

The Auditor-General

Audit Report No.23 1999–2000

Performance Audit

# **The Management of Tax Debt Collection**

Australian Taxation Office

Australian National Audit Office

© Commonwealth  
of Australia 1999  
ISSN 1036-7632  
ISBN 0 644 38828 5

This work is copyright. Apart from any use as permitted under the *Copyright Act 1968*, no part may be reproduced by any process without prior written permission from the Australian National Audit Office. Requests and inquiries concerning reproduction and rights should be addressed to  
The Publications Manager,  
Australian National Audit Office,  
GPO Box 707, Canberra ACT 2601.

Canberra ACT  
20 December 1999

Dear Madam 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 this report of this audit, and the accompanying brochure, to the Parliament. The report is titled *The Management of Tax Debt Collection*.

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



P. J. Barrett  
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.

Auditor-General reports are available from Government Info Shops. Recent titles are shown at the back of this report. For further information contact:

The Publications Manager  
Australian National Audit Office  
GPO Box 707 Canberra ACT 2601

Telephone (02) 6203 7505  
Fax (02) 6203 7798  
Email [webmaster@anao.gov.au](mailto:webmaster@anao.gov.au)

ANAO audit reports and information about the ANAO are available at our internet address:

<http://www.anao.gov.au>

### **Audit Team**

Richard Mackey  
Anna Przybylski  
Peter White

# Contents

---

Abbreviations/Glossary	7
<b>Summary and Recommendations</b>	
<b>Summary</b>	11
Background	11
Audit objective and approach	13
Overall conclusion	14
<b>Key Findings</b>	17
Overview of Tax Debt in Australia (Chapter 1)	17
Implementation of the recommendations from the Reports of the Auditor-General and the Joint Committee of Public Accounts (Chapter 2)	18
Debt management: Improved practices and reporting (Chapter 3)	18
Debt management: Better use of information (Chapter 4)	23
Acknowledgments	26
<b>Recommendations</b>	27
<b>Audit Findings and Conclusions</b>	
1. <b>Introduction and Overview of Tax Debt in Australia</b>	33
Introduction	33
The previous audit	34
Taxation debt in Australia: an overview	34
2. <b>Implementation of the recommendations from earlier reports of the     Auditor-General and of the Joint Committee of Public Accounts</b>	54
Implementation of ANAO recommendations	54
Implementation of JCPA recommendations	59
3. <b>Debt Management: Improved Practices and Reporting</b>	60
Introduction	60
Contestability of ATO debt collection	62
Opportunities for improvement	65
ATO performance information and reporting	66
Additional revenue opportunities	74
Outsourcing some ATO debt collection	85
Organisational arrangements	92
4. <b>Debt Management: Better Use of Information</b>	95
Systemic risks	95
The use of additional databases	99
Predictive compliance models	104
The use of credit reference databases	106
Quality Assurance (QA) programs	110
Persistent tax debtors	110

## **APPENDICES**

Appendix 1: The Compliance Model	119
Appendix 2: Implementation of ANAO recommendations	121
Appendix 3: Staff reductions as a result of changed Withholding Tax Arrangements	129
Appendix 4: The Ancient Debt Project	130
Appendix 5: Outsourcing the collection of tax debts	131
Appendix 6: COMPACT Problems: Data quality and other deficiencies	132
Appendix 7: Income tax debtors with investment accounts	135
Appendix 8: Payment of debt by instalments	137
Appendix 9: Tax Debtors who are Company Directors	140
Appendix 10: Individuals (Non-business) Income Tax Debtors: Untraceable Cases 30 June 1999	142
<a href="#">Index</a>	<a href="#">143</a>
<a href="#">Series Titles</a>	<a href="#">148</a>
<a href="#">Better Practice Guides</a>	<a href="#">150</a>

# Abbreviations/Glossary

---

ABS	Australian Bureau of Statistics
AIIR	Annual Income and Investment Reports
ANTS	“A New Tax System”
ASIC	Australian Securities and Investments Commission
AIS	ATO Integrated System
AQC	Australian Quality Council
ASL	Average Staffing Levels
ATLP	Additional Tax for Late Payment
ATO	Australian Taxation Office
AUSTRAC	Australian Transactions Reports and Analysis Centre
BAS	Business Activity Statement
COMPACT	Computer Assistance for the Collection of Taxes
CRF	Consolidated Revenue Fund
DoFA	Department of Finance and Administration
DWH	Data Warehouse
EPIP	Electronic Publishing Infrastructure Project
FBT	Fringe Benefits Tax
FBTAA	<i>Fringe Benefits Tax Assessment Act 1986</i>
FMAA	<i>Financial Management and Accountability Act 1997</i>
FTE	Full-Time Equivalent
GIC	General Interest Charge
GST	Goods and Services Tax
HIC	Health Insurance Commission
INB	Individuals Non Business
IT	Income Tax
IVR	Interactive Voice Recognition
ITAA	Income Tax Assessment Acts
JCPA	Joint Committee of Public Accounts (now JCPAA (Joint Committee of Public Accounts and Audit))

Kdnet	Knowledge development network
LB&I	Large Business and International
NTS	National Tax System
NZIRD	New Zealand Inland Revenue Department
OLAP	On-Line Analytical Processing
PAYE	Pay-As-You-Earn
PAYG	Pay-As-You-Go
PBS	Portfolio Budget Statement
PDI	Public Debt Interest
PPS	Prescribed Payments System
QA	Quality Assurance
QC	Queen's Counsel
QPT	Quarterly Provisional Tax
RBA	Running Balance Account
RM	Receivables Management
RMS	Receivables Management System
RPS	Reportable Payments System
SB	Small Business (formerly SBI: Small Business Income)
SES	Senior Executive Service
TAA	<i>Tax Administration Act 1953</i>
TFN	Tax File Number
WHT	Withholding Taxes



# Summary and Recommendations



# Summary

---

## Background

1. As the Commonwealth's principal revenue collection agency, the Australian Taxation Office (ATO) accounted for total net taxation revenue of \$135.3 billion in 1998–99.<sup>1</sup> There are two main types of taxes: those that are paid annually (such as income tax) and those that are paid throughout the year on a recurring basis. There are also two main types of taxpayers: individuals and businesses. This differentiation between types of taxes and taxpayers is reflected in the structure of the ATO, which is organised into business lines, supported by a number of service lines.

2. The debt collection function in the ATO is integral to the 'new tax system' of wider taxation reform. 'Debt collection' has been restyled as 'receivables management.' Receivables management includes all the processes, interactions, products and activities involved in managing the lodgment and payment obligations of a known taxpayer.<sup>2</sup> This Report is largely about receivables management as an ATO-wide activity rather than as a function performed by a particular business line or work stream. There are a range of receivables management/debt collection systems, procedures, strategies and the receivables management policy, which are all based on a single coherent framework that is common to the business lines in which the receivables management function is performed. The audit's analysis, findings and recommendations in relation to these activities have been presented across-the-board rather than specifically for particular business lines.

---

<sup>1</sup> ATO's *Annual Report 1998-99* Financial Statements for the year ended 30 June 1999, p.143. Includes some \$9.7 billion in Excise duty.

<sup>2</sup> ATO define 'receivables management' in this way: *it "...is all the processes, interactions, products and activities involved in managing the primary obligations (ie. lodge and pay) of a known client, from before the liability arises to collection of the debt, for example, advising tax liabilities, managing debts, collecting money, securing lodgment of returns, chasing outstanding debts. Managing receivables also includes the supporting business systems."* *ATO Debt Collection Initiatives: "Receivables Management"* Speech by Erin Holland (Assistant Commissioner responsible for the Receivables Management Stream) to the International Debt Collection Benchmarking Workshop Edinburgh 7 to 10 March 1999. It is to be noted that the management of receivables starts before a liability is incurred. It commences as soon as there is an obligation to consider a tax responsibility. For example, as soon as a company registers for business it has an obligation to consider its tax responsibilities and how they will be met. The ATO, at the same time, needs to consider ways to ensure that the company complies with its obligations. This involves pro-active provision of information and collection of data, as well as the collection of revenue.

**3.** As the ATO administers two broad types of taxes, income tax and the recurring taxes, there are two types of overdue tax debts.<sup>3</sup> Debt referred to ATO's computer based tax debt collect system (COMPACT) for collection by the ATO's receivables management function for 1998–99 was in the order of \$17.6 billion. The amount of debt finalised in 1998–99 was about \$15.5 billion. Disputed debt on hand increased 32 per cent from \$3.3 billion to \$4.3 billion.

**4.** Tax debt collection occurs at the end of the tax administration cycle as it arises only when taxpayers have not complied with their lawful obligation to pay assessed tax. A substantial proportion of ATO's resources is expended on the earlier stages of this cycle. Parliament expects all taxpayers to meet their taxation obligations as and when they fall due and has passed laws that require this. The ATO has the powers and resources to enforce these laws.

**5.** The integrity of the Australian tax system depends, amongst other things, on the extent of compliance by the community. The integrity, therefore, may be weakened as compliance weakens. In recognition of the continuing need to improve the integrity of the tax system, the ATO has developed a framework within which it manages all client relations. This is known as the Compliance Model. It is a strategic approach based on the comprehensive understanding of people's compliance with the law.

**6.** The Compliance Model recognises that the vast majority of taxpayers comply voluntarily with no need for ATO intervention. Others comply but need some assistance or prompting. A small proportion will not comply voluntarily and enforcement action may be required. ATO's strategic approach is designed to ensure that the debt collection action selected for a particular debtor is the most appropriate one.

**7.** The ATO is in an environment of extensive administrative and taxation policy reform. ANAO acknowledges the inevitable impact of this on the ATO's conduct of its on-going business. This audit examines a relatively small (but important) facet of tax administration. We are mindful that senior management determines priorities across a broader canvas of issues than those within our focus for this audit.

**8.** In relation to tax debt collection, the ATO has reinforced that it operates in an environment that is substantially different from commercial debt collection firms. The ANAO notes that the ATO considers broader

---

<sup>3</sup> Throughout this Report the phrase "recurring taxes" is used to refer to those taxes where the liability to lodge and/or remit is recurrent in nature. These include Sales Tax, Pay-As-You-Earn, the Prescribed Payments System, and the Reportable Payments System.

social issues and believes that a \$ expended to \$ collected equation, which applies in a commercial environment, should not be the sole consideration for the ATO.

9. The ANAO conducted a performance audit of tax debt collection in 1996–97 that was reviewed by the then Joint Committee of Public Accounts (JCPA).<sup>4</sup> The ATO agreed with the recommendations of both the ANAO and the JCPA.<sup>5</sup> In providing feedback to the Auditor-General on the ANAO’s proposed Performance Audit Work Program in June 1998, the Joint Committee of Public Accounts and Audit (JCPAA) requested that the ANAO conduct a follow up audit of ATO debt collection by nominating it as one of the audit priorities for 1998–99.<sup>6</sup>

## Audit objective and approach

10. The objectives of this audit were to improve:

- the accountability to Parliament and the Government of the ATO by the provision of advice that follows up on the ATO’s implementation of the previous ANAO Report and on the recommendations of the then Joint Committee of Public Accounts arising from its consideration of that Report; and
- the efficiency, effectiveness and equity of debt collection by the ATO.

11. In order to address the objectives of this audit we have reviewed ATO’s implementation of the recommendations of our 1996 Report and of the subsequent Report of the JCPA. The follow-up audit process reinforces the ANAO’s commitment to improving public administration and accountability through monitoring the progress of audit recommendation implementation. It is apparent that accepted recommendations are only effective when actually implemented. Improved performance is clearly foregone by partial, unnecessarily delayed or quasi-implementation.

12. The context and operation of tax debt collection administration have changed significantly since our 1996 Report. Consequently we reviewed all the main features of the current approach. We examined the scope for improvement in the following areas:

- receivables management performance information and reporting;

---

<sup>4</sup> Now retitled the Joint Committee of Public Accounts and Audit (JCPAA) as a result of the enactment of the *Auditor-General Act 1997*.

<sup>5</sup> *Joint Committee of Public Accounts Report 352, Review of Auditor-General’s Reports 1996–97, Second Quarter* September 1997.

<sup>6</sup> Letter from Chairman JCPAA to the Auditor-General dated 22 June 1998.

- the collection of more tax debt and in a more timely manner;
- outsourcing the collection of some debt;
- the better use of databases and the use of additional databases; and
- quality assurance systems.

## Overall conclusion

**13.** The ANAO has found that the ATO has implemented, or begun to implement, most of the recommendations from the 1996 ANAO audit of ATO's tax debt collection and from the subsequent JCPA Report. Due to the changes in structure and to the impact of taxation reform, some of the recommendations from 1996 have been superseded in their application to tax debt collection. The ATO has achieved better business systems, more cost-effective collections, better performance information and research and has come to a resolution on the problems of applying additional tax for late payment penalties.

**14.** The ATO has improved efficiency, effectiveness and equity in its administration of tax debt collection in the three years since the last Report. The ATO has achieved these improvements at the same time that its resourcing of the receivables management function has decreased by 20 per cent. The ATO has recently been targeting areas such as the cash economy, aggressive tax planning, and tax avoidance and evasion. This has resulted in the raising of almost 30 per cent more debt in 1998–99 than in prior years. At the same time, the ATO has reduced the amount of debt written off, and increased the value of debt finalised during the year by eight per cent.

**15.** The net cost of ATO's receivables management service to the Commonwealth Government was approximately \$142.2 million in 1998–99. On 8 November 1999 the Commissioner of Taxation announced his intention to increase the resources allocated to the receivables management function in 1999–2000, 2000–2001, and 2001–2002 by \$10 million per annum for each of the three years. The result will be an increase to the numbers of staff that would be allocated to the receivables management function, as prior to this announcement the total numbers of staff had been reduced by about seven per cent. The ATO considers that this increase, combined with the Receivables Management System currently under development, should greatly increase the ATO receivables management capacity. As a result, in 1999–2000 the net cost of ATO's receivables management service to the Commonwealth Government will be about \$150.1 million and about 2239 FTE staff will be employed on the function.

**16.** We consider that there is limited scope for improved debt collection performance within the existing legislative framework without additional resources being allocated to this function. The assessment of the precise scope for improved performance is limited in part because the full benefits of the initiatives taken by the ATO in response to the ANAO and JCPA reports will take some time to be fully achieved. Nevertheless, there is scope for improvement in a range of debt collection practices, including the tracing of apparently untraceable debtors; improving write-off practices; reducing the time taken to finalise debt; and improving lodgment behaviour of some taxpayers, particularly some business taxpayers; and generally by the implementation of the 10 recommendations of this Report. In some of these areas, the ATO could move to achieve standards of performance characteristic of the private sector. The ANAO considers that there is scope for positive revenue returns to the Commonwealth by ATO having greater response flexibility (comparable to that of the private sector) in relation to the behaviour of some tax debtors.

**17.** Additional revenue of about \$100 million could be collected from unactioned collectable aged debt, given an additional investment in ATO's receivables management function. Additional revenue of about \$20 million could be collected from the debt written off as uneconomic to collect, with a further investment in ATO's receivables management function. During the audit ATO advised that the additional investment in receivables management required to collect the total of \$120 million would be in the order of \$7 million. As mentioned above, towards the completion of the audit, the Commissioner of Taxation allocated an additional \$10 million per annum to the receivables management function for each of the next three years.

**18.** Whilst the receivables management reforms are directed at improving the management of debt collection risks, the better use of databases (some of which belong to agencies other than the ATO) would improve the ATO's capacity to manage two risks that might impact on ATO's debt collection performance over the next three years. One concerns ATO's computer systems, particularly their capacity to carry out to a satisfactory standard both existing and new, legislated functions. The other concerns the impact of the new accountabilities, systems and workloads associated with ongoing legislative change to taxation administration.

**19.** The better use of the full range of databases to which the ATO has, or could have, access would probably improve ATO's capacity to better manage some of the main risks. Improving quality assurance

systems along similar lines of financial institutions in the private sector could provide improved assurance that risks associated with systems and data are better managed. Adopting our recommendations would increase the range of compliance strategies available to the ATO and improve the overall cost-effectiveness of the operation of the Compliance Model in ATO administration.



# Key Findings

---

## Overview of Tax Debt in Australia (Chapter 1)

### Taxation debt in Australia: Statistical overview

**20.** Since 1990 there has been a steady increase in the amount of debt referred to COMPACT for collection and also in the number of cases finalised. Although the number of cases of tax debt has increased, the level of cases remaining at the end of each period has remained at a similar level, although the dollar value of this debt has risen over this time. Of the total debt on hand, the amount that has been on ATO's books for more than 90 days has been increasing over time. Whilst the amount of debt written off by the ATO has been fairly constant over the years 1994–95 to 1997–98, it has decreased significantly in the latest year, 1998–99.

**21.** There were 349 238 active tax debtors at the end of the 1998–99 financial year and the ATO had initiated action on 80 per cent of them.<sup>7</sup> The total number of cases carried a total debt of \$7.4 billion. ATO advise that about 60 per cent of this is not collectable immediately because it is the subject of dispute between the ATO and the taxpayers concerned. The remaining 40 per cent (ie. about \$3.1 billion) is collectable. "Collectable" in this context means that there are no legal or other impediments to the collection of the debt. The remaining 20 per cent of the cases consisted of a mix of cases on which initial action had been taken or on which no action had been taken.<sup>8</sup>

**22.** Most active debt has been on ATO's books for 90 days or more and is referred to as aged debt. Our analysis of total aged collectable debt showed that 55 per cent has been actioned; initial action had been taken on 38 per cent; and just under seven per cent (ie. \$154 million) is unactioned.<sup>9</sup>

---

<sup>7</sup> ACTIVE cases are those currently subject to collection action; that is they have not been finalised. Examples of active cases include cases under arrangement, cases subject to legal action, cases subject to negotiation.

<sup>8</sup> INITIAL ACTION. This means that the ATO has initiated some action as a step towards the collection of the debt. Examples of initial action include direct contact established with the tax debtor, the commencement of tracing action and the issuing of an initial demand. In many instances a debtor on whom initial action had been taken would have received the Notice of Assessment, and a Final Notice. In some instances the debtor would have also received a Standard Letter.

<sup>9</sup> UNACTIONED means that no action had been taken on the debt since it had been referred to COMPACT for collection. Our initial research indicated that the total amount of unactioned debt was \$673 million. In response to this indicative finding, ATO advised that \$528 million of disputed debt had been incorrectly coded as "unactioned" on COMPACT. We accepted ATO's advice. This is a quality assurance issue that is being progressively addressed through new quality assurance and data cleansing processes.

**23.** Almost all of the unactioned debt has been on ATO's books for between 90 days and two years. It consists of 30 203 cases with an average debt of about \$5000. ATO advise that about 70 per cent (ie. \$100 million) of this could be collected if action was now taken. We understand that unless such action is taken, much of it would be written off. We consider that the ATO should take steps to collect all unactioned debt, and suggest a range of options to support the ATO's capacity to do so. There may also be scope for additional recovery rates from the debt on which only initial action had been taken.

**24.** Our review of the structure of disputed debt showed that a very small number of cases carry a very large amount of debt. For example, almost \$1.8 billion debt is currently tied up in only 35 cases. On the basis of current disputed debt proceedings, the ATO expects to collect no more than about \$1.3 billion of the \$4.9 billion of disputed debt once all of the cases currently under dispute are settled.<sup>10</sup>

## **Implementation of the recommendations from the Reports of the Auditor-General and the Joint Committee of Public Accounts (Chapter 2)**

**25.** The ANAO has found that the ATO has implemented or begun to implement most of the recommendations from the 1996 ANAO audit of ATO's tax debt collection and the subsequent JCPA Report. Due to internal administrative changes in the ATO and the impact of changes to taxation legislation, some of the recommendations from 1996 have been superseded in their application to tax debt collection. The ATO has achieved better business systems, more cost-effective collections, better performance information and research and has come to a resolution on the problems of applying penalties.

## **Debt management: Improved practices and reporting (Chapter 3)**

### **Improved efficiency, effectiveness and equity**

**26.** The ATO has improved efficiency, effectiveness and equity in its administration of tax debt collection in the three years since the last Report. The ATO's has achieved these improvements at the same time that its level of resourcing of the receivables management function has

---

<sup>10</sup> The total amount credited to taxpayers once a dispute is determined in the favour of a taxpayer is recorded in the ATO's financial statements as the provision for credit amendments. In the financial statements for the year ended 30 June 1999, \$3 016 558 was recorded against this entry.

decreased by 20 per cent. The ATO has recently been targeting areas such as the cash economy, aggressive tax planning, tax avoidance and evasion. This has resulted in the raising of almost 30 per cent more debt than in prior years. At the same time, the ATO has reduced the amount of debt written off and increased the value of debt finalised during the year by eight per cent.

### **Improved response flexibility**

**27.** The increased flexibility of ATO's response to the wide variety of tax debtor behaviour is an important gain from the initiatives taken in response to ANAO's 1996 Report. The ATO is increasingly able to use the debt collection strategy that is the most likely, and in a more cost-effective way, to recover a debt. Some of these initiatives are in the early stages of implementation, whereas others are more advanced. As they take effect, the gains to efficiency, effectiveness and equity could be expected to improve.

**28.** The initiatives being taken also improve management's capacity to match levels of resources for receivables management to desired levels of productivity, efficiency, effectiveness and equity. This gives greater flexibility to top management in the complex task of resourcing the various functions of the ATO, particularly in this period of significant change to taxation legislation.

