

The Auditor-General
Audit Report No.55 2002-03
Performance Audit

Goods and Services Tax Fraud Prevention and Control

Australian Taxation Office

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of Australia 2003

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Canberra ACT
24 June 2003

Dear Mr President
Dear Mr Speaker

The Australian National Audit Office has undertaken a performance audit in the Australian Taxation Office in accordance 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 *Goods and Services Tax Fraud Prevention and Control*.

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 'Oliver Winder'.

Oliver Winder
Acting 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. 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 Government and the community. The aim is to improve Commonwealth public sector administration and accountability.

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Abbreviations/Glossary

ABN	Australian Business Number
AFP	Australian Federal Police
AGD	Attorney-General's Department
ANAO	Australian National Audit Office
ATO	Australian Taxation Office
AWA	Automated Work Allocation System
BAS	Business Activity Statement
CCRA	Canadian Customs and Revenue Agency
CDPP	Commonwealth Director of Public Prosecutions
CDR	Case Decision Record
CEO	Chief Executive Officer
FMA Act	<i>Financial Management and Accountability Act 1997</i>
FIRM	Fraud Investigation Reporting and Management system
FP&C	Fraud Prevention and Control Section
GST	Goods and Service Tax
HMC&E	Her Majesty's Customs and Excise (United Kingdom)
IPS	Instalment Processing System
PRISM	Portable Reference and Interactive System
RIMS	Registration Information Matching System
RQP	Risk Quantification Project
RRE	Risk Rating Engine
SNCC	Serious Non-Compliance Capability
SRM	Strategic Risk Management Unit
TCMP	Taxpayer Compliance Measurement Program
VAT	Value Added Tax

Summary and Recommendations

Summary

Background

1. Fraud against the Commonwealth is a major concern to the Government. Agencies must ensure that fraud is minimised and that, where fraud does occur, it is rapidly detected, effectively investigated, appropriately prosecuted and that losses are minimised.¹ The Commonwealth Government has outlined its fraud control policy in the *Commonwealth Fraud Control Guidelines* (Fraud Control Guidelines) issued in May 2002.
2. The Fraud Control Guidelines require Commonwealth agencies to put in place a comprehensive fraud control program that includes prevention, detection, investigation and reporting strategies. The Guidelines, which define fraud as *dishonestly obtaining a benefit by deception or other means*—include both tangible and intangible benefits² and apply to the Australian Taxation Office (ATO).
3. The ATO is the Federal Government’s principal revenue collection agency. It aims to manage and shape the revenue systems that give effect to social and economic policy, and fund services for Australians. Total cash collections by the ATO in 2001–02 were \$168.7 billion. Of this, \$26.9 billion was collected for the Goods and Services Tax (GST).³
4. The GST, which is part of the Government’s new tax system, was introduced from 1 July 2000. It is a broad-based indirect tax, imposed on goods and services at each point in the distribution chain, including at importation. The GST replaced the existing wholesale sales tax and a number of indirect State taxes. The GST rate is 10 per cent.

Audit objective and scope

5. The audit objective was to assess whether the ATO has implemented administratively effective GST fraud control arrangements, consistent with the Commonwealth Fraud Control Guidelines.

¹ Attorney-General’s Department, *Commonwealth Fraud Control Guidelines*, May 2002, p. iii.

² This definition includes: theft; obtaining property, a financial advantage or any other benefit by deception; causing a loss, or avoiding or creating a liability by deception; providing false or misleading information to the Commonwealth, or failing to provide information where there is an obligation to do so; making, using or possessing forged or falsified documents; bribery, corruption or abuse of office; unlawful use of Commonwealth computers, vehicles, telephones and other property or services; relevant bankruptcy offences; and any offences of a like nature to those listed above.

³ Commissioner of Taxation, *Annual Report 2001–02*, pp. 30–32.

6. The audit addressed the following key elements of fraud control:
- fraud control arrangements integrated within the ATO's corporate governance framework;
 - strategies, systems and processes used to prevent and detect GST fraud, including the crucial role that the ATO's Risk Rating Engine (RRE)⁴ plays in detecting fraudulent and non-compliant behaviour;
 - management of GST fraud investigations; and
 - reporting of GST fraud.

Audit findings and overall conclusion

ATO fraud control framework

7. The ATO has adopted a 'rolling plan' approach to producing its fraud control plans. Under this approach, the ATO produces a number of plans to address its fraud risks over a two-year period. Prior to December 2001, the ATO considered that focusing on internal fraud⁵ satisfied the then Fraud Control Policy of the Commonwealth. The ATO considered its internal fraud control plans, supported by its extensive compliance programs, would provide an effective response to fraud. In 2002, the ATO revised its approach to fraud control and began to look at both internal and external fraud risks when preparing fraud control plans.

8. The ATO applies the definition of fraud outlined in the Fraud Control Guidelines. This definition is implemented within the context of the ATO's Compliance Model. For example, the ATO's response to a mistake by a taxpayer is different to that where a taxpayer has sought to deliberately deceive the ATO for his or her own advantage. The ATO describes this latter category as serious non-compliance. Although the ATO does not generally use the term fraud⁶ when describing this category of compliance activity, fraud perpetrated by external parties fits within the category of serious non-compliance.

9. The Commissioner endorsed the ATO's Fraud Policy Statement in May 2003.⁷ To date, this statement has not been publicised to ATO staff. The ANAO considers that, when advising staff of its fraud policy, the ATO should provide

⁴ The RRE profiles, risk, in a 'real-time environment', for GST registrations at the time of lodgement of the registration application and incoming activity statements of clients registered for the GST. This is prior to the issue of any refund.

⁵ For the ATO, internal fraud is fraud perpetrated on the Commonwealth by ATO staff. External fraud is fraud perpetrated on the Commonwealth through the tax system by external parties.

⁶ The ATO does refer to 'serious fraud and evasion' on occasions. This relates to certain specialist activities within its Serious Non-Compliance Capability.

⁷ Attorney-General's Department, *Commonwealth Fraud Control Guidelines 2002*, p. 8.

direction and guidance on how the Commonwealth's definition of fraud is to be interpreted and implemented consistently across the ATO. This would help to ensure a shared understanding of how fraud is to be managed within the ATO's compliance framework, the development of fraud control plans, and the reporting of fraud activities.

10. In reviewing its approach to include external fraud within its overall fraud control arrangements, the ATO should consider how fraud control planning and reporting are integrated into business practices. The ANAO considers it is important that the assessment of fraud risks and the development of fraud control plans are undertaken in a way, which recognises that external fraud is a separate component of the ATO's compliance continuum. Planning will also need to integrate compliance activities, as these are an integral part of the ATO's fraud mitigation strategies.

GST fraud control planning

11. The ATO is currently revising its GST fraud control plan. The ATO's *GST Business Activity Statement Processing End to End* (January 2003) fraud control plan addressed internal GST fraud risks and a limited number of external fraud risks. The ATO advised that, as GST fraud risks were still evolving and the plan would be rapidly out of date, a second review covering internal and external fraud risks was planned. The ATO plans to complete this risk assessment and fraud control plan by 30 June 2003.

Assessment of GST fraud risks

12. There are a number of different areas within the ATO that play a role in assessing the risks relating to GST fraud. The ANAO considers that the work undertaken by these areas should form part of a comprehensive assessment for external GST fraud risks. However, this work is not coordinated or integrated as part of a comprehensive GST fraud risk assessment, sufficient to meet the requirements of the Fraud Control Guidelines. The ATO advised that this would be integrated as part of its revised GST fraud control plan.

External fraud reporting

13. The annual report to the Attorney-General's Department (AGD) required under the Fraud Control Guidelines is to include suspected fraud, matters under investigation, and completed matters.⁸ The ATO's annual report to AGD

⁸ This includes whether the fraud was proven or not, and whether the matter was dealt with by a criminal, civil or administrative remedy. *Commonwealth Fraud Control Guidelines 2002*, May 2002, pp. 29–33.

indicated that, ATO-wide, there were 884 cases in 2001-02 and that the 'estimated value of loss arising from fraud cases' in that year was \$6 389 593.⁹ However, the ATO subsequently advised the ANAO and AGD that the number of cases and the estimated value of losses were incorrectly reported. The estimated value of loss reported only covered closed GST fraud cases for the period. The ATO advised that total ATO-wide actual losses arising from closed fraud cases in 2001-02 was \$10 659 008.¹⁰ This includes GST revenue of \$515 700. Revised 2001-02 data is to be submitted to AGD.

14. The ANAO found that, currently, the ATO has difficulty in providing an accurate estimate of its external fraud losses because the data being recorded in the Fraud Investigation Reporting and Management (FIRM) system is not being appropriately updated. For example, the potential value of the fraud loss is estimated at the time the case is initially assessed and may change (increase/decrease) during the course of an investigation as more information becomes available. However, this value is not always being updated in the system to reflect the most current assessment of the fraud loss.

15. The ATO advised that this shortcoming has resulted in both the under, and over, reporting of fraud at a case level. The ATO further advised that it has instigated a system of manual checks to ensure that the losses to be reported for 2002-03 are correct. It is currently in discussions with AGD to clarify the fraud data to be collected and reporting requirements.

16. The annual report to AGD is also to include monies recovered by 'criminal prosecution, civil remedy, administrative remedy, and other'. The ATO's report to AGD noted that the 'overall total recovered' for the ATO was \$138 600. The ATO advised that this figure did not include all recoveries for external fraud cases. Currently, it is difficult for the ATO to capture this information, as the FIRM system does not record the fines and/or costs imposed by the courts, losses recovered or adjustments raised. The ATO has advised that it is reviewing the FIRM system business rules, the data captured and reports produced to ensure that data collection and reporting obligations under the Fraud Control Guidelines are met. The ATO considers that its new case management system, which is to be implemented later this year, will address this issue in subsequent years.

⁹ This value should have included all ATO fraud data.

¹⁰ Revised statistics to AGD include actual losses for successful and unsuccessful prosecutions completed during the year and matters closed as a result of the Commonwealth Director of Public Prosecutions deciding not to prosecute.

GST fraud prevention strategies

17. The ANAO found that the GST Business Line, supported by the Fraud Prevention and Control Section and Fraud Investigations, has developed an effective training program that includes internal and external fraud awareness training. This provides officers with the necessary skills to detect fraudulent activity.

18. The ATO has also invested significant resources to make its client population aware of its legislative requirements and responsibilities through a range of communication strategies. This ongoing education supports the ATO's compliance activities and the philosophy underpinning its Compliance Model. Although these activities were not specifically related to fraud, the ANAO considers they play an important role in preventing fraudulent activity and assist in improving levels of compliance.

19. Based on a high-level review of GST General Compliance, the ANAO considers that the ATO has well-structured compliance programs that, although not specifically directed at GST fraud, incorporate fraud prevention strategies, detection capabilities and enforcement policies. The emphasis on improving compliance is supported by the ongoing assessment of risks, early intervention strategies, targeted compliance activity, education programs and, where necessary, enforcement action. Publicly stating its proposed compliance activity and providing details of cases where fraud has been detected and successfully prosecuted, also engenders community confidence in Australia's taxation system and demonstrates the ATO's commitment to ensuring compliance.

20. As part of the tax reform initiatives, the ATO developed a suite of applications to process and monitor activity statements. These applications contain embedded controls to identify potentially fraudulent activities during processing of the Business Activity Statement.

GST fraud detection strategies

21. The ATO has developed the Risk Rating Engine (RRE) to assist in detecting potential fraud and non-compliance in a 'real-time environment'. The RRE risk profiles GST registrations at lodgement of the registration application and incoming activity statements of clients registered for the GST. This is prior to the issue of any refund. In addition to the RRE capability, Fraud Intelligence is responsible for detecting potential GST fraud. The compliance activities, refund assurance programs and risk identification projects undertaken by GST General Compliance may also detect potential GST fraud.

Risk Rating Engine

22. The implementation of the RRE presented considerable challenges for the ATO. A critical policy decision was made by the GST Executive in May 2000 to reduce the potentially unmanageable number of RRE stopper work items (cases) created.¹¹ It was also intended to reduce any adverse impact on the Instalment Processing System processes and the timeliness of activity statement refund processing. The change in policy was translated into new specifications, which essentially created a 'stopper work item' for activity statements with a refund over a particular dollar value.

23. The GST Compliance Executive also supported recommendations to suspend a number of compliance risk characteristic tests and exception tests because of invalid and/or insufficient data. These decisions were implemented with effect from October 2000.¹² Changes were also made to fraud risk area threshold values.¹³ These changes were designed to reduce the number of work items being generated and to avoid causing significant delays in the time taken to process work items and related refunds.¹⁴

Release management process

24. The ATO controls all changes to its key production business applications, such as the RRE, through project management committees, which oversee the selection and testing of the changes through a scheduled release program. There have been several updates to the RRE controlled through the ATO's Tax Release management projects. The ANAO concluded that there were appropriate controls over the approval, testing and subsequent release into production of the RRE changes implemented as part of those releases.

Online changes by system administrators

25. Online changes to the RRE risk characteristics and thresholds can be made outside the ATO's formal release management process. These changes are implemented by the Business Function Area Administrator through a change request approved by GST Business Systems and Technology. The ANAO notes that, in some instances, details relating to these changes were not recorded in

¹¹ A stopper is placed on a work item when there is a direct risk to revenue, for example, the payment of a GST refund.

¹² Of the 22 compliance risk characteristic tests, 10 have been suspended. Of the 10 exception tests, seven tests have been suspended; three tests relating to refunds are active. Five fraud exception tests and one fraud characteristic test have been suspended.

¹³ A threshold value is set in the risk areas for each fraud risk characteristic. Where the threshold is exceeded, a work item is generated.

¹⁴ Australian Taxation Office, *High Level Business Analysis of the Risk Rating Engine (RRE)*, February 2002, p. 38.

the change register. In July 2002, a management oversight committee was established. The RRE Change Management Committee now approves all changes to the RRE. These are to be recorded in the change register.

Reviews of the RRE by GST Business Systems and Technology

26. The ATO has undertaken a number of reviews of the RRE. The reviews noted that the majority of suspended tests have never been operational, potentially restricting the risk profiling process. The main reason that the tests have remained suspended for so long has been the lack of analytical support to overcome the reasons for their initial suspension. This has also prevented the refinement of existing tests and the advancement of new tests to ensure that the risk profiling process is relevant to the existing ATO environment.¹⁵ Modifications to the system to improve the identification of non-compliance and targeting of verification and compliance activity were also recommended. The GST Strategic Risk Management Unit is currently undertaking a holistic review of the RRE compliance business rules.

Evaluation of RRE fraud tests

27. Fraud Intelligence, as the business owner of the RRE fraud tests, has evaluated these tests to determine if they are consistent with the original business requirements. The ANAO found the evaluation of the tests to be generally comprehensive. However, there was limited documentation to support the testing process. As well, no evaluation report was prepared for ATO management.

28. Two national operations also focused on evaluating the work items generated by the RRE fraud tests: Operation Kaiser and Operation Berry. Operation Kaiser recommended modifications to the RRE fraud tests, because the tests examined were not focused enough and frequently triggered bona-fide businesses. Operation Berry recommended a more targeted case selection process because of the low level of fraud referrals being generated. The ATO advised that, to date, no changes have been made to the RRE fraud tests as a result of these national operations. However, they are being considered as part of the current review of the RRE.

Fraud intelligence detection capabilities

29. Fraud Intelligence has implemented the Registration Information Matching System (RIMS), which is designed to detect and prevent fraud through

¹⁵ Australian Taxation Office, Risk Rating Engine Business Issues Post TR4.0, *Fine Tune Risk Rating Engine Through Analysis and Review of the Risk Profiling Process*, June 2002, p. 35.

identifying potentially suspect Australian Business Number (ABN) and GST registrations.

30. The number of outstanding RIMS matches awaiting assessment suggests that the RIMS capability may not have been fully utilised, inhibiting the ATO's ability to respond to potential fraud in a timely manner. The ATO advised, during the audit, that additional analysts have been employed to work with the RIMS project officer. The ANAO considers that processes need to be put in place to ensure that all potential fraud cases are matched against RIMS data and reference list. Also, where appropriate, details of completed fraud cases should be added to the RIMS reference list for ongoing monitoring.

31. Fraud Intelligence's strategic assessment area was formed in 2001 to establish a fraud strategic intelligence and risk capability. The area is responsible for undertaking strategic assessments of identified risks. Such assessments may result in and/or support the conduct of national fraud operations. The ANAO found that only one strategic assessment has been completed. This related to a non-GST matter. The ATO advised that, because of the prioritisation of resources within Fraud Intelligence, this area has not always been fully functional. As a consequence, the ATO currently does not have a strategic fraud intelligence capability to support the effective targeting of fraud detection strategies and/or the development of fraud risk treatments. However, the ATO advised that this would be addressed following the recruitment of additional intelligence analysts and reallocation of resources within Fraud Intelligence.

32. National operations may be initiated to identify fraudulent behaviour and transactions, prevent revenue loss and develop treatment strategies that address system and/or control weaknesses. Fifteen operations have been commissioned¹⁶ but, in general, they are in the early stages of project initiation. The ANAO considers that, in order to address GST fraud risks in a more systematic manner and successfully achieve the outcomes of national operations, the Serious Non-Compliance Capability Executive should take a more active oversight role and improve the management, resourcing, monitoring and reporting of these operations. The ATO advised in May 2003 that it intends reviewing all matters nominated as national operations.

Investigating GST Fraud

33. Fraud Intelligence assesses all potential GST fraud referrals received from internal and external sources. The ANAO considers that the case referral process

¹⁶ Operations that have been assigned a name as reported in the SNCC November 2002, *Report to the GST Business Forum*. These Operations involve GST and other taxes, including Income Tax and Capital Gains Tax.

would be improved if assessment decisions were documented and intelligence assessments were completed for all fraud cases registered on the FIRM system (referred to earlier). Fraud Intelligence has access to all ATO systems and a range of external databases. Research undertaken using these systems will add value to any fraud investigation and improve the quality of referrals to Fraud Investigations.

Management of GST fraud investigations

34. The ANAO considers that the ATO has established a sound framework and implemented appropriate procedures for assessing GST fraud case referrals and conducting fraud investigations. However, these procedures were not always consistently implemented across regions.

35. The ANAO found it difficult to determine the time taken to complete investigations because of incomplete data in the reports provided from the FIRM system. For those cases (97 cases) where the information was available, on average, it took 164 days to complete an investigation, with ten cases taking fewer than seven days and two cases taking over 500 days. Complete information was available for only six of the 43 cases reviewed by the ANAO. For these cases it took, on average, 355 days to complete the investigation.

36. The ANAO considers that this lack of data makes it difficult for the ATO to accurately determine the age of cases and readily assess the viability of continuing an investigation. The ATO advised that its new case management system, which is to be implemented later this year, is designed to include a broad range of investigation milestones. The monitoring of these milestones by case officers and team leaders should improve case management.

37. The ANAO found that the FIRM system reports provided as part of the audit were generally incomplete, as information had not been entered into a number of the data fields. As a result, it was difficult to cross-reference data from one report to another. The ATO advised that reports were not designed to reconcile with one another. This is due to the nature of the business rules for data entry, the manner in which the reports have been setup and report parameters. The ANAO considers that, given these data quality issues, the accuracy and completeness of reports produced for the SNCC Executive and ATO Management are questionable. The data integrity of the FIRM system also impacts on the ATO's ability to meet its external reporting requirements under the Fraud Control Guidelines.

38. The ATO's fraud investigation guidelines require completed investigations to be reviewed to identify risk, as well as systems and control issues requiring attention by management. The ANAO found no evidence of the systematic

analysis of GST fraud trends, referral patterns, or case outcomes being undertaken on a regular basis, particularly at a national level. There was also no evidence that any formal evaluation had been undertaken of the sample cases reviewed by the ANAO. Such analysis should be documented and control weaknesses or emerging issues formally advised to the relevant business line(s). This would allow the ATO to identify and react to emerging GST fraud trends, risks and system weaknesses.

