and claim objections

Complaint handling

2.27 Since the inception of the Fuel Scheme there have been less than 30 complaints lodged and, of these, approximately half have been partially or fully upheld. The very small number of complaints provides limited insights, given:

- a number of ‘complaints’ were actually taxpayers clarifying their entitlement;
- a number of complaints resulted from calculation disputes, which related to differences in understanding the calculation methodology;
- of the complaints that were upheld, there was no commonality in the nature of the issues raised; and
- the ATO has also received complaints from taxpayers regarding their inability to meet scheme eligibility requirements, which reflects the nature of the legislative requirements.

As there were, on average, approximately 175 500 active taxpayers accessing the Fuel Scheme each year, the overall number of formal complaints received by the ATO regarding the Fuel Scheme is very low.

Objections and litigation

2.28 A taxpayer may lodge an objection in relation to a fuel tax credit claim because of dissatisfaction with the outcome of a private ruling request, the outcome of an audit or imposition of penalties/interest in relation to an audit, or as an independent action after realising that a previous claim was incorrect.

2.29 As reflected in Table 2.2, the number of objections each year has increased, although considering the number of taxpayers accessing the Fuel Scheme, the number of objections remains low. Of those objections received, approximately 50 per cent relate to compliance activity undertaken by the ATO. During the two most recent financial years, approximately 50 per cent of objections have been successful.

Table 2.2**Fuel Scheme objection and appeals**

	2006–07	2007–08	2008–09	2009–10
Objections finalised	4	16	34	56
Disallowed / withdrawn / invalid	3	6	15	28
Allowed in full or in part	1	10	19	28
Appeal to the court or AAT	-	-	2	7
Appeal outcome in ATO favour	-	-	1	-
Appeal outcome in Taxpayer favour	-	-	-	-
Appeal withdrawn by taxpayer	-	-	-	2

Source: ATO data.

Conclusion

2.30 The ATO has appropriate governance arrangements in place to support the operation of the Fuel Scheme. The key areas of focus of its governance bodies have been on the operation of the scheme, the impacts of changing taxpayer eligibility, and the identification of, and response to, risks.

2.31 To further strengthen its governance framework the ATO has underpinned the integrity of its compliance activities with two quality assurance processes. The first was the TQR, which has been progressively replaced by the IQF. The IQF applies to a broad range of administrative activities, examining procedures for soundness, integrity, correctness, appropriateness, effectiveness, transparency, consistency, timeliness and efficiency.

2.32 The ATO is experiencing difficulty in meeting its benchmarks on the time taken to complete some compliance activities, particularly where there is interaction with taxpayers. The benchmarks are used to advise taxpayers of the likely duration of an audit, inform the allocation of tasks to staff, and report internally on casework. Given their importance, there would be benefit in reviewing the current benchmarks to more accurately reflect the actual time required to undertake these activities.

Recommendation No.1

2.33 To improve the basis for compliance activity planning, and associated communication with taxpayers, the ANAO recommends that the ATO reviews the cycle times of Fuel Tax Credit Scheme compliance reviews and audits so they reflect a more realistic benchmark of the time necessary to complete these tasks.

ATO response

2.34 *Agreed.* The ATO agrees with the ANAO recommendation that the ATO review the cycle times of Fuel Tax Credit Scheme compliance reviews and audits. The ATO has already commenced reviewing these compliance product cycle times in order to ensure these are appropriate.

3. Risk identification and management

This chapter outlines how the ATO identifies, assess and mitigates the risks associated with taxpayers making Fuel Tax Credits Scheme claims.

Introduction

3.1 The ATO seeks to build confidence in its administration of taxation legislation through helping people to understand their rights and obligations, improving ease of compliance and access to benefits, and managing non-compliance with the law.²⁶ The risk of taxpayers' non-compliance with their taxation responsibilities is determined using an enterprise risk framework.

3.2 The ATO's Enterprise Risk Management Framework²⁷ examines risk through a number of lenses, enabling the office to assess the extent of the risks across the economy and to develop a range of remedial responses that are proportionate and appropriate to address the underlying areas of concern.²⁸

3.3 In relation to the Fuel Scheme, the ATO has developed specific risk mitigation strategies to address inappropriate or erroneous claims, and has a number of mechanisms in place to identify, manage and monitor the level of compliance by claimants. These mechanisms have evolved over time, to reflect the changing nature of Fuel Scheme risks. Earlier efforts by the ATO were directed towards making taxpayers aware of how the Fuel Scheme worked. As the scheme developed, new tools were provided to assist taxpayers to better understand their eligibility, and compliance activity was expanded and became more sophisticated to target specific risk.

²⁶ ATO publication: *Making a difference – the intent behind our Strategic statement 2010-15* booklet, p. 2.

²⁷ The ATO's Enterprise Risk Management Framework is an integrated risk management strategy linking tactical, operational and enterprise risk. The current version meets ISO 31000:2009 standards.

²⁸ Commissioner of Taxation, Risk: The framework, the vision, the values. Presentation to the CPA Public Sector Finance and Management Conference, 12 August 2010.

3.4 The ATO seeks to minimise Fuel Scheme risks, and hence maximise compliance, in two key ways:

- taxpayer education and guidance products: this includes measures to promote voluntary compliance through the provision of published guides, legislative interpretation products and public rulings. The ATO seeks to ensure that those who wish to voluntarily comply have the information they need to make informed and appropriate decisions; and
- multi-strategy risk identification: the ATO has a multi-strategy approach to identifying Fuel Scheme risk. It relies on multiple data systems, staff knowledge, information acquired through intelligence sources and third party data sources. In addition, the ATO uses the information maintained in its databases to develop specific, risk targeted profiles.

3.5 The ANAO reviewed the guidance products that have been issued over the life of the Fuel Scheme, as well as the technical guidance material currently available to taxpayers. The risk management strategies to identify and assess Fuel Scheme risks, the risk profiles, and the associated management tools that support the use of risk profiles in a coordinated way, were also examined.

Taxpayer education and guidance material

3.6 The ATO adopted a strategic approach to communicating with taxpayers who access the Fuel Scheme. It undertook research to inform the design and appropriate targeting of guidance publications, and established communication forums to consult with taxpayer representative groups.

3.7 General education and guidance products support taxpayers in making appropriate decisions about their self-assessed tax liability, and support the effective administration of the Fuel Scheme by encouraging voluntary compliance. For many taxpayers, particularly those without a tax agent, ATO communication products are the main information they use to make self-assessment decisions.

Published guides

3.8 Published guides inform taxpayers of their eligibility and responsibilities when calculating and claiming fuel tax credits. The guides are available on the ATO website, at shopfronts, or by post, and are designed to meet a number of taxpayer information requirements, that range from general

guidance about the Fuel Scheme, to information regarding specific industry or business circumstances. An example of general guidance includes the publication *Fuel tax credits for business*²⁹, which is provided to businesses when they initially register. It provides information that:

- introduces the Fuel Scheme;
- explains how to assess eligibility;
- demonstrates how to work out which fuel tax credit rates apply to specific business activities;
- outlines record keeping requirements; and
- demonstrates how to calculate a claim and enter it on the BAS.