### **Improved risk management**

**29.** ANAO found that in the past the ATO had, in the main, managed debt cases by debt level rather than by a more careful analysis of debt risk. Competing priorities from a mix of site based management accountabilities amongst ATO offices around Australia also had a bearing on the actioning of debt cases. As a result, there were relatively high amounts of aged debt in the lower level debt cases. We found that the actioning of lower level debt had received lower priority in preference to actioning the higher level debt.<sup>11</sup> Consequently, there is a proportion of lower level undisputed debt that has not been actioned at all.

**30.** ANAO is satisfied that, as a result of the introduction of the initiatives taken in response to the ANAO and JCPA reports, the collection of debt by the ATO is now increasingly being based on a satisfactory analysis of debt risk.

---

<sup>11</sup> The ATO classifies debt into six levels. These levels and the numbers of debtors and the amounts of debt within them are shown in Tables 1 and 2 of Chapter One. "Lower levels" refers to tax debt less than \$25 000.

## **Contestability of ATO debt collection**

**31.** The ATO considers that it is achieving a level of performance that is contestable with its counterparts in the finance sector. Notwithstanding this, the ANAO has identified a number of areas that, if addressed, could further improve ATO debt collection outcomes.

**32.** The ATO undertook an international benchmarking initiative in 1997 of receivables management processes known as the *Receivables Management Benchmarking: Critical Best Practice Guide*. The ATO is currently working with the Australian Quality Council (AQC) to develop a set of measures of operational performance for general use in the receivables management industry. These include measures such as the cost of debt collection services, stock and flow measures and the age of debt. This work has the potential to improve the transparency and accountability of ATO receivables management to the extent that it provides national (and possibly, international) performance benchmarks.

**33.** ANAO strongly supports the ATO's benchmarking studies and considers that the development of a standardised set of performance measures should improve the ATO's ability to demonstrate its efficiency, effectiveness, equity and contestability with market best practice.

**34.** We found that the ATO's debt collection performance compares well with the standards set by the New Zealand Government for the New Zealand Internal Revenue Department. We found that the ATO has finalised 75 per cent of debt within six months (and 82 per cent within 12 months) of it being identified as overdue. The equivalent NZ standard is 65 per cent and 85 per cent respectively. We found that the ATO collected \$A47 of tax debt for each dollar of expense. The NZ standard is \$NZ50. We also found that the level of collectable debt was 2.05 per cent of the total revenue collected.<sup>12</sup> The NZ standard is three per cent.

## **ATO performance information and reporting**

**35.** We found that there is scope for improving the range and quality of the information published about ATO's debt collection performance. There are two main sources of public information about the performance of the ATO generally and of debt collection in particular. These are Portfolio Budget Statements (PBSs) and the Tax Commissioner's Annual Report.

**36.** The ATO advises that it has recently reached agreement with DoFA that less detailed specifications at the PBS level are preferable to more

---

<sup>12</sup> As measured by the COMPACT case management system.

because this enables the ATO to adopt a more flexible approach to its resource management. Executive management has greater flexibility to resource those areas of administration that risk assessment shows are highest priority. ANAO accepts that this strategy allows the ATO to adopt a more flexible approach to administration and to better identify risk areas than would be possible if there were greater specification. However, during recent Senate Committee hearings into the Budget Estimates 1999–2000 concern was expressed about the lack of detail in PBSs.<sup>13</sup> Insufficient detail can hinder good accountability.

**37.** There are some shortcomings in the current high level measures of performance published in the PBS with regard to debt collection. ‘Reduction in overdue debt’ is an effectiveness measure published in the PBS. It is used to assess the achievement of the single Government outcome to which the ATO contributes. This Government outcome is: *Effectively managed and shaped systems that support and fund services for Australians and give effect to social and economic policy through the tax system.*<sup>14</sup> The measure is also used to assess the efficiency of ATO’s production of output. The PBSs identify four distinct outputs and their related appropriations, as submitted to Parliament for approval.<sup>15</sup> The measure, ‘reduction in overdue debt’, is an ambiguous measure of performance. For example, variations in the amount of debt in a given year do not necessarily point to effectiveness or efficiency changes in the same direction as the variations. The ATO could produce more reliable high level measures of performance for inclusion in the PBS that use changes in the amount of overdue debt by having a suite of more informative measures to draw upon.

**38.** ATO could also improve the range and quality of performance information published in the Annual Report for 2000–01 by publishing the key objectives of receivables management performance in the Small

<sup>13</sup> Budget Estimates 1999-2000 Report Senate Finance and Public Administration Legislation Committee June 1999; Budget Estimates 1999-2000 Report Senate Economics Legislation Committee June 1999.

<sup>14</sup> *The Portfolio Budget Statements 1999-2000: Treasury Portfolio*, Budget Related Paper No. 1.16, p. 77

<sup>15</sup> ATO’s four outputs and the appropriation for each of them for 1999-2000 are:

OUTPUT	APPROPRIATION (\$)
Contribution to Policy Advice and Legislation	78 920 000
Income and other taxes	1 347 645 000
Transfers	86 813 000
Cross Agency Support	79 826 000
Total	1 593 204 000

Source: *The Portfolio Budget Statements 1999-2000: Treasury Portfolio*, Budget Related Paper No. 1.16, p. 85.

Business and Individuals Non Business business lines that currently guide performance and the performance achieved in relation to those objectives.<sup>16</sup> ANAO considers that the ATO should provide more information about debt in relation to category of debt and time taken to process.<sup>17</sup> Any amounts of unactioned collectable debt should also be reported showing the length of time it has remained unactioned. In addition, the ATO should continue to publish in the Annual Report information about tax debt that relates more to the overall performance of the ATO than solely to the performance of the receivables management function.

## **Outsourcing**

**39.** The ANAO found that there is merit in exploring further the scope for outsourcing some aspects of receivables management work. This scope would depend on, amongst other things, outsourcing generating better returns than current practices whilst still meeting the standards of performance specified in the Taxpayers' Charter. We note that Centrelink has a flexible debt collection strategy that involves outsourcing the collection of some debts to mercantile agents. These are debts owed by former recipients of income support assistance that Centrelink regards as uneconomic to recover because of the cost involved in trying to trace and locate the debtors.

**40.** ANAO identified a potential shortfall of \$120 million revenue in the collection of unactioned aged debt or tax debts that have been written off as uneconomical to collect. This shortfall might well be cost-effectively managed by outsourcing the collection of these debts to commercial collection firms. However, the ATO might wish to explore the scope for additional internal efficiencies or the reallocation of resources from lower priority work in order to address this shortfall. There may also be scope for outsourcing the collection of lower level income tax debts from businesses.

**41.** The ATO and Centrelink have some debtors in common. Accordingly, there would be merit in the ATO evaluating the scope for a strategic partnership with Centrelink for collection of lower level income tax debts, particularly of taxpayers in receipt of income support payments, provided that the privacy of clients would remain protected and the standards of performance specified in the Taxpayers' Charter could continue to be achieved.

---

<sup>16</sup> These are stated in paragraphs 3.40 and 3.42.

<sup>17</sup> Categories include: proportions of active, collectable, finalised and unactioned debt in relation to the time taken to process, and the amounts of debt written off as per the FMAA categories of: write off authorised by another Act; debt not lawfully recoverable; and recovery of debt not economical.

## Gainsharing

**42.** ANAO was advised that, in the private sector, gainsharing within a firm of some of the firm's debt collected by the debt collection group is a common practice. Gainsharing is the retention of some revenue by the debt collection group as an incentive to enhance debt collection performance. Gainsharing may also be used to finance the deployment of additional resources to collect additional debt. This means that the private sector counterpart of the ATO's receivables management function may have greater incentives to achieve better practice, as well as greater flexibility to do so.

**43.** In Commonwealth administration, all the revenue collected by the ATO is paid into the Consolidated Revenue Fund. ATO's income comes from parliamentary appropriations. The Government has recently introduced an accruals-based outputs and outcomes budget framework for budget sector agencies. Under this framework, the appropriations relate to the achievement of Government outcomes by agencies' provision of agreed output.

**44.** Any gainsharing arrangement in the public sector would therefore have to be established within the public sector resource management framework. It would also have to have regard to two key aspects of current arrangements. These are the revenue levels the ATO is expected to achieve with the resources currently appropriated and the Commissioner's need for flexibility in addressing risk areas and managing the tax system as a whole. Gainsharing, or an equivalent incentive regime, may present an opportunity to improve efficiency, but would require resolution of associated policy and administration issues.

## Debt Management: Better use of information (Chapter 4)

### The better use of databases

**45.** We found that there is a range of databases that would help the ATO obtain more accurate and comprehensive information about a tax debtor's assets, financial situation and location. Although the ATO does have access to many of the external databases that would assist in the pursuit of some debtors, we consider that the cost effectiveness of receivables management would be improved by the systemic and the more automated use of most of them. There is a range of databases either in the possession of the ATO or available from State and/or Commonwealth Government authorities. As a first step in this direction, a number of research projects are outlined in the Report. The main purpose of these would be to evaluate the cost effectiveness of various approaches.

**46.** We undertook several data matching studies as part of this audit. Amongst other things, these indicate that there may be merit in the ATO adopting debt collection strategies appropriate for a whole class of tax debtors that focus on the primary obligation compliance of whole entities and whole classes of entities sharing common business characteristics. Such debtors have many characteristics in common, and there would be economies of scale in examining them on the proposed basis rather than on a case by case basis with the attendant additional risk of variable practice amongst ATO offices. In order to develop these strategies it would be necessary to pursue research that focuses on a whole of debtor perspective for high level debtors with complex arrangements involving associated entities.

**47.** ANAO was advised that a standard practice amongst credit providers in the private sector is the use of the databases of credit reference bureaux. Such firms generally use these databases in two ways, subject to statutory regulation. In some instances, the names and details of debtors with debts outstanding for greater than 90 days are listed with the databases. Private sector experience, as conveyed to ANAO, is that debts are paid much more promptly when a firm advises a debtor that listing may soon take place. Firms also access the databases to obtain information about a prospective client's or a debtor's credit rating. We have been advised that the use of the databases in these ways has had a significant impact on the expeditious recovery of debt.

**48.** While there is scope for improving the cost effectiveness of ATO's debt collection by the ATO having access to credit reference databases, such an approach raises policy issues that would require consideration by Government. Current legislation does not allow the ATO to use the credit reference databases. If the ATO were to use credit reference bureaux as do financial institutions that are credit providers, the *Privacy Act 1988*, the *Taxation Administration Act 1953* and the *Income Tax Assessment Acts* would require amendment. There would be issues associated with the release of taxation information and with the status of the ATO in relation to the databases. Current legislation restricts access to credit providers and we have been advised that the ATO is not considered to be a credit provider. An evaluation of the likely gains to effectiveness, as well as issues affecting taxpayers from such an approach, would be required.

### **Quality assurance**

**49.** The range of quality assurance initiatives now underway within the ATO could be more securely connected to industry better practice quality assurance standards. By aligning its QA programs more closely



with ABS statistical sampling methodology and better practice in the finance sector, the ATO could provide an improved assurance that its data and systems are of industry better practice standard.

### **Persistent tax debtors**

**50.** ATO research shows that there are three professional groups (lawyers, accountants and medical practitioners) with an average level of tax debt that is nearly five times the national average (barristers nearly ten times the national average). Whilst the average level of debt per occupation is only 2.6 per cent, over 20 per cent of taxpayers in these professions are tax debtors. In December 1997 the ATO established a project focussed on the legal profession. The project aimed to better understand the high level of debt established by the legal profession, to examine other compliance issues and to seek best practice in the collection of the profession's debts. By drawing on this project, we found that there is a group of taxpayers whose non-compliant behaviour presents the ATO with a significant risk management challenge. ATO advised that tax debtors who are legal professionals are an Australia-wide problem for the ATO in respect of the size of the debts, the number of the debts, the deteriorating tax compliance behaviour of some barristers, the time and cost of collection and their impact on other taxpayers. The ATO also advise that the great majority of taxpayers in the legal profession comply fully with Commonwealth law and do not present any compliance problem to the ATO in respect of the lodgement of tax returns, the payment of recurring taxes and the payment of tax debits.

**51.** ANAO noted the number of high-income persons with high levels of tax debt who have avoided the payment of their tax. The ATO has found that a relatively small number of high-income debtors (with substantial tax debts) use bankruptcy as a means of avoiding tax. It is a device used almost exclusively by high-income professionals, whose source of income is largely fee for service. This has no bearing on their continuing employment and receipt of substantial incomes. The ability of some debtors to continue in their profession regardless of bankruptcy or conviction for breaches of tax law assists them avoid the payment of tax. That a sizeable proportion is in professions that can promote or undermine the integrity of the tax system is also noted. The Commissioner of Taxation has recently expressed concern about this behaviour.<sup>18</sup>

---

<sup>18</sup> "A Question of Balance" Michael Carmody, Commissioner of Taxation. Address to the American Club 17 September 1999, p. 15.

**52.** ANAO considers that the incidence and nature of the avoidance of tax liabilities by some taxpayers such as those reviewed may raise questions about tax law and administration that warrant closer attention. There is now a need to examine the best methods to address these compliance problems.

**53.** ANAO found that ATO's analysis of the tax minimisation techniques used by some tax debtors has resulted in the ATO being able to put to Government options for the closure of some legislative loopholes. Some tax debtors had exploited such loopholes.

## **Acknowledgments**

**54.** The ANAO formally recognises the substantial contribution of the ATO officers who assisted in the conduct of this audit, especially for the assistance with the quantitative studies used in this audit.

## Recommendations

Set out below are the ANAO's recommendations aimed at improving the ATO's administration of the collection of taxation debt. Report paragraph references and abbreviated ATO comments are also included. More detailed responses are shown in the body of the Report. The ANAO considers that the ATO should give priority to recommendations 1, 4, 5, and 8.

**Recommendation No.1**  
**Para. 3.52** The ANAO recommends that the ATO improve the range and quality of information published about receivables management outcomes and outputs. Particular attention should be paid to:

- the examination of alternative performance measures that use debt at the Portfolio Budget Statement level; and
- the publication in ATO's annual report of key comparative information about the contestability of ATO receivables management performance.

**ATO Response:** Agreed

**Recommendation No.2**  
**Para. 3.53** The ANAO recommends that the ATO improve the accuracy of the measurement of the net cost of debt collection services by excluding the cost of other major receivables management services.

**ATO Response:** Agreed

**Recommendation No.3**  
**Para. 3.73** ANAO recommends that the ATO issue operational guidance to staff as to the meaning of 'recovery of the debt is not economical' in section 47 of the *Financial Management and Audit Act 1997*.

**ATO Response:** Agreed

**Recommendation No.4**  
**Para. 3.106** ANAO recommends that the ATO outsource the collection of some tax debt if the evaluation of outsourcing shows that it is cost effective and that compliance with the Taxpayers' Charter would be maintained.

**ATO Response:** Agreed

**Recommendation No.5  
Para. 3.108** ANAO recommends that the ATO explore opportunities for a strategic partnership with Centrelink, (consistent with the requirements of the Taxpayers' Charter and privacy arrangements) for the collection of some lower level tax debts for some of the clients that the two agencies have in common.

***ATO Response:*** Agreed

**Recommendation No.6  
Para. 4.37** ANAO recommends that the ATO adopt research-based debt collection strategies appropriate for a whole class of high level debtors with complex arrangements involving associated entities that focus on the primary obligation compliance of entities and classes of entities sharing common business characteristics.

***ATO Response:*** Agreed

**Recommendation No.7  
Para. 4.45** ANAO recommends that the ATO evaluate the cost effectiveness of making more systemic use of relevant databases in tax administration on a national basis. Relevant databases include, but are not limited to AIIR, ASIC, AUSTRAC, HIC, land titles offices, valuers-general, and registrars of motor vehicles, births, deaths and marriages.

***ATO Response:*** Agreed

**Recommendation No.8  
Para. 4.60** ANAO recommends that the ATO evaluate the effectiveness of accessing the databases of credit reference bureaux, having regard to the sensitive policy issues involved.

***ATO Response:*** Agree

**Recommendation No.9**  
**Para. 4.63** ANAO recommends that the ATO align its QA programs more closely with ABS statistical sampling methodology and better practice in the finance sector so that it can provide an improved assurance that its systems and data are of industry better practice standard.

***ATO Response:*** Agreed

**Recommendation No.10**  
**Para. 4.76** ANAO recommends that the ATO identify the best methods to address the compliance problems raised by its research into persistent tax debtors.

***ATO Response:*** Agreed



# Audit Findings and Conclusions





# 1. Introduction and Overview of Tax Debt in Australia

---

*This Chapter provides background to the audit, including an overview of the original Tax Debt Collection audit report and reasons for its follow-up. This Chapter also contains a descriptive overview of the tax debt collection function of the Australian Taxation Office including the legislative framework and an overview of key tax debt statistics. An overview of the scope, methodology and approach of the audit and of the structure of this Report is also included.*

## Introduction

### Background to the audit

**1.1** The ANAO conducted a performance audit of tax debt collection in 1996–97. The Report of that audit was tabled in Parliament in November 1996.<sup>19</sup> The Report made 29 recommendations for the improvement of tax debt collection. The ATO agreed with all the recommendations.

**1.2** In 1997, the then Joint Committee of Public Accounts (JCPA) conducted a review of that audit.<sup>20</sup> The Committee endorsed ANAO's recommendations, but also emphasised that ATO should improve the equity of its administration, particularly regarding the imposition of the additional tax on late payments, and use of risk management. In its Report, the JCPA made three additional recommendations.<sup>21</sup> These were also agreed to by the ATO.

**1.3** In providing feedback to the Auditor-General on the ANAO's proposed Performance Audit Work Program in June 1998, the Joint Committee of Public Accounts and Audit (JCPAA) requested that the ANAO conduct a follow up audit of ATO debt collection by nominating it as one of the audit priorities for 1998–99.<sup>22</sup>

---

<sup>19</sup> Auditor-General Audit Report No. 13 1996–97 Performance Audit, *Tax Debt Collection - Australian Taxation Office*, AGPS, 1996.

<sup>20</sup> Now retitled the Joint Committee of Public Accounts and Audit (JCPAA) as a result of the enactment of the *Auditor-General Act 1997*.

<sup>21</sup> *Joint Committee of Public Accounts Report 352, Review of Auditor-General's Reports 1996–97, Second Quarter* September 1997.

<sup>22</sup> Letter from Chairman JCPAA to the Auditor-General dated 22 June 1998.

## The previous audit

**1.4** In undertaking the 1996 audit, the ANAO sought to assess how efficiently and effectively the ATO managed its collection of outstanding tax debt, and provided recommendations. The audit examined key aspects of the tax debt collection process and areas that support the management of the debt collection process.

**1.5** The Report contained specific recommendations about how performance in these areas might be improved. Most of the recommendations were directed at maximizing the amount of debt collected. They addressed such issues as better business and IT systems, better quality data, better performance information and the use of it by ATO management. They also addressed better risk management, the major updating of ATO debt management policy and practices, standards and quality assurance systems, improved recovery systems and improvements in the timeliness of debt recovery.

## The audit purpose, scope and methodology

**1.6** The objectives of this audit were to:

- improve the accountability to Parliament and the Government of the ATO by the provision of advice that follows up on the ATO's implementation of the previous ANAO Report and on the recommendations of the then Joint Committee of Public Accounts arising from its consideration of the Report; and
- improve the efficiency, effectiveness and equity of debt collection by the ATO.

**1.7** The follow-up audit process also reinforces the ANAO's commitment to improving public administration and accountability through monitoring the progress of audit recommendation implementation. It is apparent that accepted recommendations are only effective when actually implemented. Improved performance is clearly foregone by partial, unnecessarily delayed or quasi-implementation.

## Taxation debt in Australia: an overview

**1.8** The Australian Taxation Office (ATO) is the Commonwealth's principal revenue collection agency. In 1998–99 the ATO accounted for total net taxation revenue of \$135.3 billion.<sup>23</sup> The main component of tax revenue is individual income tax, followed by company income tax, sales tax and fringe benefits tax. The ATO is organised into business lines,

---

<sup>23</sup> ATO's *Annual Report 1998-99* Financial Statements for the year ended 30 June 1999, p. 143. Includes some \$9.7 billion in Excise duty.

supported by a number of service lines. The business lines deal with revenue collection matters, and are organised along client lines: Large Business and International (LB&I), Small Business (SB), which was amalgamated with the Withholding Tax (WHT) business line on 1 March 1999 and Individuals (Non-business) (INB).

**1.9** The ATO's receivables management function collects a component of revenue (business and non-business). Value of debt referred to ATO's computer based tax debt collect system (COMPACT) for collection by the ATO's receivables management staff for 1998–99 was in the order of \$17.6 billion and the amount of debt finalised in 1998–99 was about \$15.5 billion. Disputed debt on hand increased 32 per cent from \$3.3 billion to \$4.3 billion.

**1.10** As the ATO administers two broad types of taxes, income tax and the recurring taxes, there are two types of overdue tax debts.<sup>24</sup> The ATO has two main types of taxpayers; individuals and businesses. The organisational structure reflects this differentiation between types of taxes and types of taxpayers.

**1.11** The INB Line of the ATO manages and maintains that part of the income tax system dealing with individual taxpayers who are not in business. It has a client base of approximately eight million taxpayers. The INB Line collects overdue tax debts from these taxpayers. Two other business lines collect the withholding and indirect taxes and income tax from businesses: the LB&I and the SB lines.