Overall Conclusion

39. The ATO has systems and processes in place to prevent, detect, investigate and report GST fraud. These activities are undertaken and implemented across business lines. However, the ANAO considers that these activities need to be better integrated and coordinated if they are to underpin an effective GST fraud control framework and fully meet the requirements of the Commonwealth Fraud Control Guidelines.

40. The ATO is currently revising its GST fraud control plan. This will allow the ATO to undertake a comprehensive assessment of all GST fraud risks. The plan should also integrate GST fraud prevention, detection and mitigation strategies across the ATO. The ANAO has identified a number of areas where improvements could be made to strengthen the ATO's fraud control framework. These include:

- articulating to staff the ATO's overall fraud control strategy and how the Commonwealth's definition of fraud is to be interpreted and implemented;
- recognising that external fraud should be treated as a separate component of the ATO's compliance continuum;
- reviewing data collection requirements and the integrity of data to be included in fraud reports; and
- enhancing the effectiveness of the RRE as a fraud detection tool.

Recommendations

41. The ANAO has made eight recommendations aimed at improving the ATO's systems and processes for preventing, detecting, investigating and reporting GST fraud. The ATO has agreed with all recommendations.

Acknowledgements

42. The ANAO would like to express its appreciation to the ATO's management and staff for their assistance in the conduct of this audit.

Recommendations

The ANAO has made eight recommendations aimed at improving the ATO's fraud control arrangements. During the audit, the ATO introduced several initiatives to strengthen its GST fraud control framework. These recommendations are designed to complement the ATO's recent initiatives.

Recommendation No.1
Para. 2.12

To underpin fraud control activities and provide a clear and consistent understanding of fraud within the ATO, the ANAO recommends that the ATO, in publicising its fraud policy statement to staff, articulate how the Commonwealth's definition of fraud is to be interpreted and implemented across the ATO.

ATO response: Agreed

Recommendation No.2
Para. 2.33

To ensure a comprehensive assessment of GST fraud risks supports the development of the revised GST fraud control plan and subsequent fraud prevention and detection strategies, the ANAO recommends that the:

- (a) GST Business Line and Fraud Intelligence undertake specific assessments of GST fraud risks; and
- (b) Fraud Prevention and Control Section coordinate all assessments of GST fraud risks undertaken by all relevant business lines.

ATO response: Agreed

Recommendation No.3
Para. 2.45

To ensure the data collection and reporting obligations required by the Commonwealth Fraud Control Guidelines are met, the ANAO recommends that the ATO review:

- (a) its data collection requirements; and
- (b) the integrity of the data to be included in its annual fraud report to the Attorney-General's Department.

ATO response: Agreed

**Recommendation No.4
Para. 4.30** To improve the effectiveness of the Risk Rating Engine fraud tests and business rules, the ANAO recommends that Fraud Intelligence continue to evaluate the tests and include the analysis of historical data, supported by the evaluation of fraud investigations and intelligence assessments.

ATO response: Agreed

**Recommendation No.5
Para. 4.42** To ensure that the Registration Information Matching System (RIMS) is being used to its maximum potential to prevent and detect GST fraud, the ANAO recommends that:

- (a) all potential and existing fraud cases are matched against RIMS data and reference list; and
- (b) details from appropriate completed fraud cases are added to the RIMS reference list for ongoing monitoring and review.

ATO response: Agreed

**Recommendation No.6
Para. 5.14** To improve the quality of referrals and add value to fraud investigations, the ANAO recommends that:

- (a) all fraud matters registered on the Fraud Investigation Reporting and Management (FIRM) system as potential fraud cases be assessed by Fraud Intelligence; and
- (b) the intelligence assessment process be properly documented by analysts.

ATO response: Agreed

**Recommendation No.7
Para. 5.38** To support the referral of high quality briefs of evidence to the Commonwealth Director of Public Prosecutions (CDPP), the ANAO recommends that the ATO include in investigation guidelines a mandatory requirement for regional managers or team leaders to review briefs of evidence prior to referral to the CDPP.

ATO response: Agreed

Recommendation No.8
Para. 5.49 To support fraud control planning and the development of fraud prevention and detection strategies, the ANAO recommends that the ATO routinely evaluate and analyse fraud referrals, investigations, case outcomes and trends nationally and disseminate this information within the ATO.

ATO response: Agreed

Audit Findings and Conclusions

1. Background and Context

This chapter outlines the Commonwealth's fraud control requirements and the Australian Taxation Office's role and responsibilities. It provides context for the introduction of A New Tax System, of which the Goods and Services Tax is an integral part, and sets out the objective and scope of the audit.

Fraud control within the Commonwealth Public Sector

1.1 Fraud against the Commonwealth is a major concern to the Government. Agencies must ensure that fraud is minimised and that, where fraud does occur, it is rapidly detected, effectively investigated, appropriately prosecuted and that losses are minimised.¹⁷ Fraud control requires the commitment and involvement of all Commonwealth agencies, employees and external service providers. The importance of agencies establishing effective fraud control arrangements has been recognised in the *Financial Management and Accountability Act 1997* (FMA Act). Under Section 45 of the FMA Act, Chief Executive Officers (CEOs) must implement a fraud control plan and report to their Minister on fraud control initiatives undertaken by the agency.

Commonwealth Fraud Control Guidelines

1.2 The Commonwealth Government has outlined its fraud control policy in the *Commonwealth Fraud Control Guidelines* (Fraud Control Guidelines) issued in May 2002.¹⁸ The Fraud Control Guidelines require Commonwealth agencies to put in place a comprehensive fraud control program that includes prevention, detection, investigation and reporting strategies.

1.3 The Guidelines, which define fraud as *dishonestly obtaining a benefit by deception or other means*—include both tangible and intangible benefits¹⁹ and applies to:

- all agencies covered by the FMA Act; and

¹⁷ Attorney-General's Department, *Commonwealth Fraud Control Guidelines*, May 2002, p. iii.

¹⁸ The Government first released its Fraud Control Policy of the Commonwealth in 1987. This policy was revised in 1994 and subject to extensive review and consultation. Consultation Draft No.1 was issued in June 1999 and Consultation Draft No.2 in April 2001.

¹⁹ This definition includes: theft; obtaining property, a financial advantage or any other benefit by deception; causing a loss, or avoiding or creating a liability by deception; providing false or misleading information to the Commonwealth, or failing to provide information where there is an obligation to do so; making, using or possessing forged or falsified documents; bribery, corruption or abuse of office; unlawful use of Commonwealth computers, vehicles, telephones and other property or services; relevant bankruptcy offences; and any offences of a like nature to those listed above.

- bodies covered by the *Commonwealth Authorities and Companies Act 1997* that receive at least 50 per cent of funding for their operating costs from the Commonwealth or a Commonwealth agency.²⁰

1.4 The Attorney-General's Department (AGD), the Australian Federal Police (AFP) and the Commonwealth Director of Public Prosecutions (CDPP) are the Commonwealth agencies with cross-government responsibilities in relation to fraud control.

Attorney-General's Department

1.5 The AGD advises the Minister on fraud control, including the implementation of the Fraud Control Guidelines, and is specifically responsible for:

- advising agencies on implementing the Fraud Control Guidelines;
- reviewing Commonwealth fraud control arrangements as directed by the Minister;
- collecting, analysing and disseminating information on the nature and extent of fraud against the Commonwealth; and
- establishing and maintaining a Fraud Trend Information Network, in conjunction with the AFP.²¹

1.6 Agencies are required to collect information relating to fraud and provide a report to the AGD annually. The information includes details of investigations undertaken, case outcomes, losses, monies recovered, fraud resources and fraud awareness training provided. A summary report combining fraud statistics from all Commonwealth agencies is then provided to the Minister for Justice and Customs.²²

Australian Federal Police

1.7 The AFP investigates serious or complex crime against Commonwealth interests. The AFP helps Commonwealth agencies in their investigations by

²⁰ Section 28 of the *Commonwealth Authorities and Companies Act 1997* provides that the responsible Minister may, after consultation, notify the directors of a Commonwealth authority in writing of general policies of the Commonwealth that are to apply to the agency.

²¹ The Commonwealth Fraud Trend Information Network is currently under development and yet to be approved by the Minister. The aim of the network is to establish a low-cost open forum fraud trend information source that will be available to all Commonwealth agencies. Information available through the network will be drawn from various sources including the Commonwealth Fraud Liaison Forums, agencies reporting to the Attorney-General's Department and the Australian Crime Commission.

²² Attorney-General's Department, *Commonwealth Fraud Control Guidelines*, May 2002, p. 29.

providing forensic and technical assistance and executing search warrants. Under the Fraud Control Guidelines, the AFP is also responsible for:

- providing case management reports on investigations it undertakes;
- conducting quality assurance reviews of agencies' investigations;
- maintaining and reviewing Commonwealth investigation standards; and
- providing a fraud control liaison and dissemination function.

Commonwealth Director of Public Prosecutions

1.8 The CDPP prosecutes offences against Commonwealth law and conducts related criminal assets recovery. All prosecution and related decisions are based on the Prosecution Policy of the Commonwealth.

Joint Committee of Public Accounts and Audit reviews

1.9 Fraud control continues to be an area of interest for the Joint Committee of Public Accounts and Audit (JCPAA). In its report, *Review of Auditor-General's Reports 2000–2001 Second and Third Quarters*,²³ the JCPAA suggests that agencies develop sub-categories of fraud to provide a better understanding of the nature and significance of various types of fraudulent activity. The JCPAA requested the Australian National Audit Office (ANAO) to develop fraud sub-categories that may be used when reporting fraud. The ANAO is developing a Better Practice Guide on Fraud Control in 2003–04 following the completion of a series of fraud audits and a second survey of fraud control arrangements in the Australian Public Service.²⁴ It will incorporate consideration of the JCPAA's suggestions.

The Australian Taxation Office

1.10 The Australian Taxation Office (ATO) is the Federal Government's principal revenue collection agency. It aims to manage and shape the revenue systems that give effect to social and economic policy, and fund services for Australians.²⁵ The ATO employs more than 21 000 officers located in 46 offices

²³ Joint Committee of Public Accounts and Audit Report No.385, August 2002, *Review of Auditor-General's Reports 2000–2001 Second and Third Quarters*, p. 8. The following fraud-related audit reports were reviewed by the Committee: *Australian Taxation Office Internal Fraud Control Arrangements*; and *Fraud Control Arrangements in the Department of Defence*.

²⁴ ANAO Audit Report No.47, 1999–2000, *Survey of Fraud Control in APS Agencies*. A second survey of APS agencies is currently being undertaken.

²⁵ The four outputs that support this outcome are: to contribute to policy advice and legislation; provide revenue; provide transfers; and support other agencies. Commissioner of Taxation, *Annual Report 2001–02*, pp. 8 and 21.

throughout Australia. The ATO is structured into business and service lines,²⁶ which are organised around market segments, revenue products and services. Total cash collections by the ATO in 2001–02 were \$168.7 billion. Of this, \$26.9 billion was collected for the Goods and Services Tax (GST). The GST, which is part of the Government's new tax system, was introduced from 1 July 2000.

Implementation of the GST by the Australian Taxation Office

1.11 The GST is a broad-based indirect tax, imposed on goods and services at each point in the distribution chain, including at importation. The GST replaced the existing wholesale sales tax and a number of indirect State taxes. The GST rate is 10 per cent.

1.12 Businesses with an annual turnover of \$50 000 or more are required to be registered for GST purposes.²⁷ Non-profit organisations have a threshold of \$100 000. Generally, registration for the GST enables a business to claim input tax credits for any GST it has paid for goods and services used during the course of its business. To remit or claim a refund for GST, businesses must have an Australian Business Number (ABN) and have registered for the GST. The ABN, a unique 11-digit number, became the identifier for businesses and a key element of the Government's new tax system. If businesses do not have an ABN, tax must be withheld (at the top marginal rate) from payments owing to them under the Pay As You Go system. At September 2002, there were 4.3 million active ABNs in the Australian Business Register.²⁸

1.13 Entities are required to complete and return to the ATO a Business Activity Statement (BAS) at the end of each tax reporting period²⁹ to report their GST obligations and entitlements. Any amount owing will be refunded only after it has been offset against any other outstanding tax debts.

The ATO Compliance Program

1.14 In December 2002, the ATO released its *Compliance Program 2002–03*. The program outlines the ATO's overall approach to GST compliance. It also indicated that there would be an increase in active compliance. The Program identified risks to Australia's revenue system and the strategies underway to manage them. The main focus of the program for GST is fraudulent or incorrect claims for

²⁶ Business Lines have an external client focus and are organised around either market segments or revenue products (eg. Small Business, GST). Service Lines have an internal client focus and produce products and services for internal ATO use (eg. information technology, payroll management).

²⁷ Businesses with an annual turnover of less than \$50 000 may choose not to register.

²⁸ ANAO performance audit of the ATO's *Administration of Australian Business Number Registrations*, report to be tabled in June 2003.

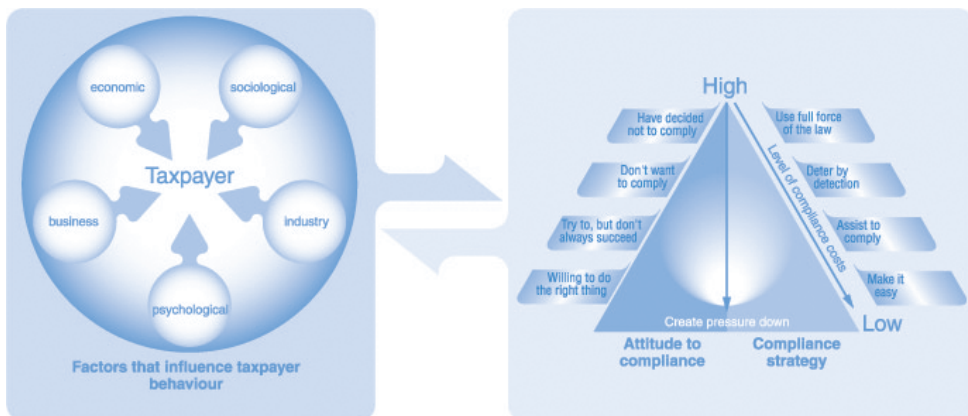
²⁹ The reporting period can be either monthly, quarterly or annually.

refunds, the cash economy, businesses not understanding their obligations and sales of business assets. The Compliance Program is built around two core policy approaches—the ATO Compliance Model and the Taxpayers’ Charter.

Compliance Model

1.15 The Compliance Model, illustrated in Figure 1, recognises that ‘one size does not fit all’ and promotes a tailored, proportional response to non-compliance. The methods outlined range from education to targeted enforcement. The model shows a continuum of taxpayer attitudes towards compliance, from ‘willing to do the right thing’ to ‘choosing to evade or opt out of the tax system’. It also provides a summary of the support and intervention that may assist in the collection of revenue and suggests that taxpayer compliance can be influenced through the response of and interaction with the ATO.³⁰

Figure 1
ATO Compliance Model



Source: Australian Taxation Office

Taxpayers’ Charter

1.16 The Taxpayers’ Charter was introduced in July 1997 to address a perceived imbalance of power between the ATO and ordinary taxpayers.³¹ It details the relationship that the ATO wants to maintain with the community—that is, to be a professional, responsive tax office that is fair, open and accountable. The way the ATO is viewed by the community is important because the ATO considers there is a direct correlation between the level of trust and respect from the community and the level of voluntary compliance. The Charter also provides information on the rights and obligations of taxpayers and incorporates input

³⁰ Australian Taxation Office *Compliance Program 2002–03*, (inside cover).

³¹ Commissioner of Taxation, *Annual Report 2001–02*, p. 117.

from the community and other stakeholders.³² The Charter is currently under review and it is anticipated that a revised Charter and implementation plan will be released in mid-2003.

The ATO's administrative arrangements for GST fraud

1.17 The areas responsible for preventing, detecting, investigating and reporting GST fraud are:

- the GST Business Line;
- the Serious Non-Compliance Capability (SNCC) in the Small Business Line; and
- the Fraud Prevention and Control (FP&C) Section in the Internal Assurance Branch.

The GST Business Line

1.18 The GST Business Line employs 3300 officers and has primary responsibility for managing GST, luxury car tax and the remaining components of the wholesale sales tax. It is also responsible for maintaining the integrity of the tax system in relation to these taxes.³³ The Business Line delivers education, advice, interpretation and field activity services.

1.19 The GST Business Line is divided into GST General Compliance,³⁴ GST Large Enterprise Compliance³⁵ and GST Government and Community Sector. GST administration costs for 2001–02 were \$521.5 million.³⁶ These costs are attributed to eleven key activities, including fraud risk and investigation, GST strategic direction, registration of GST clients and processing of BAS. During 2001–02, the ATO:

- received and processed over 14 million activity statements, including 9.5 million BAS;
- issued 2.3 million BAS refunds; and
- had 2.19 million clients registered with an active GST role.³⁷

³² ATO website <<http://www.ato.gov.au/content.asp?doc=/content/corporate/charter.htm&page=1#H1>> 'Reviewing the Charter'.

³³ Commissioner of Taxation, *Annual Report 2001–02*, p. 15.

³⁴ For clients with an annual turnover of less than \$100 million.

³⁵ For clients with an annual turnover greater than \$100 million.

³⁶ *GST Administration Final Performance Report 2001–2002*, p. 59.

³⁷ *GST Administration Final Performance Report 2001–2002*, pp. 11, 17 and 19.

The Serious Non-Compliance Capability

1.20 The SNCC, which includes Fraud Intelligence and Fraud Investigations, is part of the Small Business Line. Fraud Intelligence is responsible for identifying potential fraud cases for investigation, providing fraud detection and intelligence analysis and identifying fraud control issues to management. Fraud Investigations' primary role is to investigate GST and other taxation fraud. Investigations may be conducted jointly with the AFP, other law enforcement and Commonwealth agencies.

Fraud Prevention and Control Section

1.21 The FP&C Section is part of the Internal Assurance Branch. The Section is responsible for developing the ATO's fraud control plans; conducting internal fraud awareness training; investigating matters of potential internal fraud; and fraud reporting.

GST/VAT fraud and the overseas experience

1.22 As part of its approach to developing a compliance program, the ATO surveyed international experience in the implementation and administration of GST and Value Added Tax (VAT) systems.³⁸ The ATO found that high quality general awareness and targeted education campaigns were important to validate and provide useful advice on a new system. These programs needed to be complemented by a highly visible, high volume audit program. Refunds were identified as a severe risk because of inexperience with the system, and through false claims.

1.23 The ANAO also sought to gain an understanding of how similar overseas countries were dealing with GST/VAT fraud. Research included Canada, the United Kingdom and the European Union.

Canada

1.24 In 2001–02, the Canadian Customs and Revenue Agency (CCRA) reported that over \$C62 billion in GST and Harmonised Sales Tax was collected.³⁹ Rather than attempting to estimate overall levels of non-compliance, such as the 'tax

³⁸ In particular, New Zealand—as the best policy model; Canada—as having the best demographic fit with Australia; Singapore—for its use of modern technology; and the United Kingdom—as having a mature system.