3.9 Other guidance material is more specific, targeting areas where self-assessment is more complex. For example, this material includes:

- *Bunker Fuel and Commercial Shipping*³⁰;
- *Fuel not used in an internal combustion engine (including packaged fuel)*³¹, and
- *Fuel tax credits—domestic electricity generation and non-profit emergency vehicles or vessels*.³²

3.10 The Department of Infrastructure and Transport also publishes on its website the *Guidelines for Environmental Criteria - Fuel Tax Credit for Heavy Diesel Vehicles*³³, which ATO documents make reference to.

3.11 To provide more practical assistance to businesses and individuals claiming a fuel tax credit, the ATO also provides an online eligibility tool and fuel tax credit calculator. The eligibility tool assists businesses and individuals

²⁹ Australian Taxation Office, available online at <<http://www.ato.gov.au/businesses/content.asp?doc=/content/76594.htm>> [accessed 30 August 2010].

³⁰ Australian Taxation Office, available online at <<http://www.ato.gov.au/businesses/content.asp?doc=/content/00238793.htm&pc=001/003/095/005/015&mnu=&mfp=&st=&cy=1>> [accessed 30 August 2010].

³¹ Australian Taxation Office, available online at <<http://www.ato.gov.au/print.asp?doc=/content/76553.htm>> [accessed 30 August 2010].

³² Australian Taxation Office, available online at <<http://www.ato.gov.au/businesses/content.asp?doc=/content/76531.htm>> [accessed 30 August 2010].

³³ Department of Infrastructure, Transport, Regional Development and Local Government, available online at <http://www.infrastructure.gov.au/roads/environment/fuel_tax_credit/index.aspx> [accessed 30 August 2010].

to determine whether their fuel use may be eligible for a fuel tax credit³⁴, and the fuel tax credit calculator assists eligible businesses and individuals to calculate their eligible fuel tax credit claim rate.³⁵

3.12 The Fuel Scheme's guidance publications from the ATO and the Department of Infrastructure and Transport examined by the ANAO were of a generally high standard and would assist taxpayers to access the scheme and to meet their tax obligations.

Public rulings and determinations

3.13 Public rulings cover areas of administrative interpretation of tax law that are likely to apply to a significant group (or class) of taxpayers. The rulings provide clarity of the ATO's position on certain general circumstances so that taxpayers can understand how the ATO will treat activities if they are undertaken on a similar basis to that described in the public ruling, hence exposing taxpayers to less risk.³⁶ Taxpayers are therefore given more certainty that the ATO will interpret the law as it applies to specific circumstances in a manner consistent with the ruling. The ATO has published the following public rulings related to the Fuel Tax Credits Scheme on its web site:

- FTR 2009/1—entitlement to a fuel tax credit in a vehicle or equipment hire arrangement;
- FTR 2008/1—vehicular travel on a public road that is incidental to the vehicle's main use and the road user charge; and
- FTR 2007/1—the meaning of 'acquire', 'manufacture' and 'import' in the expression 'taxable fuel that you acquire or manufacture, or import into

³⁴ Australian Taxation Office, available online at <http://calculators.ato.gov.au/scripts/net/FTC/Welcome.aspx> [accessed 2 November 2010].

³⁵ Australian Taxation Office available online <http://calculators.ato.gov.au/scripts/ASP/FERPCalc/Main.asp> [accessed 2 November 2010].

³⁶ The ATO goes into some detail as to how it applies its own advice when undertaking dealings with taxpayers, the following extract is provided from FTR 2007/1: 'This publication (excluding appendixes) is a public ruling for the purposes of the Taxation Administration Act 1953. A public ruling is an expression of the Commissioner's opinion about the way in which a relevant provision applies, or would apply, to entities generally or to a class of entities in relation to a particular scheme or a class of schemes. If you rely on this ruling, we must apply the law to you in the way set out in the ruling (or in a way that is more favourable for you if we are satisfied that the ruling is incorrect and disadvantages you, and we are not prevented from doing so by a time limit imposed by the law). You will be protected from having to pay any overpaid net fuel amount, penalty or interest in respect of the matters covered by this ruling if it turns out that it does not correctly state how the relevant provision applies to you.'

Australia, to the extent that the taxpayer does so for use in carrying on an enterprise'.³⁷

3.14 The ATO also publishes guidance that is more technical in nature, and is suitable for taxpayers with complex circumstances, or for tax agents. For example, it has published the following determinations to clarify aspects of the operation of the *Fuel Tax Act 2006*:

- FTD 2010/1—apportionment used when determining total fuel tax credits in calculating the net fuel amount under section 60-5 of the *Fuel Tax Act 2006*;
- FTD 2009/1—meaning of 'use' for the purposes of section 41-5 of the *Fuel Tax Act 2006*;
- FTD 2006/2—records required to be kept by taxpayers to substantiate a claim for a fuel tax credit; and
- FTD 2006/3—Fuel tax: Meaning of 'enterprise' for the purposes of the *Fuel Tax Act 2006*.³⁸

3.15 The ATO continues to maintain EGCS rulings on its website. Some of the eligibility arrangements from that scheme have implications for taxpayers who wish to claim an energy grant relating to fuel used before 1 July 2006.³⁹

Taxpayer specific guidance products and assistance

3.16 The ATO uses a number of methods to assist taxpayers to voluntarily comply with their obligations in making claims under the Fuel Scheme. For example, the ATO sends advisory and educational material to those taxpayers accessing the Fuel Scheme for the first time, to inform them of their obligations. It also alerts registered taxpayers of changed circumstances in scheme eligibility.

³⁷ Available online at <<http://ato.gov.au/businesses/content.asp?doc=/content/76666.htm>> [accessed 29 September 2010]. Adopted from the ATO's web site.

³⁸ Adopted from the Australian Taxation Office web site, <www.ato.gov.au> [accessed 4 October 2010].

³⁹ These rulings draw on section 32 (FTR 2006/1), section 11 (FTR 2006/2), Section 35 (FTR 2006/3) and section 34 (FTR 2006/4) of the *Energy Grants (Credit) Scheme Act 2003*.

Client relationship management

3.17 Taxpayers who make significant use of the Fuel Scheme are offered the services of a client relationship manager within the ITX business line. Taxpayers may move in and out of this arrangement, depending on their business needs. The role of the client relationship manager is to assist the taxpayer to voluntarily comply with their obligations, and to provide contextual information to other areas of the ATO with regards to the taxpayers’ operations.

Private rulings

3.18 Taxpayers who have specific circumstances for which they consider that the general guidance provided by the ATO does not give sufficient clarity, may seek a private ruling. By outlining their situation to the ATO and receiving advice on their specific circumstances, the taxpayer increases transactional certainty and reduces the risk that their activities will be considered by the ATO in an unexpected way. Table 3.1 details the number of private rulings the ATO has issued for the Fuel Scheme.

Table 3.1

Fuel Scheme private rulings for the period 2006–07 to 2009–10

Taxpayer group	2006–07	2007–08	2008–09	2009–10
Individual	7	3	2	1
Business	141	66	64	40
Tax Agent / Consultant	21	17	31	23

Source: ATO data.