**1.12** There are about four million business taxpayers administered by the SB and LB&I business lines. The majority of these are SB taxpayers. The SB Line was established on 1 March 1999. It manages the income tax collection system for all business taxpayers (including the self-employed) with annual gross turnover of less than \$10 million.

**1.13** The SB Line collects all of the overdue tax debts that arise from the non-payment of withholding and indirect taxes as well as from the non-payment of income tax by all business taxpayers including those whose tax affairs are administered by LB&I. The SB Line also administers the collection of Interest, Royalties and Withholding (IRW), the Wool Tax, Fringe Benefits Tax and Superannuation.

**1.14** The ATO is in an environment of extensive administrative and taxation reform. ANAO acknowledges the inevitable impact of this on the conduct of business as usual. This audit examines a relatively small (but important) facet of tax administration. We are mindful that senior management determines priorities across a broader canvas of issues than those within our focus for the audit.

---

<sup>24</sup> Throughout this Report the phrase "recurring taxes" is used to refer to those taxes where the liability to lodge and/or remit is recurrent in nature. These include PAYE, PPS, Sales Tax and RPS.

**1.15** We have reviewed debt collection as a whole in the ATO but note that in some areas of the ATO it is referred to as receivables management but in other areas it is referred to as debt collection. In the SB program the phrase, “receivables management”, relates to lodgment, debt establishment and the collection of overdue tax. These functions are all managed from the one unit. In the INB program, receivables management, relates predominantly to debt collection. Debt collection refers to action taken to recover overdue tax. The ATO advises that the primary reason for the difference between business lines in the use of the terms “receivables management and “debt collection” is because many business taxes are recurring in nature several times during a year, in contrast to annually for income tax.

**1.16** Our discussion is largely about these functions as an ATO-wide activity rather than as a function performed by a particular business line or work stream. We understand that this is how the ATO prefers to view the function. There are a range of receivables management/debt collection systems, procedures, strategies and the RM policy, which are all based on a single coherent framework that is common to the SB and INB business lines. We present our analysis, findings and recommendations about these generally rather than specifically for particular business lines.

## **Policy and legislative framework**

**1.17** The *Income Tax Assessment Act 1936* (ITAA) creates an obligation on taxpayers to pay tax for each financial year. The liability for tax exists prior to assessment, as the assessment process is the ascertainment, or calculation, of the income tax that is payable for a financial year. The tax payable is an accrued obligation of the taxpayer for which the Commonwealth has the accrued benefit. The clauses in ITAA (eg. sections 204 and 208) making the tax due and payable are a legal mechanism to allow the Government to recover the tax payable in a court of law, amongst other things.

**1.18** As a debt, the Commonwealth may recover it in the ordinary way. It is a debt payable to the Commissioner of Taxation in the manner, at the place and by the date prescribed. As a matter of common English usage, a tax debt due to the Commonwealth, payable to the Commissioner is a debt owed to the Commissioner.<sup>25</sup> As tax properly payable is a debt,

---

<sup>25</sup> Income tax is due and payable on the date specified in the notice of assessment, not being less than 30 days after the service of the notice, or, if no date is specified, on the thirtieth day after the service of the notice (s204). Sub-section 208(2) provides that, for the purposes of s208(1), “income tax” includes interest under s170AA or 207A and additional tax under s207 or Pt VII.

tax debt collection is concerned with the collection of the debt (ie. tax) that has not been paid by the date prescribed. It is therefore concerned with the recovery of overdue tax. That is, the tax payable has been assessed, the taxpayer has been advised of the tax as a debt due to the Commonwealth and has not paid the debt by the due date. The collection of overdue taxes is part of the ATO's revenue collection function.

**1.19** Section 47 of the *Financial Management and Accountability Act 1997* (FMAA) governs the management of the recovery of overdue taxes.<sup>26</sup> This Act provides the framework for the administration of the provisions about tax debt that arise from specific tax legislation such as the ITAA. Section 47 states that a Chief Executive Officer must pursue recovery of each debt for which the Chief Executive is responsible unless:

- the debt has been written off as authorised by an Act; or
- the Chief Executive is satisfied that the debt is not lawfully recoverable; or
- the Chief Executive considers that the recovery of the debt is not economical.

**1.20** In relation to the first of these points, sections 265 ITAA and 133 *Fringe Benefits Tax Assessment Act 1986* (FBTAA) provide for the release of debtors in cases where payment of the income tax or fringe benefits tax debt will cause serious hardship.

**1.21** Section 166 of ITAA empowers the Commissioner to make an assessment of the taxable income and the tax payable on it from the returns and any other information in the ATO's possession. The ATO may also make default assessments where a taxpayer fails to provide sufficient information.

**1.22** Since 1 July 1986 a system of self-assessment has applied to the assessment of income tax. For recurring taxes, the employer is required to advise of the amount withheld and to then pay that amount by the legislated due date. As a result, an original assessment will be made by the taxpayer, not the ATO. As well as revenue collection the ATO has an education, post assessment and auditing function.

---

<sup>26</sup> This is because s208 of ITAA establishes a tax as a debt to the Commonwealth; hence overdue tax is an overdue debt owing to the Commonwealth. S47 of FMAA governs the management of all debt owing to the Commonwealth.

**1.23** Any assessed tax is due for payment on the earliest date specified in the assessment or the 30th day after service of the assessment. Once due and payable, income tax becomes a debt due to the Commonwealth. The tax debt may be sued for in any court of competent jurisdiction. The ATO may grant an extension of time for payment. If a taxpayer fails to pay the amount due, an interest penalty, the General Interest Charge (GIC), is applied to the debt until it is paid.

**1.24** Taxpayers who wish to challenge the correctness of an assessment may make an objection under the provisions of the *Taxation Administration Act 1953 (TAA)*.

**1.25** In taking recovery proceedings, the ATO has the same general rights and remedies as any other creditor. ANAO notes, however, that the ATO is not like a normal creditor in several respects. These include the conclusiveness of the assessment, the additional powers available to the ATO under the ITAA and the resources available to the ATO as an entity of the Commonwealth. Also, the ANAO notes that the ATO has several procedural advantages not available to other creditors that may assist with recovery. For example, through the Commissioner's broad power to make assessments, the ATO has a unilateral role in bringing the subject debt into existence and in defining its amount. In particular, the ATO is not required to provide a detailed explanation of the legal basis of an assessment to the taxpayer. If the taxpayer considers that the assessment is excessive, the taxpayer must prove that this is so. In contrast to other creditors, the ATO has no choice in the selection of its client base and cannot withhold the supply of goods and services in response to debtors.<sup>27</sup> The ATO also operates within the standards of the taxpayers' charter, tax case law and Government requirements.

**1.26** The ATO also has the general rights of a creditor to seek interlocutory orders from the court. For instance, the ATO may use *mareva* injunctions. These restrain the taxpayer from giving assets away, disposing of them or otherwise removing them from the jurisdiction pending completion of the recovery proceedings.

**1.27** A taxpayer may dispute a tax assessment in a court of law, request a review of the assessment, request a total or partial release from liability or request an extension of time to pay.

---

<sup>27</sup> For a more complete analysis of this issue see: Gumley, W and Wyatt K *Are the Commissioner's Debt Recovery Powers excessive?* Conference Paper at the Current Issues in Tax Administration Conference University of New South Wales. 11–12 April 1996.

## Recent policy and legislative developments

**1.28** Since the tabling of the 1996 Report, there has been a wide range of significant policy and legislative tax reform. In so far as these reforms affect the collection of tax debt, they are relevant to this audit.

**1.29** The *Taxation Laws Amendment Act (No.3) 1999* (TLAA) received Royal Assent in April 1999. These legislative reforms affected the administration of debt collection through the introduction of Running Balance Accounts (RBA) and the implementation of the General Interest Charge (GIC) on overdue debts. The GIC is a uniform regime for calculating and imposing a range of penalties including those for late payment of debts. It will replace most debt penalties, and is applied retrospectively in some cases.

**1.30** The TLAA provides the legislative basis for RBAs. These consolidate all withholding taxes onto one account statement that continues over financial periods. Phase 1 of the introduction of RBAs involves the establishment of four RBAs to account for and administer liabilities under Sales Tax, Pay-As-You-Earn (PAYE), PPS and RPS role types. Phase one was implemented on 1 July 1999 and the first statements issued from 23 August 1999 where 195 000 statements were dispatched. Phase 2, which is intended to apply from 1 July 2000, is the implementation of single RBA for liabilities that arise under the new tax system, including Goods and Services Tax (GST) and the Pay-As-You-Go (PAYG) tax.

**1.31** The thirty-one Acts that constitute the ‘A New Tax System’ (ANTS) reforms have been passed by the Parliament, but at the time of this audit, not all had received Royal Assent. The new GST, the Business Activity Statements (BAS) and the Australian Business Number (ABN) established by the new legislation will significantly change tax debt collection. Other measures include the change from the PAYE withholding income tax system to PAYG. The significance of this is that it will rationalise the withholding taxes (PAYE, PPS and RPS) into the PAYG tax payment regime.

**1.32** The GST will come into effect on 1 July 2000. This will have significant impacts on taxation in Australia generally and will affect the manner in which taxation debt will be administered and collected. The GST will be collected by the Commonwealth and distributed as revenue grants to the States and Territories through standing appropriations. At the time of this audit, negotiations about the intergovernmental agreements under which issues concerning any GST tax debts will be resolved had not been completed.

## **Debt collection as a component of tax administration**

**1.33** Tax debt collection occurs at the end of the tax administration cycle. The focus of this cycle is the achievement of the one Government outcome set for the ATO. This Government outcome is

*Effectively managed and shaped systems that support and fund services for Australians and give effect to social and economic policy through the tax system.<sup>28</sup>*

**1.34** The cycle has several steps, of which four are critical. These are:

- public education, advice, rulings and the provision of information;
- the lodgment of tax returns in the case of income tax or advice of a liability in the case of the recurring taxes;
- the issuing of an ATO assessment of a credit or a debit; and
- the payment of the assessed tax debit by the taxpayer.

**1.35** The debt collection function arises only when the taxpayer has not complied with their lawful obligation to pay assessed tax. A substantial proportion of ATO's resources is devoted to the first three steps of the cycle. There is a sense in which some of these resources would be wasted if the cycle is not completed for those taxpayers to whom the ATO has issued a tax debit. The assessment of the effectiveness of tax debt collection should have regard to this factor.

**1.36** There is another aspect to this cycle to consider in connection with the assessment of the effectiveness of debt collection. There is a premium attached to the collection of unpaid tax. This premium relates to the integrity of the tax system. The integrity of the Australian tax system depends on, amongst other things, the extent of compliance by the community. The integrity, therefore, may be weakened as compliance weakens. Parliament expects all taxpayers to meet their taxation obligations as and when they fall due and has passed laws that require this. It has also given the ATO the powers and resources to enforce these laws.

**1.37** The integrity of the tax system also depends on the efficiency and effectiveness of ATO's administration of the system. By not efficiently and effectively collecting tax due, the integrity of the tax system may be

---

<sup>28</sup> *The Portfolio Budget Statements 1999-2000: Treasury Portfolio, Budget Related Paper No. 1.16, p. 77.*



weakened. The ATO, via its actions, could be said to have a responsibility to ensure that the public perceives that no taxpayer could avoid the payment of tax debt because the ATO did not collect the debt.<sup>29</sup>

**1.38** ATO's approach to revenue collection relies heavily on voluntary compliance. ANAO considers that the ATO must ensure that persons who voluntarily comply are not at a relative disadvantage to those who do not. Taxpayers' relationship to the ATO is different to the relationship between a private sector firm and those to whom that firm extends credit. Taxpayers' relationship to the ATO is not a market-based relationship. People are required by law to pay tax and the ATO is in no position to withhold supply as a means of collecting debt, as are other creditors. The ANAO accepts that, in relation to tax debt collection, the ATO operates in an environment that is substantially different from commercial debt collection firms. The ATO necessarily considers broader social issues and a \$ expended to \$ collected equation, which applies in a commercial environment, should not be the sole consideration for the ATO.

**1.39** The integrity of ATO's current debt management practices would be at risk if those who have been assessed as having an overdue tax can succeed in not paying that tax even though they do not dispute the assessment that they have an overdue tax. If the integrity of the tax system is eroded, this can have long term deleterious effects on compliance behaviour and, ultimately, on revenue collected.

### **The Compliance Model**

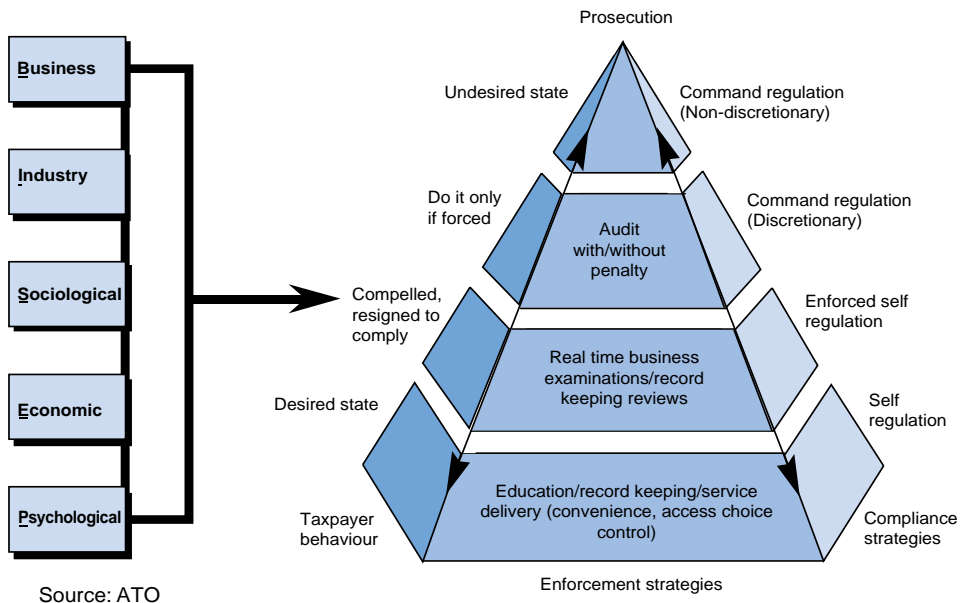
**1.40** The ATO has made use of social science research that shows that there are many different factors that determine a client's behaviour. The ANAO recognises that the ATO needs to understand these to tailor a response that is appropriate to the particular taxpayer's circumstances and suitable to the protection of Commonwealth revenue.

**1.41** The ATO has developed a framework within which it manages all client relations. This is known as the Compliance Model and it is shown in Figure 1. The Compliance Model recognises that the majority of taxpayers comply voluntarily with no need for ATO intervention. Others comply but need some assistance or prompting. Others will not comply in the first instance but will if prompted further. A small proportion will not comply voluntarily and may need enforcement action.

---

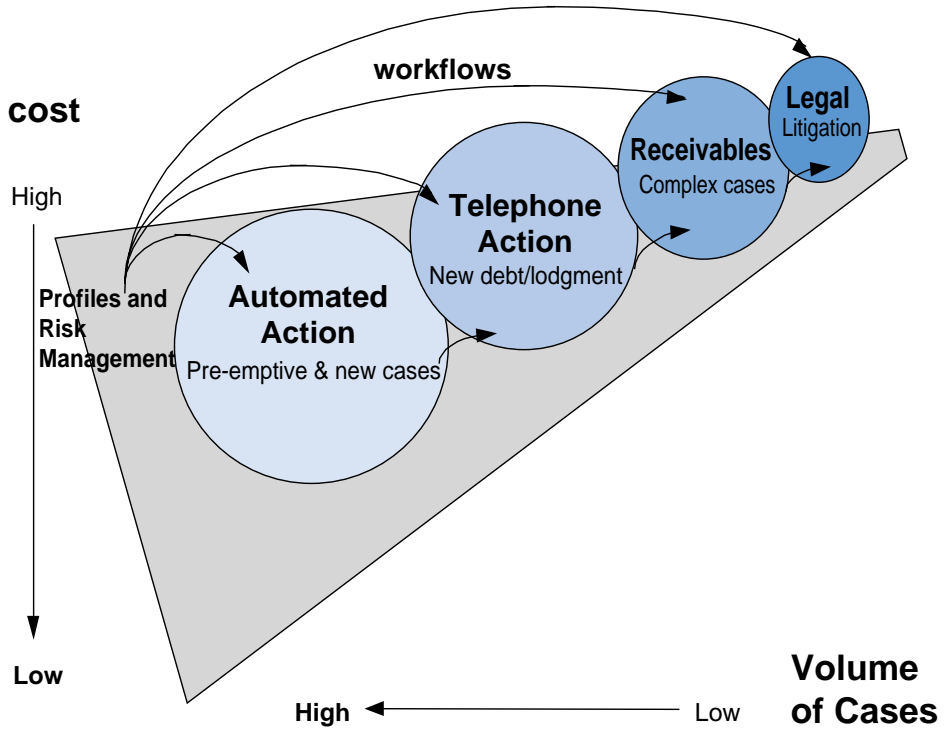
<sup>29</sup> A similar observation was made by the JCPA in its Report, *An assessment of Tax*, Report No 326 of November 1993. In that Report the Committee noted: "At the same time, the best interests of the taxation system are served by a public perception that no taxpayer can evade the payment of a legal debt by virtue of the ATO's incapacity to action debt recovery". Report 326 (November 1993) paragraph 9.67 p. 214.

**Figure 1**  
**The Compliance Model**



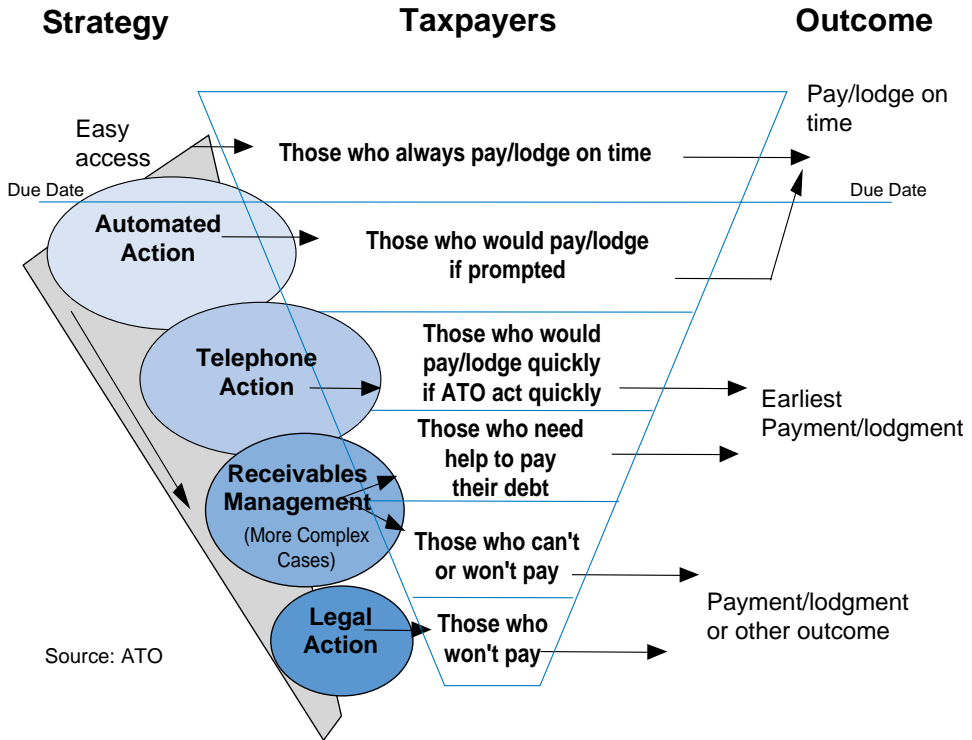
**1.42** The principles outlined in the Model apply equally to relationships that involve the administration of overdue tax (ie. tax debt). The ATO recognises that clients fail to pay for different reasons, such as short-term cash flow, insolvency or fraudulent behaviour. The ATO has developed strategies which recognise these different circumstances, which also factor in the significant impact that ATO actions can have on the future viability of a taxpayer’s earning capacity, their employment situation and their personal life. These strategies have been encompassed in the ‘HOW to Manage ATO Receivables’ model at Figure 2 and explained at Appendix 1.

**Figure 2**  
**'How to Manage ATO Receivables'**



Source: ATO

**Figure 3**  
**Tax Debt Collection Payment Strategy**



## Statistical overview of taxation debt<sup>30</sup>

**1.43** The ATO uses several key terms to differentiate various important attributes of debt. As these terms will be used throughout this Report, it is important to clarify relevant concepts at the outset. In the first instance, it is important to distinguish between debt **cases** and debt **amounts**. A debt case is the instance of raising a debt against a taxpayer. The debt amount is the dollar value of the debt. There are **active** and **inactive** cases. An active case is one that is currently subject to collection action. Cases that are the subject of legal action, or the subject of a dispute by the taxpayer, or subject to collection action are active cases. Inactive debt includes debt written off. The ATO regards debt as **collectable** when the collection of the debt is not impeded by dispute, insolvency or by not yet being due. The ATO differentiates between six incremental **levels** of debt. The ATO also classifies the **age** of debt into three categories. These are **new**, **old** and **ancient**. **New** debt is debt that is less than 90 days old. **Old** debt is debt that is between 90 days and two years old. **Ancient** debt is all debt two years of age and older. In this Report, we use the term “aged debt” to refer to old and ancient debt collectively.