³⁹ Canada Customs and Revenue Agency, 2001–2002 *Annual Report to Parliament*, 'Managing the compliance continuum' <http://www.ccr-aadrc.gc.ca/agency/annual/2001-2002/performance-e/MP_Txserv.html#wp1284258>.

gap',⁴⁰ the CCRA relies on information derived from compliance programs, and other indirect measures, to make a qualitative assessment. In the Agency's assessment, it found that, while non-compliance is material, it remains at 'relatively low levels, in line with prior years and compared to other countries'.⁴¹

The United Kingdom

1.25 VAT is Her Majesty's Customs and Excise (HMC&E) largest tax stream, representing 57 per cent of total receipts.⁴² Although it is inherently difficult to quantify with any degree of precision the tax not paid through error, evasion or avoidance, HMC&E estimated that, for 2001–02, VAT losses were between £7.1 billion and £10.2 billion.⁴³

1.26 For HMC&E, a clear evidence-based understanding of the problem faced was the key to developing effective strategies to deal with this type of fraud. In November 2002, HMC&E announced a new strategy for tackling fraud across all parts of the VAT system. This strategy will incorporate the use of additional resources, expertise and legislation to support its anti-avoidance effort. Persistent non-compliance will be addressed through:

- more effective use of intelligence to identify patterns of non-compliance;
- the establishment of specialist teams, whose visits will target high risk sectors and businesses;
- an increase in follow-up activity; and
- the use of the range of penalties and sanctions available to punish revenue evasion.⁴⁴

The European Union

1.27 The European Union has been attempting to combat VAT fraud for many years.⁴⁵ In December 2002, the European Parliament and the Council adopted the *Fiscalis 2003–2007* program to combat tax and customs fraud. The program

⁴⁰ The tax gap is the difference between what is believed to be owed and what is actually collected. The CCRA has found that attempts to estimate non-compliance are costly and unreliable.

⁴¹ Canada Customs and Revenue Agency, 2001–2002 *Annual Report to Parliament*, 'Managing the compliance continuum' <http://www.ccra-adrc.gc.ca/agency/annual/2001-2002/performance-e/MP_Txserv.html#wp1284258>.

⁴² National Audit Press Notice, *Report by the Comptroller and Auditor General*, February 2002.

⁴³ These losses included VAT Missing Trader fraud (£2.75 billion), avoidance (£3 billion), general non-compliance (£4 billion) and failure of business to register for VAT when operating above the turnover threshold (£500 million). Her Majesty's Customs and Excise, *Measuring indirect tax losses*, November 2002, paragraphs 2.1–2.41.

⁴⁴ Her Majesty's Customs and Excise, *Measuring indirect tax losses*, November 2002, p. 18.

⁴⁵ *International Tax Report*, April 1992, p.16 'European Community : Anti-fraud tax measures adopted'.

aims to help member states work together to fight tax and customs fraud by encouraging closer co-operation between the authorities in the member states; providing training on the different kinds of fraud; and developing prevention, detection and investigation methods based on risk analysis.⁴⁶

Audit objective, scope and methodology

Objective and scope

1.28 The audit objective was to assess whether the ATO has implemented administratively effective GST fraud control arrangements, consistent with the Commonwealth Fraud Control Guidelines.

1.29 The audit addressed the following key elements of fraud control:

- fraud control arrangements integrated within the ATO's corporate governance framework;
- strategies, systems and processes used to prevent and detect GST fraud;
- management of GST fraud investigations; and
- reporting of GST fraud.

1.30 Given the crucial role the Risk Rating Engine (RRE)⁴⁷ plays in detecting fraudulent and non-compliant behaviour in the processing of activity statements, the ANAO reviewed a number of the RRE's key controls.

1.31 The review of corporate governance arrangements included all GST business areas, as they are included in the ATO's Compliance Sub-Plan. Fraud prevention and detection focussed on GST General Compliance only. This is the business area identified as presenting the highest risk and where GST fraudulent activity has been identified. Within the SNCC, fraud detection strategies employed by Fraud Intelligence and the management of fraud investigations were assessed.

Audit methodology

1.32 The audit methodology adopted included quantitative and qualitative analysis, file and document reviews and interviews with agency officers.⁴⁸ A sample of 43 completed fraud investigations and 25 fraud referrals received by

⁴⁶ European Parliament and Council Decision 888/98/CE instituted the Community Action Programme called 'Fiscalis'. The program covered the period from 1 January 1998 to 31 December 2002. (http://europa.eu.int/comm/taxation_customs/taxation/fiscalis/what_is_en.htm).

⁴⁷ The RRE profiles, risk, in a 'real time environment', for GST registrations at the time of lodgement of the registration application and incoming activity statements of clients registered for the GST prior to the issue of refunds.

⁴⁸ The offices visited during the audit were Canberra, Sydney, Melbourne, Brisbane and Adelaide.

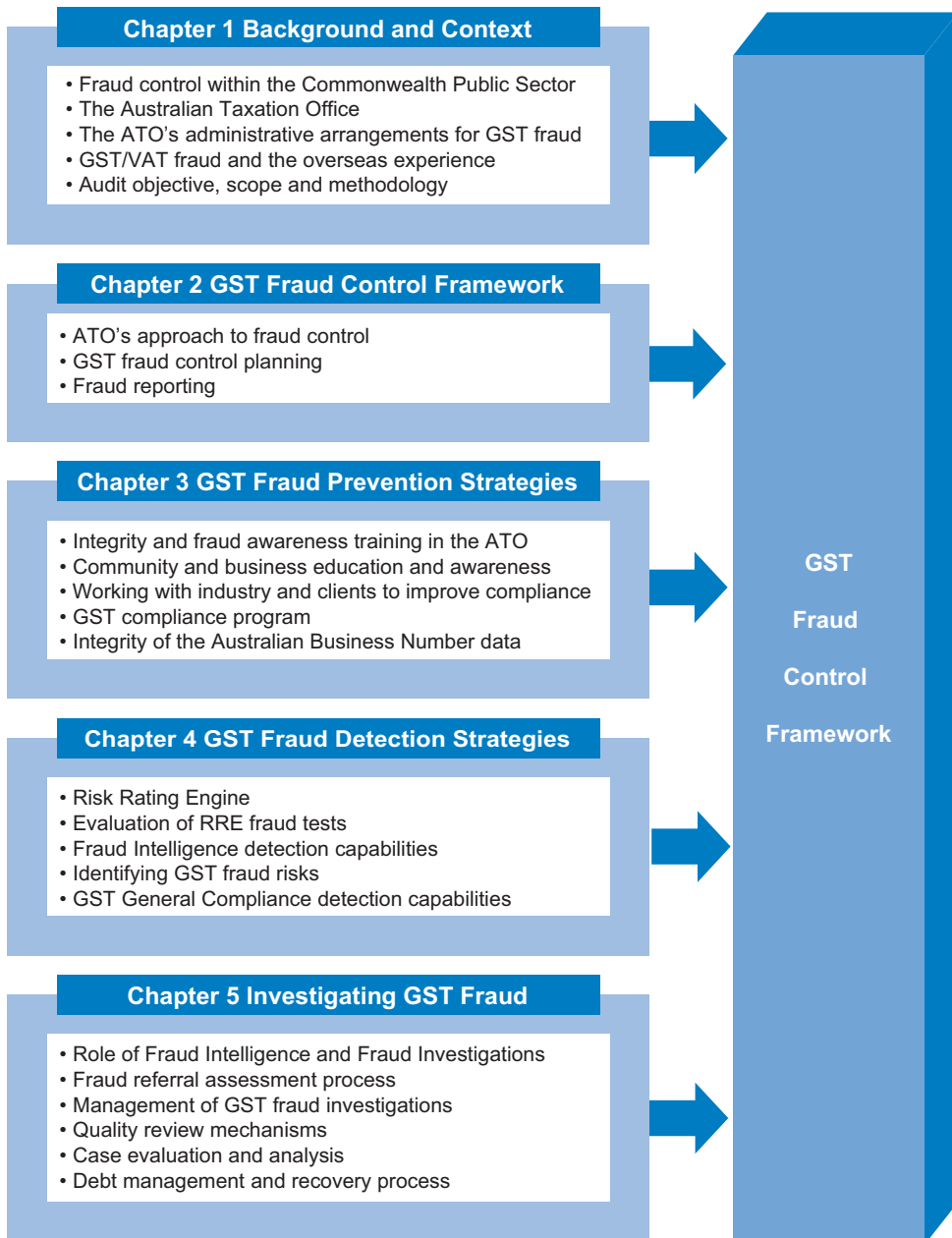
Fraud Intelligence was also reviewed.⁴⁹ The ANAO did not review cases relating to GST internal fraud as all cases were still under investigation. The ANAO consulted the AGD, AFP and the CDPP and held discussions with selected industry partner representatives.

Report structure

1.33 Figure 2 illustrates the framework the ANAO used to analyse the ATO's fraud control arrangements. This framework formed the basis for the structure of the report.

⁴⁹ The sample included cases from all regions.

Figure 2
Report structure



2. GST Fraud Control Framework

This chapter outlines the ATO's fraud control framework and its arrangements for GST fraud. Fraud control planning, assessment of GST fraud risks and fraud reporting are discussed.

Introduction

2.1 Effective fraud control needs to be integrated into an agency's business planning processes. This includes developing and maintaining a formal risk management strategy that incorporates fraud risks. Strategies to minimise fraud should be developed to create a framework for fraud control at operational and technical levels.

2.2 Key elements of the Fraud Control Guidelines require:

- CEOs to develop an overall fraud control strategy for the agency, including operational arrangements for dealing with fraud;
- agencies to prepare fraud risk assessments and fraud control plans;
- CEOs to report on fraud control activities; and
- agencies to advise the AFP annually of their current identified major fraud risks and serious or complex fraud cases.

2.3 To determine how the ATO had addressed these requirements for GST fraud, the ANAO reviewed the context in which GST fraud is managed within the ATO. Fraud control planning, including assessment of GST fraud risks, and fraud reporting were also examined.

ATO's approach to fraud control

2.4 Section 45 of the FMA Act places a responsibility on the CEO to ensure the agency has a current and effective fraud control plan in place that includes external fraud. The ATO's Chief Executive Instruction (CEI) setting out the arrangements for developing fraud control plans is currently being reviewed and will be finalised in June 2003. The responsibility for developing fraud control plans has been delegated to the FP&C Section.

2.5 The ATO adopts a 'rolling plan' approach to producing its fraud control plans. Under this approach, the ATO produces a number of plans to address its fraud risks over a two-year period. The fraud control plans for the current cycle are a combination of plans focusing on fraud risks within major processes and

fraud risks being considered under structural criteria.⁵⁰ Twenty fraud control plans are to be completed in this cycle.⁵¹ The ATO does not regard fraud control planning as restricted to any one of these plans.

2.6 Prior to December 2001, the ATO considered that focusing on internal fraud satisfied the then Fraud Control Policy of the Commonwealth. The ATO considered its internal fraud control plans, supported by its extensive compliance programs, would provide an effective response to fraud.

2.7 In 2002, the ATO revised its approach to fraud control. Between January and April 2002, the ATO began to look at both internal and external fraud risks when preparing fraud control plans. Initially, not all external risks were assessed. The ATO advised that 16 of the 20 fraud control plans since April 2002 to the end of the current rolling cycle in December 2003 will address internal and external fraud risks. The remaining four plans were commenced before April 2002. Of these, two had no external fraud risks. The scope of the third plan was extended to include external fraud risks and the plan will be amended to reflect this. As these plans did not relate to GST fraud, they have not been reviewed by the ANAO. The fourth plan, which involved GST fraud, is discussed later in this chapter.

How the ATO defines fraud

2.8 The Fraud Control Guidelines cover both internal and external fraud. For the ATO, internal fraud is fraud perpetrated on the Commonwealth by ATO staff. External fraud is fraud perpetrated on the Commonwealth through the tax system by external parties.

2.9 The ATO applies the definition of fraud outlined in the Fraud Control Guidelines. This definition is implemented within the context of the ATO's Compliance Model. The Model promotes a tailored, proportional response to non-compliance. For example, the ATO's response to a mistake by a taxpayer is different to that where a taxpayer has sought to deliberately deceive the ATO for his or her own advantage. The ATO describes this latter category as serious non-compliance. Although the ATO does not generally use the term fraud⁵² when describing this category of compliance activity, fraud perpetrated by external parties fits within the category of serious non-compliance. The ATO's approach to serious non-compliance, evasion and fraud involves:

⁵⁰ The major processes approach is followed where the risks inherent in the activity straddle many business lines. A structural-based approach is used for risks relevant in only one or two business lines.

⁵¹ As at April 2003, six plans were completed, nine were in progress and five had yet to commence.

⁵² The ATO does refer to 'serious fraud and evasion' on occasions. This relates to certain specialist activities within its Serious Non-Compliance Capability.

- undertaking compliance audits that may identify potential fraud activity;
- analysing intelligence from income tax returns, activity statements and other taxpayer returns, as well as analysing significant cash transactions and international movements of funds;
- working with other law enforcement agencies to share intelligence and target illegal activity;
- undertaking risk assessments;
- investigating cases where there is evidence of fraud; and
- referring cases to the CDPP.⁵³

2.10 External fraud is an integral part of the ATO's compliance arrangements. Accordingly, this audit has included an examination of GST external fraud control arrangements in the context that they are part of the overall compliance arrangements for GST.⁵⁴

2.11 The Commissioner endorsed the ATO's Fraud Policy Statement in May 2003.⁵⁵ To date, this statement has not been publicised to ATO staff. The ANAO considers that, when advising staff of its fraud policy, the ATO should provide direction and guidance on how the Commonwealth's definition of fraud is to be interpreted and implemented consistently across the ATO. This would help to ensure a shared understanding of how fraud is to be managed within the ATO's compliance framework, the development of fraud control plans, and the reporting of fraud activities.

Recommendation No.1

2.12 To underpin fraud control activities and provide a clear and consistent understanding of fraud within the ATO, the ANAO recommends that the ATO, in publicising its fraud policy statement to staff, articulate how the Commonwealth's definition of fraud is to be interpreted and implemented across the ATO.

Agency response

2.13 Agreed.

⁵³ Australian Taxation Office, *Compliance Program 2002–03*, p. 21.

⁵⁴ The ANAO has already undertaken a performance audit of the ATO's internal fraud control arrangements (ANAO Report No.16 2000–01 *Australian Taxation Office Internal Fraud Control Arrangements*). This audit does not address in detail matters related to internal fraud.

⁵⁵ Attorney-General's Department, *Commonwealth Fraud Control Guidelines 2002*, p. 8.

Deputy Commissioner's Serious Non-Compliance Sub-Committee

2.14 A Deputy Commissioner's Serious Non-Compliance Sub-Committee, established in mid-2002, is the forum that brings together all parts of the ATO that have responsibility for fraud matters, be they internal or external. The Committee is intended to provide strategic guidance and support to those areas of the ATO dealing with taxpayers who demonstrate extremely poor compliance behaviour. These areas include the FP&C Section, Excise Investigations and the SNCC.⁵⁶ Although the management of the staff and resources dedicated to this issue remains within the respective business lines, it is envisaged that the Committee will seek to:

- facilitate a whole of ATO approach to issues such as serious non-compliance;
- encourage the utilisation of a full range of strategies to deal with the issue;
- provide strategic oversight and assistance with prioritisation of risks and treatment strategies;
- promote an integrated and consistent best practice approach across the ATO; and
- monitor and promote conformance with the Compliance Model and the Taxpayers' Charter.

2.15 The ANAO considers that this Committee plays an important role in bringing together the different areas of the ATO that are responsible for fraud related activities. The Committee is well placed to promote a consistent and integrated approach to:

- fraud control planning;
- assessment of fraud risks;
- implementation of fraud control plan recommendations; and
- data collection and reporting of fraud control activities and outcomes.

2.16 The ANAO suggests the Committee undertake an oversight role in relation to fraud control. The Committee is in a position to provide added assurance to the Commissioner and the Audit Committee that fraud control arrangements in the ATO have been properly implemented and to monitor the ongoing effectiveness of these arrangements.

⁵⁶ The Serious Non-Compliance Capability includes Fraud Intelligence, Fraud Investigations, Special Audit and Australian Transaction Reports and Analysis Centre liaison.

GST fraud control planning

2.17 In 2001, the ATO introduced new corporate planning arrangements. There is now an ATO Strategic Statement and Plan, Compliance Sub-Plan, Operations Sub-Plan, IT Sub-Plan and the People and Place Sub-Plan. Included in the Compliance Sub-Plan is the Commissioner's Corporate Priorities for 2002–03. One of these priorities was *continuing the work on ATO control and fraud protection systems*. The Compliance Sub-Plan Risk Statement indicates that serious non-compliance, which in many cases constitutes fraud, remains a focus area and has additional resources allocated, particularly in relation to GST credits.

2.18 In reviewing its approach to include external fraud within its overall fraud control arrangements, the ATO should consider how fraud control planning and reporting relating to GST are integrated into business practices. It is important that the assessment of fraud risks and the development of any fraud control plan are undertaken in a way, which recognises that external fraud is a separate component of the ATO's compliance continuum. Planning will also need to integrate compliance activities, as these are an integral part of the ATO's fraud mitigation strategies.

GST fraud control plan

2.19 The ATO provided the ANAO with a *Goods and Services Tax Draft Fraud Control Plan* (February 2002). This draft plan did not address external GST fraud risks. The ATO advised that this plan became part of the *GST Business Activity Statement Processing End to End*, (January 2003) fraud control plan. Risk assessment workshops were conducted between May and August 2001, with follow-up work occurring through to February 2002.

2.20 The ATO advised that the plan addressed internal fraud risks and a limited number of external fraud risks, principally relating to identity fraud and the integrity of the Tax File Number (TFN) and ABN registration systems. However, the accompanying minute to the Audit Committee⁵⁷ noted that risk assessment workshops targeted internal fraud. Further, in reviewing the plan, the ANAO found potential risks focused on internal fraud controls and did not assess external fraud risks. The ATO advised that, as GST fraud risks were still evolving and the plan would be rapidly out of date, a second review covering internal and external fraud risks was planned. The ATO plans to complete this risk assessment and fraud control plan by 30 June 2003. The ANAO recognises that GST fraud risks have also been assessed by Fraud Intelligence and included in the assessment of GST compliance risks. Mitigation strategies have been implemented through the GST Compliance Program.

⁵⁷ Minute was dated 13 January 2003.

Assessment of GST fraud risks

2.21 Under the Fraud Control Guidelines, agencies are to conduct fraud risk assessments at least every two years and, where appropriate, may introduce a rolling program of updating risk assessments. Agencies are to determine the risk assessment approach that is most appropriate for their circumstances and are encouraged to assess their fraud risks as part of their business risk management process. The risk assessment process is to be fully documented and must:

- reflect the risks across the range of functions performed by the agency;
- be able to measure risks in a comparable way;
- be capable of providing a supportable rating of the risks of fraud;
- be amenable to fine-tuning as appropriate; and
- be able to be replicated.

2.22 There are a number of different areas within the ATO that play a role in assessing the risks relating to GST fraud. These include the FP&C Section, the GST Business Line and the SNCC.

Risk assessment approach used by FP&C Section

2.23 The FP&C Section is responsible for coordinating fraud control planning arrangements and developing fraud control plans. The risk assessment methodology that the Section uses is consistent with the requirements of the Fraud Control Guidelines and the Australian and New Zealand Risk Management Standard 4360. The methodology includes a series of interactive workshops with key staff to identify and assess different fraud risks. Reliance is placed on the openness of key staff and the fraud experience of FP&C facilitators. The FP&C Section advised that the business lines are the 'owners' of fraud risks and have an ongoing responsibility to assess and mitigate these risks.