3.19 The number of private rulings sought by taxpayers, rather than tax agents, has decreased over time, which is consistent with taxpayers becoming more conversant with the Fuel Scheme.

Conclusion

3.20 Overall, the ATO has developed an integrated approach to educating and communicating with participants of the Fuel Scheme. The approach encompasses general and technical guidance material, and targeted notification of alterations to Fuel Scheme eligibility which may impact on specific taxpayer groups. This approach has been based on research to understand taxpayers and their circumstances, and appropriate and timely communication methods to deliver targeted messages, as and when required.

Multi-strategy risk identification

3.21 The ATO has developed a multi-strategy approach for identifying and responding to Scheme risks. The two broad strategies applied to identifying risks are pre-issue payment and post-issue payment integrity checking.

3.22 Pre-issue payment integrity checking primarily involves the Risk Rating Engine (RRE) examining the fuel tax credit claims submitted via the BAS, and the Generic Payment System (GPS) to examine non-BAS paper based forms. These systems target unintended errors, including scanning and claim lodgement errors, as well as applying some broad risk parameters. Both systems check all claims that are submitted by taxpayers prior to payment and typically, claims are not released until identified risk payments are verified as appropriate.

3.23 Post-issue payment integrity checking identifies specifically targeted risk profiles, including suspected fraud, by using information held within ATO databases. The cases selected are further analysed by risk assessment staff, and potentially also by compliance staff during review and audit activity. The application of specifically targeted risk profiles occurs in addition to the RRE and GPS systems-based examinations.

3.24 These strategies are supplemented by other sources of intelligence received by the ATO. However, the majority of risk identification effort is internally generated through ATO systems and the work of risk assessment staff, within the ITX business line.

3.25 Fuel Scheme compliance and business risks are regularly monitored and reported internally at an enterprise-wide level through:

- the Credit Refund Integrity Steering Committee;
- the Excise Compliance Risk Forum; and
- Health of the System Assessment (HOTSAs) reports.

Pre-issue payment risk identification—Risk Rating Engine

3.26 The RRE is used to review all business activity statements (BAS) submitted to the ATO.⁴⁰ In terms of the Fuel Scheme, the RRE is primarily

⁴⁰ Only claims made by business entities through the BAS are examined by the RRE. Non-GST registered claimants who are accessing the Fuel Tax Credit Scheme for electricity generation or are non-profit organisations are examined by the General Payment System.

designed to detect ATO scanning errors, and taxpayer lodgement errors. The RRE uses business rules to assess potential risks relating to claims, such as:

- payments exceeding average claim values;
- large claims —initially established in 2006 and informed by EGCS claim patterns; and
- The Greenhouse Challenge Plus rule.⁴¹

3.27 When a claim is identified by the RRE as being of potential concern it is reviewed and, until its validity is verified, the claim amount and any refunds resulting from the BAS are withheld. For this reason, pre-issue payment reviews are to be completed within 10 days. However, for large entities that have the financial capacity to cover any subsequent debts, claims are released pending later verification on a post-issue payment basis.⁴²

3.28 If a claim is identified as part of a pre-issue payment integrity check, it is validated through a review or audit. If a claim is validated by way of review, information held within the ATO data systems will be used to assess the claim. Alternatively, if the ATO considers the claim to be of greater risk, and a higher degree of scrutiny is warranted, an audit is undertaken. An audit requires the taxpayer to provide substantiating information. The ATO conducts a more limited audit where previous claims have been verified through the taxpayer being audited within the previous 15 months.

3.29 As reflected in Table 3.2, in any one year a significant amount of work is undertaken by the ATO to substantiate the claims made by taxpayers. Much of this work, as reflected through the number of reviews, occurs without taxpayer contact. Tax officers use their knowledge of the individual taxpayer, based primarily on information held within ATO data systems, to determine if direct contact is required in order to be satisfied that a taxpayer's claims are reasonable.

3.30 Table 3.2 also shows that the number of pre-issue payment checks conducted by the ATO declined in 2009–10. The pre-issue payment risk

⁴¹ This rule was triggered when a taxpayer's Fuel Tax Credit Scheme claims exceeded \$3 million dollars. To receive fuel tax credits above this level, taxpayers were required to join the Greenhouse Gas Challenge program. This program was terminated on 1 July 2009.

⁴² A large entity is more likely to be solvent and exist in the future, and have the capacity to make good on its tax obligations, whereas the risk is higher for a small entity or individual not having the net worth or cash flow to meet previous obligations.

integrity function depends mainly on claims being flagged by the RRE. Over time, the rules of the RRE have been refined, and this is reflected in the reduction of high risk claims being identified by the system.

Table 3.2

Pre-issue payment risk integrity activity work items for the period 2006–07 to 2009–10

	2006–07	2007–08	2008–09	2009–10
Review	2 228	3 253	4 804	1 756
Maintenance check audit	1 320	515	440	381
Verification audit	1 186	2 681	3 087	977
Total	4 734	6 449	8 331	3 114

Source: ATO data.

Refinements to the Risk Rating Engine

3.31 In late 2008, based on its knowledge of claiming patterns, the ATO recognised that there was an opportunity to further refine the risk identification parameters of the RRE to improve its ability to select taxpayers with specified risks, and reduce the number of low-risk taxpayers being selected.

3.32 For small entities, which typically made very small and/or infrequent claims, the base dollar threshold level was increased to limit the number of claims that would be selected for further examination. The ATO determined that the dollar threshold level had previously been set too low, generating false positives, and creating work that had less risk mitigation value compared to other potential opportunities. The increase in the dollar threshold level struck an improved balance between managing the identified risk, the administrative costs to the ATO and the inconvenience to the taxpayer in following up on low-risk claims.

3.33 Additionally, higher claim averaging tolerances were introduced for businesses involved in certain activities that, by their nature, were impacted by cash flow variability. These changes meant that fewer low risk claims would be flagged for examination, and resources could be directed to claims assessed as being of higher risk.

3.34 These changes also need to be considered in the context of the broader multi-strategy risk identification approach employed by the ATO. For example, all claims may also be identified or selected for review or audit by

applying specific risk targeted profiles. This issue is discussed in more detail later in this Chapter.

Pre-issue payment risk identification–Generic Payment System

3.35 The Generic Payment System (GPS) is used to process claims made on non-BAS paper forms.⁴³ Although a comparatively minor proportion of Fuel Scheme funding is processed through the GPS, this system also contains a pre-issue payment risk detection capability, similar to the RRE.

3.36 The ATO provides taxpayers with pre-populated forms. These forms reduce the possibility of mis-identification of registered claimants, but not the possibility of the taxpayer making an otherwise inappropriate claim. Like the RRE, complex fraud related risks are typically identified through specifically targeted risk profiles that consider all Fuel Scheme claims. Issues and errors that the GPS is able to detect include:

- claims above pre-determined thresholds;
- unusual growth in claims;
- first time claimants⁴⁴;
- taxpayers that are already flagged for risk management purposes; and
- taxpayers that have already been flagged for debt recovery offset reasons.