**1.44** The six incremental debt levels and the numbers of debtors and amounts of debt in each level, are shown in Table 1 for total debt on hand and in Table 2 for collectable debt on hand:

**Table 1**

**Total Debt: Debts and Debtors on hand as at 30 June 1999**

<i>Debt Level</i>	<i>Classification of debt</i>	<i>Number of Debtors</i>	<i>% of Debtors</i>	<i>Value of Debt \$</i>	<i>% of Debt</i>
1	<\$2500	205 250	59	158 295 812	2
2	\$2500-7499	74 236	21	330 335 537	5
3	\$7500-\$24 999	48 786	14	654 598 780	9
4	\$25 000-\$49 999	12 461	3	431 336 760	6
5	\$50 000-\$99 999	5702	2	393 061 897	6
6	>\$100 000	4090	1	5 167 220 762	72
	<b>Total</b>	<b>350 525</b>	<b>100</b>	<b>7 134 849 548</b>	<b>100</b>

Source: ATO

<sup>30</sup> The quantitative data in this audit has been drawn from various sources indicated in the text. Unless otherwise shown, the data has been examined for reasonableness, but not audited. There are minor differences in the data reported in some of the tables in this report. This is the result of the tabulations being drawn from different databases, eg. COMPACT, the Data Warehouse and the main taxpayer databases at different times in the year. We consider that these differences have no impact on the analysis. It may be noted that not all of the tabulations have been compiled on the same date. This is because several tabulations were compiled on different dates, in some cases to clarify points of analysis and discussion during the audit. The several databases of the ATO do not allow retrospective snapshot tabulations as the relevant databases are live; that is, the information on them is under continuous change as taxpayers' debt situation changes.

**Table 2**

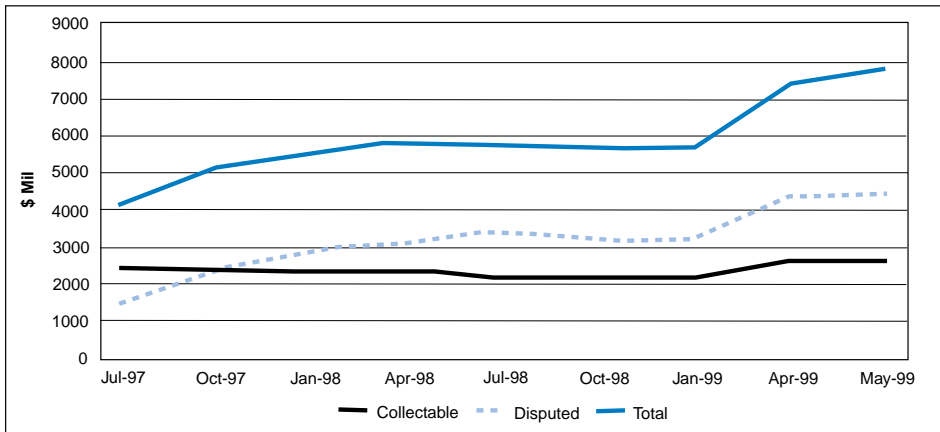
**Collectable Debt: End August 1999**

<i>Debt Level</i>	<i>Classification of debt</i>	<i>Number of Debtors</i>	<i>% of Debtors</i>	<i>Value of Debt \$</i>	<i>% of Debt</i>
1	<\$2500	179 576	55	118 548 336	5
2	\$2500-7499	70 651	22	258 804 828	10
3	\$7500-\$24 999	52 904	16	531 901 194	21
4	\$25 000-\$49 999	14 283	4	330 645 380	13
5	\$50 000-\$99 999	6509	2	285 627 953	11
6	>\$100 000	3910	1	1 036 211 409	40
	<b>Total</b>	<b>327 833</b>	<b>100</b>	<b>2 561 739 100</b>	<b>100</b>

Source: ATO

**Figure 4**

**Composition of Total ATO Debt on Hand 1998–99**



Source: ATO

**1.45** Figure 4 shows that about two-thirds of total ATO tax debt on hand is disputed debt. The remaining one-third is collectable debt, that is debt that the ATO can proceed to collect because there is no legal impediment to its collection. Figure 4 shows that there was an overall increase in total ATO debt over 1998–99. Figure 4 shows that most of the additional debt raised was disputed debt, and that most of it was raised between January and April 1999. We have been informed that the increase in disputed debt resulted from ATO campaigns directed at compliance improvement in the cash economy, high wealth individuals and schemes areas as well as the assessment of QPT, which increased the amount of collectable debt.

**1.46** The debt collection function in the ATO is integral to the ‘new tax system’ of wider taxation reform. In the business context, ‘debt collection’ has been restyled as ‘receivables management.’ Receivables management includes all the processes, interactions, products and activities involved in managing the lodgment and payment obligations of a known taxpayer.<sup>31</sup>

**1.47** In 1998–99 the receivables management (RM) function in SB formed 45 per cent of the resources of this new business line. The RM function had about 1995 FTE staff and was managed by three SES Band 1 officers. The RM function in the INB business line is within the Correct Payments Branch. In 1998–99, about 276 FTE staff in this Branch were employed on RM functions; one SES officer manages the branch overall. The ATO therefore employed a total of 2271 FTE staff on RM work in 1998–99. The net cost of this service to the Commonwealth Government was approximately \$142.2 million in 1998–99. On 8 November 1999 the Commissioner announced his intention to increase the resources allocated to the RM function in 1999–2000, 2000–2001, and 2001–2002. The result will be an increase to the numbers of staff that would be allocated to the RM function, as prior to this announcement the total numbers of staff had been reduced by about seven per cent. The ATO considers that this increase, combined with the Receivables Management System currently under development, should greatly increase the ATO RM capacity. As a result, in 1999–00 the net cost of ATO’s RM service to the Commonwealth Government will be about \$150.1 million and about 2239 FTE staff will be employed on the function.

**1.48** Table 3 shows key ATO debt collection statistics for the period 1990–91 to 1998–99. The statistics include disputed debt.

---

<sup>31</sup> ATO define ‘receivables management’ in this way: it “...is all the processes, interactions, products and activities involved in managing the primary obligations (ie. lodge and pay) of a known client, from before the liability arises to collection of the debt, for example, advising tax liabilities, managing debts, collecting money, securing lodgment of returns, chasing outstanding debts. Managing receivables also includes the supporting business systems.” *ATO Debt Collection Initiatives: “Receivables Management”* Speech by Erin Holland (Assistant Commissioner responsible for the Receivables Management Stream) to the International Debt Collection Benchmarking Workshop Edinburgh 7 to 10 March 1999. It is to be noted that the management of receivables starts before a liability is incurred. It commences as soon as there is an obligation to consider a tax responsibility. For example, as soon as a company registers for business it has an obligation to consider its tax responsibilities and how they will be met. The ATO, at the same time, needs to consider ways to ensure that the company complies with its obligations. This involves pro-active provision of information and collection of data, as well as the collection of revenue.

**Table 3**  
**ATO debt collection statistics 1990–91 to 1998–99<sup>32</sup>**

	1990–91	1991–92	1992–93	1993–94	1994–95	1995–96	1996–97	1997–98	1998–99
Cases referred	343 847	278 162	311 298	321 247	343 002	366 294	410 500	522 427	588 526
Cases finalised	319 499	318 992	331 685	324 871	367 109	352 400	395 740	494 609	551 635
Cases on hand 30 June	364 482	323 652	301 391	297 789	273 682	287 551	296 785	322 247	349 238
Debt referred (\$b) <sup>8</sup>	5.7	11.13	12.11	12.04	16.77	16.5	14.4	15.3	17.54
Debt finalised (\$b)	6.43	10.66	12.08	11.96	16.89	16.07	14	13.3	15.48
Debt on hand 30 June (\$b)	4.42	4.351	4.222	4.233	3.884	4.165	4.086	5.767	7.37
<p>Note 1: This amount excludes \$0.42b tax not due for payment at 30/6/92.</p> <p>Note 2: This amount excludes \$0.07b tax not due for payment at 30/6/93.</p> <p>Note 3: This amount excludes \$0.06b tax not due for payment at 30/6/94. Apparent increase due to rounding.</p> <p>Note 4: This amount excludes \$0.05b tax not due for payment at 30/6/95.</p> <p>Note 5: This amount excludes \$0.04b tax not due for payment at 30/6/96.</p> <p>Note 6: This amount excludes \$0.03b tax not due for payment at 30/6/97.</p> <p>Note 7: This amount excludes \$0.04b tax not due for payment at 30/6/98.</p> <p>Note 8: Debt referred includes a significant proportion of disputed debt that is not collectable whilst the dispute continues. At June 1999 the total value of disputed debt was \$4.4 billion.</p>									

Source: ATO

<sup>32</sup> The figures given in this table are as reported in ATO Annual Reports. The ANAO has reconciled the debt on hand figures with COMPACT management reports and between years and has found discrepancies with some of the data after taking into consideration the amount of tax debt not yet due. For example, the ANAO is concerned that in years such as 1991–92, when the debt referred exceeds the debt finalised, the debt on hand figure decreases, not increases. The ATO advised that these discrepancies might be the result of changes to management reports in the early 1990's.



**1.49** The above data demonstrates that there has been a sustained increase in the amount of debt referred, and there has also been an increase in the number of cases finalised over the years from 1990. The data shows that although the number of cases referred has increased, the number of cases on hand remaining at the end of each period has remained at a similar level, although the dollar value of the debt on hand has risen over this time.

**Table 4**

**New, Old and Ancient Debt on Hand for 1993–94 to 1998–99**

<i>Component of Debt</i>	<i>1993–94</i>	<i>1994–95</i>	<i>1995–96</i>	<i>1996–97</i>	<i>1997–98</i>	<i>1998–99</i>
New Debt	1.01	0.66	0.99	0.97	0.88	1.50
On Hand1 (\$b)	(24%)	(17%)	(24%)	(24%)	(15%)	(20.2%)
Old Debt	1.91	1.54	1.56	1.57	2.84	3.00
On Hand2 (\$b)	(44%)	(39%)	(37%)	(38%)	(49%)	(40.5%)
Ancient Debt	1.38	1.70	1.65	1.55	2.04	2.90
On Hand3 (\$b)	(32%)	(44%)	(39%)	(38%)	(35%)	(39.1%)
Total Debt	4.3	3.9	4.2	4.09	5.76	7.41
On Hand (\$b)						
Note 1: Debt that is on hand less than 90 days after referral to COMPACT.						
Note 2: Debt that is on hand between 90 days and 2 years after referral to COMPACT.						
Note 3: Debt that is on hand more than 2 years after referral to COMPACT.						

Source: ATO

**1.50** Table 4 shows that, of the total debt on hand, the amount that is categorised as either old or ancient has increased over time. The proportion of debt in each category, new, old and ancient has remained relatively steady due to the increase in the amount of total debt over the six years since 1993–94, notwithstanding the significant increase in total debt that has occurred over this period.

**Table 5**

**Amounts written off from 1994–95 to 1998–99**

<i>Year</i>	<i>Total Write Offs (\$m)</i>	<i>% of Total Debt Referred</i>
1994–95	782	4.6
1995–96	587	3.5
1996–97	793	5.5
1997–98	734	4.8
1998–99	417	2.3

Source: ATO Financial Statements in ATO annual reports for the years indicated

**1.51** Table 5 shows that the amount of write off of debt remained fairly constant over the years 1994–95 to 1997–98. The exception is 1995–96, which does not include PPS write offs for that year, as they were unobtainable due to the conversion of PPS to new business systems. The

amount of write offs, however, has decreased significantly in the latest year, 1998–99.

### *Age of active debt*<sup>33</sup>

**1.52** Information about the age of active debt is shown in Figures 5, 6 and 7 in Chapter Three.<sup>34</sup> These Figures show that there were 349 238 active tax debtors at the end of the 1998–99 financial year.<sup>35</sup> These cases carried a total debt of \$7.4 billion. ATO advises that, of this, only about \$2.5 billion is collectable.<sup>36</sup> Action had been initiated on 80 per cent of the active cases and these cases carried over 90 per cent of the debt. The remaining 20 per cent of the cases consisted of a mix of cases on which initial action had been taken or on which no action had been taken.<sup>37</sup>

**1.53** At 30 July 1999, debt aged 90 days or more accounted for 88 per cent of active debt (ie. about \$6.55 billion). Twelve per cent of the debt of all active cases (ie. about \$1 billion) was less than 90 days old. Debt aged 90 days or more is referred to as aged debt. Aged debt includes debt known as old debt, which is between 90 days and two years old and ancient debt, which is debt older than two years. We have been advised that the industry standard limit for finalising collectable debt is 180 days.

**1.54** Noting that some 80 per cent of the debt on ATO's books is aged debt (Table 4), we analysed its composition and status. The analysis showed that taxpayers disputed 62 per cent of active aged debt (ie. about \$3.7 billion), insolvent debtors owe four per cent (ie. \$0.24 billion) and 34 per cent is collectable (ie. about \$2 billion).

---

<sup>33</sup> Child Support Agency debts have been excluded.

<sup>34</sup> ACTIVE cases are those currently subject to collection action; that is they have not been finalised. Examples of active cases include cases under arrangement, cases subject to legal action, cases subject to negotiation.

<sup>35</sup> The data on which these Figures are based is sourced from aged debt (and credit) balance reports run on each business system at the end of each month. (The ATO's separate business systems are: NTS - Income taxes for Individuals, Companies and Super Funds, AIS - Withholding Taxes PAYE, Sales Tax etc., FBT, Superannuation Surcharge and IRW – Interest, Royalties and some Withholding taxes.) As these reports are run on the actual business systems where taxpayer accounts are maintained and therefore include all active balances, a more accurate picture of the age of active debt is obtained than if the analysis had been based on COMPACT records.

<sup>36</sup> COLLECTABLE. This means debt not impeded from collection by dispute, insolvency, not yet being due.

<sup>37</sup> INITIAL ACTION. This means that the ATO has initiated some action as a step towards the collection of the debt. Examples of initial action include direct contact established with the tax debtor, the commencement of tracing action and the issuing of an initial demand. In many instances a debtor on whom initial action had been taken would have received the Notice of Assessment, and a Final Notice. In some instances the debtor would have also received a Standard Letter.

**1.55** ATO advises that, in insolvency proceedings, the ATO is an unsecured creditor. As a result, the ATO is subject to the general distribution of proceedings of insolvency. Arising from insolvency proceedings, distributions in respect of insolvent debtors to the ATO average about 10 per cent of the outstanding insolvent debt balance. On this basis, the ATO would expect to receive no more than about \$26 million from insolvent debtors.

**1.56** Of the disputed debt, the ATO advise that, on the basis of past experience, 40 per cent of the cases will be resolved in favour of the ATO. However, the structure of total ATO disputed debt has a major bearing on the amount of debt that the ATO might ultimately collect when disputes are settled. This will result in a collectable amount. The exact value of the collectable amount depends on the amount of debt associated with a disputed case and, amongst other things, the solvency situation of the entities to which the debt is attached.

**1.57** Our review of the structure of disputed debt showed that a very small number of cases carry a very large amount of debt. For example, almost \$1.8 billion debt is currently tied up by only 35 cases. On the basis of current disputed debt proceedings, the ATO expects to collect no more than about \$1.3 billion once all of the cases currently under dispute are settled.<sup>38</sup>

## **The audit**

**1.58** In order to address the objectives of this audit we have reviewed ATO's implementation of the recommendations of our 1996 Report and of the subsequent Report of the JCPA. Our findings are reported in Chapter Two. The context and operation of tax debt collection administration has changed significantly since our 1996 Report hence we reviewed the main features of the current approach.

**1.59** The ANAO's fieldwork was focused at the National Office ATO site. Fieldwork also involved discussions with ATO officers at various sites in the Sydney, Melbourne, Brisbane and Newcastle regions. We initiated a range of quantitative analyses of ATO's databases as part of the audit. These were all carried out on our behalf by the ATO.

---

<sup>38</sup> The total amount credited to taxpayers once a dispute is determined in the favour of a taxpayer is recorded in the ATO's financial statements as the provision for credit amendments. In the financial statements for the year ended 30 June 1998, \$1 897 530 was recorded against this entry.

**1.60** The ANAO engaged the services of Mr. Terry Ledlin, Senior Partner of Ledlin Partners, Business and Commercial Lawyers, and Mr. Brian Savage of Alliance Group Holdings Pty Limited to provide expert strategic advice about receivables management/debt collection, particularly in the private sector. Ledlin Partners facts for many leading Australian firms and financial institutions. Mr. Ledlin is closely involved in the conduct of professional development programs in credit and receivables management conducted by the Australian Institute of Credit Management. Mr. Savage has practical experience in credit, receivables management and debt collection fields, especially at the senior levels of executive management in major financial institutions. Both consultants were retained because of their expertise in credit and receivables management.

**1.61** The audit was conducted in accordance with ANAO Auditing Standards at a cost of \$197 000 at the time of tabling.

## **The Report**

**1.62** This Report is a review of the progress made by the ATO since 1996 and an outline of opportunities for further improvement by the ATO in receivables management and tax debt collection. Chapter Two provides an overview and discussion of the extent to which the ATO has implemented the recommendations from the 1996 ANAO tax debt collection audit and the 1997 JCPA report arising from its consideration of that audit. Chapters Three and Four discuss the opportunities for improving tax debt collection at the ATO.

**1.63** We examined the opportunities that could arise in the following areas:

- receivables management performance information and reporting;
- the collection of more tax debt and in a more timely manner;
- outsourcing the collection of some debt;
- the better use of databases and the use of additional databases; and
- quality assurance certification.

**1.64** Chapter Three examines the extent to which the ATO is achieving a reasonable level of contestable performance in the area of receivables management. We also analyse the scope for improved reporting of performance, improved practice in the administration of debt, the potential for outsourcing some debt collection and the adequacy of existing organisational arrangements. In relation to improved practice, we review opportunities for improvement in the following areas of receivables management: shortening the time taken to finalise debt,

actioning unactioned debt, reducing the amount of debt written off on the grounds that it is uneconomical to collect, improving lodgement behaviour particularly for some business debtors, shortening lodgement time frame for some income tax debtors and the payment of tax debt by installment.

**1.65** Chapter Four reviews three important systemic risks that might impact on ATO's debt collection performance over the next three years. One concerns ATO's computer based systems, particularly their capacity to carry out both existing and new functions legislation requires to a satisfactory standard. Another concerns the impact of the new accountabilities, systems and workloads associated with ongoing legislative change to Commonwealth tax administration. The third concerns a group of taxpayers whose non-compliant behaviour presents the ATO with a significant risk management challenge that has been identified by an ATO project. We review the scope for improvement in ATO's capacity to better manage these systemic risks by the better use of the full range of databases to which the ATO has, or could have, access. The issue of the ATO obtaining external quality assurance along the lines of industry better practice standards is also discussed.

## 2. Implementation of the Recommendations from Earlier Reports of the Auditor-General and of the Joint Committee of Public Accounts

---

*This Chapter reviews the extent to which the ATO has implemented the recommendations that were made for tax debt collection from the 1996 ANAO audit and the subsequent JCPA review. In some key areas the ATO has moved beyond the recommendations. Appendix Two summarises progress of implementation against each ANAO recommendation.*

### Implementation of ANAO Recommendations

**2.1** The ANAO conducted a performance audit of ATO tax debt collection in 1996. This audit found that there was scope for improvement in the performance of ATO debt collection. The ANAO's recommendations were directed at achieving three objectives:

- minimising the amount of debt incurred by taxpayers;
- maximising the amount of debt collected from taxpayers and
- improving the equity of treatment of taxpayers by the ATO.

**2.2** The ANAO's Report contained specific recommendations about how these goals might be achieved. Most of the recommendations were directed at maximising the amount of debt collected. The recommendations addressed five key risk areas. They were:

- better business systems;
- more cost-effective collection of debt;
- better quality performance information and research;
- greater compliance by the ATO in the imposition of penalties as required by the law; and
- more up to date, and more readily useable, administrative policy and procedures.

**2.3** Other issues within these risk areas were the major updating of ATO debt management policy, practices, procedures, standards and quality assurance systems, improved recovery systems and improvements in the timeliness of debt recovery.

**2.4** The following is a summary of the recommendations, the issues they addressed and the ATO's progress in relation to the five risk areas at the time of the present audit in 1999.

### **Better business systems**

**2.5** The ATO's debt related business, including computer, systems did not reflect private sector best practice. Areas of possible systems improvement include debt identification and prioritisation, control and monitoring of the recovery process, and automation of the basic collection and penalty application processes. Despite reductions in the referral times of cases from various accounting systems to COMPACT, significant built-in delays were found at the time of the 1996 audit.

### **ATO's progress**

**2.6** The ATO made enhancements to COMPACT in 1999. One of these was to make the system national. Another was to improve significantly the ease of use of the system to staff by means of graphical user interface facilities. During the audit, the ATO also announced the successful tenderer for the replacement of COMPACT. The full implementation of recommendations concerning business systems depends on the quality of the system that replaces COMPACT. A key feature of this proposed new Receivables Management System (RMS) is that it will require a whole-of-client view of the taxpayer. If this can be achieved, it will be a significant change from current IT systems. These systems manage only on type of tax, or type of taxpayer, and currently are not set up to generate a whole of client view.<sup>39</sup> The ATO has made some progress in the improvement of data quality. Lack of data quality continues to be a serious problem and will continue to be so unless the ATO addresses systemic causes. The ATO has made changes to the downloading of debt cases from the National Taxpayer System (NTS) and from the ATO Integrated System (AIS) so that debt cases are downloaded within a week of the establishment of tax debt. The ATO has also made use of new computer based business systems to support improved debt management. Examples include the use of On-Line Analytic Processing (OLAP) software and purpose-built case profiling software.