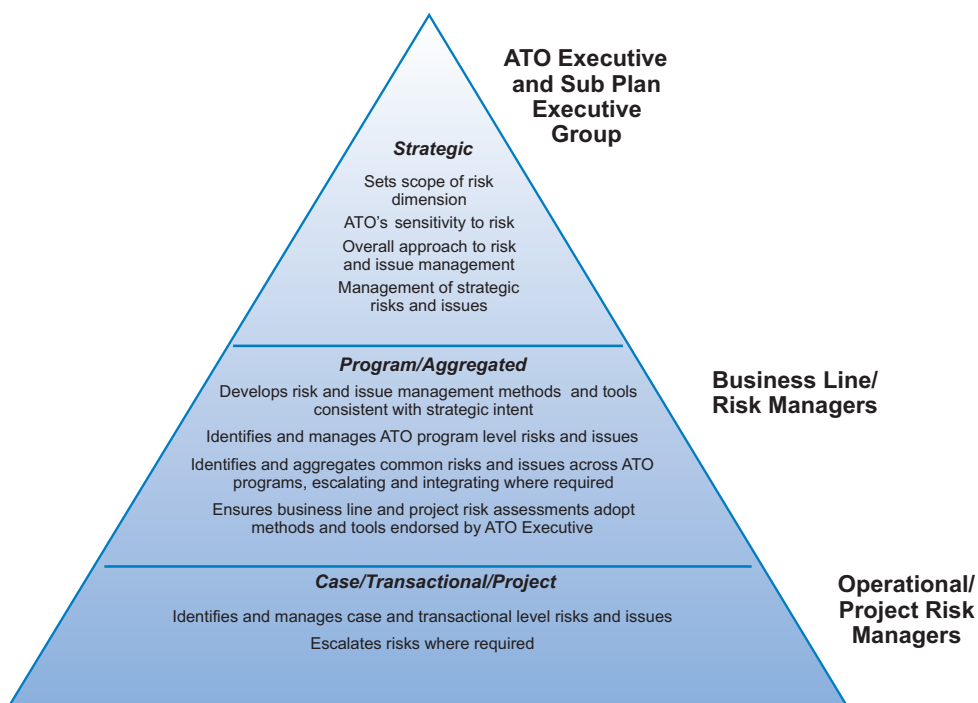
2.24 The ANAO considers a comprehensive assessment of fraud risks should include system controls being properly identified and tested. Risk mitigation strategies can then be developed to address system weaknesses. The FP&C Section currently does not have the capacity to undertake control testing but hopes to develop this during the next financial year.

Risk analysis undertaken within business lines

2.25 The ATO's *Risk Management Process Guidelines* outline three levels of perspective that need to be taken into account when assessing and managing risk. The three levels, illustrated in Figure 3, are:

- strategic—are events or actions which harm or enhance the ATO’s future progress and ability to achieve required ATO outcomes/outputs;
- program/aggregated—are case, transaction or project risks/issues that are grouped together to achieve an ATO-wide assessment; and
- case, transaction or project—are transactions, cases, events or actions, which could harm or enhance the operational/project’s future progress and required outcomes/outputs.

Figure 3
ATO’s Risk Management Approach



Source: ATO Risk Management Process Guidelines

ATO Risk Register

2.26 The national ATO Risk Register is an ATO database of compliance risks across all business lines maintained by the Knowledge Development Network (KNet).⁵⁸ The GST Strategic Risk Management (SRM) Unit’s Risk Analysis Team (RAT) is responsible for ensuring that GST risks are reflected accurately in the Register, and that the Register is up-to-date. As at February 2003, 142 GST related risks were recorded in the ATO Risk Register. This includes both GST compliance

⁵⁸ The KNet objective is to provide an intelligence, risk and knowledge management capability to support Small Business Line, Market Segment, Product Owner and Capability Executives.

and fraud risks. There is no distinction made between GST fraud and compliance risks in the Register.

GST Business Line

2.27 The SRM Unit identifies, analyses, prioritises and monitors new and existing risks and recommends risk treatment strategies. This work involves undertaking risk assessments, risk quantification projects (RQPs) and overseeing the operation of the GST National Risk Network. The GST National Risk Network is responsible for identifying current and emerging risks to the GST system and providing advice to the GST National Compliance Executive on appropriate treatment strategies. The SRM Unit RAT and a regional network of GST Risk Coordinators and Market Segment Representatives support this network. The Team:

- collates and reviews intelligence received;
- rates new risks based on the ATO's consequence and likelihood model;⁵⁹
- updates existing risks;
- registers the risks on the ATO Risk Register; and
- recommends treatment strategies.

2.28 Through RQPs, the ATO is able to identify the likely extent of non-compliance. Analysis of the outcomes of the RQPs allows the SRM Unit to develop methodologies and treatment strategies to target both the risk and the taxpayer population displaying non-compliant behaviour. This information is mainly at the operational level and generally relates to compliance risks. However, it is difficult to separate external fraud risks from the general compliance risks.

Fraud Intelligence

2.29 Fraud Intelligence is responsible for assessing external GST fraud risks. Fraud Intelligence receives considerable information regarding individual cases and projects that relate to GST fraud. Fraud referrals and potential cases are analysed and, where appropriate, data mining⁶⁰ activities undertaken. These risks are rated. The ATO advised that, as at December 2002, 48 risks had been identified and rated,⁶¹ with 30 relating to GST fraud. National operations may also be initiated to identify fraudulent behaviour and transactions, prevent

⁵⁹ Assessment rating is based on the consequence of the risk if left untreated and the likelihood of the risk occurring.

⁶⁰ Data mining is the analysis of large quantities of data in order to identify meaningful patterns, trends and/or rules.

⁶¹ Risks are categorised as severe, high, major, significant, moderate, low or trivial.

revenue loss and develop treatment strategies that address system and/or control weaknesses. Fifteen operations have been commissioned⁶² but, in general, they are in the early stages of project initiation. The ANAO considers that these activities are risk assessments at the case or aggregated level. The ATO advised that, because of the prioritisation of resources within Fraud Intelligence, no strategic risk assessments of GST fraud risks have been completed.

Risk assessment inputs to the Compliance Sub-Plan

2.30 In 2002, the GST Business Line provided input to the Compliance Sub-Plan. In relation to the assessment of GST risks, there was reference to increasing incidents of fraudulent activity and, in particular, tax avoidance and serious evasion associated with high-risk industries and practices. In relation to the cash economy, the loss of GST revenue through non-disclosure of income, failure to register and lodge a BAS, and the use of false invoices to fraudulently alter GST liabilities or refunds were identified. A range of treatment strategies addressing GST compliance risks, including serious fraud and evasion, are set out in the Sub-Plan's supporting documentation.

2.31 The ANAO found that the work undertaken by a number of different areas of the ATO should form part of a comprehensive assessment for external GST fraud risks. However, this work is not coordinated nor integrated as part of a comprehensive GST fraud risk assessment, sufficient to meet the requirements of the Fraud Control Guidelines. The ATO advised that this would be integrated as part of the second review of the *GST Business Activity Statement Processing End to End* fraud control plan to be completed in June 2003.

2.32 The ANAO considers the assessment of specific GST fraud risks should be undertaken as part of the ongoing business planning process by the relevant business line, owner or operational area. The assessments would then incorporate the technical expertise of the particular area and leverage off the work already being done for compliance risks. For example, the RQPs undertaken by the SRM Unit. The FP&C Section could then coordinate these assessments as part of the process of developing a fraud control plan.

⁶² Operations that have been assigned a name as reported in the SNCC November 2002, *Report to the GST Business Forum*. These Operations involve GST and other taxes, including Income Tax and Capital Gains Tax.

Recommendation No.2

2.33 To ensure a comprehensive assessment of GST fraud risks supports the development of the revised GST fraud control plan and subsequent fraud prevention and detection strategies, the ANAO recommends that the:

- (a) GST Business Line and Fraud Intelligence undertake specific assessments of GST fraud risks; and
- (b) Fraud Prevention and Control Section coordinate all assessments of GST fraud risks undertaken by all relevant business lines.

Agency response

2.34 Agreed. This approach will enhance our current GST fraud risk assessment processes.

Fraud reporting

2.35 The ATO produces a broad range of internal reports related to its GST compliance activities, and some reports that relate specifically to internal and external GST fraud matters. The areas that generate internal reports relating to GST fraud matters are the SNCC, the GST SRM Unit, the FP&C Section and the Strategic Directions and Programs area.

2.36 SNCC provides regular reports to the GST Executive.⁶³ Generally, these reports focus on external fraud matters. In broad terms, the reports describe the activities that are taking place, including data on the number of cases, information about individual projects or cases and the age of cases. The SNCC advised that the reports are constantly being reviewed to make more meaningful use of the available data.

2.37 The SRM Unit provides reports to the GST Compliance Executive that contain information relating to the compliance projects and RQPs that the Unit is overseeing. The resources to undertake these projects are provided by the GST Business Line. The reports do not have a particular focus on fraud matters, but relate more generally to GST compliance issues.

2.38 The FP&C Section produces quarterly reports that are provided to the Commissioner, Second Commissioners and the ATO Integrity Advisor. These reports relate to all suspected fraud that is committed by ATO staff. The reports cover significant matters that have occurred in the quarter, as well as information on the cases finalised and the types of investigations undertaken.

⁶³ The GST Executive includes the GST Board, the GST Compliance Executive and the GST Business Forum.

2.39 The Strategic Directions and Programs area is responsible for compiling the reports related to progress against the Compliance Sub-Plan, which are provided to the Compliance Executive Group (CEG) and the ATO Executive. Reporting against the Compliance Sub-Plan includes aggregated information relating to ATO-wide fraud and GST compliance.

Report to Attorney-General's Department

2.40 The annual report to the AGD required under the Fraud Control Guidelines is to include:

...suspected fraud, matters under investigation, and completed matters, whether the fraud was proven or not, and whether the matter was dealt with by a criminal, civil or administrative remedy.⁶⁴

2.41 This report is prepared by the FP&C Section and follows the format required by the Department. The FP&C Section and other areas within the ATO, including Fraud Investigations, provide the data for this report. The report to AGD indicated that, ATO-wide, there were 884 cases in 2001–02 and that the 'estimated value of loss arising from fraud cases' in that year was \$6 389 593.⁶⁵ However, the ATO subsequently advised the ANAO and AGD that the number of cases and the estimated value of losses were incorrectly reported. The estimated value of loss reported only covered closed GST fraud cases for the period. The ATO advised that total ATO-wide actual losses arising from closed fraud cases in 2001–02 was \$10 659 008.⁶⁶ This includes GST revenue of \$515 700. Revised 2001–02 data is to be submitted to AGD.

2.42 The ANAO found that, currently, the ATO has difficulty in providing an accurate estimate of its external fraud losses because the data being recorded in the FIRM system is not being appropriately updated. For example, the potential value of the fraud loss is estimated at the time the case is initially assessed and may change (increase/decrease) during the course of an investigation as more information becomes available. However, this value is not always being updated in the system to reflect the most current assessment of the fraud loss.⁶⁷ The ATO advised that this shortcoming has resulted in both the under, and over, reporting of fraud at a case level. The ATO further advised that it has instigated a system of manual checks to ensure that the losses to be reported for 2002–03 are correct.

⁶⁴ Attorney-General's Department, *Commonwealth Fraud Control Guidelines 2002*, May 2002, pp. 29–33.

⁶⁵ This value should have included all ATO fraud data.

⁶⁶ Revised statistics to AGD include actual losses for successful and unsuccessful prosecutions completed during the year and matters closed as a result of the CDPP deciding not to prosecute.

⁶⁷ Based on data extracted from the FIRM system, the ANAO found that the estimated potential value of losses relating to GST fraud cases *accepted* for investigation in 2001–02 was \$63 957 321. ATO Report No. MTH008 dated 18 December 2002.

It is currently in discussions with AGD to clarify the fraud data to be collected and reporting requirements.

2.43 The annual report to AGD is also to include monies recovered by ‘criminal prosecution, civil remedy, administrative remedy, and other’. The ATO’s report to AGD noted that the ‘overall total recovered’ for the ATO was \$138 600. The ATO advised that this figure did not include all recoveries for external fraud cases.⁶⁸ Currently, it is difficult for the ATO to capture this information, as the FIRM system does not record the fines and/or costs imposed by the courts, losses recovered or adjustments raised. For example, of the 43 cases reviewed by the ANAO during the audit, the ATO advised that \$6.4 million has been raised in adjustments and penalties. Of these, \$3.8 million has been collected to date.

2.44 The ATO has advised that it is reviewing the FIRM system business rules, the data captured, and reports produced to ensure that data collection and reporting obligations under the Fraud Control Guidelines are met. The ANAO considers that this review needs to be guided by the ATO’s overall approach to fraud to ensure that the data used to compile this report is accurate and complete, and reflects an ATO-wide perspective as well as the AGD’s requirements. The ATO considers that its new case management system,⁶⁹ which is to be implemented later this year, will address this issue in subsequent years.

Recommendation No.3

2.45 To ensure the data collection and reporting obligations required by the Commonwealth Fraud Control Guidelines are met, the ANAO recommends that the ATO review:

- (a) its data collection requirements; and
- (b) the integrity of the data to be included in its annual fraud report to the Attorney-General’s Department.

Agency response

2.46 Agreed. A new case management system scheduled for introduction in October 2003 is designed to improve our data collection and reporting capability. We are also engaged in discussions with the AGD to clarify reporting requirements.

⁶⁸ For example, one prosecution recovered \$515 000 alone.

⁶⁹ The ASISCaseManager system is to replace the FIRM system in late-2003. This system will be used by all ATO investigation areas.

Report to the Australian Federal Police

2.47 Agencies are also required under the Fraud Control Guidelines to advise the AFP annually of their current identified major fraud risks to assist the AFP in the provision of appropriate investigative services to agencies. Agencies can do this by providing the AFP either copies of their fraud risk assessments and fraud control plans or by entering into bilateral arrangements with the AFP for access to relevant information. In circumstances where agencies can investigate cases of serious or complex fraud without referral to the AFP, agencies are to advise the AFP of the details of the matters under investigation.

2.48 The ATO advised that there is regular liaison between the AFP and a number of areas of the ATO. Individual cases and emerging issues are discussed. The ATO advised the AFP of its major internal fraud risks in 2001, but no details of external risks or cases under investigation were provided. The FP&C Section advised, in April 2003, that it is coordinating an agency-wide report to the AFP outlining its major identified fraud risks and details of its serious or complex fraud cases.

Report to the States and Territories

2.49 Following the announcement of *A New Tax System* package in 1999, the Intergovernmental Agreement on the Reform of Commonwealth-State Financial Relations was revised. The States and Territories agreed to compensate the Commonwealth for the costs incurred by the ATO in administering the GST. The Agreement states that accountability and performance arrangements would be established between the ATO and the State and Territory Governments, consistent with Appendix F to the Agreement.⁷⁰

2.50 The agreement provides for a performance measure of compliance, but does not include any specific reference to fraud.⁷¹ The only Key Outcome that would have any direct impact on fraud matters is 'Compliance Maintained'. The ATO has undertaken the Taxpayer Compliance Measurement Program (TCMP) to meet its commitment, as part of the Performance Agreement, to examine a random sample of taxpayers to determine the level of compliance (and non-compliance) with GST obligations.

⁷⁰ GST Administration Performance Agreement—*Guiding Principles*.

⁷¹ Schedule A of the *Interim GST Administration Performance Agreement* contains the Key Outcome Performance Measures.

2.51 As part of the TCMP, two projects have been undertaken to measure administrative capability⁷² and technical compliance.⁷³ The ATO advised that no attempt has been made to measure the tax gap⁷⁴ because only the GST registered population was examined. In the most recent report to the States and Territories, the TCMP was not reported on as the data was still being analysed. At the time of preparing this report, the ATO advised that a report on the results of the TCMP was being prepared for the Commissioner.

2.52 The bi-annual report to the States and Territories included details of the number of GST fraud cases under investigation, referred to the CDPP for prosecution and finalised. As part of good governance, the ANAO suggests that it would be beneficial to advise the States and Territories of the fraud control arrangements in place for the GST.

⁷² This activity was to examine the administrative compliance obligations (lodgement, payment of liability, record keeping, internal controls, classification of supplies and included limited 'end-to-end' transaction testing). Random sample of 1158 entities selected—proportional to spread of population.

⁷³ This activity looked at whether legislative requirements necessary to correctly report GST liability were applied. Random sample of 261 entities selected across all States and Territories.

⁷⁴ The tax gap is defined as the difference between what is believed to be owed and what actually is collected.

3. GST Fraud Prevention Strategies

This chapter reviews the ATO's GST fraud prevention strategies. The ATO's fraud awareness, education and compliance programs are discussed.

Introduction

3.1 The ATO's fraud prevention strategies should seek to minimise potential revenue loss to the Commonwealth and to maintain the community's confidence in its administration of Australia's taxation system. In assessing the effectiveness of the ATO's GST fraud prevention strategies, the ANAO examined whether the ATO had:

- communicated to its staff the standards of conduct and ethics expected and provided fraud awareness and technical training to GST Business Line staff;
- communicated to business and the community their legislative requirements under the new tax system, their responsibilities in meeting those requirements and the consequences of acting fraudulently; and
- established intervention strategies and compliance programs.

Integrity and fraud awareness training within the ATO

3.2 The Fraud Control Guidelines make CEOs accountable for fraud control within their agency. They are also responsible, under the provisions of the FMA Act, for promoting efficient, effective and ethical use of Commonwealth resources. This includes fostering and maintaining the highest standards of ethical behavior and compliance with the *Guidelines on Official Conduct for Commonwealth Public Servants* and the *Public Service Act 1999—APS Values and APS Code of Conduct*.⁷⁵

3.3 The Fraud Control Guidelines suggest that fraud awareness training should be provided to ensure staff have an understanding of fraud control issues. Training should be ongoing, address both internal and external fraud and encompass organisational and APS values, officer conduct and ethics.

Fraud awareness and ethics training for ATO staff

3.4 The FP&C Section is responsible for conducting internal fraud awareness training, promoting ethical conduct and undertaking internal fraud

⁷⁵ Attorney-General's Department, *Commonwealth Fraud Control Guidelines*, May 2002, pp. 5–6.

investigations.⁷⁶ The FP&C Section has developed two interactive fraud and ethics training programs, *Judge for Yourself* and *Play It Again Sam* and an on-line self-paced learning package covering security, fraud, ethics, privacy and information security. These are competency-based and all staff must complete the learning package within four weeks of commencing with the ATO. The training programs are regularly reviewed to ensure they remain current. The use of log-on screen messages also reinforces officers' responsibilities in relation to fraud.⁷⁷

3.5 The ANAO found that the training programs are comprehensive. They outline legislative requirements, expectations of behaviour, give examples and exercises and provide details on where information relating to integrity and fraud may be located.

External fraud awareness training for GST staff

3.6 Fraud Investigations is responsible for providing GST external fraud awareness training. A standardised fraud awareness package was developed and implemented nationally from early 2000.⁷⁸ The course is interactive, includes practical exercises and aims to increase officers' awareness of taxpayer fraud and their responsibilities if potential fraud is detected. The ATO advised that, although the course has not been formally evaluated, its content has been reviewed to ensure that it remains up to date.

3.7 The ANAO found that the course has been delivered across the GST Business Line. However, the number of presentations and ATO officers participating in these presentations is not known because Fraud Investigations does not record this information. The ANAO considers that maintaining a training register to record courses presented in each region, staff participation rates and the business lines involved, would provide essential information when evaluating training activities. The ATO advised that the need to maintain this information, and what data is to be collected, are being considered.

Targeted fraud awareness project

3.8 Fraud Investigations also undertook a national GST fraud awareness project to address identified process weaknesses in the GST control environment. The project resulted in a customised fraud awareness program for the

⁷⁶ Where cases of internal fraud are substantiated, these are referred to the AFP for investigation.

⁷⁷ The FP&C Section has developed 15 log-on screen messages that are rotated on a regular basis. These screen messages are displayed on boot-up and/or log-on to the ATO network.

⁷⁸ The training package includes some regional variations, for example, contact details.

Compliance Verification Centres (CVCs).⁷⁹ The ATO advised that this program was delivered to CVC officers from the South Australian/Northern Territory and Western Australian regions in early 2003. The intention is for the program to be delivered to all GST staff. The out-posting of Fraud Investigations' staff to the CVCs has also supported the program and established closer working relationships between the two areas.

Technical training for GST compliance staff

3.9 All GST Business Line staff participate in an intensive skilling program that focuses on training staff to undertake compliance related activities and assist businesses transitioning to the new tax system. To support the GST Business Line staff in their advisory and compliance roles, the ATO established the Portable Reference and Interactive System (PRISM). PRISM is the central repository for all policies, procedural documentation, templates and other GST-related information and can be accessed by all GST staff. The ANAO found that the information on PRISM is corporately maintained to ensure GST staff are using the latest tools, consistent verification and advisory products and methods and are aware of any changes to policy and procedures. The ANAO considers that, although the training for GST staff relates to their compliance activities, it underlies their capacity to prevent and detect GST fraud.