3.37 The issues examined represent a limited number of the risk parameter ‘triggers’ available within the GPS. Overall, there are approximately thirty specific risk parameter triggers that could result in further examination and risk assessment, potentially including review and audit. Some triggers are also able to be set according to specific expectations unique to the taxpayer, including for example individual payment thresholds. In the Fuel Scheme context, the GPS provides the ATO with a far greater level of risk discrimination than the RRE.

⁴³ Primarily covering claims related to electricity generation by individuals, non-profit organisations and fuel used in emergency vehicle applications.

⁴⁴ There are low barriers to becoming registered for the Fuel Tax Credit Scheme. The capability to flag first time claimants provides the basis for the ATO to verify through a review or audit that the taxpayer is eligible and is calculating their claim appropriately. Detecting inappropriate claiming at this early stage not only reduces the ongoing risk to the ATO, but also may assist the taxpayer by detecting activity which may attract significant penalties and interest at a later date.

3.38 The number of claims actioned through the GPS, typically non-business claimants, has not increased significantly over time. In total, 8475 taxpayers processed under the GPS transitioned from the EGCS in 2006–07. Since that time, less than 300 additional non-business taxpayers per annum have registered for the Fuel Scheme.

Post-issue payment risk identification—specifically targeted risk profiles

3.39 The final element of the risk identification process is applied on a post-payment basis and relies on analysing the information retained within ATO databases.

3.40 The ATO uses targeted risk profiles to select taxpayers with certain risk attributes, typically based on several variables and constraints that define the matter being examined. The ATO uses these profiles for three major groups of post-issue payment risk assessment activity including:

- internal reviews: work is of a limited nature, does not directly involve the taxpayer, and is typically used as a screening tool in response to intelligence leads from other sources or as a means of exploring potential risk profiles;
- assurance work: designed to ensure that taxpayers are claiming appropriately, or to quantify the extent of specific risks, which may also include testing the utility of a risk profile; and
- work identified as responding to specific risks: resources are directed to assess potentially fraudulent matters.

3.41 As illustrated in Table 3.3 the ATO has increased the number of profiles targeted at different risk behaviours each year. The first year of risk identification was limited by a reliance on data from the EGCS. This was expanded upon once a historical body of Fuel Scheme data became available for interrogation and analysis.

Table 3.3**Fuel Scheme risk specific profile activity for the period 2006–07 to 2009–10**

	2006–07	2007–08	2008–09	2009–10
Number of review profiles	24	23	11	17
Number of audit profiles	1 ¹	28	15	24
Number of specific risk profile reviews and audits initiated.	541	1 064	1 404	956

Note 1: The low number of 2006–07 audit profiles reflects Energy Grants Credits Scheme data being used to select Fuel Tax Credits Scheme cases in the early stages of the latter scheme.

Source: ATO data.

3.42 By using contemporary and historical data, the ATO is able to target specific risks. It has built on the experience gained by administering the EGCS, and applied this to the current scheme. As a result, over a period of four years, the risk identification efforts of the ATO have increased, and become more sophisticated, particularly with regards to specifically targeted risk profiling.

3.43 The ATO monitors the effectiveness of its risk profiles. Not all risk profiles remain appropriate and, as a specific risk is treated and the number of identified cases declines, the profile will become less useful over time.⁴⁵ At the operational risk management level, the ATO uses spreadsheet tools to track the effectiveness of its risk-targeted profiles, and to also assist in recording and capturing individual profile outcomes. The risk profile performance tracking tool currently used by the ATO also allows for more informed management decisions in respect of post-issue payment risk targeting compliance activity.

Benchmarking assessment of Fuel Scheme taxpayer errors

3.44 During July 2008, the ATO conducted a statistically-based benchmarking exercise to assess levels of taxpayer compliance with the Fuel Scheme. The methodology applied by the ATO included splitting a sample into two groups: those claiming more than \$4000 per financial year; and those claiming less than \$4000 in a financial year. This approach was designed to ensure the appropriate use of compliance resources by concentrating efforts on the large client group (those claiming more than \$4000) yet still providing

⁴⁵ As the ATO became aware of risks, new risk targeting profiles were initiated and tested. Not all of these profiles were successful, and it was a matter for professional judgement to determine if a profile needed to be re-worked or if the risk had been sufficiently targeted and treated.

some insight into the compliance level of smaller clients.⁴⁶ The overall result of the benchmarking exercise suggests that 33 per cent of all the clients audited made an error in preparing their fuel tax credit claims, although the size of that error was comparatively small (less than 1.2 per cent of the total value of fuel tax credits claimed).⁴⁷

3.45 The ATO considered that, given that the sample had been stratified, it was not possible to accurately assess the impact of non-compliance for the Fuel Scheme overall. However, the exercise was considered to provide a broad indicative measure of incorrect claims. The results of the benchmarking exercise are presented in Appendix 5. Through this exercise, the ATO found that, as expected, there were differences between the stratified groups, but also that there was an impact caused by non-compliance with the requirements of the Fuel Scheme's environmental criteria. While taxpayers were aware of the environmental criteria, they often lacked an understanding of the detailed requirements. The criteria specifically applied to vehicles with a gross vehicle mass greater than 4.5 tonnes, travelling on a public road, and where the vehicle was manufactured prior to January 1996.

3.46 The ATO concluded that, whilst the sample for the benchmarking exercise was substantially compliant, '20 per cent of those clients claiming for on-road use would have potentially failed the environmental criteria in relation to one or more vehicles'. The ATO responded to the potential risk highlighted by this exercise by producing additional guidance publications to assist taxpayers to better understand and voluntarily comply with their obligations, specifically in relation to the environmental criteria. It also referred taxpayers to documentation that was published by the then Department of Infrastructure, Transport, Regional Development and Local Government regarding the application of the Fuel Scheme's environmental criteria.

⁴⁶ Australian Taxation Office, 2008, Fuel Tax Credit Scheme internal benchmarking analysis.

⁴⁷ *ibid.*

3.47 By examining the results of the benchmarking exercise, the ATO determined that there were four key areas where taxpayers made mistakes in submitting claims as follows:

- clerical errors;
- incorrect calculations from using the wrong Fuel Scheme claiming rate;
- incorrectly apportioning eligible/ineligible fuel use; and
- claiming for ineligible operations or vehicles.⁴⁸

3.48 A significant proportion of the identified errors resulted from the inappropriate application of environmental criteria when making a claim.⁴⁹ Consequently, the ATO noted that the quantitative measure of the potential error rate for claims extrapolated by the benchmarking exercise, given the size of the program, is within acceptable tolerances.

Conclusion

3.49 The ATO has in place various risk management strategies to address inappropriate or erroneous Fuel Scheme claims. The strategies range from providing taxpayers with guidance material to promote voluntary compliance, to the application of risk identification processes at both the pre- and post-issue payment stages. All claims are risk assessed at the pre-issue payment stage. In the post-issue environment, claims may be further examined by the ATO, using the information retained within its data systems to identify claims that occur over multiple payment periods.

