Administration of Fringe Benefits Tax
Canberra ACT
2 June 2005

Dear Mr President
Dear Mr Speaker

The Australian National Audit Office has undertaken a Business Support Process Audit across agencies 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 Administration of Fringe Benefits Tax.

Following its tabling in Parliament, the report will be placed on the Australian National Audit Office’s Homepage—http://www.anao.gov.au.

Yours sincerely

Ian McPhee
Auditor-General

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

The Auditor-General is head of the Australian National Audit Office. 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

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<tbody>
<tr>
<td>ANAO</td>
<td>Australian National Audit Office</td>
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<tr>
<td>Annual return or FBT return</td>
<td>An annual fringe benefits tax return must be lodged with the Australian Taxation Office by 21 May each year, unless an extension of time to lodge has been granted.</td>
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<tr>
<td>Associated entities</td>
<td>For the purpose of this report associated entities refers to all Australian Government departments and authorities of the Commonwealth.</td>
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<tr>
<td>ATO</td>
<td>Australian Taxation Office (ATO)</td>
</tr>
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<td>AWAs</td>
<td>Australian Workplace Agreements</td>
</tr>
<tr>
<td>Benefit</td>
<td>A benefit includes any right, privilege, service or facility.</td>
</tr>
<tr>
<td>CSIRO</td>
<td>Commonwealth Scientific and Industrial Research Organisation</td>
</tr>
<tr>
<td>Declaration</td>
<td>A declaration is a written statement given to an employer by an employee providing information relating to fringe benefits.</td>
</tr>
<tr>
<td>Defence</td>
<td>Department of Defence</td>
</tr>
<tr>
<td>DFAT</td>
<td>Department of Foreign Affairs and Trade</td>
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</table>
| Employee | Employee means:  
  - a current employee;  
  - a future employee; or  
  - a former employee.  

An employee is generally someone who receives, or is entitled to receive, salary and wages in return for work or services provided, or for work under a contract that is wholly or principally for the person’s labour.  
For fringe benefits tax purposes ‘employees’ includes company directors, office holders, common law employees and recipients of compensation payments. |
<table>
<thead>
<tr>
<th>Term</th>
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<tbody>
<tr>
<td>Exempt benefit</td>
<td>Exempt benefits are benefits that are not considered to be fringe benefits and therefore are not subject to fringe benefits tax.</td>
</tr>
<tr>
<td>GST</td>
<td>Goods and Services Tax (GST)</td>
</tr>
<tr>
<td>FBT</td>
<td>Fringe Benefits Tax (FBT)</td>
</tr>
<tr>
<td>Fringe benefit</td>
<td>A fringe benefit is a benefit provided in respect of employment. This effectively means a benefit provided to an employee or their associate because they are an employee. The employee may even be a former or future employee.</td>
</tr>
<tr>
<td>FBT year</td>
<td>The FBT year is 1 April to 31 March.</td>
</tr>
<tr>
<td>RFBA</td>
<td>Reportable Fringe Benefit Amount (RFBA). Any employer who provides fringe benefits to an employee or their associate with a total taxable value of more than $1,000 for an FBT year (1 April to 31 March), must record the grossed-up taxable value of the benefits on the employee’s payment summary for the corresponding income year (1 July to 30 June).</td>
</tr>
<tr>
<td>FBTAA</td>
<td>The Fringe Benefits Tax Assessment Act 1986 establishes the rules for assessing and collecting the tax.</td>
</tr>
<tr>
<td>FBT(AC)A</td>
<td>The Fringe Benefits Tax (Application to the Commonwealth) Act 1986 ensures that the FBT law applies to Australian Government departments and authorities.</td>
</tr>
<tr>
<td>FMIS</td>
<td>Financial Management Information System</td>
</tr>
<tr>
<td>Grossing up</td>
<td>Grossing up means increasing the taxable value of benefits provided to reflect the gross salary employees would have to earn at the highest marginal tax rate (including Medicare Levy) to buy the benefits after paying tax.</td>
</tr>
<tr>
<td>LAFHA</td>
<td>Living Away from Home Allowance (LAFHA) is an allowance the employer pays to an employee to compensate for estimated expenses incurred, or estimated expenses and any disadvantage suffered, because the employee is required to live away from their usual place of residence in order to perform their employment related duties.</td>
</tr>
<tr>
<td>Term</td>
<td>Definition</td>
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<td>---------------------------------------------------------------------------</td>
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<tr>
<td>Otherwise deductible rule</td>
<td>The taxable value of a benefit may be reduced by the amount which an employee would have been entitled to claim as a once only income tax deduction in their personal tax return if the benefit was not paid for, reimbursed or provided, by the employer.</td>
</tr>
<tr>
<td>Private ruling</td>
<td>The Australian Taxation Office (ATO) issues rulings and determinations to advise taxpayers of their views on the interpretation and application of tax law, including FBT law. Any person, uncertain about their FBT liability arising from a particular arrangement, may apply to the ATO for a private ruling on that arrangement.</td>
</tr>
<tr>
<td>RBA</td>
<td>Reserve Bank of Australia</td>
</tr>
<tr>
<td>Residual benefit</td>
<td>Any fringe benefit that is not subject to any of the other valuation rules (such as housing, meal entertainment, car parking, etc) is called a residual fringe benefit. Essentially, these are the fringe benefits that are left over because they are not one of the more specific categories of fringe benefits.</td>
</tr>
<tr>
<td>Taxable value</td>
<td>This is the value of a fringe benefit before it is grossed up.</td>
</tr>
<tr>
<td>Type 1 benefit</td>
<td>The ‘Type 1’ gross-up rate is used where an employer (or other provider) is entitled to claim an input tax credit whether claimed or not.</td>
</tr>
<tr>
<td>Type 2 benefit</td>
<td>The ‘Type 2’ gross-up rate is used where an employer (or other provider) is not entitled to claim an input tax credit.</td>
</tr>
</tbody>
</table>
Summary and Recommendations
Summary

Background

1. Fringe benefits tax (FBT) was introduced on 1 July 1986 in order to tax benefits provided in place of, or as well as, salary and wages. FBT was designed to address previous deficiencies in the income tax law, which meant that fringe benefits were in effect, a form of tax-free income. FBT is levied on the grossed-up\(^1\) taxable value of the fringe benefits provided and the FBT liability is the responsibility of the employer. The FBT is self assessed and employers are required to calculate the liability and pay the tax within legislative timeframes.

FBT legislation

2. The FBT legislation was enacted in a package of four Acts, they include\(^2\):
   - The Fringe Benefits Tax Assessment Act 1986 which establishes the rules for assessing and collecting the tax;
   - The Fringe Benefits Tax Act 1986 which imposes tax on the taxable value of the fringe benefits. Any change to the rate of tax is effected by amending this Act;
   - The Fringe Benefits Tax (Application to the Commonwealth) Act 1986 which applies the FBT laws to Australian Government authorities and departments; and
   - The Fringe Benefits Tax (Miscellaneous Provisions) Act 1986 which amended the Income Assessment Act 1936 so that employees would not be liable for income tax on any fringe benefits received.

3. The Australian Taxation Office (ATO) administers the collection of FBT. Application of FBT law can be relatively complex and resource intensive for many employers. The complexity and extent of resources employers require to effectively administer FBT will largely depend on the number of people they provide fringe benefits and the range and number of benefits provided. There are also specific requirements relating to different categories of benefits and for certain benefits the employer is given some choice over the method used to...
calculate their FBT liability. This level of complexity increases the risk of non-compliance.

4. There have been several changes to the FBT law since its inception. Some of the more recent changes include:

- from 1 April 1999, employers were required to record the grossed-up taxable value of fringe benefits on the payment summary of any employee receiving total relevant fringe benefits exceeding $1,000; and
- the introduction of the Goods and Services Tax (GST) in July 2000 impacted on the calculation of an employer’s FBT liability. Specifically a higher FBT gross-up rate is applied for FBT return calculations where the benefit provider is entitled to claim an input tax credit in respect of GST paid on goods or services acquired in order to provide the fringe benefits.

5. The move away from standard public sector terms and conditions of employment in favour of Certified Agreements and Australian Workplace Agreements (AWAs) has increased the accessibility by employees to salary packaging options and the payment of allowances and other benefits in place of salary and wage payments. Together, these changes have expanded the administrative and reporting requirements for FBT within employing entities. Some entities have outsourced various aspects of their FBT administration, such as salary packaging to external service providers. However, where this has occurred, the entity remains responsible for the calculation of the value of the benefit and payment of the FBT.