3.10 The ANAO found that the GST Business Line, supported by the FP&C Section and Fraud Investigations, has developed an effective training program that includes internal and external fraud awareness training. This provides officers with the necessary skills to detect fraudulent activity.

Community and business education and awareness

3.11 The introduction of the new tax system, including the GST, was supported by comprehensive communication and information campaigns facilitated and coordinated by ATO Relations. The aim of the campaigns was to provide well-targeted information to businesses and the community, so that taxpayers are aware of legislative requirements and can meet their new compliance obligations. These campaigns commenced in 1999 with information provided via multiple media channels. The ANAO found that the activities undertaken by the ATO have covered a broad spectrum, with seminars and field visits, direct mail outs to businesses and consumers, and information call centre services.

⁷⁹ The GST Compliance Verification Centres have primary responsibility for office-based initiatives focusing on the review and verification of information provided to the ATO (generally on the BAS) primarily through the use of telephone, fax and electronic media.

3.12 The ANAO considers the scope of the communication and education task undertaken by the ATO has been significant. For example, in 2000–01, the ATO responded to over 16 million telephone inquiries; it established a widely dispersed help and education field force to assist and educate clients; and conducted around 400 000 advisory visits. Activities also included pre-testing of advertising campaigns and ‘flagship’ products, such as the *GST Guide* and *Business Activity Instructions*. Between July and December 2001, it distributed 2.3 million GST-related publications.

3.13 Through market research, the ATO seeks to develop an understanding of taxpayers needs. This information is then used to refine and develop communication programs. The ANAO found that the focus of more recent information and communication programs has been on emerging issues. For example, empirical data analysis has identified common errors that people make in completing their activity statements and issues regarding lodgement by due dates. To address these concerns, the ATO has implemented a revised Activity Statements Communications Strategy.⁸⁰

3.14 The ANAO found that the ongoing evaluation of the effectiveness of the ATO’s communication and information programs has supported their further development. This research has been used to tailor programs to the specific needs of the ATO’s clients. ATO Relations continues to provide support to the GST Business Line. However, following the completion of the first two years of GST, related marketing and education activities have been scaled down with the increased focus on active compliance.

3.15 The ANAO considers that the ATO has invested significant resources to make its client population aware of its legislative requirements and responsibilities through a range of communication strategies. This ongoing education supports the ATO’s compliance activities and the philosophy underpinning its Compliance Model. Although these activities were not specifically related to fraud, the ANAO considers they play an important role in preventing fraudulent activity and assist in improving levels of compliance.

Working with industry and clients to improve compliance

3.16 The ATO views fraud as being an element of serious non-compliance and its efforts to prevent fraud are undertaken as part of its compliance strategies. Compliance activities provide the opportunity for the ATO to give ‘one-on-one’

⁸⁰ As part of this strategy, the ATO forwarded with activity statements for the September 2002 quarter, an *Activity Statement Update* that provides businesses with information about completing their activity statements, common errors to avoid, changes to taxation arrangements and where to get more information on issues that might affect their business.

support and training to clients when non-compliant practices are identified. Compliance activities may also highlight particular areas of concern or information gaps across industry sectors. Education strategies can then be developed to address these deficiencies.

New Business Service

3.17 The ATO has identified, from its own and overseas experience, that new businesses and/or GST registrants new-to-business are at risk of adopting non-compliant practices and fraudulent behaviour. To address this, the ATO established the New Business Service. The concept behind the New Business Service is 'compliance through education and assistance'.⁸¹ The Service is responsible for delivering a whole of ATO compliance strategy for the new business sector. Between June 2001 and April 2002, approximately 19 000 advisory visits were completed to clients across Australia. These visits can be either client requested⁸² or ATO initiated.⁸³

3.18 To obtain early quantitative data on the impact of these advisory visits on taxpayer compliance, an evaluation of ATO initiated visits on BAS lodgements and associated work items was completed in August 2002. The analysis identified that, for clients visited, BAS lodgements by the due dates were higher and that the number of verification/compliance work items generated was lower, than for the control group. The control group was a sample of new business clients that had not participated in the New Business Service project.

Industry partnerships

3.19 The ATO has established on-going relations with a wide range of industry sectors through the creation of 20 industry partnerships.⁸⁴ Through these partnerships, the ATO aims to inform industry about business tax reform and ensure that its strategies are meeting their education and information needs. The partnerships are a consultative forum where issues affecting industry are

⁸¹ The Service focuses on providing assistance to ensure new businesses understand their taxation obligation and have established the systems and processes to comply with these requirements.

⁸² For client requested visits the Commissioner's Guarantee applies. The Commissioner's Guarantee is an undertaking, provided in writing to ATO clients, that client requested advisory visits from the ATO are an educational initiative and any information gained will not be used for any other purpose. The Guarantee also states that the ATO will not take any action as a result of an advisory visit unless specifically requested by the client. The aim of the Guarantee is to encourage use of the ATO's Advisory Service by clients in order to help them understand and meet their obligations under A New Tax System.

⁸³ For ATO initiated visits, any information obtained during the visit can be disseminated to other areas of the ATO or used for other purposes.

⁸⁴ For details of industry partnerships see <<http://www.taxreform.ato.gov.au>>.

discussed and resolved.⁸⁵ The ANAO found that the aims of the individual partnerships varied, depending upon the knowledge, experience and specific tax reform issues affecting the industry. However, the partnerships have several common goals, including to:

- encourage, support and assist industry to understand and meet its GST obligations;
- be proactive in developing and maintaining communication networks;
- provide an efficient and effective procedure for industry seeking ATO determinations on the GST status of their products and services; and
- establish a successful industry alliance in a focussed and coordinated way.⁸⁶

3.20 The ANAO considers that the partnerships provide an opportunity for the ATO to assist the business community in resolving industry specific issues and to engage them in wider discussions. During the audit, the ANAO met with representatives from a number of industry partnerships. All expressed positive views about the effectiveness of the partnerships and the professionalism of the ATO in managing the process.

GST compliance program

3.21 A well-developed and structured GST compliance program that targets risks to compliance and revenue is important in maintaining the community's confidence in the new tax system. The ATO has implemented a highly visible GST compliance program with broad coverage across businesses that aims to:

- identify incorrectly calculated and/or avoided tax;
- provide assurance that the GST system is working as intended; and
- assess the effectiveness and targeting of education programs.⁸⁷

3.22 The *Compliance Program 2002-03* identified a number of high-risk areas of focus for the GST Business Line including fraudulent or incorrect claims for refunds and the cash economy. These areas will be addressed through a range of compliance strategies. As part of its overall approach to GST Compliance in 2002-03, the ATO plans to undertake 20 000 field visits relating specifically to the cash economy, and to conduct 50 000 advisory visits, mainly to new businesses.

⁸⁵ Examples of such issues include: the sale of a going concern, such as a taxi/licence where the seller or purchaser is not registered for GST; GST status of medical and related services; and GST implications of exports with regard to the mining and energy industries.

⁸⁶ Industries Partners at <<http://www.taxreform.ato.gov.au>>.

⁸⁷ Australian Taxation Office *Compliance Program 2002-03*, p. 22.

3.23 During 2001–02, the ATO reviewed more than 67 000 GST refunds resulting in 3000 adjustments, saving \$101 million in extra revenue; and verified 72 per cent of the value of all refunds being issued (\$17 billion). During the same period, the ATO audit program targeted nine per cent of GST-registered businesses resulting in adjustments of a net additional \$363 million in GST.⁸⁸

Structure of GST General Compliance

3.24 The ANAO found that the GST General Compliance program is based on the ongoing assessment of the GST compliance risks facing the ATO and forms part of an overarching compliance plan.⁸⁹ The GST General Compliance field officers implementing this program are a mobile workforce that interacts face-to-face with ATO clients or their agents. It is divided into three teams: General Compliance, Complex, and Serious Evasion. The work undertaken by each team is dependent on the level of complexity of the compliance activity. These officers use a number of compliance products when assessing clients including health of the system checks,⁹⁰ record keeping reviews,⁹¹ specific checks,⁹² and BAS reviews.⁹³

3.25 Complex matters, or cases with a higher probability of fraud, are referred to the Serious Evasion Teams for further investigation. Depending on the circumstances and available evidence, such matters may be referred for investigation as potential fraud cases. The Fraud Investigation Section Referral Procedures state that *all instances of serious fraud need to be referred to the Serious Non-Compliance Capability—Fraud Investigations*.⁹⁴ The procedures identify several categories of cases that must be referred, including those:

- that are particularly serious, blatant or involve persistent offenders;
- for which there is no effective means of ensuring compliance or no other appropriate sanctions; and

⁸⁸ Australian Taxation Office *Compliance Program 2002–03*, p. 22.

⁸⁹ Details of how compliance risks are assessed and the planning that underpins the Compliance Program are discussed in detail in Chapter Four *GST Fraud Detection Strategies*.

⁹⁰ The Health of the System (HOTS) check incorporates testing for record retention, internal controls, GST classification and transaction testing of a GST registrant. The purpose of the test is to provide some assurance that the client's record keeping and accounting systems will result in the correct figures being placed on the report document.

⁹¹ This procedure reviews the record keeping practices of a business to determine whether these practices are likely to lead a client to be able to complete an accurate BAS.

⁹² The specific check is applied to cases where one or two risks have been identified. It will assess the likely existence of other risks and is intended to be a real time review.

⁹³ BAS review incorporates tests to ensure all supplies and acquisitions are accurately recorded in the client's records.

⁹⁴ Serious Non Compliance Capability, *Fraud Investigation Unit Referral Procedures*, Section 6.

- involving significant/prevalent non-compliance practices, the use of false documents and/or multiple suspects.

Serious Evasion Teams

3.26 The Serious Evasion Teams are a relatively new initiative, with the first team being formally established in NSW in March 2001. There are now six teams in NSW with a staff complement of ten officers per team. Similar teams are currently being formed in the other regions. Cases investigated by the teams often involve:

- multiple entities (possibly with inter-entity transactions);
- multiple identities (maybe false or non-existent identities or false property holdings);
- aggressive tax planning practices; and
- non-compliant behaviour such as serial bankruptcies or abuse of legacy taxes.

3.27 Working jointly with other areas of the ATO and external agencies, such as Centrelink and the NSW Department of Fair Trading, the teams have been able to identify non-compliant behaviour, undertake compliance activity and raise corresponding adjustments. The ANAO found, for the period July to November 2002, the NSW teams made net GST adjustments of approximately \$69 million. The teams also referred 32 potential fraud cases to Fraud Investigations in 2001–02. These cases had a total quantifiable risk to revenue of \$8.6 million.

3.28 The ANAO found that the Serious Evasion Teams and Fraud Investigations have developed close working relationships to support the referral of suspected fraud matters. In NSW, the two areas meet fortnightly to discuss the status of cases referred and cases that may be referred. This helps both areas to get the best outcome for the ATO. Similar arrangements are being established in the other regions.

Compliance Verification Centres

3.29 The ATO has to balance the need to maintain the integrity and revenue of the GST system against minimising impacts on genuine and compliant taxpayers. The ATO instituted the telephone based Compliance Verification Centres (CVCs) as a means of quickly verifying large numbers of refund claims. Officers verify information provided by the taxpayer verbally or by requesting supporting documentary evidence of the claim. If further verification is required, the case will be referred to GST field staff. Where potential fraud is detected, it will be referred in accordance with the ATO's Fraud Referral Guidelines.

ATO business processes and system controls

3.30 The ATO included in the GST system a number of controls to prevent potential fraud. Key features of the system include:

- issuing the BAS to taxpayers based on their GST registered status and reporting period (monthly, quarterly or annually). These documents are coded with a unique Document Identification Number (DIN). The DIN is linked to the BAS, providing a high level of confidence that the BAS lodged relates to the GST registered business. Clients do not have the ability to access a blank generic BAS and submit a refund claim; and
- requiring businesses with an annual turnover of \$20 million or more to lodge their BAS electronically through the use of Public Key Infrastructure. This technology guarantees the privacy, security and authentication of the entity and transaction.

3.31 Also, as part of the tax reform initiatives, the ATO developed a suite of applications to process and monitor activity statements.⁹⁵ These applications contain embedded controls to identify potentially fraudulent activities during the processing of the BAS.

Appropriate use of GST adjustments and penalties

3.32 The ANAO was advised that the ATO does not generally impose a penalty on taxpayers who, inadvertently, have incorrectly calculated their GST resulting in an underpayment, or where the error is due to a genuine mistake or misunderstanding. Where a taxpayer has blatantly avoided the remittance of GST and/or collected or over-claimed input-tax credits, the ATO has the ability to impose both a penalty and general interest charge. These processes can be an effective deterrent in preventing non-compliant and fraudulent behaviour. In 2001–02, the ATO made adjustments of a net additional \$363 million in GST.

Media coverage of compliance activities

3.33 Publicising the efforts of the ATO in preventing fraud and non-compliance is an important part of the ATO's fraud prevention strategy. In its *Compliance Program 2002–03* published in December 2002 the ATO noted that, during 2001–02, there were five prosecutions for GST fraud and a further 38 cases referred to the CDPP. The ATO also publicised the successful prosecution of two high profile GST fraud cases involving in excess of \$500 000 each, where custodial sentences were imposed for both defendants.

⁹⁵ These applications include the Instalment Processing System, Pay-As-You-Go, Fringe Benefits Tax, Risk Rating Engine and Refunder.

Conclusion

3.34 Based on a high-level review of GST General Compliance, the ANAO considers that the ATO has well-structured compliance programs that, although not specifically directed at GST fraud, incorporate fraud prevention strategies, detection capabilities and enforcement policies. The emphasis on improving compliance is supported by the ongoing assessment of risks, early intervention strategies, targeted compliance activity, education programs and, where necessary, enforcement action.

3.35 Publicly stating its proposed compliance activity and providing details of cases where fraud has been detected and successfully prosecuted, engenders community confidence in Australia's taxation system and demonstrates the ATO's commitment to ensuring compliance. The ANAO considers that the compliance activities undertaken by GST General Compliance would be an integral part of the fraud prevention and detection strategies developed to support a GST Fraud Control Plan.

Integrity of Australian Business Number data

3.36 The ATO has identified that serious non-compliance and fraud relating to ABN/GST registration and integrity is increasing. This risk was reported to the GST Executive in August 2002 as the third highest risk category. This is based on the number of incidents identified and reported by GST General Compliance staff through its National Risk Network. To address this risk, the ATO has established quality assurance processes targeting both the ABN registration process and existing data holdings. This risk is also being addressed through the Registration Information Matching System (RIMS).

Registration Information Matching System

3.37 Following the introduction of the GST, the ATO implemented RIMS. The system has both a fraud prevention and detection capability. However, it is primarily targeted towards the prevention of fraud. RIMS uses data matching techniques to identify potentially fraudulent ABN registrations and amendments with an active GST role. RIMS checks new ABN/GST registrations against a reference list and other criteria. The system highlights high-risk applications that can then be referred to intelligence analysts for further analysis. A refund stopper⁹⁶ may also be placed on the ABN and related accounts, restricting any refund payments being made against this ABN. RIMS is discussed in more detail in Chapter 4.

⁹⁶ A refund stopper is placed on the taxpayer's file to stop the processing of any refund.

4. GST Fraud Detection Strategies

This chapter reviews the ATO's fraud control environment and fraud detection strategies.

Introduction

4.1 Effective fraud detection strategies protect an agency's integrity, assets and revenue. They also assist in identifying and prosecuting perpetrators of fraud. Robust system controls, supported by intelligence and targeted compliance activities, underpin effective fraud detection.

4.2 As part of its fraud detection capability, the ATO has developed the Risk Rating Engine (RRE) to assist in detecting potential fraud and non-compliance in a 'real-time environment'. The RRE risk profiles GST registrations at lodgement of the registration application and incoming activity statements of clients registered for the GST. This is prior to the issue of any refund. In addition to the RRE capability, Fraud Intelligence is responsible for detecting potential GST fraud. The compliance activities, refund assurance programs and risk identification projects undertaken by GST General Compliance may also detect potential GST fraud.

4.3 The ANAO sought to determine whether the ATO had established a control framework that would detect GST fraud. This review included:

- assessing key controls within the RRE system;
- reviewing the effectiveness of the RRE fraud and compliance tests;
- examining Fraud Intelligence's systems and processes for detecting GST fraud and identifying fraud risks; and
- reviewing GST General Compliance's strategies and processes for detecting serious non-compliance, which may include fraud. The ANAO did not audit the GST compliance programs.

Risk Rating Engine

4.4 Within the RRE, the risk profile of a taxpayer consists of the results of calculated risk characteristic scores and exception tests. A calculated risk score is the comparative level of risk that a taxpayer represents in a specific risk area.⁹⁷ Each risk area is made up of a number of risk characteristics. These characteristics are multiplied by their associated magnitude rating to determine a risk score. Exception tests measure the risk of fraud or non-compliance based on either a

⁹⁷ Currently there are five compliance risk areas and three fraud risk areas.

single criterion or multiple criteria, with the fraud tests being given higher priority.

4.5 The RRE process identifies potential risks and assesses the risk characteristics and exception tests against a threshold value. A threshold value has been set in the risk areas for each risk characteristic. Where the threshold is exceeded, a workflow item⁹⁸ (or case) is generated in the Automated Work Allocation (AWA) System for the business area to review. A stopper may also be placed on the taxpayer's file to ensure a refund is not issued until the work item has been assessed.⁹⁹ Fraud work items are actioned by Fraud Intelligence and compliance-related works items are referred to the CVCs. During 2001–02, the RRE generated 67 000 compliance and fraud work items resulting in 3000 adjustments, saving \$101 million in extra revenue. Appendix 1 provides an overview of how the RRE system operates.

Original intent of the RRE

4.6 The RRE was originally designed as the main mechanism for risk rating and selecting cases for the GST compliance program. Risk cases were to be automatically generated by the RRE and reviewed by GST compliance operatives. Prior to the implementation of the GST, the GST Business Line conducted analysis to:

- assess the estimated number of work items that would be generated by the RRE;
- determine if available resources could action the work items within a reasonable period of time; and
- establish any negative impacts the RRE might have on the Instalment Processing System (IPS) processes, particularly the timely processing of activity statement refunds.

4.7 The GST Executive agreed to make a number of changes to the RRE in May 2000. A critical policy decision was made to reduce the potentially unmanageable number of RRE stopper work items created. It was also intended to reduce any adverse impact on IPS processes and the timeliness of activity statement refund processing. The change in policy was translated into new

⁹⁸ The system will generate a workflow item for the highest risk identified. Results of the other tests that have also created a work item are attached to this work item.

⁹⁹ A stopper is placed on a work item when there is a direct risk to revenue, for example, the payment of a GST refund. Non-stopper work items relate to either GST registrations or clients who have a debit situation with the ATO. That is, the client is required to remit to the ATO GST charged and collected on the provision of goods or services. Non-stopper work items are generally created as a result of risk profiling in the RRE as opposed to the activity statement failing one or more of the RRE fraud exception tests.

specifications, which essentially created a ‘stopper work item’ for activity statements with a refund over a particular dollar value. Following a number of incorrect refunds being issued, further changes were implemented in September 2000 to ensure a larger proportion of the refund population was reviewed and to impose additional controls in IPS.

Suspension of RRE compliance tests and characteristics

4.8 During the initial implementation period of the RRE, the original RRE risk tests and characteristics were evaluated. As a result, the GST Compliance Executive supported recommendations to suspend a number of compliance risk characteristic tests and exception tests because of invalid and/or insufficient data. These decisions were implemented with effect from October 2000. Of the 22 risk characteristic tests, 10 have been suspended.¹⁰⁰ Of the 10 exception tests, seven tests have been suspended; three tests relating to refunds are active.

Impact of suspension of RRE compliance tests and characteristics

4.9 Due to the restricted nature of the RRE tests, a project was undertaken by the GST Strategic Risk Management (SRM) Unit to:

- replicate some RRE risk tests in a data warehouse environment; and
- provide an alternative means of selecting cases for the GST compliance program.