### **More cost-effective collection**

**2.7** Debtor risk profiling would provide a cost-benefit basis for debt prioritisation, and enable the ATO to target a range of customised

---

<sup>39</sup> This means that existing IT systems are structured in relation to the type of tax paid (there are two main types of taxes, income tax and the recurring taxes) or in relation to the types of tax payers (there are two main types of tax payers, individuals and business).

educational and enforcement activities. These enhancements, together with improved automation, would help reduce delays in the recovery process which, in turn, enable staff to apply their expertise to those cases where individual attention would prove most productive. These issues will be better managed with the implementation of the new Receivables Management System.

### **ATO's progress**

**2.8** The ATO has implemented custom made and highly sophisticated profiling software designed to match the most appropriate ATO response to the particular characteristics of the debtor. This has been part of a wider restructuring of the receivables management function. The ATO has also implemented a model for the management of lodgment and collection activities. This is shown in Figure 2 in Chapter 1. The action strategies in this model align with the ATO's Compliance Model, which is shown in Figure 1. This alignment is shown in Figure 3. The full implementation of these reforms, which was in progress during the audit and which will continue for the next year or two, has the potential to achieve significant gains in more cost-effective collections.

### **Better performance information and research**

**2.9** The value of the performance information compiled at the time of the 1996 audit could be improved regarding the accuracy with which the age of debt and the cost of finalisation were measured. There was also scope for improving the usefulness of performance information in the assessment of the contestability of ATO performance. Performance information did not measure the relative success or costs of alternative collection strategies on various segments of the debtor population. Accurate cost-benefit information was required in order to decide which strategies to pursue and to identify which debts are uneconomic to pursue.

### **ATO's progress**

**2.10** In 1997, the ATO undertook an international benchmarking initiative of receivables management processes and published the results as *Receivables Management Benchmarking: Critical Best Practice Guide*. This was a helpful step towards improved debt collection performance. As part of the reengineering of ATO's receivables management function, the ATO is developing a new set of performance measures. The ATO is also participating in the development of nationally comparable measures of receivables management performance as a result of joining an Australia Quality Council (AQC) initiative. We note that the ATO is pioneering the development of performance measures with these initiatives. Whilst



the ATO is better placed than previously to evaluate alternative collection strategies, there is a range of strategies not now in use. As discussed in Chapters 3 and 4 of this Report, most of these alternative strategies would require new Government or legislative authority. The ATO has been investigating ways of improving the capacity to prevent the occurrence of tax debt. The ATO's Kdnet facility has produced useful research about the nature, causes and prevention of tax debts. Quality Assurance initiatives have been progressively implemented since 1997. They have been directed at improving the quality of decision-making as well as monitoring compliance of debt collection actions with legislation, ATO policies and procedures. Poor quality data, systems rigidities and the variable priorities of operational management have impeded the full implementation of ANAO's quality assurance recommendations.

### **Additional Tax for Late Payment (ATLP)**

**2.11** ANAO considered that greater compliance by the ATO in the imposition of penalties (specifically the ATLP) was required. Insufficient information was available to assess the ATO's performance regarding the imposition, remission and collection of additional taxes on late payment. The ANAO found that there was a high risk of penalties not being imposed in accordance with legislation. A capacity to automatically impose late payment penalties was needed.

### **ATO's progress**

**2.12** The Government has changed the legislative basis of the administration of some tax penalties as a result of a review undertaken by the ATO in response to the audit, amongst other things. The new Act, *Taxation Laws Amendment Act No 3 1999*, (which received Royal Assent on 1 April 1999) provides for the establishment of the Running Balance Account (RBA). It also provides for the replacement of a number of penalties, particularly the additional tax for late payment (ATLP), by a General Interest Charge (GIC). This charge is applied to the debit balance on the RBA. We expect that the imposition of the new GIC will address all the concerns raised in our 1996 Report.

### **Policy and procedures**

**2.13** The ANAO recommended that the ATO introduce technology that presents key risk data in a structured format and provides interpretive information (such as financial ratios and risk indicators).

### **ATO's progress**

**2.14** The ATO has published for the use of staff nationally consistent debt collection standards and procedural guidelines that are

systematically reviewed. The ATO has also implemented nationally consistent delegations and authorisations. There has been a major focus on the professional development of staff, the training of staff in new legislation, policy and procedures and the new receivables management framework. We have been advised that procedures, particularly collection techniques could be improved with better training of staff. The introduction of call centres might be an opportune time for improving this aspect of training.

## **Potential net benefits to the Commonwealth**

**2.15** A feature of the audit was analysis that demonstrated a relationship between efficiency and effectiveness of debt management. The Report showed that relatively small joint gains in the efficiency of several debt management services (eg. a five per cent reduction in time taken to finalise debts and a reasonable gain in ATO action on overdue debts) would result in additional financial benefits to the Commonwealth. The Report showed that a potential financial benefit of \$142 million was readily achievable.

**2.16** We consider that the ATO's implementation of the Report's initiatives have resulted in improved efficiency, effectiveness and equity. The ATO has advised that the financial benefits of the ATO's improvements since the 1996 audit exceed the potential net benefits identified by ANAO. We find the ATO is now more efficient at debt collection than it was in 1996.

**2.17** The ATO has also moved beyond ANAO's 1996 recommendations in several areas. The following are the main examples:

- the introduction of Running Balance Accounts and the General Interest Charge;
- the establishment of the receivables management function and associated strategic and operational planning, organisational restructuring and business process reengineering;
- the use of profiling, which involves advanced mathematics, statistics and data mining to maximise the probability that the most cost effective action will be taken in respect of a particular tax debtor. By means of profiling, a range of debt collection strategies will be automatically assigned to debt cases. ATO's mathematical algorithm has the unique capacity to learn about the distinctive characteristics of different files of tax debtors. This gives the process of profiling a dynamic capacity. The profiling algorithm can find the means of matching the most appropriate administrative response to a taxpayer even though the nature and range of the variables that characterise tax debtors might

change. The ATO is using technology with the potential to markedly improve public administration;

- the decision to replace COMPACT with a new receivables management system;
- the use of interactive voice response (IVR) systems; and
- the use of call centres.

## Implementation of JCPA recommendations

**2.18** The JCPA recommendations addressed aspects of ATO administration that followed up on issues of equity and systems capacity that were identified in the 1996 ANAO Report.<sup>40</sup> Two recommendations focused on the ATO's administration of the ATLP and its use as a negotiating tool in some cases. The identified problems have been addressed by the legislated reforms to tax penalties, discussed in paragraphs 2.11 and 2.12. The third recommendation deals with the ATO's capacity to understand its debtor population. This has been addressed in the new approach to receivables management that is now being implemented with the strategic RM models as shown in Figures 1 to 3 and the two stage reforms to the debtor databases.

---

<sup>40</sup> The Joint Committee of Public Accounts recommended that:

1. In order to ensure that additional tax on late payment (ATLP) is imposed in accordance with the law, and to ensure that ATLP is not used as an inappropriate negotiating tool when seeking to collect tax debts, the Australian Taxation Office should give high priority to improving the capacity of its business systems to automatically impose ATLP when a debt is paid late.
2. The Australian Taxation Office should take action to ensure that all taxpayers that are subject to the imposition of additional tax on late payment (ATLP) are advised of their right, irrespective of the size of their tax debt, to seek remission of ATLP.
3. The Australian Taxation Office should give high priority to improving the capacity of its business systems to segment the debtor population by risk characteristics of the debt.

## 3. Debt Management: Improved Practices and Reporting

---

*This Chapter finds that the efficiency, effectiveness and equity of ATO's debt collection has improved since 1996 as a result of the implementation of the recommendations of the 1996 ANAO Report. Continued gains to efficiency, effectiveness and equity could be expected over the next three years, although the precise impact of legislative change on workload is yet to be fully assessed. Improvement in the quality and usefulness of performance information published by the ATO about debt collection could improve performance. The use of better practice management approaches of the private sector has potential to also improve performance. As current and new initiatives take effect, ATO's debt collection performance could also become more contestable. The evaluation of the cost-effectiveness of outsourcing of the collection of some classes of tax debt to the private sector is warranted in view of the potential that outsourcing has to improve contestability and performance, including the collection of additional revenue. It may also be in the best interests of the Commonwealth for the ATO and Centrelink to develop a strategic partnership for the collection of some lower levels of income tax debt for debtors common to both agencies, provided satisfactory privacy arrangements can be established.*

### Introduction

**3.1** We found that the ATO has made significant progress with the implementation of most of the main recommendations of our 1996 Report. The ATO has also moved beyond those recommendations in several important areas. These were outlined in Chapter 2.

**3.2** We consider that the initiatives outlined in Chapter Two ought to result in continuing improved efficiency, effectiveness and equity in future years. ANAO notes that as a result of the initiatives, the ATO has been able to improve debt collection performance and reduce the cost of debt collection services by about 20 per cent over three years. In 1997–98 the resource expended by the Government on ATO's debt collection services was about \$230 million. In 1999–00 it will be about \$150 million. We are satisfied that ATO's allocation of resources to the receivables management/debt collection functions for 1999–2000 in the ATO is, in the main, relatively sound. As we have found scope to raise additional revenue, the question arises as to whether additional resources would be required to collect it or whether a change in work practices or aspects of the legislative framework of receivables management warrant adjustment. We also examine the issue of whether a funding arrangement

more in line with the incentive structures that apply to the management of this function in the private sector might be tested, given the scope for additional revenue.

**3.3** In past years some of the reductions to the cost of debt collection services appear to be based on considerations other than those of the efficiency, effectiveness and equity of those services. The circumstances are outlined in Appendix 3. As about 2239 FTE staff will be employed during 1999–2000, the average accrual expense of an ATO FTE receivables management staff member is about \$67 000. We were advised that the comparable average expense in the private sector would be considerably lower, but we were not able to establish whether the costing of the expense of staff in the private sector was on the same basis as that used by the ATO.

**3.4** The increased flexibility of ATO's response to the wide variety of tax debtor behaviour is an important gain from the initiatives. The ATO is increasingly able to use the debt collection strategy that is the most likely, and in a most cost-effective way, to recover a debt. Some of these initiatives are in the early stages of implementation whereas others are more advanced. As they take effect, the gains to efficiency, effectiveness and equity could be expected to improve.

**3.5** The initiatives also improve management's capacity to match levels of resources for receivables management to desired levels of productivity, efficiency, effectiveness and equity. This gives greater flexibility to top management in the complex task of resourcing the various functions of the ATO. This enhanced flexibility is of heightened importance in the current environment.

**3.6** In this Report, we make a number of recommendations that could further increase the flexibility of ATO's response in both senses mentioned above. We expect that some recommendations would further enhance the flexibility of ATO's response to the variety and extremes of tax debtor behaviour. Others would improve management's capacity to adjust resources in response to Government, and/or ATO, priorities.

**3.7** Tables 1 and 2 in Chapter 1 shows the debt profile for all taxation debt, and collectable tax debt, in relation to debt levels for 1998–99. These tables show a distinctive feature of the structure of ATO's debt, its *Pareto* structure.<sup>41</sup> This means, broadly speaking that 80 per cent of ATO's

---

<sup>41</sup> *Pareto*: This term applies to any relationship between variables such that in general 80 per cent of one variable accounts for 20 per cent of the other and vice versa. For example, a common observation is that in organisations, 20 per cent of effort achieves the first 80 per cent of results, whereas the achievement of the remaining 20 per cent of results might take 80 per cent of the effort. The relationship is named after an Italian social scientist of the 19<sup>th</sup> Century who discovered the relationship.

collectable debt is wrapped up in only 20 per cent of the cases. Historically, the tax debt collection workload has exceeded ATO's capacity to manage all tax debt cases and the ATO had concentrated its effort on this 20 per cent, in order, according to the ATO, to maximise revenue collections. As a result, some tax debt remained unactioned and uncollected. In the past, the management philosophy within ATO had been to manage on the basis of the *Pareto* principle. This was not an explicit objective, but one to which the ATO debt collection function operated.

**3.8** ANAO found that in the past the ATO had, in the main, managed debt cases by debt level rather than by a more careful analysis of risk. Competing priorities from a mix of site-based management accountabilities from ATO offices around Australia also had a bearing on the actioning of debt cases. There were consequently relatively high amounts of aged debt in the lower level debt cases.

**3.9** ANAO is satisfied that as a result of the introduction of the initiatives reviewed in Chapter 2, the collection of debt by the ATO is now increasingly being based on a satisfactory analysis of risk.

## Contestability of ATO debt collection

**3.10** The taxpayers' relationship to the ATO is not a market-based relationship. We have been advised that there is an increasingly competitive market amongst creditors for the debts owed to them. Some creditors are likely to obtain payment ahead of other creditors. We understand that there is keen competition amongst creditors to secure payment ahead of other creditors. In this situation, creditors may get paid ahead of others because of the flexibility they have in responding to debtors. We understand that many corporates regard as essential to their way of doing business the establishment and enhancement of their reputation as requiring high levels of credit compliance from those to whom they extend credit. Strategies that creditors might use to achieve priority of payment ahead of other creditors include:

- following up on debts more promptly;
- being more persuasive that priority should be given to them; and
- being more able to impress upon debtors that the consequences of not attending promptly to the payment of the debt owing to them can be more serious than those of other creditors.

**3.11** In Chapter One we noted that there are a number of critical differences between that environment within which the ATO operates and the commercial environment. Importantly, the ATO is an involuntary creditor: it cannot refuse supply of goods/services to limit debt. The relationship between ATO and taxpayers may be more enduring than

that which applies between financial institutions and their debtors. ATO actions can influence compliance behaviour but they can also impact on a taxpayer's situation of hardship. The ATO has stressed that from its perspective, debt collection is not a pure financial equation, ie. \$s collected in relation to \$s expended. For this reason, the drawing of direct comparisons between ATO's debt collection practice and commercial collection practice is problematic.

**3.12** Notwithstanding these difficulties, the ATO has initiated a number of benchmarking studies to determine its contestability with other private and public sector collection agencies. In a keynote address the Commissioner of Taxation emphasised that the community has entrusted the ATO with a unique and important role as the custodian of the taxation system. He has stressed that the community has a strong interest in just how well the ATO performs that role. He stated further that the test of contestability is one of the measures used to assess how well that role is performed.

**3.13** The ATO undertook an international benchmarking initiative in 1997 of receivables management processes. The Commissioner of Taxation has noted that making the ATO one of the best at receivables management would be one of the leadership challenges for 1998. He further stated that, "At the end of 1998, we will re-examine our receivables management effectiveness with a view to determining whether we should proceed to formal market-testing of all or some of our processes."<sup>42</sup>

**3.14** ANAO notes that the project, *Receivables Management Benchmarking: Critical Best Practice Guide*, was a helpful step towards improved debt collection performance. The ATO has now progressed beyond this.

**3.15** ATO considers that there is a lack of consistent performance measures in wide spread use that could be readily adapted to its needs. We have been advised that there are some consistent measures that could be applied to the ATO's situation with the appropriate consideration of the ATO's unique status. The ATO is currently working with the Australian Quality Council (AQC) to develop a set of measures of operational performance for use by the ATO and for general use in the receivables management industry. These include measures such as the cost of debt collection services, stock and flow measures and the age of debt. This work has the potential to improve the transparency and accountability of ATO receivables management to the extent that it provides national (and possibly, international) performance benchmarks.

**3.16** ANAO strongly supports the ATO's benchmarking studies and

---

<sup>42</sup> "Leadership, contestability and shaping our future" speech by the Commissioner of Taxation, December 1997

considers that the development of a standardised set of performance measures will improve the ATO's ability to demonstrate its efficiency, effectiveness, equity and contestability with market best practice.

**3.17** The New Zealand Government specifies standards of debt collection performance for the New Zealand Inland Revenue Department (NZIRD).<sup>43</sup> In the Forecast Report of NZIRD the Government has specified a range of quantity, quality and timeliness standards to be achieved. As the New Zealand Government specifies separately required outputs for overdue tax returns and for overdue tax, it also specifies separately required standards for both outputs. In NZIRD's Annual Report there is a full account of achievement against these standards.<sup>44</sup> The Department also gives its reasons for under or over achievement.

**3.18** The standards specified for the management of overdue returns include the number of overdue returns collected and actioned and the proportion of overdue returns in particular categories to be collected within a specified number of months.

**3.19** The standards specified for the management of overdue tax include the amount of debt to be recovered, the number of cases to be actioned and proportions of debts relating to specific periods to be reduced and/or cleared. These include clearing 65 per cent of collectable debt within six months of the debt being identified as overdue and 85 per cent within 12 months. The standards also specify that NZIRD recover in cash \$NZ50 of tax debt for each dollar of expense and that the level of collectable debt not exceed three per cent of the total revenue collected.

**3.20** The ANAO notes that the ATO's achievements compares well with the standards set by the New Zealand Government. We found that the ATO has finalised 75 per cent of debt within six months (and 82 per cent within 12 months) of it being identified as overdue. Preliminary research indicated that the ATO might collect as much as \$A47 of tax debt for each dollar of expense.<sup>45</sup> We also found that, for the ATO, the level of collectable debt was 2.05 per cent of the total revenue collected.<sup>46</sup>

**3.21** We note that the ATO is not reporting against the full set of measures specified by the NZ Government. Nevertheless there are clear indications that the level of performance of the ATO in this area of administration aligns well with that of the NZIRD.

---

<sup>43</sup> *New Zealand Inland Revenue Department: Inland Revenue Departmental Forecast Report 1997–98*, pp. 47–48.

<sup>44</sup> *New Zealand Inland Revenue Department: Annual Report 1997–98*.

<sup>45</sup> We consider that these figures are indicative estimates only.

<sup>46</sup> As measured by the COMPACT case management system.



**3.22** The ATO considers that it is achieving a level of performance that is contestable with its counterparts in the finance sector. Notwithstanding this, the ANAO has identified a number of areas that if addressed could further improve ATO debt collection outcomes.

## Opportunities for improvement

**3.23** The implementation of the initiatives reviewed in Chapter Two has improved ATO's flexibility of response to the variety of tax debt cases arising in the community. This flexibility is expected to increase as the initiatives are more fully implemented. The ATO considers that these initiatives, particularly call centres, timely automated actioning strategies and the new Receivables Management System (when introduced in 2000) will substantially address the uncollected revenue workloads noted above. While the ANAO accepts that these initiatives will improve ATO's capacity to address these workloads, it is mindful however that the introduction of new taxation laws and systems has the potential to impact significantly on receivables management workloads.

**3.24** In the emerging environment it is possible that despite improved systems, the identified collection shortfalls will not be adequately addressed. Consequently, the ANAO has reviewed ways and means of improving performance. ANAO also considers that to be able to respond more effectively to some tax debt cases, the ATO may require additional flexibility of response. Industry best practice indicates strategies that the Government might consider appropriate for the ATO if it wants to be able to 'purchase' best-practice tax debt collection services from the ATO. There are also relatively low cost strategies (some of which might require legislative change) that could improve the timeliness of collection and taxpayer compliance.

**3.25** In the following sections, we review a range of opportunities that could lead to improved performance. Some of these relate to the use and publication of better quality information, whilst others relate to better performance by the collection of more tax debt and in a more timely manner. In particular, we review opportunities for improvement in the following areas of receivables management: shortening the time taken to finalise debt, actioning unactioned debt, reducing the amount of debt written off on the grounds that it is uneconomical to collect, improving lodgment behaviour particularly for some business debtors and shortening lodgment time frame for some income tax debtors. We consider that improved reporting and the use of better measures of receivables management performance would also result in better overall receivables management performance.

## ATO Performance information and reporting

**3.26** There are two main sources of public information about the performance of the ATO generally and of debt collection in particular. These are Portfolio Budget Statements (PBSs) and the Commissioner of Taxation's Annual Report. In the following, we review the value of performance information in these two publications.

### The Portfolio Budget Statement

**3.27** Tax debt collection, as a function of a Budget Sector Commonwealth agency, takes place within the Commonwealth's financial management framework. The key elements of this framework relevant to this audit are the Commonwealth's Budget-based resource management arrangements and the legislation governing the financial management of the Budget sector.

**3.28** In the 1999–2000 Budget the Government introduced new resource management arrangements. The appropriation bills were changed to relate appropriations to Government outcomes. The format of the PBSs was changed to show the relationship between the contributing outputs of the agency, Government outcomes and the allocation of appropriations amongst the outputs.<sup>47</sup>

**3.29** The ATO and the Department of Finance and Administration (DoFA) have recently concluded a 'Pricing Agreement'. This Agreement relates to the appropriations for the ATO in the 1999–2000 Budget, the output produced by the ATO and the outcomes for the Government.<sup>48</sup> The Agreement does not require any change in the level of ATO's debt collection performance from that achieved in previous years.

**3.30** The Agreement constitutes a development in Commonwealth budgetary arrangements. Amongst other things, it introduces an arrangement for the monitoring of ATO performance that gives practical expression to the Government's redefinition of the appropriation process. This redefinition identifies the Government as the purchaser of agency outputs. The relationship of the Government and the ATO is that the Government is a monopsony purchaser and the ATO is a monopoly

---

<sup>47</sup> The outcome/output resource management framework that the Commonwealth introduced in the 1999–2000 Budget was based on those introduced by State and Territory Governments since 1993. The Commonwealth has adapted frameworks pioneered by the other governments to the Commonwealth's situation, making some minor modifications to detail.