6. The Fringe Benefits Tax (Application to the Commonwealth) Act 1986, FBT(AC)A, provides for the notional application of fringe benefits tax to benefits provided to Australian Government employees. The total aggregated FBT liability for all Australian Government public sector entities for the 2003 FBT year was approximately $365 million and $380 million for 2004. The ANAO audit was undertaken in four entities whose combined total FBT liability for 2003 was approximately $300 million or 82 per cent of the total liability for Australian Government public sector entities for that year.

Audit objectives

7. The objectives of the audit were to:

- determine whether entities had established effective internal control frameworks and processes to mitigate the risks associated with FBT obligations and transactions;

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3 Figures based on assessment data as provided by the ATO to ANAO on 8 February 2005.
assess whether the internal control frameworks and processes supported the payment of FBT and the reporting of reportable fringe benefit amounts (RFBAs) on employee payment summaries in accordance with the legislation;

identify sound and better practices in the administration, management and operation of systems for collecting, collating, calculating, reporting and remitting FBT; and

as necessary, recommend improvements in the controls and practices relating to the administration of FBT in the audited entities.

Scope of the audit

8. The scope of the audit encompassed the following:

• assessing whether FBT was paid in accordance with legislation;
• identifying the range of FBT administrative arrangements in place, including those where the administration of salary packaging had been outsourced;
• assessing the controls in place in respect of systems for the administration of FBT;
• testing a sample of transactions processed within each entity to assess whether transactions were assessed appropriately and in accordance with legislative and procedural requirements;
• assessing the processes and controls in place to ensure that RFBAs were correctly reported on employee payment summaries;
• assessing the processes and controls in place designed to ensure that FBT balances were accounted for correctly in the FBT return; and
• the identification of sound and better practice principles, where appropriate.

Selected entities

9. The audited entities were:

• The Commonwealth Scientific and Industrial Research Organisation (CSIRO);
• The Department of Defence (Defence);
• The Department of Foreign Affairs and Trade (DFAT); and
• The Reserve Bank of Australia (RBA).
Audit conclusion

10. Complying with the requirements of FBT legislation can be relatively complex and resource intensive for many employers including Australian Government public sector entities. Overall the ANAO considers that most of the audited entities had committed sufficient resources and effort to meet their FBT obligations and some had established a range of sound and better practices in relation to the administration of FBT.

11. The ANAO concluded there would be benefit in some of the audited entities re-examining their risk assessments with a view to addressing, in a comprehensive manner, the risks related to the administration of FBT. The ANAO also concluded that in some entities the guidance used to assist with the administration of FBT needed to be improved, as in some cases it was incomplete, incorrect, out of date and/or insufficiently detailed. As a result there was an increased risk that entities would not fully meet their FBT obligations.

12. The audit identified that all of the audited entities had provided benefits to employees that had not been subject to FBT. In particular, two of the audited entities had continued to rely on advice issued by the ATO in 1986 relating to the application of FBT on overseas conditions and allowances which the ANAO considers, based on ATO advice, to be no longer applicable. As a result the ANAO considers that these two entities may have significantly understated their FBT liability and the resultant reportable fringe benefits amounts for their employees. Based on the audit findings, the ANAO considers that there would be benefit in entities undertaking a comprehensive review of those benefits provided to staff that are not currently subject to FBT with a view to improving the completeness of benefit calculations. In particular, the ANAO considers it would be appropriate for private tax rulings to be sought from the ATO in respect of a number of benefits that entities considered were not subject to FBT.

13. The audit also identified a number of incorrect calculations supporting the determination of FBT payable. The incorrect calculations were due to inaccurate, inconsistent or inappropriate methods used to calculate the value of benefits provided and a lack of appropriate supporting documentation. The ANAO also found there were a number of arrangements and processes associated with the administration of FBT that could be improved in some entities. In particular, the ANAO considers entities need to be satisfied that review functions undertaken in relation to FBT administration are conducted by people with sufficient FBT knowledge to fully understand the requirements for complying with FBT legislation.
Sound and better practice

14. The ANAO identified examples of sound and better practice in several entities. These are listed in the table below.

Table 1
Examples of sound and better practice

<table>
<thead>
<tr>
<th>Control Framework</th>
<th>Sound and Better Practice</th>
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| Risk management                                   | • risk registers that identified specific FBT risks, existing controls to mitigate the risk and the staff members with responsibility for the risks and controls; and  
• clear guidelines provided to various groups within the entity to enable a consistent approach in respect of risk assessment arrangements. |
| Control structure (control environment and control activities) | • maintenance of staffing levels commensurate with FBT administrative requirements and/or the utilisation of external service providers for FBT guidance and information;  
• annual training session for staff responsible for compiling work area FBT returns;  
• up-to-date and detailed FBT operating procedures; the maintenance of a register of all ATO correspondence and rulings; and the utilisation of templates and standard proformas for FBT data collection;  
• a structured approach to determining the FBT implications of any new employee benefits and arrangements;  
• where an account code relates to a benefit that is a reportable fringe benefit, ensuring that an entry to that account code is accompanied by a valid employee identification number;  
• the conduct of an annual review of general ledger codes to identify incorrectly coded FBT transactions; and  
• the completion of an annual variance analysis to compare the balances on the FBT return with those of previous years. |
| Information and communication                     | • designated staff authorised to contact the ATO on FBT issues;  
• regular communication and agreed working relationships between all work areas that were involved in, or had responsibility for, the administration of FBT;  
• employees being notified of their RFBA prior to the issue of payment summaries; and  
• guidance provided to employees detailing the impact of their RFBA. |
### Control Framework vs. Sound and Better Practice

| Monitoring and review | • a program of internal review or internal audits of FBT related controls and payments;  
|                       | • peer review of work performed when collating data for inclusion in the FBT return;  
|                       | • obtaining external expert and technical advice and engaging external advisors to undertake a quality assurance review of the FBT return; and  
|                       | • the periodic review of pay and conditions to assist in ensuring benefits are treated correctly for FBT purposes. |

15. These practices are addressed further in the report itself and, where appropriate, are reflected in the report’s recommendations.

16. The ANAO considers that the audited entities, and other Australian Government public sector entities, may benefit from enhancing their FBT administration processes and arrangements by adopting the above sound and better practices if they have not already done so.

### Recommendations

17. The ANAO has made 13 recommendations aimed at improving the administration of FBT in the audited entities. A number of these recommendations are likely to have relevance to all Australian Government entities that provide fringe benefits to their employees.
Recommendations

The summary of recommendations below are based on the findings from the entities reviewed. The ANAO considers that they are likely to be relevant to all Australian Government entities that provide fringe benefits to their employees.

Recommendation No.1
Para 2.6
The ANAO recommends that entities not already doing so should include risks related to FBT in their operational risk assessments. FBT related risks should include consideration of all risks associated with the administration of FBT, particularly the risks of not meeting their legislative obligations.

Recommendation No.2
Para 3.5
The ANAO recommends that entities provide comprehensive guidance material to those staff with FBT responsibilities and periodically review the guidance for completeness, accuracy and relevance.

Recommendation No.3
Para 3.12
The ANAO recommends that at the time entities are considering introducing new benefits or arrangements, formal consideration be given to whether such benefits or arrangements are likely to be subject to FBT and, if so, consider the potential FBT implications from both an employer and employee perspective.

Recommendation No.4
Para 3.24
The ANAO recommends that entities undertake a complete review of those benefits provided to staff that are not currently subject to FBT to provide assurance that the FBT treatment of these benefits complies with contemporary legislative requirements.

Recommendation No.5
Para 3.38
The ANAO recommends that employees responsible for the administration of FBT, particularly those approving FBT data, be provided with FBT training, commensurate with their level of responsibility and the entity’s individual circumstances.

Recommendation No.6
Para 3.47
The ANAO recommends that entities only utilise FBT concessions when employees submit all relevant documentation, including declarations.

Recommendation No.7
Para 3.55
The ANAO recommends that entities review the application of the two gross-up rates used to calculate the taxable value of benefits provided, to ensure they are consistent with the requirements of the FBTAA.
Recommendation
No.8
Para 3.63

The ANAO recommends that entities ensure that they comply with the requirement to disclose all required RFBAs on an individual’s payment summary. If any entity has RFBAs that have not previously been allocated to individuals, and therefore have not been disclosed on an individual’s payment summary, the entities should decide, in consultation with the ATO, on the appropriate course of action in relation to those unallocated RFBAs.

Recommendation
No.9
Para 3.74

The ANAO recommends entities review, and amend as appropriate, their methodology for the calculation of the reduction in taxable value of LAFHA and satisfy themselves that the methodology used reflects legislative requirements.

Recommendation
No.10
Para 3.81

The ANAO recommends that entities review their approach to advising other associated entities of benefits it had provided to their employees consistent with the requirements of the FBTAA.