4.10 A complementary risk rating capability, that operates in a post-issue environment, has been developed and supports what the ATO considers to be a more flexible basis of assessing, rating and selecting compliance risk cases. The post-issue work undertaken by the SRM Unit is discussed later in this chapter.

Impact on fraud risk profiling

4.11 There are 17 exception tests that have the potential to generate a fraud related work item. Of these, five tests have been suspended because of known deficiencies in the values used.¹⁰¹ Of the 14 risk characteristic tests, one has been suspended.

4.12 Although the fraud risk areas and characteristics are active, each of the risk area¹⁰² thresholds is currently set at 99 per cent. This means that only those

¹⁰⁰ The remaining 12 tests address four of the eight risk areas, three relate to compliance and one to registrations. The Australian Taxation Office, Risk Rating Engine Business Issues Post TR4.0, *Fine Tune Risk Rating Engine Through Analysis and Review of the Risk Profiling Process*, June 2002, p. 12.

¹⁰¹ Australian Taxation Office, *High Level Business Analysis of the Risk Rating Engine (RRE)*, February 2002, p. 3.

¹⁰² There are three fraud risk areas.

taxpayers with a risk score of 99 per cent or above will be flagged for review. The rationale for increasing these thresholds is that the system was generating an unmanageable number of work items because of known deficiencies in the make-up of some characteristics. The ATO advised that lowering the threshold could potentially result in three times the current number of work items being generated, causing significant delays in the time taken to process work items and related refunds.¹⁰³

Release management process

4.13 The ATO controls all changes to its key production business applications, such as the RRE, through project management committees, which oversee the selection and testing of the changes through a scheduled release program. There have been several updates to the RRE controlled through the ATO's Tax Release management projects.¹⁰⁴

4.14 The ANAO reviews the management controls that underpin the release management process as part of the annual financial statement audit process. Specific update testing was undertaken for the RRE related changes in the TR 3.1 (November 2001) and TR 4.0 (July 2002) releases. The ANAO concluded that there were appropriate controls over the approval, testing and subsequent release into production of the RRE changes implemented as part of those releases.

Online changes by system administrators

4.15 Online changes to the RRE risk characteristics and thresholds can be made outside the ATO's formal release management process. These changes are implemented by the Business Function Area Administrator¹⁰⁵ through a change request approved by GST Business Systems and Technology. The ANAO notes that, in some instances, details relating to these changes were not recorded in the change register.¹⁰⁶ In July 2002, a management oversight committee was established. The RRE Change Management Committee¹⁰⁷ now approves all changes to the RRE and these are recorded in the change register.

¹⁰³ Australian Taxation Office, *High Level Business Analysis of the Risk Rating Engine (RRE)*, February 2002, p. 38.

¹⁰⁴ Key implementation dates for the RRE since July 2000 are: TR 2.0 (July 2000); TR 2.1 (Nov 2000); TR 3.0 (July 2001); TR 3.1 (Nov 2001); and TR 4.0 (July 2002).

¹⁰⁵ The Administrator can only adjust thresholds relevant to their own business tests.

¹⁰⁶ An Excel spreadsheet is used to record online system changes.

¹⁰⁷ The RRE Change Management Committee was established in July 2002 and is made up of the three Deputy Commissioners from the Small Business Line, GST Business Line, and ATO Operations.

Review of RRE by GST Business Systems and Technology

4.16 The ATO has undertaken a number of reviews of the RRE. The reviews noted that the majority of suspended tests have never been operational, potentially restricting the risk profiling process. The main reason that the tests have remained suspended for so long has been the lack of analytical support to overcome the reasons for their initial suspension. This has also prevented the refinement of existing tests and the advancement of new tests to ensure that the risk profiling process is relevant to the existing ATO environment.¹⁰⁸ Modifications to the system to improve the identification of non-compliance and targeting of verification and compliance activity were also recommended.

4.17 In response to these reviews, the GST Executive has directed the SRM Unit to undertake a holistic and ongoing review of the RRE GST compliance business rules.¹⁰⁹ The RRE project involves a comprehensive analysis and testing of the business rules and magnitudes on activity statement processing and refund integrity using historical data.

System testing of RRE by ANAO

4.18 The ANAO undertook a review of the RRE data model and identified key data fields, which could be tested through analysis. Data queries were developed in consultation with the ATO and run in the ATO's data warehouse environment. The analysis identified the following outcomes:

- Although 15 exception tests in the RRE are active, outputs from the RRE are heavily focused towards two tests: one compliance test and one fraud test. For the months of June and July 2002, 86 per cent and 87 per cent respectively of work items created during the period resulted from a BAS failing either one of the two tests.
- For the period June to July 2002, 21 029 work items were generated. By 11 March 2003, 56 per cent of these work items had been finalised, 43.5 per cent were still open and 0.5 per cent had been deleted from the system. The ATO advised in May 2003 that the majority of these are non-stopper cases (i.e. low priority cases) and the remainder have been referred to GST field for further assessment. Of the 56 per cent finalised, 92 per cent were completed within 30 days.¹¹⁰

¹⁰⁸ Australian Taxation Office, Risk Rating Engine Business Issues Post TR4.0, *Fine Tune Risk Rating Engine Through Analysis and Review of the Risk Profiling Process*, June 2002, p. 35.

¹⁰⁹ Australian Taxation Office, *GST SRM Business Plan for GST Compliance Tests in the Risk Rating Engine (RRE)*, August 2002, p. 3.

¹¹⁰ The test was to provide an indication of the work item clearance rate. The work items are a combination of fraud and compliance.

- There have been 12 419 instances (all relating to the period May—July 2000)¹¹¹ where the RRE flagged a BAS for review and no work item was created in the AWA system. The ATO advised that work items were created from ABN registrations with a view to undertaking advisory visits to clients registering for the GST. However, when it was decided not to undertake these visits unless requested by the client, the work items were bulk deleted in the AWA system.

4.19 The ANAO considers that the level of thresholds set within the RRE risk areas, in combination with the number of suspended risk characteristics and exception tests, could negate the effectiveness of the RRE. The thresholds being set for the exception tests and in the risk areas for each risk characteristic test could minimise the number of work items created. The ATO advised that thresholds are set to provide the right balance of work items, given the need to protect the integrity of the system, provide legitimate refunds in a timely manner and deal with high-risk refunds.

Conclusion

4.20 Fraudulent or incorrect claims for refunds are a major risk for the GST system. The ANAO recognises that the RRE is not the only tool used by the ATO to detect fraudulent activity and that there has been a move away from the original intent of the RRE. However, it remains the only system capable of risk profiling activity statements at the time of processing and prior to the issue of any refund. The ATO has identified a number of areas within the RRE that need to be further developed and refined if it is to be a fully effective tool for detecting non-compliant and fraudulent behaviour and filtering out potentially correct and genuine refunds. These areas are subject to continual review.

Evaluation of RRE fraud tests

4.21 Fraud Intelligence, as the business owner of the RRE fraud tests, has evaluated these tests to determine if they are consistent with the original business requirements. The ANAO found the evaluation of the tests to be generally comprehensive. However, there was limited documentation to support the testing process. As well, no evaluation report was prepared for ATO management.

4.22 Two national operations have also focused on evaluating the work items generated by the RRE fraud tests: Operation Kaiser and Operation Berry. The ATO advised that, to date, no changes have been made to the RRE fraud tests as

¹¹¹ The RRE was used from May 2000 to assess ABN and GST registrations.

a result of these national operations. However, they are being considered as part of the current review of the RRE.

Operation Kaiser

4.23 In February 2002, the GST Compliance Executive was concerned that RRE fraud work items, which did not become fraud cases, were being overlooked as potential compliance risk cases. As a consequence, in April 2002, the SRM Unit initiated, in conjunction with Fraud Intelligence, a national project to refer the fraud 'no further action' work items to the SRM Unit for review. The project also sought to determine the usefulness of the RRE fraud tests from a GST compliance perspective.¹¹²

4.24 The operation focused on assessing clients who had failed RRE fraud refund tests but who had not been previously subject to compliance activity. Between April and September 2002, a sample of 932 cases was reviewed and profiled by the SRM Unit. Of these cases, 175 were referred to the CVCs or GST field for further verification. Of the 73 cases finalised, adjustments have been made to 23 refunds to the value of \$857 509 with \$851 344 being in the ATO's favour. Most adjustments resulted from inadvertent error. One case of potential fraud with a value of \$198 705 was identified.¹¹³

4.25 The project recommended modifications to the RRE fraud tests, because the tests examined were not focused enough and frequently triggered bona-fide businesses. This project formed the basis for the ongoing referral of fraud work items to the GST Business Line as part of its Refund Assurance Program, discussed later in the chapter.

GST Registrations (Operation Berry)

4.26 As at 31 December 2002, the ATO had on hand 74 344 non-stopper fraud work items.¹¹⁴ The majority related to ABN/GST registrations.¹¹⁵ These work items are considered to be low risk but records are maintained for possible future verification. Fraud Intelligence advised that sample testing of this population had been undertaken. It was found that the fraud test triggers for ABN registration are not identifying potential fraud.

¹¹² GST Strategic Risk Management, *Operation Kaiser SRM Input into the Review of Fraud Tests in the RRE*, printed November 2002, p. 3.

¹¹³ GST Strategic Risk Management, *Operation Kaiser Update*, 7 February 2002, p. 3.

¹¹⁴ Non-stopper work items are generally created as a result of risk profiling in the RRE as opposed to the activity statement failing one or more of the RRE fraud exception tests.

¹¹⁵ For example, in the November 2002 Report to the GST Business Forum noted there were 72 737 non stopper work items with 68 905 relating to ABN registrations.

4.27 Fraud Intelligence, in conjunction with the New Business Service, initiated Operation Berry to evaluate fraud exception tests relating to GST registrations. Its purpose was to review clients who previously held an income tax registration, but had a status of no further income tax returns necessary and had recently registered for an ABN. GST field staff reviewed and finalised 405 cases. The sample largely consisted of cases that did not require further assessment as potential fraud cases.¹¹⁶ The project recommended a more targeted case selection process because of the low level of fraud referrals generated. Although the cases were selected on the basis that they had triggered an RRE fraud exception registration test, only six cases (1.5 per cent) were referred to Fraud Intelligence for further assessment as potential fraud cases.¹¹⁷

RRE as a fraud referral source

4.28 To assess the RRE fraud tests as an indicator of potential fraud, the ANAO analysed the referral sources of GST fraud cases between July 2000 and November 2002. Of the 412 potential GST fraud cases registered on the FIRM system, only 1.9 per cent of registrations identified the RRE as the referral source. Referrals from GST field staff and the CVCs accounted for 39 and 14 per cent of cases respectively. The ANAO recognises that the referrals from the CVCs and GST field staff would, in all probability, have originated from work items generated by the RRE. In the sample cases examined by the ANAO, the RRE was not identified as the referral source for any cases.

Conclusion

4.29 The systematic and comprehensive analysis of historical data, supported by the evaluation of fraud investigations and intelligence assessments, would allow Fraud Intelligence to determine whether the RRE fraud risk characteristics and exception tests are effective in detecting GST fraud. The SRM Unit is undertaking this type of analysis for the RRE compliance tests. The ANAO suggests that Fraud Intelligence draw on this expertise to evaluate the effectiveness and relevance of the fraud business rules and tests. This would also ensure alignment between current business requirements and the functionality of the RRE.

¹¹⁶ *Operation Berry Pilot Status Report*, 2 August 2002, p. 4.

¹¹⁷ *Operation Berry Pilot Status Report*, 2 August 2002, p. 7.

Recommendation No.4

4.30 To improve the effectiveness of the Risk Rating Engine fraud tests and business rules, the ANAO recommends that Fraud Intelligence continue to evaluate the tests and include the analysis of historical data, supported by the evaluation of fraud investigations and intelligence assessments.

Agency response

4.31 Agreed.

Fraud Intelligence detection capabilities

4.32 The ANAO examined Fraud Intelligence's systems and processes for detecting GST fraud and identifying fraud risks. Fraud Intelligence is responsible for:

- assessing operational referrals relating to suspect fraud matters received from internal and external sources;
- data-matching ABN/GST registrations using the Registration Information Matching System (RIMS); and
- completing fraud intelligence assessments and strategic risk assessments.

Assessment of fraud work items

4.33 Fraud Intelligence is responsible for reviewing fraud work items generated by the RRE. Work items are based on the nature of the tests triggered and the size of the risk score, not the potential monetary value of the refund. A senior project officer is responsible for undertaking a preliminary review of all RRE fraud work items. This review involves assessing the work items and other ATO systems from a whole of client perspective.

4.34 Cases may be considered to warrant no further action from a fraud perspective or, if fraud is suspected, the case is referred to a fraud intelligence analyst for further review. Following a more detailed review by the analyst, the work item may be registered as a potential fraud case and referred to Fraud Investigations, referred to the CVCs for further verification or completed as no further action. The refund stopper is maintained until the case is finalised. Table 1 outlines the work items received and actioned for the period July 2000 to December 2002.

Table 1**Number of fraud related work items for period July 2000 to December 2002**

Period	Fraud Stopper Work Items				Fraud Non-Stopper Work Items			
	Created	Completed	On Hand	Referred to Intell. Analyst	Created	Completed	On Hand	Referred to Intell. Analyst
2000–01	9 147	9 144	3	1 923	23 768	22 251	1 517	2 773
2001–02	12 480	12 472	8	1 281	47 493	4 306	43 187	10
Jul–Dec 2002	8 227	8 217	10	37	29 740	100	29 640	0
Total	29 854	29 833	21	3 241	101 001	26 657	74 344	2 783

Source: Australian Taxation Office

4.35 The ATO advised that the significant reduction in the number of work items referred to intelligence analysts in 2002–03 is due to the ongoing refund assurance work of Operation Kaiser. From December 2002, fraud work items that involve refunds over a particular threshold and refunds relating to new businesses with no previous tax history are forwarded to the CVCs for verification. The refund stopper is maintained pending advice from the CVCs.

4.36 The ANAO found that, given the number of work items and that only one officer undertook the initial assessment of these work items, the quality of initial assessments could have been compromised. During the audit, the ATO advised that, following the recruitment of additional intelligence analysts; the resources to deal with RRE work items have been increased.

Operational Referrals

4.37 Fraud Intelligence is the central repository for fraud referrals from internal and external sources. Referrals are analysed to identify potential fraud and to determine if further investigation is warranted by Fraud Investigations. If the information is not fraud-related, but rather a compliance issue, the information is passed to the relevant business line. The processes involved in assessing fraud referrals are discussed in more detail in Chapter 5.

Registration Information Matching System

4.38 Since July 2000, 7.9 million new ABN registrations and amendments have been processed through RIMS. The system flagged 21 397 (0.27 per cent) of these for further review. Following a cursory assessment and prioritisation by the RIMS project officer, the matches may be considered to either warrant no further action, be referred to an intelligence analyst for further examination or retained for further assessment. Table 2 outlines the RIMS matches and action taken for the period July 2000 to December 2002.

Table 2**Number of RIMS matches for period July 2000 to December 2002**

Period	Registration downloads	RIMS matches	Matches cleared ⁽¹⁾	Referred to intelligence analyst ⁽²⁾	Matches on hand pending further assessment ⁽³⁾
2000–2001	2 827 248	1 906	540	566	800
2001–2002	2 188 417	12 931	8 303	2 754	1 874
June 2002 to December 2002	2 885 830	6 560	5 133	512	915
Total	7 901 495	21 397	13 976	3 832	3 589

Source: Australian Taxation Office

Note 1: These are matches identified but examination has not identified any suspect behaviour.

Note 2: These matches generally relate to entities already under analysis or investigation.

Note 3: This is a cumulative work bank on hand for the year.

4.39 The RIMS project officer also data matches requests for information and operational referrals against the RIMS data and reference list. The ATO advised that the number of operational referrals and/or requests for information processed through RIMS ranges from approximately 120 to 180 per month.

4.40 Given the volume of work and that only one officer has been responsible for assessing all RIMS matches, requests for information and operational referrals, the ANAO considers the level of completeness and quality of the assessments undertaken could have been compromised. The number of outstanding matches awaiting assessment also suggests that the RIMS capability may not have been fully utilised, inhibiting the ATO's ability to respond to potential fraud in a timely manner. The ATO advised during the audit that additional analysts have been employed to work with the RIMS project officer.

Unrealised potential of RIMS

4.41 Data matching fraud investigations with RIMS data allows related entities and additional links to other data sources to be identified. Historically, not all fraud cases under investigation have been data matched against RIMS. These cases were generally those that have been referred directly to Fraud Investigations. Details from completed fraud cases can also be added to the reference list to monitor the future activities of the individuals/entities concerned. However, the ANAO found no evidence that this information is being provided by Fraud Investigations or any processes developed by Fraud Intelligence to monitor and evaluate these cases on a regular basis. The ANAO recognises that not all fraud cases will need to be monitored and that the focus should be on the more serious or complex cases.

Recommendation No.5

4.42 To ensure that the Registration Information Matching System (RIMS) is being used to its maximum potential to prevent and detect GST fraud, the ANAO recommends that:

- (a) all potential and existing fraud cases are matched against RIMS data and reference list; and
- (b) details from appropriate completed fraud cases are added to the RIMS reference list for ongoing monitoring and review.

Agency response

4.43 Agreed. This already occurs in most cases, but it is acknowledged that a universal application would strengthen the overall risk management approach.

Identifying GST fraud risks

4.44 Risks are intuitively identified by intelligence analysts through the assessment of operational referrals and requests for information. If a matter relates to a potential system weakness or appears to warrant further review, the analysts can undertake a more detailed review or data mining exercise of ATO and external systems, to identify whether the modus operandi for the potential fraud is being duplicated.

4.45 Significant potential risks and/or issues are escalated through the team leaders to the Manager, Fraud Intelligence and SNCC Executive. These matters are also reported to the other business lines through the distribution of a weekly Fraud Intelligence *Significant Issues Report*. This information is passed to the Strategic Assessment area, which is responsible for recording the risk and assigning a risk rating. The ATO advised that by year-end 2002, 48 risks had been identified and rated in accordance with the *ATO Risk Management Process Guidelines*.¹¹⁸ Thirty risks related to GST fraud.

4.46 The Strategic Assessment area was formed in 2001 to establish a fraud strategic intelligence and risk capability. This area is responsible for undertaking strategic assessments¹¹⁹ of identified risks. Such assessments may result in, and/or support, the conduct of national fraud operations. The ANAO noted that only one strategic assessment has been completed. This related to a non-GST matter. The ATO advised that, because of the prioritisation of resources within Fraud Intelligence, this area has not always been fully functional. As a

¹¹⁸ Risks are categorised as severe, high, major, significant, moderate, low or trivial.

¹¹⁹ Strategic assessments involve researching the scope of possible risks, methods of operation and recommending treatment strategies.

consequence, the ATO currently does not have a strategic fraud intelligence capability to support the effective targeting of fraud detection strategies and/or the development of fraud risk treatments. However, the ATO advised that this would be addressed following the recruitment of additional intelligence analysts and reallocation of resources within Fraud Intelligence.

Fraud risk operations

4.47 To initiate a national operation a brief is prepared for the SNCC Executive. If approved, a project manager is assigned, generally from Fraud Investigations. The project manager has overall responsibility for the operation, including developing an operation plan, negotiating resources, and monitoring and reporting on its status. One successful operation resulted in 26 referrals to Fraud Intelligence, with 15 cases under investigation, and approximately \$20.7 million in BAS adjustments.¹²⁰

4.48 Although the ATO advised that the SNCC Executive approves and monitors the status of these operations, the ANAO found no documentation to support consideration of proposals by the SNCC Executive and only limited progress reporting on some operations. The operations may involve staff from Fraud Intelligence, Fraud Investigations and other business lines, in particular GST field staff. Access to staff has to be negotiated on an operation-by-operation basis. The ATO advised that the lack of resources has hindered the progress of some operations.