<sup>48</sup> DoFA explains that the purpose of the Agreement is to establish the appropriate level of resourcing for the ATO to administer Australia's taxation, excise and superannuation systems. One of the main intentions of this Agreement is to provide the ATO with a degree of certainty over its future funding, whilst at the same time avoiding the need to approach Government for additional resources for minor policy variations.

provider. That is, that the Government can only ‘purchase’ this output from the ATO, and the ATO can only ‘sell’ this output to the Government.

**3.31** These features of the new resource management arrangements require agencies to measure correctly on an accrual basis the net cost of producing their outputs. ATO’s PBSs for the 1999–2000 Budget list ATO outputs for which the ATO received appropriation. The PBSs identify four distinct outputs and their related appropriations, as submitted to Parliament for approval.<sup>49</sup> These are:

**Table 6**  
**ATO Outputs and Appropriation 1999–2000**

<i>Output</i>	<i>Appropriation (\$)</i>
Contribution to Policy Advice and Legislation	78 920 000
Income and other taxes	1 347 645 000
Transfers	86 813 000
Cross Agency Support	79 826 000
<b>Total</b>	<b>1 593 204 000</b>

**3.32** The PBSs indicates that these four outputs and the appropriations for them are necessary for the achievement of the one Government outcome set for the ATO. This Government outcome is, *effectively managed and shaped systems that support and fund services for Australians and give effect to social and economic policy through the tax system*. The PBSs also indicate the measures to be used for the achievement of that outcome.

**3.33** ‘Reduction in overdue debt’ is one of several measures used to assess the achievement of the single Government outcome to which the ATO contributes. It is an ambiguous measure of performance. Simply increasing the amount of debt written off can reduce debt. This has not been ATO’s practice. As previously reported, we find that there has been a significant decrease in the amount of debt written off since 1995–96. However, unless it is known that reduction in overdue debt is not a result of increases in the amount of debt written off, a reduction in overdue debt remains an ambiguous measure of performance. Hence “reductions in both overdue debt and debt written off” would be more valid measures of the maintenance of overall compliance levels.

**3.34** An increase in the amount of overdue debt can mean that the ATO is functioning with increasing effectiveness. The ATO has recently been targeting areas such as the cash economy, aggressive tax planning, tax avoidance and evasion. This has resulted in the raising of almost

<sup>49</sup> *The Portfolio Budget Statements 1999-2000: Treasury Portfolio*, Budget Related Paper No. 1.16, p. 85.

30 per cent more debt in 1998–99 than in prior years. Not all of this debt will be collected in the year that it was raised. Some might never be recovered. The result could be that there is no decline, and perhaps an increase, in the level of collectable debt as a percentage of total collections. In this case, even the more complete measure ‘reductions in both overdue debt and debt written off’ could rise. This could be taken to indicate a decline in ATO’s performance, when performance had actually improved. At the same time as 30 per cent more debt was raised, the ATO has reduced the amount of debt written off. During this time ATO debt collection productivity has also increased and eight per cent additional debt has been finalised. However, the PBS measures would imply that ATO performance has declined, which is contrary to what has actually happened.

**3.35** This suggests that measurement of variations in the amount of overdue debt is inadequate even as a partial indicator of the achievement of the single outcome specified by the Government for the ATO.

**3.36** The PBSs specify the measures of quantity and quality that would be used to measure the provision of the four outputs. These measures include two that are part of the receivables management framework: the reduced level of collectable debt as a percentage of total collections and an improved professionalism in debt collection. The measure “the reduced level of collectable debt as a percentage of total collections” may be an inadequate measure of the achievement of the Government outcome for the reasons advanced above. It might also be an inadequate measure of the efficiency of producing output for these same reasons. We consider that measures of improved professionalism in debt collection are best obtained from the work underway with the AQC. This matter was discussed in more detail in paragraph 3.15.

**3.37** Other revenue collection agencies and major finance sector firms operate against more detailed specifications of performance. As noted in paragraphs 3.16 to 3.21, the New Zealand Government’s equivalent of the PBSs contains more information about the goods and services produced and the levels of performance achieved by its national revenue collection agency. We note that the more detailed performance information published by the New Zealand Government about NZIRD’S administration of receivables management may improve the accountability and transparency of NZIRD in respect of that function.

**3.38** The ATO advise that it has recently reached agreement with DoFA that less detailed specifications at the PBS level are preferable. Less detail in the specification of performance is considered preferable because less detail enables the ATO to adopt a more flexible approach in its

management of resources. Executive management has greater flexibility to resource those areas of administration that risk assessment shows are of highest priority. ANAO notes that this strategy allows the ATO to adopt a more flexible approach to administration and management to better identify risk areas than would be possible if there were greater specification. However, during recent Senate Committee hearings into the Budget Estimates 1999–2000 concern was expressed about the lack of detail in PBSs.<sup>50</sup> Insufficient detail can hinder good accountability. In addition, ANAO draws attention to the shortcomings in the current high level measures of performance published in the PBS with regard to debt collection.

### **Annual reporting**

**3.39** The ATO's Annual Report publishes some information about the performance of the receivables management function. The information includes tabulations showing debt collection results over several years and a commentary about some features of the increasing debt collection workload. The 1997–98 Annual Report included some information about the international benchmarking study of debt collection practices. The Report also contains a graph showing a continuing decline in the amount of collectable debt as a percentage of total collections. The publication of such information is an important component of accountability. However, the ANAO considers that publication in the Annual Report of better information about receivables management results would be highly desirable. An accurate and comprehensive picture of receivables management performance could be provided by giving an account of performance against objectives.

**3.40** The ATO has a strategic plan for the receivables management function. Amongst other things, this will result in a statement of the function's goals, objectives and strategies. We understand that the objectives will include:

- ensure that all debt is managed and minimise the debt written off;
- improve the integrity of the tax system and minimise the amount of debt;
- improve cost effectiveness of recovering maximum debt in minimum time;
- achieve cost effective recovery of all cases of collectable debt; and
- improve the equity of debt collection.

---

<sup>50</sup> Budget Estimates 1999–2000 Report Senate Finance and Public Administration Legislation Committee June 1999; Budget Estimates 1999-2000 Report Senate Economics Legislation Committee June 1999.

**3.41** This clear statement of effectiveness, equity and efficiency objectives assists good management, as does the translation of them into operational performance targets for which management and teams can be held accountable. Actual performance against those targets can then be readily assessed and reviewed regularly, perhaps monthly.

**3.42** The ATO has translated the above objectives into operational performance targets, such as:

- recover percentages of collectable debt within a specified time (eg. 30, 60, 90 days);
- take (to be specified) administrative action on every case within a specified number of days of the date due for the payment of tax; and
- manage every debt collection case.

**3.43** The ATO has developed and uses a range of qualitative performance measures of such variables as: the security and privacy of information about tax debtors, the appropriateness and completeness of actions taken by ATO staff and the currency of information recorded on COMPACT screens.

**3.44** Performance and accountability of the receivables management function could be strengthened if proportionate reductions in the amounts of debt and the numbers of cases for future years in relation to prior years were specified in the annual report. We acknowledge that the adoption of such quantitative measures of achievement and the publication in the annual report of performance in relation to them should have regard to three considerations. One is the extent to which debt collection workload can increase because of factors outside the control of debt collection management. Examples of such factors include legislative change, the nature and extent of non-compliant behaviour and the conduct of campaigns by the ATO to detect and prevent such non-compliant behaviour. These factors might have no equivalents in the operations of the private sector.<sup>51</sup> The second consideration is the extent to which debt collection management can resource debt collection work in response to variations in the debt collection workload. The third factor is the relative priority of the collection of debt amongst the various functions of the ATO.

---

<sup>51</sup> In relation to this point, we have been advised that the workload of the debt collection group within a private firm can increase by factors outside the control of the group including, initiatives taken by management to increase sales, to promote a particular product or to achieve market dominance. The impact on debt collection can be an unanticipated and large increase in the workload and a greater proportion of difficult to collect debt.

**3.45** ANAO recognises that the deployment of additional resources to debt collection may have an opportunity cost for the ATO. Whilst additional debt might be recovered with additional resources, those same resources if utilised elsewhere in the ATO, might well have a more significant impact on the overall level of compliance. We understand that debt collection management in the private sector has a greater degree of flexibility in matching resources to workload than does its ATO counterparts. The receivables management group in a major financial institution would normally have greater flexibility than its ATO counterpart to resource meeting targets such as proportionate reductions in the amounts of debt and the numbers of cases for future years in relation to prior years. Such targets could be set for the ATO's receivables management function. We recognise, however, that there would seem little point in setting such performance objectives for the ATO if the achievement of them required a flexibility in the resourcing of debt collection that is currently unavailable.

**3.46** As a result of the management changes referred to in Chapter 2, the ATO includes the measurement of variables for which such specifications about targets for proportionate reductions might be made, including the following:

- amounts of collectable debt in the categories new, old and ancient;
- the percentage of debt written off as uneconomic to collect;
- the proportion of debt on which there has been minimum action; and,
- the cost of various debt collection services.

**3.47** We note that management may make trade-offs amongst these variables. For example, there may be a greater focus on the collection of new debt. As resources are limited and flexibility of response constrained, this could mean that the amount of aged debt increases.

**3.48** The inclusion of targets in annual management plans that would be used to govern the work of the ATO receivables management teams around Australia would help develop a performance oriented culture more like that to be found in the major firms in the private sector. We have been advised that a high performance culture characterises the more successful firms. Targets for management teams and staff that relate to improvements in performance in measures of the above variables are standard practice. Qualitative information is usually used as well. These relate to the professionalism of staff, and the growth of firm's client base, particularly in relation to those categories of clients most valued by the firm. In response to these observations, the ATO has commented it operates to a set of national operational performance standards and

business deliverables and that as a result of the move to a national data base under enhanced COMPACT, the ATO will have the means of allocating work nationally to receivables teams' staff (ie. so that staff in one site can work on cases emanating from anywhere across Australia) and that COMPACT-based management reports already report on a site basis. The ATO stated that a national focus is already in place for ATO's Call Centre operations. The ATO considers that against this background, and given the potential industrial sensitivity of site targets, it would question whether there would be any further net gain from moving to site based targets.

**3.49** The establishment of a tax debt is different from the activity of collecting a debt. The workload arising from ATO's need to establish a tax debt means that the ATO is different, at least in this respect, from other debt collection firms. A standard commercial relationship sees a debt established as part of a commercial transaction arising directly from the supply of good and services. The ATO, on the other hand, requires taxpayers to advise of amounts withheld from employee payments and/or to obtain lodgment of an incomplete return to establish the value of the outstanding debt. This task of debt establishment is a key part of tax administration but inclusion of it in the costing of debt collection services might mean that the ATO is costing its debt collection services on a different basis to its private sector counterparts. If the ATO wishes to be able to compare accurately the cost of its debt collection services with those of the private sector, debt establishment activity ought not to be included in the costing.

**3.50** ANAO found that there is a substantial workload associated with the establishment of tax debts for the recurring taxes. We also found that this cost is included in the cost of debt collection services. However, in the case of the recurring taxes, the establishment of a tax debt is not readily disentangled from the collection process. Nor is it necessarily desirable to do so. We consider that the nature of revenue collection often means that debt establishment and collection are aspects of the one greater task. We suggest that, nevertheless, the ATO should maintain costing systems that more accurately measure these two aspects of revenue collection. Inclusion of the cost of debt establishment as part of the cost of debt collection services inflates the cost of those services. We consider that they should be separated in the information published about receivables management performance.

**3.51** ANAO considers that the ATO could improve the range and quality of performance information published in the Annual Report for 2000-01 by publishing the key objectives of receivables management performance in the SB and INB business lines that currently guide



performance and the performance achieved in relation to those objectives. ANAO considers that the ATO should provide more information about debt in relation to category and time taken to process.<sup>52</sup> Any amounts of unactioned collectable debt should also be reported showing the length of time it has remained unactioned. In addition, the ATO should continue to publish in the Annual Report information about tax debt that relates more to the overall performance of the ATO than solely to the performance of the receivables management function. The ATO could produce more reliable high level measures of performance for inclusion in the PBS that use changes in the amount of overdue debt by having a suite of more informative measures such as these to draw upon.

## Recommendation No.1

**3.52** ANAO recommends that the ATO improve the range and quality of information published about receivables management outcomes and outputs. Particular attention should be paid to:

- the examination of alternative measures that have regard to debt at the Portfolio Budget Statement level; and
- the publication in ATO's annual report of key comparative information about the contestability of ATO receivables management performance.

*ATO Response: Agreed*

The ATO will continue to review its debt collection performance measures, in the context of the major changes to the ATO systems and work practices currently under way or planned over the next 12–18 months.

Publication of contestability-related information in the annual report will follow, as soon as those changes are complete and implemented.

## Recommendation No.2

**3.53** ANAO recommends that the ATO improve the accuracy of the measurement of the net cost of debt collection services by excluding the cost of other major receivables management services.

*ATO Response: Agreed*

The ATO will review, and continue to refine its costing methodology with a view to isolating the net cost of debt collection services; and to developing contestability measures which are consistent with industry practice.

<sup>52</sup> Categories include: proportions of active, collectable, finalised and unactioned debt in relation to the time taken to process, and the amounts of debt written off as per the FMAA categories of: write off authorised by another Act; not lawfully recoverable; and, recovery not economical.

The ATO notes that the task of separating the component costs of the receivables management process is likely to be complicated, due to the different natures, recurrences and inter-relationships of various taxes.

## Additional revenue opportunities

### Shortening the time taken to finalise debt

**3.54** There is opportunity for increased revenue by shortening the time frames in which debt is finalised. We analysed, on the ATO's data warehouse<sup>53</sup>, the time taken by the ATO to finalise debt<sup>54</sup>. The results are presented in Figures 6 and 7. These cases carried total tax revenue of \$4.3 billion. The ATO finalised 318 440 cases (ie. 52 per cent of a total of 611 930 cases) within 30 days, resulting in the recovery of overdue tax of \$1.8 billion (ie. 42 per cent). A total of 562 019 cases (ie. 92 per cent) were finalised within one year, resulting in the collection of \$3.56 billion (ie. 82 per cent). The analysis shows that the ATO collected as much collectable debt within the first 30 days as it did in the remaining 330 days. At the end of 12 months, 18 per cent (\$774 million) of collectable debt was still uncollected.

**3.55** We have been advised that the standard guideline in the private sector is to collect all collectable debt within 180 days. We were advised that all debt is actively pursued and the difficult to collect cases may be actioned several times until settled. As a result the proportions of aged and written off debt in the private sector may well be lower than in the ATO.

**3.56** We consider that the ATO may be able to recover higher rates of tax debt than we have found. This view is based on two factors. One is our examination of ATO's experience with the collection of aged debt (in particular, ancient, small business income tax debt). The other is that taxpayers' relationship to the ATO is different to the relationship between a private sector firm and those to whom that firm extends credit. Taxpayers' relationship to the ATO is not a market-based relationship. People are required by law to pay tax and the ATO is in no position to withhold supply as a means of collecting debt, as are other creditors.

---

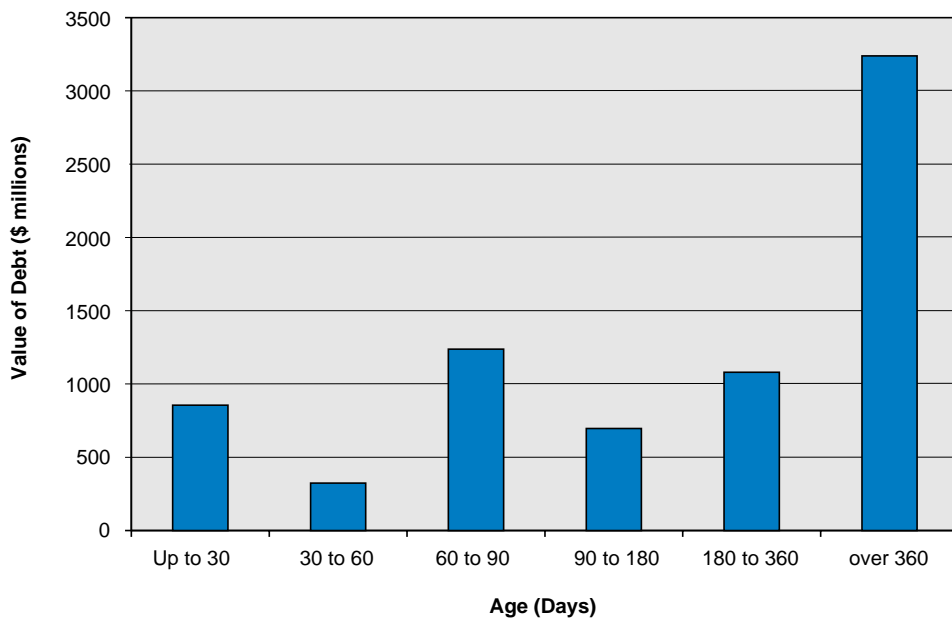
<sup>53</sup> There are shortcomings in the quality of the data on the data warehouse. These are discussed in Appendix 6.

<sup>54</sup> Child Support agency debts have been excluded.

**3.57** Opportunities for further improvement in the cost effectiveness<sup>55</sup> of debt collection depend upon the scope for the quicker finalisation of active debt and the speed and accuracy with which all collectable debt is collected. There could, however, be an additional expense incurred in obtaining the further improvement. There may also be limitations in debtors' capacity to pay within decreasing timeframes. This is likely to be the case with some debtors. To the extent that this is the case, there would be a limit to further improvement in the timeliness of debt recovery. Nevertheless we consider that the ATO could collect collectable debt more quickly and may need to work to higher standards of collection.

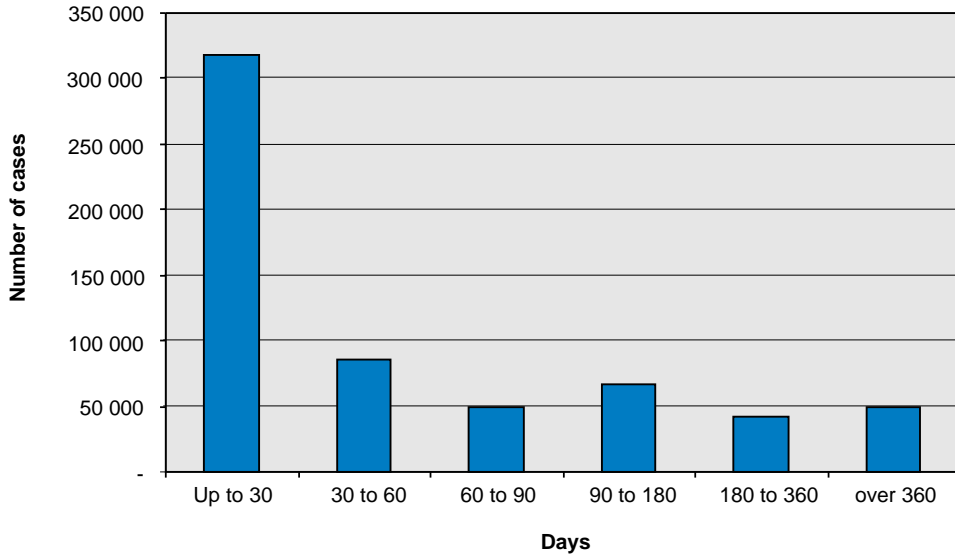
### Figure 5

**Age Profile of Overdue Debt on hand at 30 June 1999**

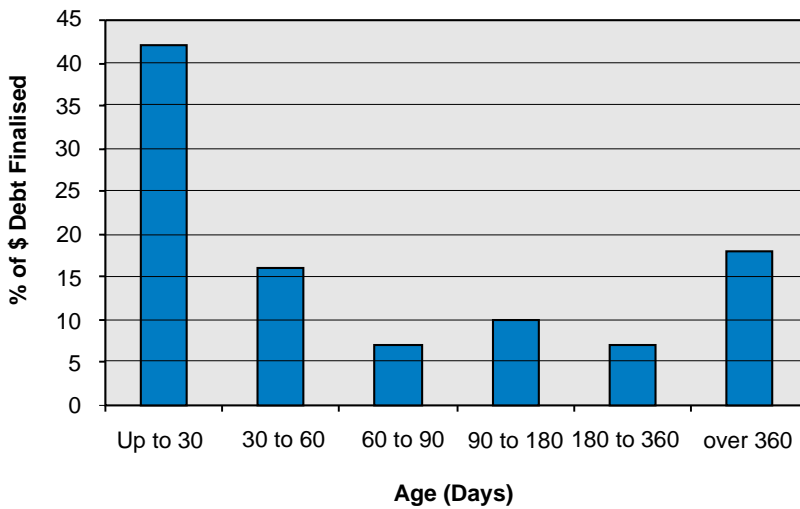


<sup>55</sup> Cost effectiveness is a procedure used to evaluate alternative ways of achieving an objective in terms of measuring their relative contribution to the achievement of that objective. A good account of the procedure can be found in the *Handbook of Cost/Benefit Analysis* published by the Department of Finance in 1991.