3.50 Over time, the ATO has modified its risk identification and management processes to better target known risks, and has sought to quantify new risks through adding, and altering, risk identification parameters—at both the pre-issue and post-issue payment stages. Overall, the application of the various risk management strategies has been effective in identifying, responding to, and reducing Fuel Scheme risks.

⁴⁸ *ibid.*

⁴⁹ The environmental criteria are outlined in the publication 'Fuel Tax Credit for Heavy Diesel Vehicles—guidelines for satisfying the Environmental Criteria', available online at http://www.infrastructure.gov.au/roads/environment/fuel_tax_credit/guidelines.aspx [accessed 13 April 2010]

4. Compliance management

This chapter outlines how the ATO manages compliance activities to address identified risks for Fuel Tax Credits Scheme claims.

Introduction

4.1 In administering the taxation system, the ATO strives to provide an environment conducive to high levels of voluntary compliance with Australia's tax laws and community confidence in tax administration. The ATO's approach to compliance is based on a model of taxpayer behaviour, which aims to better understand what motivates people to comply or not comply with their taxation obligations. The model assists the ATO to plan interventions that are proportionate and appropriate to address the underlying cause of non-compliance. The compliance interventions are graduated, and range from providing guidance, advice and support, through to compliance reviews and audits, and finally, if warranted, applying the full force of the law.⁵⁰

4.2 The ANAO reviewed the compliance activities undertaken by the ATO to address non-compliance with Fuel Scheme requirements. For the Fuel Scheme, the ATO allocates its compliance resources in response to the perceived risks of certain taxpayer activities. Commensurate with the identified risk, different compliance tools are used.

4.3 The ATO undertakes two key types of compliance interventions subsequent to Fuel Scheme claims being paid:

- compliance reviews; and
- compliance audits.

Compliance reviews

4.4 Compliance reviews provide the ATO with an opportunity to assess the risk concerning an individual taxpayer, or a group of taxpayers, in a less intrusive way. Where appropriate, issues detected through a review will be

⁵⁰ The ATO undertakes review and audit activity for a range of reasons, including risk quantification of specific population groups, in addition to the more typical targeting of specific perceived risks.

escalated to a more expansive audit. Generally, there are three types of review, reflecting increasing levels of taxpayer intrusiveness and resource cost to the ATO. These include:

- internal review: where the ATO uses the information that is already known about the taxpayer to form a preliminary view of the risks presented to the Fuel Scheme. It is not expected that a taxpayer will be contacted for an internal review.
- high volume-low value review: which may entail limited inquiries of the taxpayer to substantiate the claims made, for example that a taxpayer is claiming:
 - dollars, not litres;
 - the correct scheme rate for their activities; and
 - the correct road user charge for the location where their activities are conducted.
- standard review: which is likely to be of limited scope, validating one or two BAS periods. The taxpayer is likely to be contacted in order to collect limited evidence to substantiate a claim, or an element of claiming history.

4.5 Table 4.1 outlines the number of Fuel Scheme reviews conducted by the ATO.

Table 4.1

Fuel Scheme compliance reviews by market segment for the period 2006–07 to 2009–10

Market segment	Number of reviews conducted			
	2006–07	2007–08	2008–09	2009–10
Micro enterprises and individuals	1 280	1 581	1 666	573
Small and medium enterprises	999	1 688	2 839	985
Large Business	346	400	661	436
Government organisations	96	191	508	337
Non-profit organisations	96	118	147	106
Total	2 817	3 978	5 821	2 437

Source: ATO data.

4.6 Over the four year period 2006–07 to 2009–10, these reviews resulted from:

- general system risk parameter triggers: 12 305 reviews (or approximately 78 per cent) were initiated by the RRE and the GPS; and
- specific risk profiling: 2748 reviews (or approximately 22 per cent) were initiated by the risk profiling of specific taxpayer circumstances.

Compliance audits

4.7 An audit is a more intrusive and resource intensive examination of the affairs of a taxpayer. It is typical for some preliminary work to have been undertaken to justify an audit. Generally, this would be a review, which is used to inform the scope and methodology of the audit.

4.8 Most audits are ‘desktop audits’. That is, ATO officers contact the taxpayer via correspondence and/or telephone to clarify aspects of the transactions undertaken by taxpayers and request copies of substantiating documentation. The ATO may also seek verification from third parties of the facts provided by the taxpayer; for example, fuel purchase records from fuel distributors.

4.9 The ATO may alternatively conduct ‘field audits’, where evidence is collected from the premises of the taxpayer. A field audit need not necessarily indicate an escalation in the inherent risk of the taxpayer, but acknowledges that in some cases matters can be resolved more efficiently through an on-site visit. Whilst on-site visits permit ATO staff to better appreciate the business context, they are more expensive and require increased levels of coordination and preparatory work. For this reason, field audits may occur as part of a geographically based campaign.⁵¹

4.10 Table 4.2 outlines the number of Fuel Scheme audits conducted by the ATO. As reflected in the data, compliance activity commenced part way through 2006–07, increasing with a full year of activity in 2007–08. The ATO also introduced new pre-issue testing part way through 2007–08, adding to compliance workload volumes. As previously discussed, pre-issue risk targeting was refined in 2009–10 to remove lower risk cases.

⁵¹ Geographically based campaigns occur where risk behaviours are limited to a defined area. For example, where a tax consultant operates within a reasonably defined hinterland, or, where a specific industry exists within a region and they appear to be adopting potentially similar inappropriate practices.

Table 4.2**Fuel Scheme compliance audits by market segment for the period 2006–07 to 2009–10**

Market segment	Number of audits conducted			
	2006–07	2007–08	2008–09	2009–10
Micro enterprises and individuals	1 016	1 432	1 496	851
Small and medium enterprises	598	1 231	1 665	658
Large Business	495	508	443	26
Government organisations	308	362	310	176
Non-profit organisations	74	78	79	66
Total	2 491	3 611	3 993	1 777

Source: ATO data.

4.11 The ANAO examined 44 randomly selected cases that included both reviews and audits, covering the period 2006–07 to 2009–10, and for each case examined that the:

- letter sent to the taxpayer accurately reflected the ATO’s findings;
- case plan accurately addressed the risk;
- outcome was appropriately recorded, including in any correspondence to the taxpayer;
- evidence outlined in the case was clearly reconciled with the outcome; and
- management oversight of the case, where warranted, was clearly evidenced.

While the sample size was not statistically significant, the findings indicated appropriate processes and practices were utilised by the ATO, with cases generally documented appropriately.⁵²

4.12 For a minor number of cases, where there was a finding against the taxpayer, the ATO had reached an appropriate decision. However, the technical explanation for this decision could have been better communicated to

⁵² From 2006–07 to 2009–10, the ATO conducted 15 053 reviews and 11 872 audits in relation to the fuel scheme.

the taxpayer so that it was more readily understood. This issue was noted by the ATO's quality assurance processes and is discussed further below

Compliance activity outcomes

4.13 Taxpayers selected for review or audit, that are found to have either under-stated their tax obligations or over-stated the amount of their claims, will have their obligations adjusted by the ATO. Adjustments may potentially include a penalty. Adjustments to taxpayers' claims under the Fuel Scheme since its introduction are presented in Table 4.3.