Recommendation
No.11
Para 3.100

The ANAO recommends that entities review their general administrative processes relating to FBT to assist in ensuring that processes are effective in facilitating entities meeting their FBT obligations. This review should address areas such as record-keeping, resourcing, reconciliations, delegations, authorisations and the completeness of calculations.

Recommendation
No.12
Para 4.10

The ANAO recommends that agreed formal communication arrangements in relation to FBT be established between staff responsible for the administration of FBT and other relevant work areas and the ATO.
Recommendation No.13
Para 5.6

The ANAO recommends that entities enhance, where relevant, existing monitoring and review arrangements by:

- undertaking an annual analytical review of FBT balances that includes the analysis and documentation of the reason for any significant variances over-time; and
- subjecting FBT administration to regular review through, for example, internal audit coverage or other review arrangements.

Responses to the recommendations

18. The audited entities, together with the ATO have indicated agreement with the audit recommendations.

19. Entities’ responses to the recommendations are provided following each recommendation in the main body of the report. General comments provided by the audited entities and the ATO have been included at Appendix 1.
Audit Findings and Conclusions
1. Introduction

This chapter discusses the legislative, administrative and reporting requirements of Fringe Benefits Tax (FBT) and outlines the objectives, scope and audit criteria of the audit.

Background

1.1 Fringe benefits tax was introduced on 1 July 1986 in order to tax benefits provided in place of, or as well as, salary and wages. FBT was designed to address previous deficiencies in the income tax law, which meant that fringe benefits were in effect, a form of tax-free income. FBT is levied on the grossed-up\(^4\) taxable value of the fringe benefits provided and the FBT liability is the responsibility of the employer. The FBT is self assessed and employers are required to calculate the liability and pay the tax within legislative timeframes. The FBT reporting year runs from 1 April to 31 March.

FBT legislation

1.2 The FBT legislation was enacted in a package of four Acts, they include\(^5\):

- *The Fringe Benefits Tax Assessment Act 1986* which establishes the rules for assessment and collection of the tax;

- *The Fringe Benefits Tax Act 1986* which imposes tax on the taxable value of the fringe benefits. Any change to the rate of tax is effected by amending this Act;

- *The Fringe Benefits Tax (Application to the Commonwealth) Act 1986* which applies the FBT laws to Commonwealth Government authorities and departments; and

- *The Fringe Benefits Tax (Miscellaneous Provisions) Act 1986* amended the *Income Assessment Act 1936* so that employees would not be liable for income tax on any fringe benefits received.

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\(^4\) Grossing up means increasing the taxable value of benefits provided to reflect the gross salary employees would have to earn at the highest marginal tax rate (including Medicare Levy) to buy the benefits after paying tax.

1.3 The Australian Taxation Office (ATO) administers the collection of FBT. There are 13 categories of fringe benefits. These are:

- car;
- debt waivers;
- loans;
- expense payments;
- housing;
- living away from home allowances (LAFHA);
- airline transport;
- board;
- entertainment;
- entertainment provided by tax exempt entities;
- car parking;
- property; and
- residual benefits.

1.4 The application of FBT law can be relatively complex and resource intensive for many employers. The complexity and extent of resources employers require to effectively administer FBT will largely depend on the number of people they provide fringe benefits and the range and number of benefits provided. There are also specific requirements relating to different categories of benefits and for some benefits the employer is given some choice over the method used to calculate their FBT liability. This level of complexity increases the risk of non-compliance.

1.5 There have been several changes to the FBT law since its inception. Some of the more recent changes include:

- from 1 April 1999, employers were required to record the grossed-up taxable value of fringe benefits on the payment summary of any employee receiving total relevant fringe benefits exceeding $1 000; and
- the introduction of the Goods and Services Tax (GST) in July 2000 impacted on the calculation of an employer’s FBT liability. Specifically, a higher FBT gross-up rate is applied for FBT return calculations where the benefit provider is entitled to claim an input tax credit in respect of GST paid on goods or services acquired in order to provide the fringe benefit.
1.6 The move away from standard public sector terms and conditions of employment in favour of Certified Agreements and Australian Workplace Agreements (AWAs) has increased the accessibility by employees to salary packaging options and the payment of allowances and other benefits in place of salary and wage payments. Together, these changes have expanded the administrative and reporting requirements for FBT within employing entities. Some entities have outsourced various aspects of their FBT administration, such as salary packaging to external service providers. However, where this has occurred, the entity remains responsible for the calculation of the value of the benefit and payment of the FBT.

1.7 The Fringe Benefits Tax (Application to the Commonwealth) Act 1986, FBT(AC)A, provides for the notional application of fringe benefits tax to benefits provided to Australian Government employees. The total aggregated FBT liability for all Australian Government public sector entities for the 2003 FBT year was approximately $365 million and $380 million for 2004. The ANAO audit was undertaken in four entities whose combined total FBT liability for 2003 was approximately $300 million or 82 per cent of the total liability for Australian Government public sector entities for that year.

Audit objectives

1.8 The objectives of the audit were to:

- determine whether entities had established effective internal control frameworks and processes to mitigate the risks associated with FBT obligations and transactions;

- assess whether the internal control frameworks and processes supported the payment of FBT and the reporting of reportable fringe benefit amounts (RFBAs) on employee payment summaries in accordance with the legislation;

- identify sound and better practices in the administration, management and operation of systems for collecting, collating, calculating, reporting and remitting FBT; and

- as necessary, recommend improvements in the controls and practices relating to the administration of FBT in the audited entities.

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6 Figures based on assessment data as provided by the ATO to ANAO on 8 February 2005.
Scope of the audit

1.9 The scope of the audit extended to:
• assessing whether FBT was paid in accordance with legislation;
• identifying the range of FBT administrative arrangements in place, including those where the administration of salary packaging had been outsourced;
• assessing the controls in place in respect of systems for the administration of FBT;
• testing a sample of transactions processed within each entity to assess whether transactions were assessed appropriately and in accordance with legislative and procedural requirements;
• assessing the processes and controls in place to ensure that RFBAs were correctly reported on employee payment summaries;
• assessing the processes and controls in place designed to ensure that FBT balances were accounted for correctly in the FBT return; and
• the identification of sound and better practice principles, where appropriate.

Selected entities

1.10 The audited entities were:
• The Commonwealth Scientific and Industrial Research Organisation (CSIRO);
• The Department of Defence (Defence);
• The Department of Foreign Affairs and Trade (DFAT); and
• The Reserve Bank of Australia (RBA).

Audit criteria

1.11 The FBT administration arrangements in each entity were assessed on the basis of audit criteria that addressed standard elements of the internal control structure. The internal control structure is made up of the following interrelated components:
• risk assessment;
• control environment and control activities;
• information and communication; and
Introduction

- monitoring and review.

1.12 The audit criteria for each element of the control framework are shown at the start of the relevant section of the report and are set out in full at Appendix 2.

**Audit methodology**

1.13 The audit focussed on the FBT administration processes and controls in place at each entity and on specific transactions that were tested on a sample basis, in respect of the FBT return for the year ended 31 March 2003 and where appropriate controls and practices applicable to the 2004 FBT return.

1.14 The audit process involved interviews with selected officers, the examination of files and records supporting FBT processing activity, general observation and inspection and testing of key controls.

1.15 The audit was undertaken by the ANAO, with the assistance of Ernst & Young and KPMG on a contract managed basis, in accordance with ANAO auditing standards. The audit cost approximately $440 000.

**Audit findings**

1.16 The ANAO provided each of the selected entities with a detailed report of the findings relating to their entity as part of the audit process.

1.17 The results of the audit, including entities’ specific responses to each of the recommendations, are set out in Chapters 2 to 5. Sound and better practices identified within the audited entities are also provided. The ANAO considers that the audited entities, and other Australian Government public sector entities, may benefit from enhancing their FBT administration processes and arrangements by adopting the sound and better practices identified if they have not already done so.
2. Risk Assessment

This chapter considers the risk management arrangements within the entities in relation to the administration of FBT.

Background

2.1 All entities encounter some form of risk that can adversely impact on the achievement of its objectives.

2.2 With regard to taxation, the ANAO noted that the Commissioner for Taxation has ‘directly raised with Managing Directors of listed companies the importance of managing tax risk as part of good corporate governance’.\(^7\)

2.3 In order to effectively manage risk, each entity should undertake a formal risk assessment process, involving all levels of management. The assessment should identify and evaluate significant exposures to risk, and the entity should implement appropriate controls and systems to ensure that risk is kept to an acceptable level. As part of the audit, the ANAO considered the risk management arrangements at the organisational and operational levels, in relation to the administration of FBT.