**Figure 6**  
**Days Taken to Finalise Cases 1998–1999**



**Figure 7**  
**Age Profile of Debt Finalisation 1998–99**



## Unactioned active debt

**3.58** There is also scope for additional revenue by the collection of unactioned debt. Of total collectable aged active debt (ie. about \$2.2 billion), 55 per cent has been actioned, initial action had been taken on 38 per cent (ie. \$836 million) and just under seven per cent (ie. \$154 million) is unactioned.<sup>56</sup> Almost all of this unactioned debt is in the “old” category. It consists of 30 203 cases with an average debt of about \$5000. ATO advise that about 70 per cent (ie. \$100 million) of this is now collectable. There is scope for additional recovery rates from the initially actioned category of debt. Unless this debt is actioned there is, in ANAO’s view, an unacceptable risk that it would not be collected and may even be written off. We understand, furthermore, that the ATO might not be able to collect it, given the current resource base for receivables management. We consider that the ATO should take steps to collect all unactioned debt. If the current resource base is insufficient for this purpose, ATO management might wish to consider the scope for the reallocation of resources to receivables management from lower priority activities. There is also scope for different and possibly better work methods and strategies, including outsourcing some debt collection work. The ATO might wish to raise with Government changes to legislative arrangements such as those indicated elsewhere in this Report.

## Ancient debt

**3.59** During 1997–98 the ATO undertook a project to collect ancient debt on hand in one region. A summary of this project is at Appendix 4. Although accurate records of the project were not kept, the ATO estimated that the project examined about 1400 ancient debt cases that had a total of approximately \$25 million in overdue tax debt owing. These were small business tax debtors and the debt related mainly to income tax. The ATO advised that the likely revenue that will accrue from this project when all negotiations and arrangements are settled would be about \$12 million. Only 16 per cent of the debt was written off when strict rules were applied to the writing off of debt. We were advised that there was nothing unusual about the ancient, small business debt cases examined in this project. The ATO regarded them as typical of “ancient”, small business income tax debt cases.

---

<sup>56</sup> UNACTIONED means that no action had been taken on the debt since it had been referred to COMPACT for collection. Our initial research indicated that the total amount of unactioned debt was \$673 million. In response to this indicative finding, ATO advised that \$528 million of disputed debt had been incorrectly coded as “unactioned” on COMPACT. We accepted ATO’s advice. This is a quality assurance issue that is being progressively addressed through new quality assurance and data cleansing processes.

**3.60** The ATO advises that all of the debt examined by the project would have been written off had the project not been initiated. The project may suggest that some of the debt written off as uneconomic to collect may be collectable, if additional investment was applied to this area. Accordingly, ANAO examined the legislative framework for the write off of Commonwealth debt, the guidance provided by management to staff about write offs and alternative strategies for pursuing debt that might otherwise be written off.

### **Debt write-off**

**3.61** Section 47 of the *Financial Management and Accountability Act 1997* (FMAA) governs the management of the recovery of overdue taxes.<sup>57</sup> The FMAA provides the framework for the administration of the provisions about tax debt that arise from specific tax legislation such as the ITAA.

**3.62** Section 47 of the FMAA states that a Chief Executive Officer must pursue recovery of each debt for which the Chief Executive is responsible unless:

- the debt has been written off as authorised by an Act; or
- the Chief Executive is satisfied that the debt is not lawfully recoverable; or
- the Chief Executive considers that the recovery of the debt is not economical.

**3.63** As previously noted, some taxpayers dispute debt. As well, insolvent debtors owe some debt. A further proportion of tax debts will not be recoverable under the terms of section 47 of FMAA. In addition, section 265 of ITAA and section 133 of FBTA provide for the release of debtors in cases where payment of the income tax or fringe benefits tax debt will cause serious hardship.

**3.64** We reviewed the guidelines provided by management to staff about the operational meaning of ‘uneconomic to collect’. We suggest that ATO set out clearer guidance to staff than that currently provided. In some cases, the ATO should, and does, pursue the recovery of debt even when the cost of doing so is greater than the amount of the debt. In these cases, there could be a public policy premium related to the

---

<sup>57</sup> This is because s208 of ITAA establishes a tax as a debt to the Commonwealth; overdue tax is a debt owing to the Commonwealth. Section 47 of FMAA governs the management of all debt owing to the Commonwealth.

clarification of a question of law or because compliance considerations might be compelling. Guidance to staff could be clearer on these points. Current guidance is silent, however, about the relationship between the amount of debt and the cost of recovering it when no other considerations apply. We suggest that this be rectified.

**3.65** Our 1996 Report found that there had been a decrease in uneconomic to collect write offs of 75 per cent between 1994–95 to 1995–96. The ATO advises that the amount of debt expected to be written off in 1998–99 will be \$417 million. Of this amount that the ATO expects to be written off as uneconomic to collect is \$73 million. Some of the uneconomic to collect write offs arise because the ATO cannot trace the debtor. We examined the number of untraceable income tax non-business debtors and the amount of debt associated with them. We were not able to produce a similar tabulation for untraceable business tax debtors because of shortcomings in the quality of the data on this matter.

**3.66** ATO staff place an “untraceable indicator” on the COMPACT record of a taxpayer that they cannot trace. By counting the number of COMPACT records for INB income tax debtors with this indicator, we found that there were 6989 untraceable individual income tax debtors who had a total debt of \$27.6 million. There were 12 individuals who could not be traced with income tax debts greater than \$100 000. In total, these 12 owed \$5.42 million; that is, an average of about \$450 000 each. Table 10 in Appendix 10 provides further detail on untraceable debt cases. We have been advised that the private sector has special expertise for tracing difficult to locate debtors. A rate of about 60 per cent success after three to four months is not uncommon. We consider that the ATO should examine scope for using this expertise for location of debtors currently regarded as untraceable. For example, the ATO could trial, with a firm, a group of between 500 and 1000 untraceable debtors to locate the debtor for the ATO.

**3.67** We found that where a debit balance falls below a certain level, it is no longer recorded on COMPACT and therefore no longer the subject of the collection actions enabled by COMPACT. This occurs because the amount is considered to be uneconomic to collect.<sup>58</sup> ANAO understands that the ATO retains the capacity to apply any future refund to acquit the debt until the debt is paid.

---

<sup>58</sup> We note that this practice has the potential to distort final case balance and collections data.

**3.68** Cases are automatically removed from COMPACT when they fall below specified debt levels as follows:

- NTS cases (income tax): \$100;
- AIS cases (PAYE, PPS, Sales Tax): 50 cents;
- FBT cases: \$100.

The debt may comprise primary tax and/or penalty amounts.

**3.69** There may be now no justification for writing off these amounts as uneconomic to collect. They may be recoverable by sending the taxpayer an automatically prepared letter. If resources permitted, there may be scope to use the call centres to pursue these debts in some instances.<sup>59</sup> We have been advised that making outgoing and adequately managing incoming telephone calls is very important to good recovery action. We raised this matter with the ATO which advised that the issue of the automatic removal of a case from COMPACT where a debit balance falls below a certain level will be addressed in the design of the new RMS.

**3.70** ATO advised that about 30 per cent (ie. about \$20 million) of the \$73 million debt written off as uneconomic to collect could be collected, given sufficient additional investment. Financial institutions also write off debts because such debts are uneconomic for them to collect. The collection of these is then usually outsourced to mercantile agents. We have been advised that private debt collecting agents would collect at least half (rather than 30 per cent) of such debts.

**3.71** FMAA requires that all debt be pursued. We raise for consideration whether this requires the ATO to more vigorously manage those debts on which COMPACT codes and records indicate little or no action has taken place.<sup>60</sup> The legal meaning of “pursue” also has a bearing on the pursuit of debtors that are difficult to locate especially where the debts are below Level 3.

**3.72** We note that debt classified as uneconomic to collect is still potentially available for collection. The ATO advise that it may be able to collect the debt in the future in response to future tax returns.

---

<sup>59</sup> The ATO advises that although there may be scope to use Call Centre to pursue *small* level debts (eg. less than \$100), the first priority will be to continue to focus on *higher* level debts in line with ATO's case profiling strategy.

<sup>60</sup> In response to this comment, the ATO advise that the minimal action that would be taken would include sending a debtor the Notice of Assessment, a Final Notice and (usually) a Standard Letter. The ATO further advise that the new Receivables' environment now being progressively adopted should enable the more rigorous management of the overall workload and that nonetheless, the underlying objective of the ATO will always be to maximise debt collection at minimal cost.



## Recommendation No.3

**3.73** ANAO recommends that the ATO issue operational guidance to staff as to the meaning of ‘recovery of the debt is not economical’ in section 47 of the *Financial Management and Audit Act 1997*.

### *ATO Response: Agreed*

The ATO accepts that some clarity is needed to better define the meaning of “recovery of the debt is not economical”.

The ATO will revise its Debt Collection Policy and standard work practices to provide greater guidance as to the meaning of “recovery of the debt is not economical”. That guidance will cover the direct costs of collection, risk management, contestability and the opportunity cost of using those resources elsewhere.

## Improved lodgment

**3.74** The first step in establishing debt is assessment of tax lodgments. There is a need for a higher volume of lodgment enforcement work to be carried out and for the quicker actioning of current year return outstanding cases. Research undertaken for higher level business debtors indicates that at least 25 per cent of high level debtors are also late lodgers or non-lodgers; more persistent action to secure lodgment in these cases seems warranted. Improved lodgment compliance could result in the prevention of debt. ANAO considers that there is scope for improvement in the detection of non-lodgers and late lodgers, particularly in relation to business taxes. More timely and effective action on lodgment matters could increase revenue and reduce debt in the longer term. However, it would have the short-term impact of increasing the amount of debt to be actioned and recovered by receivables management teams.

**3.75** In order to improve lodgment compliance and to expedite collection, the ATO might consider immediate tracing and location of taxpayers if correspondence and Final Notices, particularly those relating to debit assessments, are returned to the ATO and marked ‘address unknown’. We found that most of the branch offices visited during the audit did not take tracing action in response to correspondence being returned. We understand that it is standard practice in the private sector to mark returned mail on the system and then take action to locate the addressee.

## **Shortened lodgment timeframes**

**3.76** There is a time interval between the time at which income tax is due and the taking of action by the ATO to recover unpaid overdue tax. The time interval has four main components. These are:

- the time interval between the date on which the income tax is due and the date on which the lodgment of income tax returns is required;
- the time taken by the ATO to issue an assessment notice upon the receipt of an income tax return;
- the time interval between the due date of the Notice of Assessment and the subsequent issue of the Final Demand Notice; and,
- the time taken by debt collection teams to recover debt.

**3.77** Our main focus in the following paragraphs is on the scope for shortening the first time interval. It is also one that the ATO can shorten subject to the constraints of administrative law and public expectations. As we have not reviewed ATO's assessment of income tax in this audit, we make no comment on the scope for shortening the second interval. In this audit, we have reviewed the timeliness of ATO performance in respect of the fourth time interval and we have made recommendations for improvement.

**3.78** We found that there was not much scope using COMPACT to improve the third time interval. The tax should be paid by 30 days after the receipt of the assessment notice. If the tax is not paid by this time, there is a further delay before the Final Demand Notice is issued. As a result of recent initiatives, all NTS debt Levels 1 to 6 cases are now referred to COMPACT for collection seven days after the Final Demand Notice is triggered. The Final Demand Notice is triggered by an accounting review on the first Saturday after a debit is at least 10 days overdue. The Notice will be issued three days after the tenth day. NTS Standard Letter criteria stipulate that letters will not be issued on any case within three weeks of the due date. ATO administrative practice has the consequence that 24 days might elapse between the due date for the payment of overdue tax and the taking of collection action. There may be scope for some reduction in this number of days in light of the implementation of the new RMS.

**3.79** The following is an analysis of the scope for, and benefits from, shortening the first time interval. Most INB income tax payers have paid their tax by the due date because tax has been deducted by PAYE installments. The ATO has a lodgment program by which the orderly lodgment is managed. The ATO issues to these people a debit assessment after their income tax returns have been assessed. For such taxpayers

the income tax that they owe was notionally due at the time the income tax was due to be paid. This is usually the end of the financial year, June 30. The ATO exercises administrative discretion and does not require the lodgment of returns for many months. For example, in the case of returns lodged through tax agents, lodgment of an income tax return for income tax payable for the financial year ending June 30 might not be due for nine more months: that is, until the end of April in the following year.

**3.80** The Commonwealth incurs a Public Debt Interest (PDI) expense for the interval between the time when income tax is due and when tax payable is received for those persons who have an assessed income tax liability at June 30. The imposition and payment of the General Interest Charge (GIC) is of the same order as the PDI expense incurred whilst the debt remains an active debt on COMPACT.

**3.81** An issue for consideration is the reduction of the time interval between the date on which the income tax is due and the date on which the lodgment of income tax returns is required for some (or all) income tax debtors. The ATO has the administrative discretion to do this, and there may be scope for improved financial benefits from earlier collection. Reducing the interval might also function to improve compliance for some income tax debtors. The experience of debt collection firms suggests that reducing the time interval between the date on which a debt is due and the date on which action is taken to recover it, increases the likelihood that the debt will be paid.

**3.82** Twelve months could elapse between the end of the financial year for which income tax is payable and the first collection action by ATO's debt collection teams. In a small proportion of income tax debtors, a further 6–12 months or more might elapse before the debt is paid.

**3.83** The time delay between the time at which the tax is due and the time at which it is actually paid has a financial cost. This cost could be estimated for the total number of income tax debtors. An ABS study undertaken on 1996–97 income year data, found that 18 per cent (ie. 1.2 million people) of INB taxpayers receive a debit assessment. About seven per cent of these, (ie. approximately 80 000), subsequently became overdue tax debtors.

**3.84** Under current arrangements, it is reasonable to expect that the 80 000 or so INB tax debtors would be aware of the gap between the date due for tax payment and the date the tax might be eventually paid. Many would be aware that several months would have elapsed between the date on which tax was notionally due (ie. June 30) and the date on which collection action would be taken to ensure that the debit assessment

is paid. They would also be aware that an interest charge would accumulate if a tax debt is not paid by the date for payment of tax debts specified by the ATO.

**3.85** The ATO has the discretion to vary the date by which taxpayers must lodge income tax returns. There may be benefits to the Commonwealth from shortening lodgment time frames for some income tax debtors. The income tax debtors to whom this may apply would be those who in the previous year were overdue debtors and were recorded on COMPACT. This would be achieved by requiring particular income tax debtors to lodge their income tax returns for next year much closer to June 30 than is now required. If taxpayers with a particular debtor profile were required to pay their tax earlier and did pay their tax earlier, there may be financial benefits to the Commonwealth from earlier collection. This profile could be constructed to exclude those on incomes below a specified threshold or in circumstances of hardship for whom the shortening of lodgement timeframes could prove an unfair detriment. There may also be an overall improvement in compliance behaviour.

### **Estimated additional revenue**

**3.86** In paragraph 3.58 we reported that additional revenue of about \$100 million could be collected from unactioned collectable aged debt, given an additional investment. In paragraph 3.70 we reported that additional revenue of about \$20 million could be collected from the debt written off as uneconomic to collect, given an additional investment. During the audit, the ATO advised that this investment to collect the total of \$120 million would be in the order of \$7 million. If this investment were applied to the recovery of this amount, the ATO has estimated that it would collect up to \$17 additional revenue for each dollar expended. This is in contrast to the current average return for debt collection, that ATO data indicates is \$47 revenue for each dollar expended.<sup>61</sup>

**3.87** We acknowledge that ATO management must trade-off the expenditure of resources to recover debt against expected levels of revenue from the cases actioned. Relevant to this trade off is a feature of tax debt collection that the cost of collecting a debt rises with the difficulty and complexity of collecting the debt. Our preliminary research suggests that pursuit of the more difficult to collect debt might generate less than one half of the average debt collection revenue for each dollar of expense, other things being equal. The ATO has emphasised that it considers broader social issues and believes that a \$ expended to

---

<sup>61</sup> We consider that these figures are indicative estimates only.

\$ collected equation, which applies in a commercial environment, should not be the sole consideration for the ATO. On this basis the higher cost of, and lower revenue from, the collection of the more difficult to collect debt need not itself be an impediment to the pursuit of such debt.

**3.88** We consider that there is limited scope for improved debt collection performance within the existing legislative framework without additional resources being allocated to the function. This depends on the scope for improved efficiency in the use of the current resource base of the receivables management function. The assessment of the precise scope for improved performance is limited in part because the benefits of the initiatives outlined in Chapter 2 will take some time to be achieved fully. Towards the completion of the audit, the Commissioner of Taxation allocated an additional \$10 million per annum to the receivables management function for each of the next three years. Nevertheless, the ANAO considers that there is scope for positive revenue returns to the Commonwealth by the ATO having greater incentives to achieve better practice, as well as greater flexibility to do so, to an extent comparable to its private sector counterparts as outlined in this Report.

## Outsourcing some ATO debt collection

**3.89** The ATO has, with the knowledge of the Government, initiated discussions with some financial institutions about ways in which these firms could assist the Commonwealth to recover tax debts. We found that there is a range of feasible options for examination. The application of these to the collection of tax debt owed by both individual and non-individual taxpayers and in relation to income and recurring taxes might also be raised with Government. There are four main options to consider. A number of these options raise complex issues of tax administration as well as sensitive issues of public administration. Some would require legislative change, a step that would presuppose the careful evaluation of possible gains to effectiveness tempered by the consideration of the complex and sensitive issues. In the following we review the broad range of these issues and highlight the main areas of benefit.

**3.90** The four options, not all of which are equally feasible at this time, are:

- Financial institutions might be prepared to take over some tax debts as loans.
- There may be scope to sell some tax debt to interested financial institutions. In the private sector, debt is sometimes a saleable asset.

We have been advised that there is an emerging industry trend towards this option. The initial step for the ATO would be the conduct a due diligence study to identify benefits.

- The ATO might be able to negotiate arrangements with financial institutions so that some tax debtors could use credit cards to repay debt.
- Fee for service to be paid where the ATO contracts with commercial debt collection firms for the collection of some debts.

**3.91** As each of these options involves the use of an agency outside the ATO to take a significant role in the collection of all or some of the debt, the four options are collectively referred to as outsourcing the collection of tax debt.

**3.92** The first two options could include arrangements whereby the financial institutions pay out an agreed amount of the debt to the ATO and then proceed to recover the debt from the taxpayer.<sup>62</sup> This could be achieved by the financial institution advancing the taxpayer a special loan or by the taxpayer simply using existing credit facilities.

### **The use of credit cards**

**3.93** It is a common, but not universal, practice in the private sector to allow debtors to use credit card facilities to pay debts. We have been advised that private sector credit providers aim to offer their clients every means of payment, including by credit card. Giving the customer a range of payment options to pay decreases the limitations of payment. There is no facility for tax debtors to use credit cards to pay tax debts. The use of credit cards to pay overdue tax (ie. tax debts) raises the wider issue of the use of credit cards to pay tax. The ATO has undertaken detailed research on the feasibility of using credit and debit card facilities to meet taxation payment obligations.

**3.94** The ATO research identified scope for Commonwealth revenue flows to be adversely impacted, and noted that the ATO could face large administrative (eg. merchant service fee, and some opportunity) costs were it to move to introduce credit card costs for the payment of overdue tax debts. Concurrently, with some welfare recipients being among the overdue tax debtors the ATO could anticipate some adverse community reaction, particularly from social welfare groups, arising from the effective transfer of debt from the Commonwealth to the private sector. Nonetheless, the ATO has indicated its preparedness to keep this matter

---

<sup>62</sup> The agreed amount would in some instances be the total amount of debt; in other cases it would be a reduced amount.

under observation. One complex aspect of the issue is the transfer of debt from the Commonwealth to the private sector. We understand that some finance institutions have the arrangement whereby if a debtor chooses to pay their debt by credit card, the debtor also pays the merchant fee. There may be scope for the ATO to re-visit this issue given the increasing use of credit cards in the finance sector and the ATO client base<sup>63</sup>.

### **Outsourcing to commercial debt collection firms**

**3.95** Centrelink has a flexible debt collection strategy that involves outsourcing the collection of some debts, known as “suspended debts”, to mercantile agents. A suspended debt is a debt that Centrelink has determined to be either not cost-effective to pursue or is that of a debtor whose whereabouts is unknown. Former recipients of income support assistance owe the suspended debts. Approximately 10 per cent of Centrelink’s debt base is suspended debt. The mercantile agents are paid a percentage commission on each debt collected.

**3.96** The former Department of Social Security sought and obtained Government approval for the strategy because of the Department’s concern that the increasing amount of debt that would be written off would be too high, if no further action was taken to trace the debtors. At the time that Government approved the flexible debt collection strategy, the Department wrote off approximately \$20 million, one third of which (about \$7 million) the Department considered was uneconomic to collect. The same concern applies to the ATO, as it writes off about 10 times more debt for the same reason.

**3.97** Centrelink has advised the ANAO that the arrangement with mercantile agents is working satisfactorily. The mercantile agents collect about 10 per cent of debt that would otherwise have been written off as uneconomic to collect.

**3.98** Centrelink has advised that currently about 60 000 debts are being referred per year to mercantile agents. Centrelink has recently concluded a national internal audit of the flexible debt recovery initiative. This found that the arrangement with mercantile agents is working satisfactorily. The mercantile agents are achieving 108 per cent of the 1998–99 nominal target set for them.

---

<sup>63</sup> In response to this observation, the ATO has commented that depending on the scope and funding arrangements of making credit card facilities available and the possibility of some adverse community responses, the ATO, if it were to proceed, would most likely raise the matter with the Government (ie. as it did in 1998).