Table 4.3

Adjustments resulting from compliance activity by market segment for the period 2006–07 to 2009–10

Market segment	2006–07 \$'000	2007–08 \$'000	2008–09 \$'000	2009–10 \$'000
Micro enterprises and individuals	4 358	7 279	14 651	10 240
Small and medium enterprises	3 177	8 912	9 964	20 474
Large Business	4 092	12 213	14 116	2 412
Government organisations	531	8 636	1 140	1 843
Non-profit organisations	98	129	119	142
Total	12 256	37 169	39 990	35 111

Source: ATO data.

4.14 Not all adjustments are initiated by the ATO. For example, at the commencement of a review and audit exercise, taxpayers are offered the opportunity to make a voluntary disclosure; voluntary disclosures are likely to reduce the penalty applied, should the claim subsequently be found to be incorrect. The ATO has commenced tracking voluntary disclosures made since January 2009. The systematic collecting of voluntary disclosure (and actual audit results) information may in time provide an important tool for the ATO to inform future risk indicators.

Serious Non-Compliance and prosecutions

4.15 Taxpayers involved in significant fraud or serious tax evasion activity may become the responsibility of the Serious Non-Compliance (SNC) business line and investigations may only be undertaken by appropriately qualified or supervised staff. The work undertaken by the SNC business line includes identifying people who seek to operate outside the tax system, detecting illicit activity in relation to excise legislation, investigating schemes that are fraudulent in substance and gathering intelligence concerning activities involving serious tax evasion.⁵³

4.16 Taxpayers that are the subject of compliance activities, including audit, may be referred to SNC for investigation. These cases may, in turn, be referred to the Commonwealth Director of Public Prosecutions (DPP) for prosecution when there has been fraud or serious evasion. Whilst the decision to prosecute ultimately rests with the DPP, prosecution is a powerful deterrent and is the firmest of the compliance strategies available to the ATO. The SNC currently has four fuel tax cases under investigation. A fifth case has been finalised and required no further action. As of March 2011, one prosecution case was submitted to the DPP for consideration, resulting in a successful prosecution.

Quality management

4.17 The ATO applies a quality management process to the administration of the Fuel Scheme. Over the period the scheme has been in operation, the ATO has used two quality frameworks. The first was the Technical Quality Review (TQR) framework, which was replaced, in respect of compliance audit, on 1 July 2009 by the Integrated Quality Framework (IQF).

4.18 Initially, the focus of the quality processes was to facilitate the consistency and correctness of administrative decisions made by ATO staff. As the ATO moved to the IQF the number of issues which were considered was expanded, and the process was more tightly integrated into the day to day operations of ATO staff.

⁵³ Adapted from the ATO web site: <<http://www.ato.gov.au/corporate/content.asp?doc=/content/24463.htm&page=18&H18>> [accessed 5 January 2011]

Technical Quality Review

4.19 From 1 July 2006 when the scheme commenced, until approximately July 2008, technical quality reviews (TQRs) operated by providing independent quality assurance of ATO processes for compliance reviews and audits. The TQR consisted of a panel that reviewed the operational conduct of compliance cases.⁵⁴ The panel considered various quality indicators, including whether the administrative decisions that were made for the case were technically correct, whether any tax liability amendments and any penalties were appropriate and accurate, and if the communication with the taxpayer was appropriate. Elements considered as part of TQR review included:

- understanding clients' questions;
- accurately identifying and/or addressing all issues;
- whether the correct administrative decision was made;
- if there was appropriate and sufficient documentation on the case file to support that decision;
- if there was sufficient evidence from the taxpayer to support decisions made; and
- examining the application of any penalty provisions.⁵⁵

The ANAO examined TQR results applicable to the Fuel Scheme from July 2007 through to January 2009. The outcomes from the TQR exercise are outlined in Table 4.4. The ATO graded the audits on a range of criteria, and assigned an overall grade, with 'A', 'B', and 'C' representing a pass, with 'A' being the most correct. 'D' and 'E' grades were regarded as fails.

⁵⁴ Review panels were held approximately every six months, and included representatives who were independent of the compliance process from within the ATO, knowledgeable experts and a community representative. The process adopted by the ATO is outlined in Practice Statement Law Administration PSLA 2001/11.

⁵⁵ Source: ATO, Practice Statement Law Administration PS LA 2001/11, with some editing to enhance readability.

Table 4.4**TQR outcomes – Excise Business Line for the period July 2007 to January 2009**

Date	Total Cases	Grade A % pass	Grade B % pass	Grade C % pass	Grade D % fail	Grade E % fail
July 2007	67	83	-	16	1	-
January 2008	80	65	5	24	-	6
July 2008	116	69	8	20	1	2
January 2009	103	98	1	1	-	-

Source: ATO data

4.20 The majority of the cases which were reviewed under the TQR scheme were of high quality, as reflected in the significant Grade A pass performance. For those cases which received a Grade D and E (fail), the analysis of TQR reports highlighted that, whilst the ATO had made an appropriate administrative decision, the way in which the technical explanation supporting the decision was communicated to the taxpayer could have been improved.

4.21 As a result of the TQR process, the ATO made process procedural improvements, particularly with regards to the clarity of the advice it provided to taxpayers. Additionally, TQR validated that appropriate decisions were being made, as reflected in TQR assessment scores.

4.22 While the TQR process was beneficial, the ATO recognised that considerable time often elapsed between the conduct of review and audit work, the review of cases by the review panel and providing feedback to case officers and management. This served to reduce the opportunities for timely improvement and reinforcement. The IQF replaced the TQR on 1 July 2009.

Integrated Quality Framework

4.23 When introduced in relation to compliance audits, the IQF expanded the approach adopted in the TQR. The IQF is broader in scope and provides for more timely feedback to assessors and team leaders. It includes processes for continuously improving and assuring:

- the management of quality;
- people capability with regard to quality;
- assessment of quality;
- integrated reporting;

- continuous improvement; and
- culture.⁵⁶

4.24 Accordingly, the IQF considered a broader range of administrative activities, and examined procedures for soundness, integrity, correctness, appropriateness, effectiveness, transparency, consistency, timeliness and efficiency. The IQF also provided more timely feedback through a within-team and external case review mechanism.

4.25 The IQF process for review and audit compliance work has been in place for a relatively short period of time and it is therefore not possible to reflect with any degree of confidence what impact the IQF has had on scheme administrative performance. However, certain elements of the IQF structure are worthy of highlighting:

- Team Leaders are required to review the work of assessors using the IQF and provide immediate feedback to staff undertaking assessment work;
- beyond work teams, an independent review is also undertaken by a dedicated quality assurance specialist, applying a level of consistency across all assessment teams; and
- the ATO tracks IQF outcomes within a database, allowing comparisons of performance throughout the organisation where the IQF methodology is applied.