4.49 The ANAO considers that, in order to address GST fraud risks in a more systematic manner and successfully achieve the outcomes of national operations, the SNCC Executive should take a more active oversight role and improve the management, resourcing, monitoring and reporting of these operations. The ATO advised in May 2003 that it intends reviewing all matters nominated as national operations.

GST General Compliance detection capabilities

4.50 Whilst the ANAO did not audit GST General Compliance's strategies and processes, the ANAO undertook a high-level review of its compliance programs, as they can be instrumental in detecting potential GST fraud.

4.51 The ANAO found that a well-developed operational risk management process, overseen by the SRM Unit, underpins the GST compliance program. The elements of this program that may detect serious non-compliance, including potential fraud are:

¹²⁰ Serious Non-Compliance Capability Executive Briefing Note, *Operation Cicada*, October 2002, pp. 1–2.

- GST compliance work items generated by the RRE;
- project-based compliance activity; and
- the refund assurance program.

Compliance work items generated by the RRE

4.52 Compliance work items generated by the RRE are forwarded to the CVCs for initial verification and, if further investigation is warranted, cases are referred to the GST field staff. If potential fraud is detected, cases are referred to Fraud Intelligence and/or Fraud Investigations. Following an internal review of activity statement processing, discussed later in this chapter, it was recommended that CVC procedures be reviewed and a quality assurance review of CVC refund/credit activities be undertaken. The ATO advised that these recommendations have been implemented.

Project-based compliance activity

4.53 The ANAO found that the SRM Unit oversees the end-to-end processes for identifying, quantifying and mitigating GST compliance risks. This work is generally undertaken through project-based compliance activity such as RQPs and national compliance projects. Projects are managed by a national project manager, with cases selected by the SRM Unit. The CVCs and field staff undertake the associated verification and/or compliance work. Compliance results are analysed to aid in developing treatment strategies and the targeting of future compliance activities.

Refund assurance program

4.54 The SRM Unit, in conjunction with Fraud Intelligence, has put in place a refund assurance program to assess at-risk refunds. A major area of concern is that refunds triggering a RRE fraud test may be released to the client without verification. The ANAO found that, since April 2002, Fraud Intelligence has been forwarding to the SRM Unit, on a weekly basis, a list of cases involving refunds between specific thresholds that require no further action from a fraud perspective. These cases are profiled by the GST Serious Evasion Teams post-issue of any refund.

4.55 Since December 2002, a list of fraud work items involving refunds over a particular threshold and refunds relating to new business compliance test cases is also forwarded, on a weekly basis, to the CVCs for verification. As at February

2003, of the 168 cases referred, 115 had been finalised, with four cases adjusted for a total ATO gain¹²¹ of \$703 123.¹²²

4.56 To evaluate the extent of the ATO's refund risk, the SRM Unit, CVCs and field staff are also analysing all refunds issued from July 2000. The ATO advised that the Refund Assurance Program is strengthening current systems through a combination of pre-issue assessment and post-issue evaluation.

Refund Integrity Project

4.57 Following a major overpayment in June 2002, an internal review of refund processing was undertaken and identified a number of weaknesses in the processing of activity statement refunds. The Refund Integrity Project was established in October 2002 to implement the recommendations of this review. The ATO also appointed a Refund Custodian. Specific areas involved in this review such as the RRE and its associated work items fell within the scope of this audit. Four recommendations from the Refund Integrity Review related to the RRE.

4.58 The ATO advised that three recommendations were implemented in July, August and September 2002 respectively. The remaining recommendation (review of RRE tests and operation) is to be implemented by 30 June 2003. An additional control pending full implementation of the project's recommendations is the work being undertaken by the SRM Unit and Fraud Intelligence as part of the ongoing Refund Assurance Program.

¹²¹ The reasons for the ATO Gain Adjustments were inadvertent error (three cases) and misunderstanding (one case).

¹²² GST Strategic Risk Management, *Operation Kaiser Update*, 7 February 2002, p. 5.

5. Investigating GST Fraud

This chapter discusses the ATO's systems and processes for investigating external GST fraud.

Introduction

5.1 Perpetrators of fraud have used false documentation and bogus business registrations in their attempts to defraud the GST system. Incorrect claims for refunds can also be a deliberate attempt to evade GST. Under the Fraud Control Guidelines, the ATO has the authority to investigate criminal matters; gather evidence; and prepare briefs of evidence for the CDPP.

5.2 The ANAO reviewed the ATO's case management framework for investigating external GST fraud. As part of this review, a sample of 43 investigations commenced between 2000–02 and 25 fraud referrals received by Fraud Intelligence during 2001–02 were assessed.¹²³ The ANAO did not review cases relating to GST internal fraud because all cases were still under investigation. The review placed particular emphasis on the following:

- case referral assessment by Fraud Intelligence;
- investigation process and preparation of prosecution briefs;
- quality review mechanisms;
- case evaluation and analysis; and
- debt management and recovery processes.

Role of Fraud Intelligence and Fraud Investigations

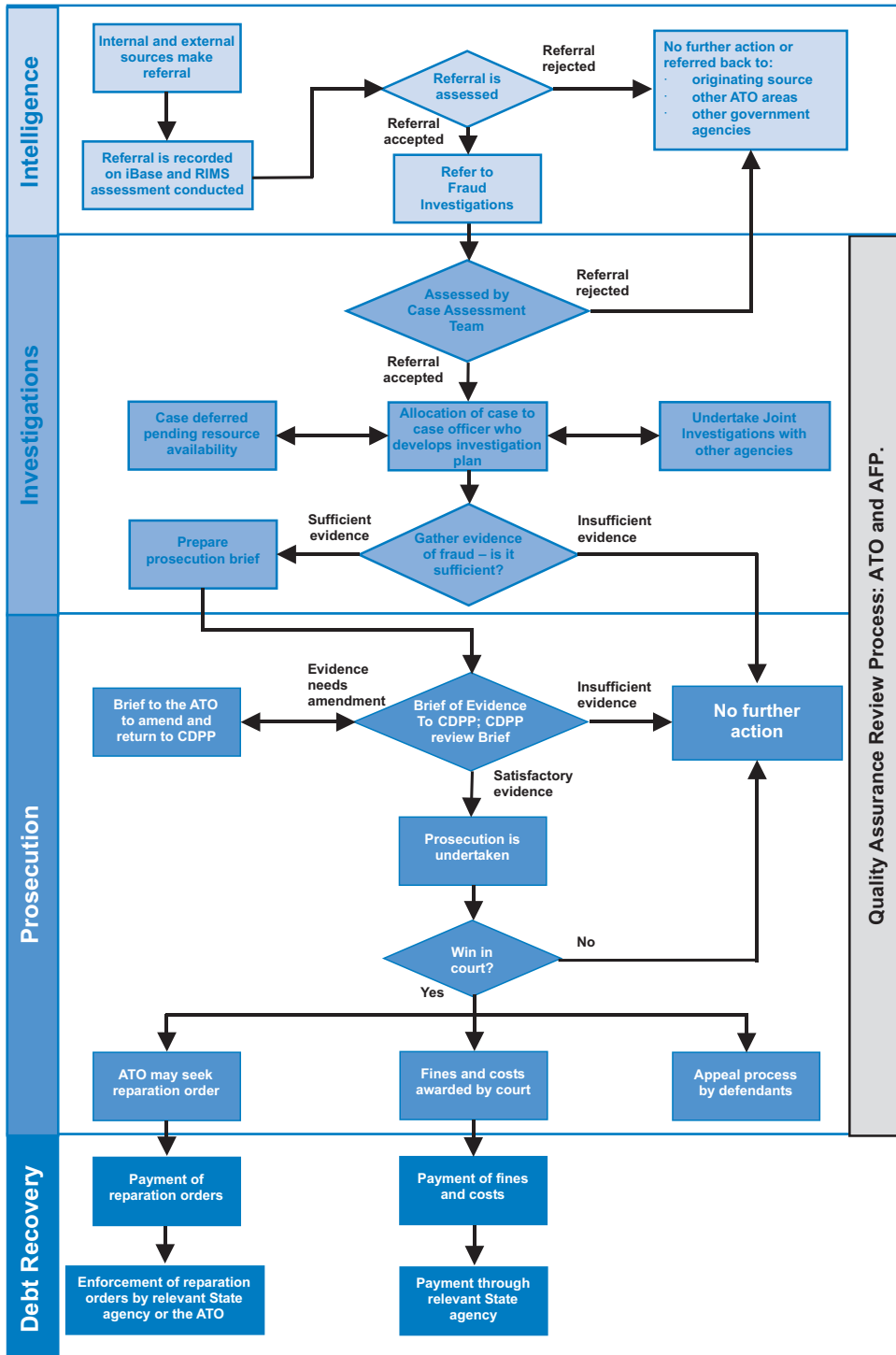
5.3 Fraud Intelligence and Fraud Investigations are part of the SNCC. Fraud Intelligence is responsible for assessing potential fraud referrals, providing fraud detection and intelligence analysis, and identifying fraud control issues to SNCC management.

5.4 Fraud Investigations, located in each of the major regions,¹²⁴ investigate GST and other taxation fraud. Investigations may be conducted jointly with the AFP, other law enforcement and/or other Commonwealth agencies. Figure 4 provides an overview of the investigation process, from the initial referral of a matter to Fraud Intelligence through to prosecution by the CDPP and case review.

¹²³ Of these 43 cases, 33 were completed and 10 have been referred to the CDPP for prosecution. Five involved the AFP. Of these five cases, one was completed, one has been prosecuted and is pending an appeal and three have been referred to the CDPP for prosecution.

¹²⁴ NSW/ACT and QLD are part of the North East region and SA/NT, WA, and VIC/TAS are part of the South West region.

Figure 4
GST fraud investigation process



Source: ANAO analysis of ATO data

Fraud referral assessment process

5.5 Fraud Intelligence assesses all potential GST fraud referrals received from internal and external sources.¹²⁵ Referrals are registered on an electronic document system (iBase) and a preliminary assessment is undertaken. If fraud is suspected, a more detailed intelligence assessment is completed prior to the referral being registered on the FIRM system and being forwarded to the relevant region for investigation.¹²⁶

5.6 Table 3 provides an overview of GST fraud referrals received for the period 1 March 2001 to 31 October 2002 and referrals registered on the FIRM system from July 2000. Prior to March 2001, fraud referrals were registered manually and statistical data relating to these referrals could not be provided by the ATO. Fraud Intelligence advised that it does not categorise fraud referrals received into GST and non-GST categories. Information relating to potential fraud referrals passed to Fraud Investigations has been recorded in the FIRM system (or its predecessor) since July 2000.¹²⁷

Table 3

Summary of GST referrals received and registered for the period July 2000 to October 2002

Referrals received and registered	2000–01	2001–02	July–Oct 2002
Total referrals received between 1 March 2001 and 31 October 2002	168	843	542
Total referrals registered on FIRM	98	230	64
Completed cases	2000–01	2001–02	July–Oct 002
Total number of cases	35	92	37
Actual losses of cases ⁽¹⁾	Nil ⁽²⁾	\$1 402 030	\$2 680 651
Fraud prevented for cases ⁽¹⁾	Nil ⁽²⁾	\$895 769	\$582 850
Annual exposure of cases ⁽¹⁾	Nil ⁽²⁾	\$11 574 994	\$1 811 908

Source: Australian Taxation Office—FIRM reports MTH008 and GSTQ03 and SNCC report to GST Business Forum, November 2002.

Note 1: The estimated value of the actual losses, fraud prevented and annual exposure was not recorded for a number of cases, resulting in an understatement of the estimates for the period.

Note 2: For 2000–2001, zero dollar values were recorded in the FIRM system.

5.7 The estimated value of the potential fraud involved in the referrals ranged from \$150 to \$6.5 million, with 13 referrals valued at over \$1 million. The estimated value of the potential fraud was not recorded on the system for a

¹²⁵ Internal sources include the Community Information, Storage, Communication and Observation database, ATO Business Lines, and Fraud Investigations. External sources include law enforcement agencies, other government agencies and financial institutions.

¹²⁶ Referring areas may refer fraud matters directly to Fraud Investigations, who are then required to forward these matters to Fraud Intelligence for registration and assessment.

¹²⁷ The FIRM system replaced the GST Fraud Case management system (GSTFC) in December 2002.

number of the cases, making it difficult to provide an accurate estimate for the period. The ANAO recognises that it is not always possible to quantify the value of the fraud involved as some cases may not necessarily involve a monetary value or have a value that is readily determined. However, in order to meet its data collection and reporting requirements under the Fraud Control Guidelines and assist in case prioritisation and selection, the ANAO considers that the ATO should, where possible, quantify the value of potential fraud cases on referral. The potential loss (value of the fraud) could be recorded and updated during the investigation.

Fraud referral guidelines

5.8 The referral guidelines for CVC staff (*CVC Referral Procedures*) require all fraud matters to be referred to Fraud Intelligence for initial assessment. The *SNCC Fraud Investigation Referral Guidelines and Procedures*, which are available to all ATO staff (including GST field staff), require all fraud matters to be referred to Fraud Investigations by completing the ATO Fraud Referral Form. This form is then automatically e-mailed to Fraud Intelligence. If this form is not completed, Fraud Investigations are to provide an information report to Fraud Intelligence for the case to be assessed and registered on the FIRM system.

Intelligence assessments

5.9 In assessing fraud referrals, Fraud Intelligence uses a range of internal and external systems and data sources. The ANAO found that there were no documented guidelines or procedures outlining the intelligence assessment process. During the audit, the ATO advised that these are being developed.

5.10 For the 43 sample cases reviewed, the ANAO examined the investigation case files and their corresponding Fraud Intelligence files to assess the level of involvement of Fraud Intelligence in the initial assessment of the fraud referral. Only 17 intelligence assessments were found in the case files reviewed. The ANAO observed that, for 12 cases where it was not evident that an intelligence assessment had been completed, the nature of the potential fraud and persons suspected of perpetrating the fraud warranted, in the ANAO's view, the early and/or ongoing involvement of Fraud Intelligence.

5.11 The ANAO also reviewed an additional 25 fraud matters referred to Fraud Intelligence in 2001–02. The ANAO found that the information and documentation relating to these assessments were minimal. Evidence of the work undertaken by intelligence analysts, such as system checks, analysis of data, and/or the outcome of the assessment process, was not always recorded. Further, the decision on whether to progress the referrals was not always clear. Referrals were not always signed off by either the analyst or team leader.

Assigning a priority rating

5.12 As part of the referral assessment process, Fraud Intelligence assigns a priority rating to each case registered on FIRM. A priority rating describes the nature and seriousness of a fraud matter, using a set of criteria, which measures potential impacts against the ATO.¹²⁸ The ANAO found that only 12 of the case files reviewed (less than 30 per cent) contained documentation for the priority rating applied.

5.13 The ANAO considers that the case referral process would be improved if assessment decisions were documented and intelligence assessments were completed for all fraud cases registered on the FIRM system. Fraud Intelligence has access to all ATO systems and a range of external databases. Research undertaken using these systems will add value to any fraud investigation and improve the quality of referrals to Fraud Investigations.

Recommendation No.6

5.14 To improve the quality of referrals and add value to fraud investigations, the ANAO recommends that:

- (a) all fraud matters registered on the Fraud Investigation Reporting and Management (FIRM) system as potential fraud cases be assessed by Fraud Intelligence; and
- (b) the intelligence assessment process be properly documented by analysts.

Agency response

5.15 Agreed. While current procedures require intelligence assessments for particular fraud cases, this requirement will now be extended to all registered fraud matters.

Management of GST fraud investigations

5.16 Investigations must comply with the *Commonwealth's Fraud Investigation Standards Package* (CFISP). The ATO has developed a case management process for investigating GST fraud perpetrated against the Commonwealth. A Statement of Investigation Standards and Procedural Guidelines were implemented in March 2001. The FIRM system records all investigation details. The Fraud Control Guidelines introduced mandatory training qualifications for fraud

¹²⁸ Priority ratings can be graded with a '1' rating (High Priority), a '2' rating (Medium Priority) or a '3' rating (Low Priority). A '1' rating requires an immediate Fraud Intelligence response, the commencement of an Intelligence Assessment and immediate referral to Fraud Investigations.

investigators.¹²⁹ The ATO's investigators have either acquired or are in the process of studying for these qualifications.¹³⁰

Assessment of case referrals

5.17 Fraud Investigations does not automatically investigate all referrals registered on the FIRM system. In deciding to accept or reject a referral, regional case assessment teams consider the nature and seriousness of the alleged offence, the threat posed to ATO systems, resource availability and their capacity to undertake an investigation. If a case is particularly serious or forensically complex, it may be referred to the AFP for investigation.¹³¹ A set of working guidelines between the ATO and AFP outline the conduct of joint investigations and arrangements for out-posting of AFP officers.

5.18 Fraud Investigations assign a complexity rating to all cases registered on the FIRM system. The complexity model used considers the offences involved, jurisdiction, resource implications and the expertise of investigators.¹³² A case is then allocated to an individual case officer or an investigating team to undertake the investigation. The referring area, officer or agency is to be advised when a case referral has been received, is allocated to a case officer, or when an investigation will not be conducted.

5.19 The ANAO found that 31 of the 43 sample cases reviewed contained some form of investigation assessment. Of these:

- 12 were assessed as no further action;
- 18 clearly documented the person(s) making the decision to accept or reject a case using a case decision record or other documentation; and
- 13 contained evidence of Fraud Investigations advising the outcome of investigation assessments to the referral source.

¹²⁹ Guideline 6 of the Fraud Control Guidelines requires that relevant employees are to gain the Certificate IV in Government (Fraud Control Investigation) qualification by 30 June 2003. Relevant employees are required to gain the Diploma of Government (Fraud Control Investigation) qualification by 30 June 2004.

¹³⁰ As of 25 November 2002, 37 investigators had obtained the Diploma of Government (Fraud Control Investigation), 45 investigators had obtained the standard Certificate IV in Government (Fraud Control Investigation) and eight investigators were in the process of finishing the Certificate IV in Government (Fraud Control Investigation) qualification.

¹³¹ From July 2000 to November 2002, 19 GST cases were referred to the AFP for investigation. Cases referred to the AFP resulted in either joint investigations being conducted by the ATO and AFP, or the AFP conducting investigations, with assistance from the ATO.

¹³² There are three types of complexity rating: 'A' (High Complexity Resource), 'B' (Medium Complexity Resource) and 'C' (Low Complexity Resource).

Investigation process

5.20 When a case is accepted for investigation, case officers and case managers are required to follow the case management process outlined in the ATO's Procedural Guidelines.

Case planning

5.21 An investigation plan outlines what tasks need to be undertaken, who should do them and when they are to be completed. The ANAO found that 15 of the 22 sample cases accepted for investigation included an investigation plan.¹³³ Fraud Investigations' management advised that the use of investigation case plans is viewed as an area for improvement.

5.22 Effective case management requires important decisions taken during the course of an investigation be recorded. The ANAO found that case running sheets were evident in 90 per cent of case files reviewed; whereas case decision records (CDRs) and case referral forms were evident in only 56 per cent and 63 per cent of the cases respectively. The ANAO considers there should be greater use of CDRs as they outline the details of, and reasons for major decisions during an investigation. CDRs also provide a basis for reviewing cases and support the transfer of files between case officers.

Evidence gathering

5.23 An evidence matrix¹³⁴ determines the evidence required to prove an offence, where the evidence may be located and the process for collecting this evidence. The CFISP recommend the use of evidence matrices, although the ATO's investigation standards do not explicitly require their use in case planning. The ANAO found that nine of the 15 sample cases with an investigation plan contained evidence matrices. The ANAO encourages the use of these matrices and considers the ATO's guidelines should be revised to make them mandatory in all serious or complex cases.

Review of investigations

5.24 The ANAO found that the framework for monitoring and reviewing cases was effective, with monthly and weekly meetings to review the status of active cases occurring across regions. Informal, ongoing reviews are also held within teams and these are recorded using CDRs, minutes or e-mails. Nineteen of the 22 sample cases accepted for investigation contained some form of ongoing review. The ANAO also found that regional managers report monthly to the

¹³³ In two cases referred to the AFP, the joint investigation agreement incorporated an investigation plan.