Audit criteria

Table 2.1

| Audit Criteria | At either an organisational or operational level the entity would be expected to have identified the risks associated with FBT processes and assessed those risks with respect to impact, likelihood and controls. This assessment could have included consideration of the complexities associated with the legislation, the need for appropriately skilled staff, consideration of an outsourcing option and a quality assurance function. |

Source: ANAO

Audit findings

2.4 There are a number of risks associated with the administration of FBT. These include:

- incomplete capture of transactions or benefits that result in FBT liabilities for the entity;

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\(^7\) Australian Taxation Office, *Focus on compliance issues for the tax office in 2005*, Speech by the Second Commissioner, Jennie Granger, 28 February 2005.
• unauthorised, inaccurate, untimely or non-compliant payment of FBT;
• failure to meet external reporting deadlines (including the FBT return);
• incorrect or inaccurate recording of payments and entitlements;
• incorrect or inaccurate recording and reporting of RFBAs on payment summaries;
• inappropriate resources and/or skill levels of staff involved with the administration of FBT;
• undue reliance on key staff and/or the loss of key staff; and
• failure to maintain, retain and/or handle information and other supporting documentation.

2.5 All entities audited had a risk management framework at the strategic level. In relation to FBT, most of the entities had undertaken a risk assessment at the operational level. However, the audit identified that in many cases not all relevant risks had been identified and considered as part of the operational risk assessment. The ANAO considers there would be benefit in entities re-examining their risk assessments with a view to including all risks related to the administration of FBT. Such risk assessments could also include consideration of the risk of fraud in relation to benefits provided to employees and in relation to the administration of FBT within the entity.

Recommendation No.1

2.6 The ANAO recommends that entities not already doing so should include risks related to FBT in their operational risk assessments. FBT related risks should include consideration of all risks associated with the administration of FBT, particularly the risks of not meeting their legislative obligations.

Entities’ responses

CSIRO

2.7 Agree. Risks will be assessed annually.

Defence

2.8 Agree. The recommendation is already incorporated as part of Defence tax management best practice.

DFAT

2.9 Agree. Appropriate FBT related risks will be added to the department’s Risk Management Register by 30 June 2005.
2.10 The RBA accepts the recommendation and complies with it.

Sound and better practice

2.11 The ANAO noted the following examples of sound and better practice in respect of the entities operational risk assessment arrangements:

- risk registers that identified specific FBT risks, existing controls to mitigate the risk and the staff members with responsibility for the risks and controls; and
- clear guidelines provided to various groups within the entity to enable a consistent approach in respect of risk assessment arrangements.
3. Control Structure

This chapter provides audit findings with regard to the control environment and control activities of the audited entities.

Background

3.1 A control environment is the organisational context that reflects management’s commitment and attitude to the implementation and maintenance of an effective control structure. The control environment which management promulgates through the entity will strongly influence the design and operation of control policies and procedures.  

3.2 Control activities are the specific practices, processes and methodologies that help an entity ensure that:

- risks are reduced whilst opportunities for improvement are identified;
- irregularities are prevented or detected and addressed;
- assets are safeguarded; and
- financial records and relevant data are complete and accurately reflect the activities of an entity.

Audit criteria

Table 3.1

<table>
<thead>
<tr>
<th>Audit Criteria</th>
<th>The entity would be expected to have:</th>
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<tbody>
<tr>
<td></td>
<td>• issued policy and guidance on FBT legislation to staff and FBT administrators;</td>
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<tr>
<td></td>
<td>• substantiated requirements and determined responsibilities for managing the administration of FBT within the entity;</td>
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<td></td>
<td>• ensured that staff involved in the administration of FBT are appropriately skilled and that quality assurance processes are adequate;</td>
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<td></td>
<td>• systems for capturing and reporting FBT information in accordance with legislation, with close links between the general ledger and payroll management information systems; and</td>
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<tr>
<td></td>
<td>• established specific controls for the administration of FBT incorporating authorisation and approval of FBT balances, identification, collection, calculation, reporting and remitting of FBT liabilities, including adequate verification procedures in relation to outsourced services.</td>
</tr>
</tbody>
</table>

Source: ANAO

Audit findings

Policies and guidelines

3.3 The ANAO found that all entities audited had established policies and guidance relevant to the administration of FBT. However the audit identified that in some cases the guidance was incomplete, incorrect, out of date and/or insufficiently detailed.

3.4 The ANAO considers that entities need to give greater priority to ensuring guidance material is complete, accurate and up-to-date. In addition, the ANAO considers that entities would benefit from providing staff with more detailed guidance, particularly in respect of specific processes and requirements relating to the preparation and completion of the FBT return. Such guidance could incorporate target or milestone dates for FBT compliance processes to be initiated and completed as part of the completion of the annual return. Entities could also lessen the risk that inaccurate and/or out of date FBT information is made available to staff by introducing a formal review process prior to relevant information being released to all staff. Such a review should be undertaken by a person with appropriate FBT expertise, and evidence of the review should be documented.

Recommendation No.2

3.5 The ANAO recommends that entities provide comprehensive guidance material to those staff with FBT responsibilities and periodically review the guidance for completeness, accuracy and relevance.

Entities’ responses

CSIRO

3.6 Agree.

Defence

3.7 Agree. The recommendation is already incorporated as part of Defence tax management best practice.

DFAT

3.8 Agree. DFAT’s FBT Manual is available to all employees and is periodically reviewed. FBT workbooks and associated documentation have been reviewed to ensure that guidance is complete, accurate and relevant.

RBA

3.9 The RBA accepts the recommendation and complies with it.
Introduction of new benefits

3.10 The likelihood of all relevant benefits being recognised as benefits to which FBT is applicable increases if documented processes are in place that outline how entities address the introduction of a new benefit to employees which may have FBT implications. The audit identified that not all entities had such processes in place. In some instances entities relied on regular communication between various work areas to identify and highlight new benefits. This informal process was dependent on relevant staff having the appropriate skills, training and guidance to identify when a potential FBT liability may arise. However, this approach increases the risk of FBT information being incomplete and the entity’s FBT liability being understated, particularly where staff are not sufficiently skilled or experienced to recognise potential FBT issues associated with benefits payable to staff. The ANAO found that, in some instances, benefits were being provided that were not being included in the FBT return, as staff had not recognised them as a benefit.

3.11 Introducing new fringe benefits will also incur administrative costs associated with training/advising employees, FBT data collection, FBT calculation, reporting and remitting of FBT liabilities. The ANAO considers that at the time an entity is considering introducing a new benefit or arrangement, formal consideration be given to the potential FBT implications, from both the employers and employees perspective.

Recommendation No.3

3.12 The ANAO recommends that at the time entities are considering introducing new benefits or arrangements, formal consideration be given to whether such benefits or arrangements are likely to be subject to FBT and, if so, consider the potential FBT implications from both an employer and employee perspective.

Entities’ responses

CSIRO

3.13 Agree.

Defence

3.14 Agree. The recommendation is already incorporated as part of Defence tax management best practice.

DFAT

3.15 Agree. New staff benefits and arrangements are reviewed for FBT implications by the Finance Management Branch (FMB).

RBA

3.16 The RBA accepts the recommendation and complies with it.
Benefits provided but not subject to FBT.

3.17 The ANAO found that in all of the audited entities, benefits had been provided that had not been subject to FBT. In some cases entities had considered the benefits they were providing were exempt from FBT. This included car parking and a range of benefits relating to long-term overseas postings. In other cases, entities had not recognised that they had provided their employees with a benefit that was subject to FBT. As a result the value of the benefit had not been included in the FBT return.

3.18 In relation to those benefits which entities considered exempt from FBT, the majority (by value) affected the two audited entities that had a large number of employees on long-term overseas postings. This understanding was based on advice contained in a letter issued by the ATO to the Office of Public Service Board dated, 13 November 1986 that provided guidance on the FBT treatment of a number of overseas conditions and allowances. The ANAO sought advice from the ATO in relation to whether entities providing benefits to employees on long-term overseas postings should still be relying on the aforementioned advice.

3.19 The ATO advised the ANAO that entities should no longer be relying on this advice as it was given shortly after the introduction of the legislation and since then the FBT legislation and the related administrative policies have gone through substantial changes. In addition, many of the arrangements addressed in the advice such as the payment and treatment of overseas conditions and allowances may have changed, and as a result of these changes substantial aspects of the advice may now no longer be considered appropriate. In light of the ATO advice, the audit identified that these entities may have significantly under disclosed their FBT liability and RFBAs for 2003, and subsequent FBT years. For one entity the undisclosed FBT liability in relation to one of their major benefit categories (utilities) could be approximately $3 million and the related undisclosed RFBA approximately $6 million. For the other entity, given the nature of entitlements provided to employees and the number of people receiving the benefit, the ANAO considers the non-capture of separate benefits such as utilities would also result in a large under-disclosure of the entity’s FBT liability. As these benefits were not captured separately at the time of the audit, an exact amount of the under disclosure could not be obtained.