4.26 Only one year of data was available for the IQF process, reflecting its relatively recent introduction. Unlike the TQR data, the IQF data could be attributed to the Fuel Scheme. Overall, during 2009–10, the ATO conducted 134 third-party reviews, including both reviews and audits. Disaggregating the results, 88 per cent of reviews passed the IQF criteria, whereas audits, being more complex, resulted in a 73 per cent. The primary reason for reviews not passing the IQF was the timeliness in completing the review/audit task within cycle times.

Call-over process

4.27 ATO managers are involved in the oversight of the scheme's compliance reviews and, more particularly, compliance audits. Compliance

⁵⁶ Australian Taxation Office Practice Statement 2009/6.

cases that appear to be taking more time than budgeted, or where the case has not progressed sufficiently, are subjected to an examination by a case call-over committee.

4.28 The case call-over committee consists of ATO staff who have authority over the compliance process and are empowered to make decisions to bring about timely case resolution. Officers on the committee include officers at the Assistant Commissioner, Senior Director and Director level. Team leaders and case auditors explain to the committees their plan to bring cases to a conclusion within the required timeframes and, if required, seek additional authority to do so.⁵⁷

4.29 The call-over committee process is an important support mechanism for case officers undertaking compliance activities, which reinforces a culture of engaged case management and accountability. Additionally, the process provides an opportunity to identify areas for improvement and processes which may benefit from streamlining. A number of ATO compliance auditors advised the ANAO that the call-over process:

- is an important mechanism to assist them to ‘break through’ where a case was challenging. The process allowed auditors to deliberately engage with the call-over committee to seek authority so they could move forward and resolve a case; and
- applied a level of scrutiny that could be avoided by completing cases on time. Sometimes this was not possible, for example, where a taxpayer was not cooperative or where internal resources were reallocated to meet higher priorities.

4.30 Management at the team leader and director levels were, overall, strongly supportive of the call-over process and appreciated its importance in ensuring that there is a shared understanding of compliance case issues between staff and management; and an active engagement by all concerned to assist in reaching appropriate and timely case resolution in accordance with timeliness commitments under the Taxpayers Charter.

⁵⁷ For example, a case may not be completed on time because a taxpayer decides not to cooperate with the ATO. In extreme circumstances where all avenues of follow up have been exhausted the ATO may consider that the taxpayer is intentionally avoiding meeting their obligations. After excluding available options, the ATO may make an adjustment determination on the basis of known information, which may include zeroing the Fuel Tax Credits Scheme claim, placing a hold on all future scheme claims in order to manage scheme risk, and, issue the revised tax assessment - potentially including penalties. If the taxpayer wishes to then cooperate through a formal objection process there is an opportunity to do so.

Conclusion

4.31 The ATO has in place generally effective and appropriate compliance strategies that support the integrity of the administration of the Fuel Scheme. The ATO identifies high risk cases on an ongoing basis that are then subject to reviews and audits. Based on the ANAO's analysis of 44 randomly selected reviews and audits, covering the period 2006–07 to 2009–10, the ANAO concluded that the processes and practices undertaken in implementing the compliance management program were appropriate and generally effective.

4.32 The ATO has also put in place a quality management framework to support the technical accuracy and consistency of its compliance activities. The TQR and the IQF have, over time, reinforced the quality of administration of the Fuel Scheme through a variety of qualitative assessments. The call-over process further assists with the processing of compliance activities by allowing ATO staff conducting audits or reviews to engage with senior level officers who have the expertise and authority to bring a case to conclusion.



Ian McPhee

Auditor-General

Canberra ACT

21 June 2011

Appendices

Appendix 1: ATO response to the Audit

Ms Barbara Cass
Acting Group Executive Director
Performance Audit Services Group
Australian National Audit Office
GPO Box 707
Canberra ACT 2601



Dear Ms Cass

Performance Audit: Administration of the Fuel Tax Credit scheme

Thank you for your letter of 11 May 2011 regarding the proposed audit report on the Administration of the Fuel Tax Credit scheme to the Australian Taxation Office (ATO). The ATO appreciates the opportunity to comment on the findings and the recommendation.

It is pleasing to note that the ANAO considers the ATO's risk management strategies are appropriate for the administration of the Fuel Tax Credit Scheme's and that the compliance program addresses identified risks and non-compliant practises. We also note that the ANAO found the ATO's governance arrangements support the administration of the Fuel Tax Credit Scheme at both the strategic and operational levels.

The ANAO has made one recommendation in the report and the ATO agrees with the recommendation.

Recommendation No.1

To improve the basis for compliance activity planning and associated communication with taxpayers, the ANAO recommends that the Tax Office reviews the cycle times of Fuel Tax Credit Scheme compliance reviews and audits so they reflect a more realistic benchmark of the time necessary to complete these tasks.

ATO response: Agreed.

The ATO agrees with the ANAO recommendation that the ATO review the cycle times of Fuel Tax Credit Scheme compliance reviews and audits. The ATO has already commenced reviewing these compliance product cycle times in order to ensure these are appropriate.

The collaborative approach of your audit team in this review has been greatly appreciated and has led to an informative report.

If there are any questions concerning our response, please contact James O'Halloran, Deputy Commissioner, Indirect Tax on (02) 6216 1516.

Yours sincerely

A handwritten signature in dark ink, appearing to read 'Bruce Quigley', with a long horizontal flourish extending to the right.

Bruce Quigley
Second Commissioner Compliance
9 June 2011

Appendix 2: ATO administered transfer payments

	2000–01	2001–02	2002–03	2003–04	2004–05	2005–06	2006–07	2007–08	2008–09	2009–10
Fuel Tax Credits Scheme	-	-	-	-	-	-	3 715	4 648	5 014	5 016
Energy Grants Credits Scheme	2 470	2 850	3 100	3 142	3 471	3 517	664	-	-	-
Fuel Sales Grants Scheme	221	209	223	233	258	243	32	-	-	-
Product Stewardship For Oil Scheme	-	8	10	13	16	17	32	36	41	33
Cleaner Fuels Grants Scheme	-	-	-	-	2	22	92	116	101	35
Total Energy/Fuel Schemes ⁵⁸	2 691	3 067	3 333	3 388	3 747	3 799	4 535	4 800	5 156	5 084
Other administered payments ⁵⁹	51	565	847	1 072	2 411	3 644	4 773	4 471	11 822 ⁵⁹	3 587 ⁶⁰
TOTAL PAYMENTS AND TRANSFERS	2 742	3 632	4 180	4 460	6 158	7 443	9 308	9 271	16 978	8 671

Source: Australian Taxation Office Annual Report 2009–10, p. 42, supplemented by additional information supplied by the Australian ATO.

⁵⁸ This line item includes: Family Tax Benefit, Baby Bonus, Private Health Insurance Rebate, Wine Equalisation Tax Rebate, Superannuation Co-contribution Scheme, Large Scale Film Production Tax Offset, Fringe Benefits Tax transitional grants and the Distribution of Superannuation Guarantee charge entitlements.

⁵⁹ This sub-total includes 'Tax Bonus For Working Australians', a one-off economic stimulus payment administered by the then Government, accounting for a \$7 368 million expense during the 2008–09 financial year and \$364 million during 2009–10 financial year.