¹³⁴ An evidence matrix is an investigation tool used to document the offenders involved and evidence required to prove the offence.

national managers on the progress and status of all fraud cases. As well, national managers provide monthly reports to SNCC management.

5.25 The ANAO considers that the ATO has established a sound framework and implemented appropriate procedures for assessing GST fraud case referrals and conducting fraud investigations. However, these procedures were not always consistently implemented across regions.

Timeliness of investigations

5.26 The ANAO recognises that some investigations will take longer to complete than others, depending on their seriousness or complexity. However, the ANAO found it difficult to determine the time taken to complete investigations because of incomplete data in the reports provided by the ATO.¹³⁵ In its reports to the GST Business Forum, the SNCC notes the age of all open cases. However, this data is based on when a case is created (by Fraud Intelligence) and does not account for the various milestones of an investigation.

5.27 The ANAO considers that this lack of data makes it difficult for the ATO to accurately determine the age of cases and readily assess the viability of continuing an investigation. The ATO advised that its new case management system, which is to be implemented later this year, is designed to include a broad range of investigation milestones. The monitoring of these milestones by case officers and team leaders should improve case management.

5.28 For those cases (97 cases) where the information was available, on average, it took 164 days to complete an investigation, with ten cases taking fewer than seven days and two cases taking over 500 days. Complete information was available for only six of the 43 cases reviewed by the ANAO. For these cases it took, on average, 355 days to complete the investigation. The ANAO considers that in addition to steps to improve data quality, the ATO should also review the timeliness of its investigations.

Data quality and integrity

5.29 The ANAO found that the FIRM system reports provided as part of the audit were generally incomplete, as information had not been entered into a number of the data fields. As a result, it was difficult to cross-reference data from one report to another. The ATO advised that reports were not designed to reconcile with one another. This is due to the nature of the business rules for

¹³⁵ For example, of the 164 cases outlined in FIRM Report Number NAT009, 72 cases had no data entered for the Regional Allocation Date and/or Investigation Start Date, 67 cases had zero days registered between the start and completion of the investigation and two cases were recorded as having negative days for the time between allocating the cases to a region and starting an investigation.

data entry, the manner in which the reports have been setup and report parameters. The ANAO considers that, given these data quality issues, the accuracy and completeness of reports produced for the SNCC Executive and ATO Management are questionable. The data integrity of the FIRM system also impacts on the ATO's ability to meet its external reporting requirements under the Fraud Control Guidelines.

5.30 A quality review of the data integrity of the FIRM system was completed in December 2002. The review concluded that the more recent cases showed a greater use of the FIRM system and that staff now have a better understanding of the system's capability since the completion of staff training in November 2002.¹³⁶ The ATO advised the quality of data had improved since this training. Strategies are also being adopted to continually improve the quality and completeness of the data captured by the system.

ASISCaseManager System

5.31 The ASISCaseManager system, which is to be used by all ATO investigation areas, is to replace the FIRM system in late-2003. The design of the new case management system incorporates greater functionality. The system will include case milestones, allowing case officers and team leaders to monitor actions required within set timeframes. Enhancements to the level and type of information recorded will improve reporting capabilities, with standard reports created at the case level and management reports across all cases.

5.32 The ATO advised that, prior to the implementation of ASISCaseManager, system documentation and training would be provided to all staff that will use the system. The ATO considers that this training will give greater assurance that the data being input into the system is accurate; increasing the confidence level that the reports produced will be accurate and meaningful.

Preparation of prosecution briefs

5.33 Following completion of an investigation, a brief of evidence is prepared and referred to the CDPP for possible prosecution under the *Crimes Act 1914*. A brief of evidence not accepted for prosecution is returned to the ATO, where either no further action occurs, or the brief is reviewed and subsequently returned to the CDPP.

5.34 Table 4 provides an overview of cases referred to the CDPP, the number of cases not accepted for prosecution, the number of successful prosecutions and the number of cases in progress for the period July 2000 to October 2002.

¹³⁶ Although the FIRM system, and its predecessor, has been in use for a number of years, Fraud Investigations and Fraud Intelligence staff were only provided with formal training in November 2002.

Table 4**Overview of GST cases referred to the CDPP for the period July 2000 to October 2002**

Cases referred to the CDPP	2000-2001	2001-2002	Jul-Oct 2002	Total
Number of cases referred	4	25	15	44
Number of cases not accepted by CDPP for prosecution	1	3	Nil	4
Number of successful prosecutions	2	5	6	13
Number of cases in progress	1	11	15	27

Source: Australian Taxation Office

5.35 Due to the timing of cases being referred to the CDPP and prosecution action, a case can be carried across financial years. Seventeen cases from the ANAO's representative sample were referred to the CDPP. Eight cases were successfully prosecuted, three were not accepted for prosecution, and six are still in progress. The reasons cases were not accepted for prosecution included:

- insufficient evidence to substantiate fraud claims;
- inability to prove intent; and
- a prosecution not being in the public's interest.

Quality of prosecution briefs

5.36 The ANAO consulted with the CDPP on the quality of prosecution briefs prepared by Fraud Investigations. The CDPP advised that most briefs were considered to be of a quality standard. However, others had been returned to the ATO for further work. The early involvement of the CDPP in an advisory capacity has assisted the ATO in scoping and undertaking investigations.

5.37 The ATO advised that case officers and/or team leaders prepare prosecution briefs. The ANAO found that only five of the 17 briefs of evidence referred to the CDPP had been reviewed. For several briefs where a review was not evident, the CDPP had requested Fraud Investigations to conduct further inquiries before accepting the brief for prosecution. The ATO's investigation guidelines do not explicitly require briefs of evidence to be reviewed before referral to the CDPP. The ANAO considers a mandatory review of briefs of evidence by either a team leader or regional manager would assist in ensuring high quality briefs are referred to the CDPP and would provide the opportunity to identify areas for improvement.

Recommendation No.7

5.38 To support the referral of high quality briefs of evidence to the Commonwealth Director of Public Prosecutions (CDPP), the ANAO recommends that the ATO include in investigation guidelines a mandatory requirement for regional managers or team leaders to review briefs of evidence prior to referral to the CDPP.

Agency response

5.39 Agreed. This will involve better documentation of current operating procedures.

Quality assurance surveys

5.40 The ATO advised that the CDPP provides feedback to cases officers on a case-by-case basis. The ANAO was advised that Fraud Investigations in Western Australia have developed a quality assurance survey for the CDPP to complete when briefs of evidence are referred.¹³⁷ The survey contains three questions relating to the quality of the contents and structure of the brief of evidence. The survey provides the regional manager with a mechanism to measure the quality of briefs referred and identify areas for improvement. The ANAO suggests consideration be given to implementing the quality assurance survey in other regions.

Liaison arrangements between the ATO and CDPP

5.41 The ANAO found that the ATO and CDPP have established guidelines for referring taxation-related matters for prosecution. Fraud Investigations advised that it has good relationships with the CDPP across the regions, and they meet regularly with the CDPP and AFP to review the progress of cases and discuss potential cases for referral. The CDPP has also conducted educational seminars to ensure investigators are aware of any issues relating to the preparation of briefs of evidence and other emerging legal issues

Quality review mechanisms

5.42 The ATO has established a quality assurance review (QAR) program to identify and support the development of best practice and promote consistent standards across regions. All regions are subject to the bi-annual internal QAR program. The Quality Assurance and Training Manager and a peer officer from another region undertake the reviews. A summary of the review's findings and

¹³⁷ The relevant CDPP case officer completes these surveys.

recommendations is presented in a report to each region and in a consolidated national report to the SNCC Executive.¹³⁸ National and regional managers are responsible for implementing any recommendations.

5.43 The ANAO found that two QAR programs have been completed since the reviews were implemented in June 2001, with the most recent in December 2002. This review found that the majority of the files satisfied the Commonwealth guidelines. The ATO advised that the current QAR process is being reviewed.

Quality assurance reviews by the AFP

5.44 The AFP has conducted one QAR on an ATO fraud case since 2000.¹³⁹ This review confirmed that the standard of the file was high and that the investigation was well planned and managed. The ATO advised that it intends to liaise with the AFP to arrange for further external QARs to be carried out.

Case evaluation and analysis

5.45 The ATO's fraud investigation guidelines require every completed investigation to be reviewed to identify risk, as well as systems and control issues requiring attention by management. The ANAO found no evidence of the systematic analysis of GST fraud trends, referral patterns, or case outcomes being undertaken on a regular basis, particularly at a national level. There was also no evidence that any formal evaluation had been undertaken of the sample cases reviewed by the ANAO.

5.46 Fraud Investigations advised that it does not undertake trend analysis relating to the types of cases or fraud perpetrated. In some regions, systems and control issues identified by case officers, team leaders or regional managers were addressed during the course of investigations and on an individual case basis. However, it was not always evident that the broader implications of these issues were considered nor that the information was disseminated to other regions or business lines to be included in any assessment of GST fraud risks.

5.47 There were no formal feedback processes to advise Fraud Intelligence on the outcome of investigations or to provide details of any specific control issues, system weaknesses or methods of operation. This information is particularly important from an intelligence perspective and builds up the ATO's understanding of GST fraud. During the audit, the ATO advised that procedures for advising Fraud Intelligence and disseminating this information are being developed.

¹³⁸ The national report is forwarded to the SNCC Executive, which comprises of an Assistant Commissioner, the two National Managers and the Manager, Fraud Intelligence.

¹³⁹ The case was reviewed in November 2001 and related to PAYE fraud.

5.48 The ANAO considers that the ATO should comply with its own guidelines and regularly evaluate and analyse GST fraud referrals, investigations and case outcomes, particularly from a national perspective. Such analysis should be documented and control weakness or emerging issues formally advised to the relevant business line(s). This would allow the ATO to identify and react to emerging GST fraud trends, risks and system weaknesses.

Recommendation No.8

5.49 To support fraud control planning and the development of fraud prevention and detection strategies, the ANAO recommends that the ATO routinely evaluate and analyse fraud referrals, investigations, case outcomes and trends nationally and disseminate this information within the ATO.

Agency response

5.50 Agreed. Again, this will involve formalisation and better documentation of current operating procedures.

Debt management and recovery process

5.51 Prior to a fraud investigation, the GST Business Line may undertake activity that results in an adjustment to the GST payable or refunded. These adjustments create a tax liability, which is a legally enforceable debt under the provision of the *Tax Administration Act 1953*. The recovery of these debts is the responsibility of Client Account Management (CAM). As the compliance activity that initiated the adjustment is generally completed before the fraud investigation commences, recovery action can be undertaken in parallel with the fraud investigation.

5.52 Within CAM, Advanced Legal Teams have been established to manage the recovery of overpayments, including those involving fraudulently obtained refunds or other credits. Liaison arrangements have been established between the Advanced Legal Teams, the GST Business Line and Fraud Investigations. This is further supported by guidelines covering the referral, coordination and management of cases arising from taxation fraud, particularly GST fraud.

5.53 The ATO has broad powers under the *Tax Administration Act 1953* in regard to the collection of debt that allows it to commence a range of recovery actions.¹⁴⁰ The Crimes Act also provides that reparation orders may be made in respect of any loss suffered or expense incurred by the Commonwealth. For example, if a

¹⁴⁰ These actions may include the issue of: Garnishee Notices to attach to the bank accounts containing refunds; Summons/Writs in Civil proceedings; and Mavera Injunctions to restrain assets.

fraud involves GST, on conviction, the ATO can apply to the courts for a reparation order to recover the revenue lost. The CDPP is not responsible for the enforcement of any reparation orders made under the Crimes Act. The ATO must take legal action to convert the reparation order to a civil debt and implement appropriate recovery action.

5.54 Of the 43 cases reviewed during the audit, approximately \$6.4 million in adjustments and penalties has been raised by the ATO. Of these, about \$3.8 million has been collected. The ATO advised that no amounts relating to these debts have been written off.

5.55 Currently, the value of adjustments, court-imposed fines, costs and penalties and recoveries are not recorded in the FIRM system. The ANAO was advised that consideration is being given as to how this data may be captured for reporting purposes. The ATO also advised that fines, costs and penalties would be recorded and reported in the new ASISCaseManager system to be implemented later this year.

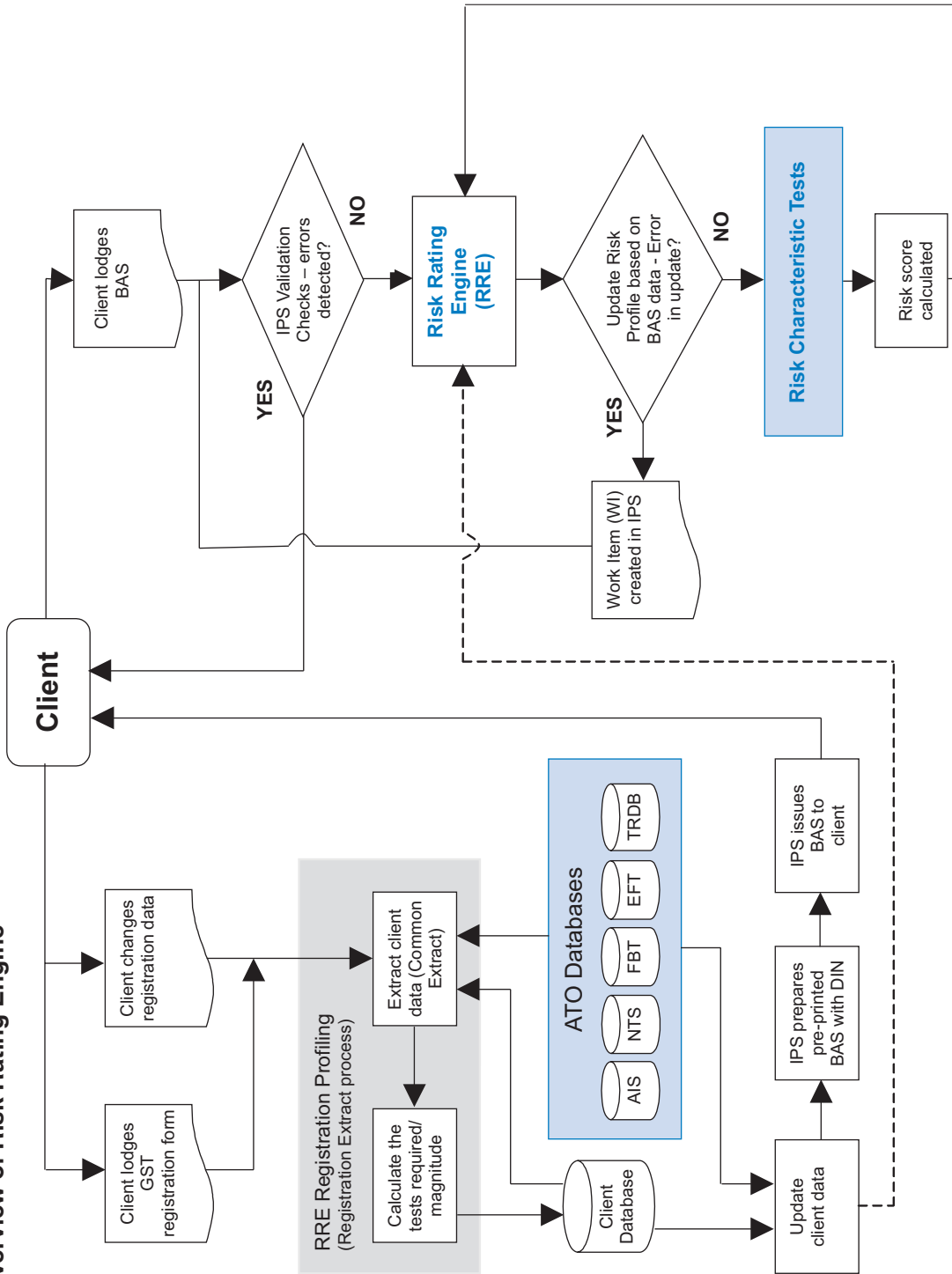
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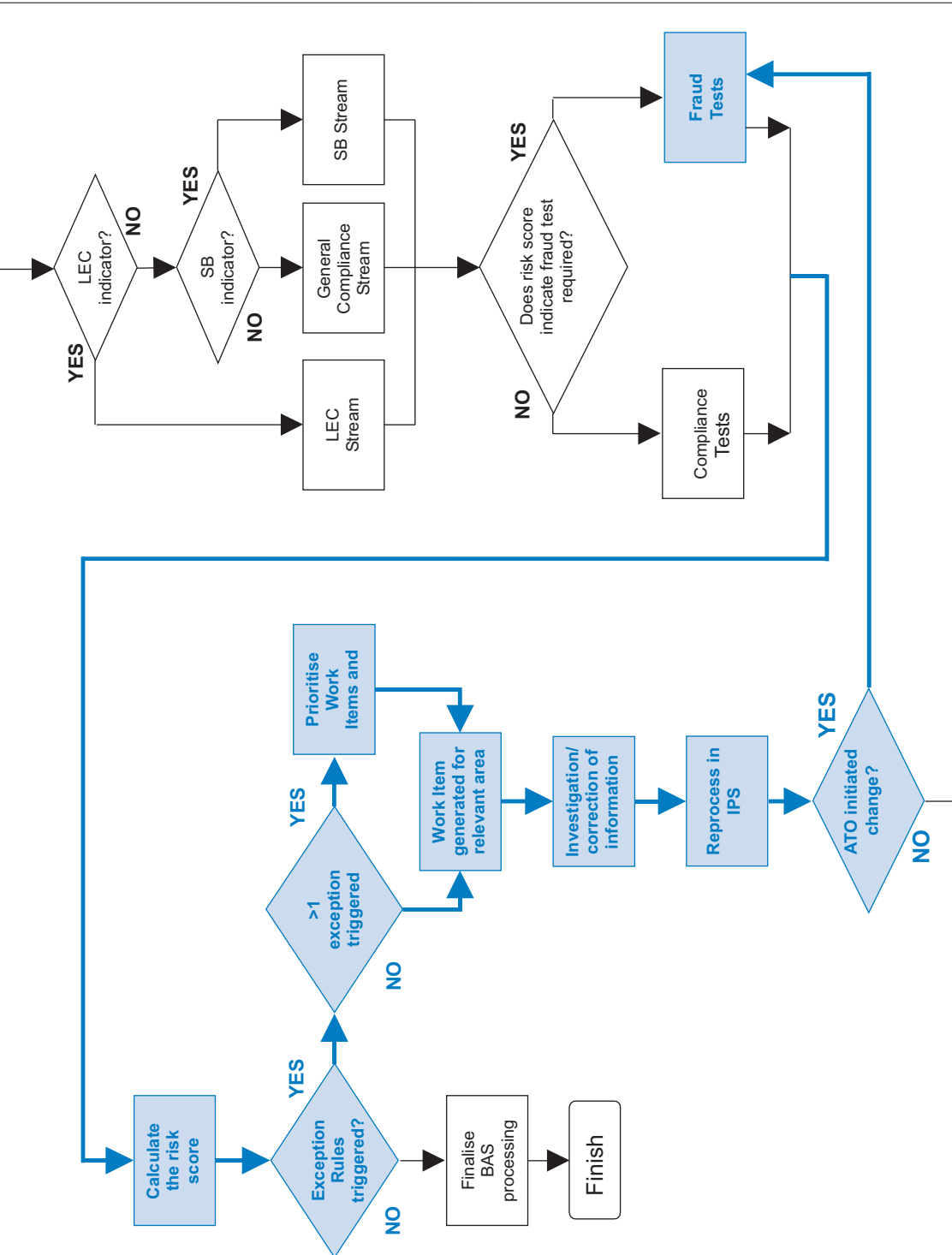


Oliver Winder
Acting Auditor-General

Appendix

Appendix 1 Overview of Risk Rating Engine





Source: ANAO analysis of ATO data.

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