3.20 The ANAO considers entities should review those benefits that are provided but are not subject to FBT. A suggested starting point to identify all benefits that could be subject to FBT would be a review of documents, such as:

- current certified agreements;
- AWAs;
• any other documents that outline conditions of service; and
• FBT manuals, policies and procedures.

3.21 For those entities with employees overseas, the review should include, but not be limited to, the treatment of benefits provided to staff on long-term postings, such as:
  • utilities;
  • education costs;
  • preschool costs;
  • excess commuting costs;
  • flexible travel options provided to staff; and
  • the treatment of benefits arising from such matters as compensation for loss of possessions in storage or during removal, the loss on sale of vehicle and the loss on furniture disposal.

3.22 The review should be undertaken by people with sufficient FBT knowledge to confirm the treatment is appropriate and complies with contemporary legislative requirements. The review should also include the examination of relevant ATO correspondence, including tax rulings, to determine what correspondence is/is not being relied on, and whether continued reliance on such correspondence is appropriate. Entities should obtain formal advice or private rulings from the ATO, as appropriate, in respect of those benefits that they consider are not subject to FBT.

3.23 Amendments to policies, procedures and guidance documents should be made as benefits change. Any proposed amendments should be reviewed and signed off by personnel with sufficient FBT knowledge to confirm that the treatment continues to be appropriate, and complies with legislative requirements.

Recommendation No.4

3.24 The ANAO recommends that entities undertake a complete review of those benefits provided to staff that are not currently subject to FBT to provide assurance that the FBT treatment of these benefits complies with contemporary legislative requirements.
Entities’ responses

CSIRO
3.25 Agree.

Defence
3.26 Agree. Defence will review its remuneration and entitlement policies received by ADF members and civilian employees to ensure correct taxation treatment. The Defence Tax Management Office (DTMO) will take responsibility for this review as part of its tax sign off process consistent with Defence CEI 1.3 Tax Management.

DFAT
3.27 Agree. A review of benefits provided to staff has been completed. DFAT is seeking clarification regarding a small number of benefits from the Australian Taxation Office (ATO).

RBA
3.28 The RBA accepts the recommendation and complies with it.

Resourcing
3.29 In most cases, the ANAO considered the level of resources devoted to the administration of FBT was sufficient. In one entity, the ANAO noted that responsibility for preparing the FBT return rested largely with one person. In this case the ANAO considered the level of resources devoted to FBT given the complexities of FBT and the relative volume (both in number and dollar value) of its transactions, may not have been sufficient to enable it to meet its FBT obligations.

Training
3.30 The provision of regular training for staff involved in the administration of FBT is important to help ensure staff are appropriately skilled to address changes in legislation and resultant FBT reporting requirements, as well as the FBT implications of any new benefits provided. While the ANAO acknowledges that those staff involved in the collection of FBT data do not require the same level of training or expertise as those responsible for preparing FBT returns, the level of training should be commensurate with the staff member’s level of involvement in, and responsibility for, administering FBT.

3.31 A lack of training increases the risk of FBT information being incomplete and the entity’s FBT liability being incorrect. Where relevant staff do not have an appropriate level of knowledge and training, there is a risk that not all benefits will be identified and/or captured correctly. A lack of sufficient
training may also result in an omission or miscalculation not being identified and corrected in the review and approval process.

3.32 The ANAO identified three levels of personnel for whom the provision of some level of FBT training or information is considered appropriate:

- the staff responsible for the FBT return - staff required to prepare, review and lodge the FBT return for the entity;
- the staff responsible for FBT data collection – staff collecting and/or providing information relevant to the administration of FBT; and
- the employees who are receiving fringe benefits.

**Staff responsible for the FBT return**

3.33 The ANAO found that all of the audited entities had made suitable arrangements for those staff responsible for the FBT return to have access to guidance material on FBT. Such material included various publications, internally developed information, subscription services, the ATO website and help lines, expert advice or some form of commercially available software. There were also opportunities for such personnel to attend FBT seminars. Overall training for staff at this level was considered to be generally satisfactory.

**Staff responsible for FBT data collection**

3.34 The audit found that not all staff responsible for FBT data collection were offered, or were required to participate in, formal FBT training. This lack of training was evident in one entity where audit testing revealed that incorrect information, due to a lack of understanding, was being entered into FBT spreadsheets. This had resulted in an overpayment of FBT.

3.35 The audit also identified the need for increased training tailored to each entity's particular circumstances, particularly for some staff based in overseas locations.

3.36 The ANAO considers that the development of a checklist or set of open-ended questions would be useful in allowing staff with FBT information collection responsibilities to raise questions and provide information to assist in identifying whether any other fringe benefits may have been provided. Such a checklist would enhance the ability of staff collecting FBT information to be assured all fringe benefits provided are reported.

**Employees receiving fringe benefits**

3.37 The ANAO found that the level of information provided to employees receiving fringe benefits was satisfactory.
Recommendation No.5

3.38 The ANAO recommends that employees responsible for the administration of FBT, particularly those approving FBT data, be provided with FBT training, commensurate with their level of responsibility and the entity’s individual circumstances.

Entities’ response

CSIRO
3.39 Agree.

Defence
3.40 Agree. The recommendation is already incorporated as part of Defence tax management best practice.

DFAT
3.41 Agree.

RBA
3.42 The RBA accepts the recommendation and complies with it.

Declarations and utilisation of concessions

3.43 A number of fringe benefits attract concessional treatment. The concession is a reduction in the taxable value of the fringe benefit that results in a reduced amount of FBT or, in some cases, no FBT being paid. In order to take advantage of some of these concessions, specific documentary evidence may need to be collected and retained. Such documentation can include invoice and/or receipts and declarations. Examples of the types of declarations required include:

- LAFHA;
- expense payment;
- remote area holiday transport;
- employees car; and
- loans.

3.44 If an entity chooses to utilise a concession available by use of an employee declaration, ATO guidance indicates that all employee declarations must be obtained no later than the day on which the FBT return is due to be lodged with the ATO, unless an extension is granted by the ATO. Although there is no need to notify the ATO of the utilisation of declarations, it is
expected that an entity’s business records will include the appropriate declarations.

3.45 The audit identified that, although entities were aware that declarations were required from employees in order to be entitled to certain concessions, not all declarations were collected before the concession was claimed. At times there was no supporting documentation provided to the staff responsible for preparing the FBT return to indicate that the required declarations had been completed by employees.

3.46 As previously mentioned, the audit found that some benefits were not recognised as a benefit subject to FBT. Therefore, in some instances, the relevant declarations were not obtained by the entity, as the benefit had not been recognised as a fringe benefit for FBT purposes.

**Recommendation No.6**

3.47 The ANAO recommends that entities only utilise FBT concessions when employees submit all relevant documentation, including declarations.

**Entities’ responses**

*CSIRO*

3.48 Agree.

*Defence*

3.49 Agree. Defence will apply to the Commissioner of Taxation to accept Defence application forms in relation to certain benefits be used in place of the ATO prescribed declarations to reduce administrative costs and handling.

*DFAT*

3.50 Agree. The FBT workbooks have been redesigned to ensure that all FBT concessions are supported by declarations. As part of a quality assurance review the signed declarations are checked against the FBT workbooks by the Taxation Manager.

*RBA*

3.51 The RBA accepts the recommendation and complies with it.

**The application of appropriate gross-up factors**

3.52 The GST affects the calculation of an entity’s FBT liability. Where the entity has provided fringe benefits to employees, there are two gross-up rates that can be used to calculate the amount subject to FBT - a higher (called Type 1) and a lower (called Type 2) gross-up rate. The higher gross-up rate is used where the entity is entitled to claim (whether claimed or not) an input tax
credit for GST paid on benefits provided to an employee, and the lower gross-up rate is used where there is no entitlement to an input tax credit.

3.53 The audit identified instances where the application of the gross-up rates were incorrect. In some cases:

- the same benefits were treated inconsistently;
- benefits provided both in Australia and overseas were treated the same way, even though expenditure incurred in providing benefits overseas would generally not have GST included in the cost, and the entity would therefore not be entitled to a GST input tax credit; and
- all benefits of the same type were assumed to be subject to the same gross-up rate for ease of processing, or due to a lack of recognition that benefits could require the applications of either of the gross-up factors.

3.54 The ANAO also noted that one entity used standard payment request forms that did not always disclose the GST component of the total amount payable. In these circumstances, there is a risk that amounts may all be treated as if they included GST. This in turn could result in GST input tax credits being incorrectly claimed for items not subject to GST.