⁶⁰ The Family Tax Benefit is no longer administered by the ATO commencing 2009–10.

Appendix 3: Fuel Scheme claims by industry

The information presented in Table A 1 reflects information provided to the ATO through Business Activity Statements submitted by taxpayers who advise an industry classification on the basis of self determination.

There are, however, some Fuel Tax Credits Scheme claimants that do not claim Fuel Tax Credits through the Business Activity Statement, and instead use a paper based form. These tend to be individuals claiming for fuel tax credits for power generation and also non-profit entities claiming for fuel acquired and used in emergency vehicles and vessels. This latter category has been classified within the Unknown/Other category for completeness, in the table overleaf, and, overall, represents a minimal subset of total claims, in dollar terms.

Table A 1**Fuel Scheme claims by industry**

Industry	2006–07			2007–08			2008–09			2009–10		
	No. Claims	Claims \$m		No. Claims	Claims \$m		No. Claims	Claims \$m		No. Claims	Claims \$m	
Mining	1 060	1 390		1 282	1 439		1 539	1 689		1 518	1 700	
Transport, Postal and Warehousing	33 067	1 090		38 229	1 165		40 612	1 164		39 008	1 118	
Agriculture, Forestry and Fishing	79 553	533		90 289	618		94 920	629		94 108	641	
Professional, Scientific and Technical Services	1 047	288		1 343	240		1 796	300		1 834	342	
Manufacturing	3 684	268		4 452	271		5 310	268		5 346	268	
Financial and Insurance Services	586	212		714	219		866	212		902	217	
Construction	11 415	164		14 909	215		21 211	275		22 423	277	
Electricity, Gas and Waste Services	1 461	150		1 809	141		2 093	110		2 136	106	
Public Administration and Safety	606	96		749	112		786	137		804	120	
Wholesale Trade	3 934	72		4 707	81		5 354	81		5 305	72	
Rental, Hiring and Real Estate Services	2 212	26		2 756	36		3 507	43		3 709	43	
Retail Trade	2 981	19		3 531	22		4 164	24		4 234	24	

Industry	2006–07				2007–08				2008–09				2009–10			
	No. Claims	Claims \$m	No. Claims	Claims \$m	No. Claims	Claims \$m	No. Claims	Claims \$m	No. Claims	Claims \$m	No. Claims	Claims \$m	No. Claims	Claims \$m	No. Claims	Claims \$m
Other Services	1 881	15	2 376	17	2 980	18	3 132	19								
Unknown/Other	461	14	629	8	687	8	742	6								
Administrative and Support Services	1 141	13	1 493	13	2 983	16	3 293	17								
Accommodation and Food Services	681	10	865	11	1 298	11	1 330	10								
Arts and Recreation Services	469	10	604	19	945	18	1 008	24								
Information Media and Telecommunications	90	3	111	15	139	6	131	4								
Education and Training	361	2	465	4	713	4	775	5								
Health Care and Social Assistance	307	2	375	2	436	2	457	2								
Total	146 997	4 379	171 688	4 648	192 339	5 014	192 195	5 016								

Source: ATO data.

Appendix 4: Fuel Scheme eligible activities and net claiming rate

Business activity	Eligible fuel	From 1 January 2009	From 1 July 2009	From 1 July 2010
Vehicles greater than 4.5 tonnes GVM travelling on a public road (diesel vehicles acquired before 1 July 2006 can equal 4.5 tonne GVM). ⁽¹⁾	Diesel and petrol.	17.143	16.443	15.543
Emergency vehicles greater than 4.5 tonnes GVM travelling on a public road (diesel vehicles acquired before 1 July 2006 can equal 4.5 tonnes GVM). ⁽¹⁾	Diesel and petrol.	17.143	16.443	15.543
Specified activities eligible from 1 July 2006 in agriculture, fishing, forestry, mining, marine transport, rail transport and nursing and medical.	Diesel, petrol and fuel oil.	38.143	38.143	38.143
Burner applications.	Diesel, petrol, heating oil, kerosene and fuel oil.	38.143	38.143	38.143
Non-fuel uses such as fuel used directly as a mould release used as an ingredient in the manufacture of products.	Kerosene, fuel oil, toluene, mineral turpentine and white spirit.	38.143	38.143	38.143
Packaging fuels in containers of 20 litres or less for non-internal combustion engine use.	Mineral turpentine, white spirit, kerosene and certain other fuels.	38.143	38.143	38.143
Supply of fuel for domestic heating.	Heating oil and kerosene.	38.143	38.143	38.143
Electricity generation by a commercial generation plant, a stationary generator or a portable generator.	All diesel, petrol, heating oil, kerosene, and fuel oil.	38.143	38.143	38.143
Emergency vessels.	Diesel, petrol and fuel oil.	38.143	38.143	38.143

Business use activity	Eligible fuel	From 1 January 2009	From 1 July 2009	From 1 July 2010
<p>All other activities, machinery, plant and equipment are eligible for fuel acquired from 1 July 2008. Examples of activities are:</p> <ul style="list-style-type: none"> • construction • manufacturing • wholesale/retail • property management, and • landscaping. 	<p>All taxable fuels – for example, diesel and petrol.</p> <p>These activities have only been eligible since 1 July 2008.</p>	19.0715 ⁽²⁾	19.0715	19.0715

Note 1: Claim rates are expressed in terms of cents per litre and are current as of 1 January 2009. These rates are net of the road user charge, which is subject to change. Heavy vehicles greater than 4.5 tonnes GVM travelling on a public road are entitled to a full fuel tax credit of 38.143 cents per litre, minus the road user charge.

Note 2: The rate of 19.0715 cents per litre is 50 per cent of the full rate of 38.143 cents per litre. The full rate will apply to all these activities from 1 July 2012.

Source: Australian Taxation Office, Fuel Tax Credits and eligible fuels. < <http://www.ato.gov.au/businesses/content.asp?doc=/content/00174722.htm&pc=001/003/044/009/008&mnu=&mfp=&st=&cy=1> > [accessed 21 February 2011].

Appendix 5: Fuel Scheme compliance assessment summary

Including environmental criteria impacts		Excluding environmental criteria impacts		
Category	Claims >\$4 000 per year	Claims <\$4 000 per year	Claims >\$4 000 per year	Claims <\$4 000 per year
Claimants	46 740	94 797	46 740	94 797
Sample size	137	34	137	34
Error rate ¹	32.8 %	35 %	28 %	32 %
Estimated potential adjustment	1.19 %	7.3 %	0.63 %	-1.6 %
Outcome	Extrapolated net adjustment for 2006–07 for taxpayers >\$4000: \$49 720 325	Extrapolated net adjustment for 2006–07 for taxpayers <\$4000: \$10 813 352	Extrapolated net adjustment for 2006–07 for taxpayers >\$4000: \$26 322 525	Extrapolated net adjustment for 2006–07 for taxpayers <\$4000: -\$2 370 050

Note 1: The error rate is calculated by considering the number of claimants who incorrectly claimed more or less than they should have, as a percentage of the sample set. It is not a measure of statistical error.

Source: ATO data.

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