**Recommendation No.7**

3.55 The ANAO recommends that entities review the application of the two gross-up rates used to calculate the taxable value of benefits provided, to ensure they are consistent with the requirements of the FBTAA.

**Entities’ response**

*CSIRO*

3.56 Agree. When the RFBA requirements came into effect, CSIRO was aware and complied with the use of the correct gross-up rate to calculate the taxable value of benefits.

*Defence*

3.57 Agree. Defence will implement best practice for identifying the source and type of benefits provided independently of Defence purchasing data to ensure the correct classification is made.

*DFAT*

3.58 Agree. DFAT ensures that the correct gross-up rates are applied through controls and configurations of its financial system. Upon entry, each transaction must be accompanied by the appropriate ‘tax code’ indicating the GST status of the transaction. This ensures that the appropriate gross-up rates are used when calculating FBT summaries for each employee.
3.59 The RBA accepts the recommendation and complies with it.

**Allocation of reportable fringe benefits amounts**

3.60 Employees receiving relevant benefits exceeding a total taxable value of $1 000 are required to have the grossed-up taxable value of fringe benefits recorded on their payment summary. This amount is based on the cumulative total value of all benefits provided to the employee during the FBT year. In order to capture the value of benefits provided to staff, entities usually establish mechanisms for allocating benefits provided to the individuals who receive them. The Type 2 gross-up rate is always applied to calculate RFBAs irrespective of the gross-up rate applying for the FBT return. The audit identified that:

- in one entity the total value of a certain benefit was pro-rated across a number of employees. This resulted in employees being allocated a small RFBA even if they did not receive the particular benefit; and
- in another entity there were a large number of benefits that could not be attributed to individual employees, and therefore were not included on employees’ payment summaries.

3.61 In addition, as mentioned in paragraphs 3.17 to 3.23, a number of benefits were considered exempt from FBT. As a result the entities did not include them in employees’ RFBAs.

3.62 In some cases the inability to allocate RFBAs to an individual was due to a lack of data in the entities’ financial management information system (FMIS) or insufficient information being held within the entity. In other cases, the benefits related to former employees. Notwithstanding the practical difficulties of allocating benefits to employees, the ANAO considers that entities should continue to make efforts to increase their level of compliance in this area. Where necessary, entities should review their identification and data collection methods and consider the implementation of system-based mechanisms to assist in the allocation of benefits to individual employees. For example, an employee identifier could be entered into the entity’s FMIS whenever an expense is coded to an ‘FBT code’ which gives rise to an RFBA.

**Recommendation No.8**

3.63 The ANAO recommends that entities ensure that they comply with the requirement to disclose all required RFBAs on an individual’s payment summary. If any entity has RFBAs that have not previously been allocated to individuals, and therefore have not been disclosed on an individual’s payment summary, the entities should decide, in consultation with the ATO, on the appropriate course of action in relation to those unallocated RFBAs.
Entities’ response

CSIRO

3.64 Agree. CSIRO uses an FBT software to ensure all RFBAs are allocated and disclosed to the correct employee’s payment summary.

Defence

3.65 Agree. In relation to certain loan fringe benefits to former ADF members, Defence will contact the bank concerned to develop working arrangements to assist Defence to comply with reporting requirements.

DFAT

3.66 Agree. DFAT will ensure that all required RFBAs are disclosed on an individual’s payment summary. DFAT’s financial system requires that a personnel number be entered whenever an expense is coded to a ‘FBT code’. This ensures that RFBAs are allocated to employees.

3.67 Following a review of benefits provided to employees, DFAT has produced a list of benefits which are to be included as RFBAs on 2004-2005 Payment Summaries. Some of these benefits were not previously included as RFBAs and DFAT has begun consultation with the ATO to determine the appropriate course of action regarding these unallocated RFBAs.

RBA

3.68 The RBA accepts the recommendation and complies with it.

Living away from home allowance

3.69 For FBT purposes, a LAFHA is an allowance the employer pays to an employee to compensate for additional expenses incurred and any disadvantages suffered because the employee is required to live away from their usual place of residence in order to perform their employment related duties. Two of the audited entities provided their employees, on long-term overseas postings, with LAFHA benefits. The components of LAFHA benefits provided included:

- cost of living allowance;
- child allowance;
- child reunion allowance;
- hardship post dependant child allowance; and

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9 Australian Taxation Office, op.cit., p.62. The term ‘expenses’ does not include expenses which the employee would be entitled to claim as an income tax deduction.

* Different terms are used by different organisations
post adjustment (one entity).

3.70 The taxable value of the LAFHA is the amount of the allowance paid. However, this taxable value can be reduced by:

- any part of the allowance that is reasonable compensation for the cost of accommodation for the employee (and, if applicable, the employee’s family)\(^\text{10}\) and/or
- any part of the allowance that is reasonable compensation for additional expenditure on food (that is; the exempt food component is the estimate of the additional food and drink costs over and above the food and drink costs that would have been incurred by the employee (and their family) had they remained in Australia).\(^\text{11}\)

3.71 The ANAO acknowledges that the calculation of LAFHA and the associated reduction in taxable value can be relatively complex and time consuming particularly when there are a high numbers of employees involved and/or employees work in a large number of overseas countries. To fully reflect each employee’s individual circumstances the entity would, amongst other things, have to take into account the employees family composition and arrangements whilst the employee is working overseas and the different cost of living at each location.

3.72 In relation to LAFHA the audit identified that in one entity there was an absence of documentation supporting some of the components used to calculate LAFHA payable. The audit also identified that entities may not be using the most appropriate methods in determining the reduction in the taxable value of LAFHA for the exempt food component.

3.73 Both entities utilised an externally provided index\(^\text{12}\) to assist them calculate LAFHA payable. The ANAO considers that entities should review their approach to determining any reduction in taxable value of LAFHA benefits provided. As part of the review, entities should have regard to using information it already maintains. For example, details of location and family composition are already used in the calculation of LAFHA payable and entities already use external entities to provide different indices relevant to different countries. Therefore, entities should consider using individual family composition and country indices to provide a more accurate adjustment as the

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\(^{10}\) In the two entities that provided LAFHA for employees on long-term overseas posting the accommodation is provided separately to employees. Consequently no component on the LAFHA paid relates to accommodation and therefore there can be no reduction in the taxable value claimed in relation to accommodation.

\(^{11}\) Australian Taxation Office, op.cit., p.63.

\(^{12}\) There are external organisations that provide data to subscribers on the cost of living index for a range of overseas countries compared to Australia.
calculation of the exempt food component reduction in taxable value. As part of this review, entities should satisfy themselves that the methodology adopted is defensible and reflects the requirement of the FBT legislation. The methodology used should be appropriately documented and signed off by someone with sufficient FBT expertise to fully understand the implications of the particular methodology adopted. Given the potential complexity and amounts involved, it may be prudent for entities to obtain formal advice or a private ruling from the ATO to confirm the approach is appropriate to their particular circumstances.

**Recommendation No.9**

3.74 The ANAO recommends entities review, and amend as appropriate, their methodology for the calculation of the reduction in taxable value of LAFHA and satisfy themselves that the methodology used reflects legislative requirements.

**Entities’ response**

*CSIRO*

3.75 Agree.

*Defence*

3.76 Agree. Defence will review taxable value calculations for overseas living allowances, with focus on identifying appropriate methods with the ATO for determining the exempt food component.

*DFAT*

3.77 Agree. DFAT has sought legal advice regarding this issue and is satisfied that the methodology used for the calculation of the reduction in taxable value of LAFHA reflects legislative requirements.

*RBA*

3.78 The RBA accepts the recommendation and complies with it.

**Inter-entity allocations**

3.79 Section 132(2) of the FBTAA requires entities that have provided benefits to employees of other associated entities, to provide those other associated entities with records of the relevant transactions.

3.80 Employees of two of the audited entities had received benefits from other associated entities. When the audited entities had been advised that their employees had received the benefits this data had been included in their FBT
return. However, when the same two audited entities had provided benefits to the employees of other entities the audit identified that:

- one entity had not advised the other associated entities in all instances. In particular, the audited entity had paid FBT on all meal entertainment it had provided, regardless of whether the recipient was an employee, and entertainment benefits provided to employees of the other associated entity had been included in the audited entity’s FBT return; and

- one entity did not have arrangements in place to advise other associated entities of benefits it had provided to their employees.

**Recommendation No.10**

3.81 The ANAO recommends that entities review their approach to advising other associated entities of benefits it had provided to their employees consistent with the requirements of the FBTAA.

**Entities’ response**

*CSIRO*

3.82 Agree.

*Defence*

3.83 Agree. Defence will develop workable, cost-effective methods and system to capture and report details of fringe benefits provided to employees of other Australian government entities.

*DFAT*

3.84 Agree. DFAT has reviewed its approach to advising other associated entities of benefits provided to their employees to ensure it is consistent with the requirements of the FBTAA.

*RBA*

3.85 The RBA accepts the recommendation and complies with it.

**General administrative issues**

3.86 The following administrative matters were identified by the ANAO as issues common to each of the audited entities.

*Supporting documentation and record keeping*

3.87 The ANAO found that, in most entities, an appropriate level of source documentation was contained on FBT files and that, in most cases, data not contained on files could easily be accessed. However, where not already in
place, the ANAO considers that the following improvements regarding supporting documentation and record-keeping could be made:

- retaining on file source data relating to each FBT return that is sufficient to support the details contained in the FBT return;
- ensuring there is documentation to support the number of employees declared as having received fringe benefits;
- cross-referencing work papers to supporting papers; and
- ensuring ATO correspondence and ATO rulings are readily available and accessible.

Reconciliations

3.88 Reconciliation procedures are an important control designed to ensure that the calculation of the FBT liability is based on data that is complete and consistent.

3.89 The ANAO found instances where information provided by work areas regarding specific FBT items, for example vehicles, could not be reconciled to information used to prepare the FBT return.

3.90 The ANAO considers that reconciliations should form an integral part of the process for completing the annual FBT return, and be subject to periodic review.

Responsibilities, delegations and authorisations

3.91 The ANAO found that documentation of the roles, responsibilities and delegations in relation to the administration of FBT in most of the audited entities was appropriate. However, the ANAO did note that in one entity, at the time of the audit, there was no formal job description detailing the responsibilities of the Tax Manager. The ANAO has since been advised that this entity has now prepared a detailed job description of the Tax Manager’s position. The ANAO also noted that in one entity the existing delegations did not cover the responsibility for approval and signing of the FBT return.

3.92 The ANAO found that most FBT payments were appropriately authorised and approved. However, in one entity although instalments were being authorised by an employee with the appropriate delegation, three out of the four FBT instalments for the year had been varied and each variation had been calculated incorrectly and not in accordance with legislative requirements.

Systems for capturing and reporting FBT information

3.93 In most of the audited entities the compilation of FBT information for the entity’s annual FBT return is devolved to line areas. Generally this process
involved an FBT data collection package being completed for each major work area, with the central corporate finance areas being responsible for the collection and consolidation of information provided into a single FBT return for the entity itself.

3.94 Depending on the type of fringe benefit, there are many areas from where FBT information can be obtained. These include:

- the accounts payable and general ledger systems;
- work areas responsible for fleet and vehicle leasing arrangements, salary packaging, corporate payroll; and
- overseas staff who are responsible for capturing FBT data information relevant to benefits provided to employees while overseas.

3.95 The audit identified that, in one entity, data provided by sources outside the area responsible for completing the FBT return was not subject to review for accuracy, appropriateness or completeness. The ANAO considers that all data prepared by individual work areas should be reviewed before being used as source data for preparation of the FBT return. This will assist with the identification of inaccuracies or instances where data is incomplete or has been treated inconsistently.

FBT calculations and completeness of FBT information

3.96 As mentioned previously, the FBT legislation is relatively complex and has a range of rules and options available in calculating various benefits. The audit identified a number of instances of entities using methods to calculate FBT that did not accord with relevant legislative requirements. For example:

- car parking treated as FBT exempt;
- the use of an incorrect base cost in applying the statutory formula method in relation to motor vehicle benefits; and
- the treatment of benefits being based on an incorrect method of calculation or classification.

3.97 As also noted earlier, a key risk for entities’ FBT administration is that data is incomplete and that transactions subject to FBT are not fully identified, captured and reported. Entities can seek to address these risks through their overall control environment and specific control activities, with a particular focus on the use of the FBT spreadsheets and software packages, FBT manuals, review of transaction codes and appropriate training for staff responsible for the administration of FBT.

3.98 The ANAO identified that two of the audited entities had also conducted a review of general ledger codes and/or their individual terms and conditions, such as their Certified Agreements. The other two entities had no
such review arrangements in place, increasing the risk that the completeness of the FBT related transactions may be incorrect.

3.99 The ANAO considers there is merit in entities reviewing a range of administrative arrangements and processes in relation to FBT taking into account the need for:

- regular reconciliations of data supporting the completion of the FBT return, the investigation of discrepancies and reconciliations and supporting documentation being maintained and being readily accessible;
- delegations to be reviewed to ensure that details of officers who approve and sign the annual FBT return are properly delegated to do so;
- FBT payments being reviewed by staff and/or the entity’s external tax advisor and authorised by a designated staff member with appropriate FBT knowledge;
- FBT data, particularly data collected by individual work areas and external parties, being reviewed for accuracy, appropriateness and completeness;
- a register of all ATO correspondence, including private rulings, being maintained;
- a review of staff terms and conditions to identify benefits not being captured for FBT; and
- a periodic review of general ledger codes to identify any incorrectly coded FBT transactions.

**Recommendation No.11**

3.100 The ANAO recommends that entities review their general administrative processes relating to FBT to assist in ensuring that processes are effective in facilitating entities meeting their FBT obligations. This review should address areas such as record-keeping, resourcing, reconciliations, delegations, authorisations and the completeness of calculations.

**Entities’ response**

*CSIRO*

3.101 Agree.
Defence

3.102 Agree. The recommendation is already incorporated as part of Defence tax management best practice.

DFAT

3.103 Agree. DFAT has performed a thorough review of general administrative processes relating to FBT. This review covered all aspects of FBT administration. Business process and financial system improvements have been implemented to allow DFAT to meet its FBT obligations in an efficient and effective manner.

RBA

3.104 The RBA accepts the recommendation and complies with it.

Sound and better practice

3.105 The ANAO noted the following sound and better practices in respect of FBT control structures:

- maintenance of staffing levels commensurate with FBT administrating requirements and/or the utilisation of external service providers for FBT guidance and information;
- annual training session for staff responsible for compiling work area FBT returns;
- up-to-date and detailed FBT operating procedures; the maintenance of a register of all ATO correspondence and rulings; and the utilisation of templates and standard proformas for FBT data collection;
- a structured approach to determining the FBT implications of any new employee benefits and arrangements;
- where an account code relates to a benefit that is a reportable fringe benefit, ensuring that an entry to that account code is accompanied by a valid employee identification number; and
- the conduct of an annual review of general ledger codes to identify incorrectly coded FBT transactions.
4. Information and Communication

This chapter discusses the information flows in relation to FBT within the audited entities.

Background

4.1 Timely and relevant information communicated across an entity is a key element of effective control. By getting the right information to the right people at the right time, an entity can enhance decision-making, performance reporting and the ability to meet strategic objectives efficiently and effectively.\(^{13}\)

4.2 Effective information and communication arrangements are required to ensure that FBT is administered appropriately. Generally the arrangements will involve:

- internal information and communication flows between an entity’s human resources, payroll, finance and FBT administration function; and
- external information and communication flows between an entity and the ATO, outsource providers, other entities and taxation advisors.

Audit criteria

<table>
<thead>
<tr>
<th>Audit Criteria</th>
<th>The entity would be expected to have two way information flows between (a) the staff responsible for payment processing and those responsible for managing FBT and (b) the personnel/payroll section and individual employees. It is also important that the entity has communicated with employees the impact of electing to receive a particular benefit.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Source: ANAO</td>
<td></td>
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</table>

Audit findings

Work areas

4.3 The ANAO found that in most of the audited entities there was regular communication during the compilation of the annual FBT return, and throughout the year, between the area responsible for the administration of FBT and other work areas such as human resources, payroll and finance that have particular FBT responsibilities.

\(^{13}\) ANAO, op.cit., p.28 and 29.
4.4 The ANAO considers that the risk that FBT is not paid on benefits provided is likely to be reduced where there are formal arrangements in place that provide for the area responsible for FBT administration to be advised of new benefits or changes to existing benefits that may have FBT implications.

Recipients of benefits

4.5 The ANAO found that all of the entities audited provided staff with information regarding the FBT and RFBA implications of receiving various benefits. The release of information generally occurred when a new benefit arose through either legislative change or changes to employment terms and conditions. Entities used various ways to communicate with employees including conducting awareness sessions, providing written guidance, using entity intranets and issuing circulars or newsletters.

ATO and external taxation advisors

4.6 Recognising the inherent complexity that can be involved with FBT legislation, the ANAO considers that, as the ATO is available to offer technical advice regarding FBT, entities should utilise this service, or other specialist tax advice, whenever necessary.

4.7 Two of the entities audited had either a specific contact at the ATO or had established working protocols for contacting the ATO regarding specific queries or to seek clarification on FBT related issues. Another entity used the ATO hotline to seek information or clarification of FBT issues. The remaining entity did not have regular contact with the ATO regarding FBT matters, but had engaged external tax advisors to assist with their FBT administration.

4.8 Two of the audited entities also advised that once they had researched an issue internally, they would then seek information and advice from external taxation advisors where necessary.

4.9 The ANAO considers entities should establish internal protocols that provide for all contact with the ATO and external taxation advisors in relation to FBT be advised to the work area with overall responsibility for the entity’s FBT return.

Recommendation No.12

4.10 The ANAO recommends that agreed formal communication arrangements in relation to FBT be established between staff responsible for the administration of FBT and other relevant work areas and the ATO.

Entities response

CSIRO

4.11 Agree.
Defence

4.12 Agree. The recommendation is already incorporated as part of Defence tax management best practice.

DFAT

4.13 Agree. DFAT representatives have met with representatives from the ATO to discuss relevant FBT issues, and were provided with a contact for any follow-up issues. Furthermore, the Taxation Manager consults with the FBT section of ATO as required.

RBA

4.14 The RBA accepts the recommendation and complies with it.

Sound and better practice

4.15 The sound and better practice identified by the ANAO in respect of information and communication arrangements included:

- designated staff authorised to contact the ATO on FBT issues;
- regular communication and agreed working relationships between all work areas that were involved in, or had responsibility for, the administration of FBT;
- employees being notified of their RFBA prior to the issue of payment summaries; and
- guidance provided to employees detailing the impact of their RFBA.
5. Monitoring and Review Processes

This chapter outlines the monitoring and review activity undertaken by the audited entities.

Background

5.1 Monitoring and review is the final component of an effective control framework. It is a key element of an entity’s continuous improvement process that helps ensure the entity implements effective processes and tools to monitor and review relevant data. An effective monitoring and review environment is based on an established chain of accountability and includes use of periodic reviews, such as those undertaken by internal audit and external consultants, as well as in-built review mechanisms. 14

Audit criteria

Table 5.1

| Audit Criteria | The entity would be expected to have regular monitoring and review processes designed to ensure that policies and procedures are adhered to and properly applied, and to identify changes and weaknesses in the operating environment. Effective monitoring and review processes are of particular relevance where the entity has outsourced elements of its FBT administration. This might be achieved by reporting, internal checking, external quality assurance reviews and auditing processes. |
| Source: ANAO |

Audit findings

5.2 Generally entities had implemented at least one of a range of review processes including:

- the peer review of work performed when collating data for inclusion in the FBT return;
- the analytical review of FBT return balances to identify and investigate significant movements between FBT balances compared with previous year’s returns; and
- an assessment of FBT implications resulting from new benefits or changes in legislation.

14 ANAO, op.cit., p. 33 and 34.
Analytical review

5.3 Analytical review which involves comparing current and prior year FBT balances can be an effective means of identifying significant or material movements and can be a useful tool in identifying omissions or errors in the compilation of the FBT return. Movements between current and prior year figures should be able to be explained through such factors as staff movements, legislative changes or amendments to an entity’s terms of employment. The ANAO noted that most of the audited entities had performed an analytical review that involved comparing variances from one year to the next, although only one had documented the reasons for any significant variances.

Internal review

5.4 The ANAO found, that in two of the entities audited, internal reviews or audits of FBT related controls and payments had been undertaken. The ANAO considers that the periodic audit review of FBT compliance can be an effective way of obtaining assurance about the effectiveness of an entity’s practices in this area and the extent of compliance with legislative requirements.

Project planning

5.5 The ANAO found that generally FBT returns had been submitted to the ATO on a timely basis. The ANAO also noted that the development of an overall project plan and the incorporation of target or milestone dates for FBT compliance processes in detailed FBT operating guidelines could assist entities in the timely collation of information and the submission of their FBT return.

Recommendation No.13

5.6 The ANAO recommends that entities enhance, where relevant, existing monitoring and review arrangements by:

• undertaking an annual analytical review of FBT balances that includes the analysis and documentation of the reason for any significant variances over-time; and

• subjecting FBT administration to regular review through, for example, internal audit coverage or other review arrangements.

Entities’ responses

CSIRO

5.7 Agree.
Defence

5.8 Agree. The recommendation is already incorporated as part of Defence tax management best practice.

DFAT

5.9 Agree. Annual analytical reviews of FBT balances will be undertaken, beginning with the 2004-2005 FBT return.

RBA

5.10 The RBA accepts the recommendation and complies with it.

Sound and better practice

5.11 The ANAO identified the following sound and better practice in the monitoring and review arrangements in the audited entities:

- the completion of an annual variance analysis to compare the balances on the FBT return with those of previous years;
- a program of internal review or internal audits of FBT related controls and payments;
- peer review of work performed when collating data for inclusion in the FBT return;
- obtaining external expert and technical advice and engaging external advisors to undertake a quality assurance review of the FBT return; and
- the periodic review of pay and conditions to assist in ensuring benefits are treated correctly for FBT purposes.

Canberra ACT
2 June 2005
Ian McPhee
Auditor-General
Appendices
Appendix 1: Entities’ responses to the audit report

This Appendix contains general comments received on the audit report that are not shown in the body of the report.

Each of the entities selected for audit and the ATO were provided with the opportunity to comment on the proposed audit report in accordance with the provisions of section 19 of the Auditor-General Act 1997.

Entities’ responses to the recommendations have been included in the main body of the report under the subheading ‘Entities’ responses’ directly following each recommendation. In addition to specific entity responses to each recommendation, general responses were also provided by CSIRO, Defence and the ATO. These general responses are reproduced below.

CSIRO

The report and recommendations provide a sound and better practice guide to improving the administration and legislative FBT compliance in Government agencies. CSIRO will use the specific audit findings relating to its FBT administration to address areas requiring improvement.

Defence

Defence appreciates the very thorough and detailed audit report that the ANAO has provided. The outcome for Defence is both positive and pleasing given the complex and diverse range of conditions and entitlements that apply to ADF members and civilian employees within the Department. Defence agrees with the ANAO’s overall finding that it commits significant effort to meeting its FBT obligations, and has established a number of sound and better practices in relation to the administration of FBT. Defence notes that the ANAO has identified a large number of sound and better practices in Defence’s administration of FBT processes.

Defence is committed to providing sound and robust management systems to comply with its taxation obligations and will continue to resource its Defence Tax Management Office (DTMO) to provide high quality levels of compliance service and tax advice to Defence. The DTMO is presently undertaking a review covering a range of issues related to FBT and remuneration programs and will incorporate the report’s recommendations as part of those processes.
ATO

We have reviewed the thirteen recommendations proposed in your report. The Tax Office agrees with each of the recommendations.

We look forward to the opportunity some of your recommendations will provide for us to work more closely with Australian Government organisations to assist them in complying with their FBT obligations. We are committed to helping taxpayers understand and comply with their tax obligations.
## Appendix 2: Audit criteria

<table>
<thead>
<tr>
<th>Control Framework</th>
<th>Audit Criteria</th>
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<tr>
<td><strong>Risk assessment</strong></td>
<td>At either an organisational or operational level the entity would be expected to have identified the risks associated with FBT processes and assessed those risks with respect to impact, likelihood and controls. This assessment could have included consideration of the complexities associated with the legislation, the need for appropriately skilled staff, consideration of an outsourcing option and a quality assurance function.</td>
</tr>
</tbody>
</table>
| **Control structure** (control environment and control activities) | The entity would be expected to have:  
- issued policy and guidance on FBT legislation to staff and FBT administrators;  
- substantiated requirements and determined responsibilities for managing the administration of FBT within the entity;  
- ensured that staff involved in the administration of FBT are appropriately skilled and that quality assurance processes are adequate;  
- systems for capturing and reporting FBT information in accordance with legislation, with close links between the general ledger and payroll management information systems; and  
- established specific controls for the administration of FBT incorporating authorisation and approval of FBT balances, identification, collection, calculation, reporting and remitting of FBT liabilities, including adequate verification procedures in relation to outsourced services. |
| **Information and communication** | The entity would be expected to have two way information flows between (a) the staff responsible for payment processing and those responsible for managing FBT and (b) the personnel/payroll section and individual employees. It is also important that the entity has communicated with employees the impact of electing to receive a particular benefit. |
| **Monitoring and review** | The entity would be expected to have regular monitoring and review processes designed to ensure that policies and procedures are adhered to and properly applied, and to identify changes and weaknesses in the operating environment. Effective monitoring and review processes are of particular relevance where the entity has outsourced elements of its FBT administration. This might be achieved by reporting, internal checking, external quality assurance reviews and auditing processes. |

Source: ANAO
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