**3.99** Centrelink advised the ANAO that privacy considerations were a major concern when the initiative was developed. Centrelink's national internal audit included an examination of the mercantile agents' physical and information security safeguards. This found that mercantile agents' were complying with the privacy, physical security and information security requirements of the Commonwealth. The internal audit concluded that the mercantile agents are meeting these requirements of the Commonwealth. The internal audit also found that there had been only three complaints that specifically referred to privacy issues. Centrelink advised the ANAO that the low number and materiality of the privacy complaints was also evidence for this conclusion. Centrelink considered that the debt collectors employed by the mercantile agents displayed a good understanding of the Information Privacy Principles. Centrelink advise that since July 1999 debts are automatically referred to mercantile agents in those cases where the debt has not been collected for three months. Centrelink also advise that the performance statistics of its Area Offices now include the debt collection performance of the mercantile agents as part of Area Offices' performance statistics.

**3.100** The Centrelink experience with the use of mercantile agents, and the widespread practice in the private sector of outsourcing the collection of some debt to mercantile agents, indicates that this strategy is a feasible option for the ATO. The ATO could evaluate the cost effectiveness of outsourcing the collection of unactioned aged debt or tax debts that have been written off as uneconomical to collect, subject to the development of suitable guidelines. The ATO could also trial, with mercantile agents, the locating a group of between 500 and 1000 untraceable debtors. Under this arrangement, the ATO would outsource the task of locating hitherto untraceable tax debtors, if the privacy of clients would remain protected and the standards of performance specified in the Taxpayers' Charter could continue to be achieved. Upon receipt of information from mercantile agents about a tax debtor's new location, the ATO could proceed with debt collection action, if a cost-effectiveness analysis showed collection by the ATO was more cost-effective than collection by mercantile agents.

**3.101** The Table at Appendix 5 summarises the differences between outsourcing the collection of debt to commercial debt collection firms of the different types of tax debts. There are advantages and disadvantages associated with the outsourcing of the collection of income tax debts and/or recurring tax debt. The table suggests that there is scope for the outsourcing of the collection of some debt, but that the identification of which debts to collect by outsourcing the collection of them is quite complex. Another issue of relevance is the status of the taxpayer as a



natural person or as a corporate entity. There may be sensitivities that arise regarding the collection of personal income tax debts by private sector mercantile agents that do not arise to the same extent for corporate tax debts.

**3.102** The ability to collect some types and levels of income taxes is constrained by the complexities that occur when debts are disputed or when amendment or release provisions are raised. These do not apply to recurring taxes. The complications of hardships such as family breakdown and unemployment that may apply to income tax debtors also make the prospect of outsourcing these debts to a private collector less socially attractive and commercially risky. Checking of a debtor's liquidity is a more sensitive procedure for individuals and may be more difficult to ascertain than for companies.

**3.103** Overall, there are more complexities associated with the outsourcing of individual income tax debts than there are for business debtors. The problems of solvency and cash flow management that sometimes lie behind debts arising from the recurring taxes might not be solved by the use of mercantile agents in the recovery of the debt. The Commonwealth might not find the outsourcing of high value complex debts cost effective. Furthermore, private sector debt collectors might not find the collection of these debts commercially attractive. The prospect of engaging private debt collectors to recover Commonwealth tax debt from individuals is tempered heavily by legal and social constraints. On balance, apart from the outsourcing of the collection of unactioned aged debt or tax debts that have been written off as uneconomical to collect, the area of greatest potential for outsourcing may be the collection of Level 1, 2 and 3 income tax debts from businesses.

#### **Recommendation No.4**

**3.104** ANAO recommends that the ATO outsource the collection of some tax debt if the evaluation of outsourcing shows that it is cost effective.

*ATO Response: Agreed*

The ATO will examine the cost effectiveness, opportunity cost and contestability of outsourcing the collection of some tax debt, once the current systemic and operational changes are implemented and stabilised. This should provide an improved framework against which decisions on any outsourcing options can be taken.

Discussions have already commenced with Centrelink with a view to the ATO having access to their contractual arrangements for outsourcing aspects of debt collection work (eg. notice serving), if such aspects were to be found to be cost effective.

## Centrelink

**3.105** The ATO and Centrelink have some debtors in common. These are people who have a debt with Centrelink and with the ATO, who are, or have been, income support recipients. ANAO considers that the Government would achieve better client service and have the scope to reduce duplication of administrative effort by assigning to Centrelink the collection of ATO's tax debts relating to people on income support or who have an income support debt. Given Centrelink's expertise in the collection of relatively small debts from individuals, there may also be merit in the ATO exploring opportunities for a strategic partnership with Centrelink for the collection of some lower level INB tax debt for some debtors that both agencies have in common. ATO may wish to examine the cost effectiveness of a collaborative approach with Centrelink for collection of these debts. Such an arrangement may be in the best interests of the Commonwealth, provided arrangements can be established which protect and maintain the privacy of individuals and that the standards of performance specified in the Taxpayers' Charter could continue to be achieved.

### Recommendation No.5

**3.106** ANAO recommends that the ATO explore opportunities for a strategic partnership with Centrelink, (consistent with privacy arrangements) for the collection of some lower level tax debts for some of the clients that the two agencies have in common.

*ATO Response: Agreed*

Discussions exploring opportunities for synergies with Centrelink have already commenced, and seek to build on inter-agency consultations developed over recent years.

The ATO will decide on extending the existing arrangements as soon as those opportunities, potential cost/benefits, and any associated issues, have been identified.

## Gainsharing

**3.107** In the commercial environment, the retention of some of the proceeds of a firm's income by the debt collection group functions is an incentive for improved performance. This retention arrangement is referred to as gainsharing. It provides a mechanism that allows for more extensive debt collection activity as the need arises. The amount retained by the group is generally used to finance the collection of additional debt. The amount retained depends on the value and the complexity of the recovery. This arrangement, which is used in the private sector, works

as an incentive to enhance debt collection performance. There is no similar incentive applying in the ATO because in Commonwealth administration, all the revenue collected by the ATO is paid into the Consolidated Revenue Fund. As applied to the ATO, gainsharing would mean funding the additional expense of collecting additional revenue from the additional revenue collected.

**3.108** ATO's income comes from parliamentary appropriations. The Government has recently introduced an accruals based outputs and outcomes budget framework for budget sector agencies. Under this framework, the appropriations relate to the achievement of Government outcomes by agencies' provision of agreed output. The Government has recently described this process as the Government purchasing outputs from Budget sector agencies.

**3.109** The absence of a gainsharing arrangement for tax debt collection might mean that the ATO is unable to achieve optimal levels of performance, because of the absence of the incentive impact that gainsharing is said to produce. This could mean that a private sector counterpart of the ATO's debt collection function might have greater incentives to achieve best practice and greater flexibility to do so.

**3.110** Any gainsharing arrangement in the public sector would have to be established within the public sector resource management framework. In this light, the issue of gainsharing as applied to the ATO would require resolution of associated policy and administration issues. The ATO has emphasised that, in relation to tax debt collection, it operates in an environment that is substantially different from commercial debt collection firms. The ATO believes that a \$ expended to \$ collected equation, which applies in a commercial environment, should not be the sole consideration for the ATO. In this case, the evaluation of opportunity cost in relation to gainsharing would have to take into account the social impact of the application of gainsharing, not simply the resolution of the \$ expended to \$ collected equation.

**3.111** The issue of gainsharing has been raised because of the incentive impact for improved performance that it is said to promote. We have not raised it simply as an alternative funding arrangement. There may be scope within the ATO to re-allocate resources to tax debt collection from lower priority areas to provide any additional resources required to collect the additional debt. There may also be scope for the achievement of additional internal efficiencies in the administration of the receivables management function as a source of any additional resources required to collect the additional revenue identified.

**3.112** In response to the above discussion of gainsharing, the ATO advised that it does not support the gainsharing proposal. The ATO commented that funding arrangements for the ATO have been agreed with the Department of Finance and Administration and the Government for the overall administration of the ATO. The ATO informed ANAO that as part of the ATO's mid-year funding review and assessment of priorities, additional funding of \$10 million per annum has been re-allocated to the debt collection function for each of the next three years. The ATO further advised that a commission-based arrangement has potentially serious implications and sensitivities for both the ATO's administration and its relationship with the community.

## Organisational arrangements

**3.113** Under existing organisational arrangements for the tax debt collection function in the ATO, it is treated as part of receivables management for business taxpayers but as debt collection for individual taxpayers. In both cases, the debt collection function is part of a business line. It is managerially subordinate to the priorities of the business line of which it is part. The business lines resource the function in relation to their priorities, which in turn reflect broader ATO priorities and goals.

**3.114** Elsewhere in this Report we have recommended a range of measures directed at improving the efficiency, effectiveness, equity and accountability of tax debt collection. If implemented, they would help assure Government that it would be purchasing from the ATO debt collection services of a high standard. A related issue for consideration is whether the ATO could provide the quality of services to which these measures are directed at achieving, given existing organisational arrangements.

**3.115** The ATO prefers to have two organisational units handling tax debt collection because of the predominantly different attributes of individual income tax debtors and business tax debtors. The ATO point to the different client bases of these two groups and to the recurring taxes that apply to businesses and not individuals. The ATO moved to the current arrangements in 1994, with those arrangements not only facilitating a 'market segment' focus on debtors, but also a 'whole of client' perspective within the different market segments. The ATO has stressed these considerations have been paramount for retaining receivables management within existing business lines.

**3.116** We acknowledge the careful planning that lies behind the decision to adopt the current structure. We recognise that the ATO now faces an environment of major change. In these circumstances, we understand

that the ATO would not wish to initiate further change unless there is a sound case to do so. Nevertheless, the structural choices being made by large corporates in the private sector could be indicative of a better way.

**3.117** ANAO accepts that the ATO's current organisational arrangements for debt collection reflect a well-considered approach to tax administration. Furthermore, as the ATO has only recently moved to integrate receivables management functions for business taxes and business taxpayers we consider that now is not an appropriate time to consider other organisational configurations for the receivables management/debt collection function.

**3.118** We have been advised that it is better practice in the private sector to have one receivables management group that is responsible for all the receivables management functions of the firm. Furthermore, the private sector experience has been that any other arrangement, such as that which currently applies in the ATO, is likely to result in sub-optimal debt collection.

**3.119** Recent private sector research of emerging trends in credit management in the United States indicates that highly centralised models tend to be standard practice. Firms are increasingly moving to a single national debt management group, which consist of fewer but more highly educated and skilled professionals. The benefits of a centralised debt collection unit include economies of scale, better opportunities for career development and greater ability to gain efficiencies. We have been advised that if the function is centralised, there is increased opportunity to develop a strong performance culture of the receivables management team, which can lead to improved compliance behaviour from clients. Information technology is increasingly used to eliminate routine work and to displace dispersed administrative structures such as the branch office structure of the ATO. Information technology is increasingly used to break down hitherto rigid barriers between separate organisational work areas, such as between debt collection and sales in the private sector. Increasingly, business processes are being re-engineered, enabling work teams to be configured as process teams rather than on the basis of functional administrative structures. We consider that application of these practices in the ATO might result in higher levels of performance from fewer staff. The ATO considers that the notion of centralisation has been adopted already in large part, with the consolidation of some debt collection work locations, and moves to a national approach to business operations and the COMPACT computer system.

**3.120** We have been advised that large private sector firms have a client structure consisting of corporate and personal debtors not dissimilar to

the structure of ATO's debtor population. Many of the debtors will have a continuing relationship with the firm. Major corporates also aim to have a corporate culture that sees the management of debt as a corporate responsibility, shared amongst those areas such as sales and marketing in which debt may originate. Based on this advice, we consider that although the ATO is a unique agency in both the private and public sectors in Australia, it has much in common with many large private firms, particularly in relation to receivables management. We suggest that the ATO re-evaluate organisational arrangements for receivables management when the initiatives discussed in this Report have been implemented and the strengths and weaknesses of current arrangements can be fully appraised.

## 4. Debt Management: Better Use of Information

---

*This Chapter reviews three systemic risks that might impact on ATO's debt collection performance over the next three years. One concerns ATO's computer based systems. Another reviews the impact of the new accountabilities, systems and workloads associated with ongoing legislative change to Commonwealth tax administration. The third draws on a major ATO project where we found that there is a group of taxpayers whose non-compliant behaviour presents the ATO with a significant risk management challenge. The better use of the full range of databases to which the ATO has, or could have, access would probably improve ATO's capacity to better manage these risks. Further, improving quality assurance systems so that they align more closely with ABS statistical sampling methodology and better practice in the finance sector could provide an improved assurance that its systems and data are of industry better practice standard.*

### Systemic risks

**4.1** We note that the more effective the ATO is at improving the compliance of taxpayers, the better that risks associated with debt collection can be managed. Conversely, because it focuses on the relatively small proportion of taxpayers unable or unwilling to pay tax, the performance of debt collection can influence compliance behaviour. We have previously noted that the receivables management reforms are directed at improving the management of debt collection risks. ATO's conceptual framework, 'HOW to manage receivables management', is a key part of this approach.

**4.2** In Chapter 3 we have reported gains to ATO debt collection performance and noted that these gains are continuing. Notwithstanding these improvements, ANAO considers that there are systemic risks to the continued improvement of ATO debt collection outcomes that warrant closer scrutiny. These are the risks associated with ATO's data and systems and the new risks associated with the new accountabilities established by new tax legislation. There is an interaction between these risks. The quality of data on all of ATO's systems may have to be improved to better manage the new risks. To better manage the systemic risks reviewed in this Chapter, and improve receivables management performance, the ATO might need to make better use of the data it has as well as have access to additional databases.

**4.3** ANAO considers that specific ATO strategies aimed at improving, or at the very least, maintaining, the integrity of the tax system would seem to be a key feature of good tax administration. The substantial effort that the ATO has invested in the achievement of improved receivables management demonstrates that the ATO is committed to improving the integrity of the tax system. It demonstrates that the ATO considers that improving the performance of receivables management is a key leverage point for improving the overall compliance of the community.

#### *Information technology systems*

**4.4** We have concerns about potential additional workloads arising from systems failures that may occur as the new systems that will support the administration of the new taxes are introduced. The ATO has in the past experienced sizable reverse workflows arising from systems failures. The most recent of these in January this year had a significant detrimental effect on debt collection performance. This related to an upgrade of the ATO's two main taxpayer databases, the National Taxpayer System (NTS) and the ATO Integrated System (AIS). Most problems arose as a result from changes to the NTS system.

**4.5** The details of the problems arising from this upgrade (NTS/AIS Release 3, as it is known within the ATO) are reported in Appendix 6. The impact on debt collection performance from these problems was significant. The causes of the problems were largely to do with characteristics of NTS. Because of this the impact of the problems was greatest on the administration of taxpayers whose tax files are on NTS. These are the income tax taxpayers administered by INB and SB. As much as one third of the debt collection workforce handling income tax debtors with tax records on NTS may have been diverted from debt collection to the remedying of NTS/AIS Release 3 problems for up to three months. About 50 Full Time Equivalent (FTE) staff in a workforce of some 2300 people were engaged on this work. This is roughly equivalent to the loss of about 50 FTE staff annually or two per cent of overall FTE resources.

**4.6** The new computer based administrative systems required for 'A New Tax System' could well have a higher risk of systems failure than that of a modification to existing systems such as the NTS/AIS Release 3. The ATO has reviewed the causes of the NTS/AIS problems and their impact. We consider that the ATO has endeavoured to learn and apply the lessons learnt from NTS/AIS Release 3 to ensure that similar problems do not occur again. We consider that there is still the potential for similar problems, given the nature and extent of change required by the new tax system and the underlying problems of data quality.



### *Taxation reforms*

**4.7** Recent tax legislation has introduced new accountabilities for the ATO. Specifically, the *Taxation Laws Amendment Act (No. 3) 1999* (which received Royal Assent on 1 April 1999) provides for the establishment of Running Balance Accounts (RBA) for business taxes in the first instance and income tax in due course. It also requires the replacement of the additional tax for late payment (ATLP) by a General Interest Charge (GIC) for all taxes. The new arrangements became operational for recurring taxes on 1 July 1999. The ATO has advised that the arrangements will be extended to all taxpayers by 1 July 2000. In August 1999 legislation for the new tax system (ANTS) became law. This consists of 31 separate acts and includes legislation for the Goods and Services Tax (GST) and the Business Activity Statement (BAS). These measures will have a significant impact on tax debt collection. Legacy obligations on some accounts will continue to be administered under the pre-ANTS law. The ANTS laws become operational on 1 July 2000.

**4.8** The next three years will see the implementation of the GST, the settling in of the RBA/GIC, the new PAYG legislation and significant improvements in ATO's enforcement of lodgment requirements. The RBA requires the ATO to advise taxpayers regularly of their debit or credit standing with the ATO, showing the debt outstanding and the general interest charge that has accrued on that debt.

**4.9** This is a new accountability relationship between the ATO and taxpayers because the ATO has never had this requirement before. The bottom line debt may be the result of the non-payment of more than one tax. Upon receipt of a partial payment from a debtor, the ATO will assign the payment to reduce or eliminate the total outstanding account balance. The ATO has advised that the RBA/GIC advice to be sent to all tax payers setting out the credit/debit relationship with the ATO will mean that any debt so advised will have to be actively pursued and collected promptly.

**4.10** The impact of the RBA/GIC reforms could be to reduce the amount of debt over the long-term. The ATO considers that taxpayers will be more likely to reduce arrears at a faster rate as a result of the new client account statements that detail the rate of debt escalation. For example, there may be an increased workload arising from tax debtors making greater contact with the ATO in response to RBAs and, in due course, BASs. Although ATO has planned that much of this work will be handled by the newly established call centres, the ATO's drive to manage debt more on the basis of risk could be deflected by the incidence of tax debtor query, if the incidence is high enough.

**4.11** The ANTS legislation enables the ATO to collect a Commonwealth tax, the GST, and provides that all revenue from the new tax will be paid to the States and Territories as revenue grants through standing appropriations. The GST will be collected monthly and quarterly. These arrangements, many of which are still being worked out, also introduce new accountability relationships for the ATO. The Budget papers provide that the ATO will charge a fee to State and Territory Governments for the collection of the tax.

**4.12** ANAO understands that the GST amounts to be remitted to the States and Territories will be determined by, amongst other things, ATO's lodgment enforcement arrangements. With all existing taxes there is a time gap between the assessment of tax following lodgment and the actual payment of tax. We consider that it would be prudent to plan for a GST liability. At the time of this audit, negotiations about the intergovernmental agreements under which issues concerning any GST tax debts will be resolved had not been completed.

**4.13** There are new risks associated with the new accountabilities summarised above. The quality of data on all of ATO's systems may have to be improved to better manage these risks. We recognise the initiatives that the ATO has undertaken to improve data quality, but we are not confident that ATO's databases are of the requisite quality standard at this point in time. For the reasons outlined above, it would be prudent for the ATO to plan on the basis that debt collection workload will increase.

**4.14** Although there are continuing improvements to efficiency, effectiveness and equity arising from initiatives implemented since ANAO's 1996 Report, the level of resources expended by the ATO on debt collection are declining, yet the workload is increasing. For example, we understand that ATO's 1999–2000 budget for all receivables management functions (in both SB and INB) will be about \$150 million. In 1998–99 it was about \$211 million. In 1997–98 it was about \$230 million. We have been advised that it is a common element of debt collection in the private sector that management expects the level of performance to improve in an environment of increasing debt and diminishing resources. In the context of the new liabilities that the ATO will administer under ANTS, the ANAO considers that the ATO should closely monitor the level of resourcing to receivables management to maintain current improvement levels.

## The use of additional databases

**4.15** The ATO has undertaken a range of initiatives that make better use of existing databases or that integrate into tax administration the use of additional databases. Initiatives such as streaming, profiling, data mining, Kdnet research, the use of sophisticated On-Line Analytic Processing (OLAP) software and the “Net Risk” risk profile tool are examples of the scientific use of all relevant data bases to collect debt and to minimise the occurrence of tax debt. ANAO supports these beneficial, innovative advances in public administration.

**4.16** The use of databases in this way sometimes gives rise to concern about the possible invasion of personal privacy. This is understandable. ANAO notes that the Commonwealth has a range of functioning legislative measures that are designed to protect individual privacy and to safeguard the security of taxpayers’ personal information. In two recent audits we have found that the ATO functions in a way that respects personal privacy and protects the security of taxpayers’ personal information.<sup>64</sup> The ATO should continue to comply with these safeguards. In view of this, ANAO considers that while there is no additional risk to privacy, there are further benefits that can be gained from the better use of existing databases or by the integration into tax administration of the use of additional databases.

**4.17** There is a range of databases either in the possession of the ATO or available from State and/or Commonwealth Government authorities that may be used to improve debt collection action. These databases would help the ATO obtain more accurate and comprehensive information about a tax debtor’s assets and location.

**4.18** The assessment of the credit worthiness of the debtor and the assessment of the debtor’s total assets can be difficult, but they can be made easier by the use of all the relevant databases and suitable information-matching computer systems. Relevant databases include, but are not limited to AIIR, ASIC, AUSTRAC, HIC, land titles offices, valuers-general, and registrars of motor vehicles, births, deaths and marriages. Special legislation would be required for the use of some of these (eg. HIC, AUSTRAC (if matching was to be TFN based)) whereas others could be accessed within existing law. The use of most of these databases incurs an expense. Our suggestions for the more systemic use of them presuppose evaluation of the costs and benefits and the completion of a business case to determine the matter. ANAO notes that it has been the ATO’s regular practice in debt collection to access most such databases (HIC and AUSTRAC excluded), albeit on an ad hoc basis.

---

<sup>64</sup> For example, *Management of Tax File Numbers*, Australian Taxation Office, Audit Report No. 37, 1998–99, and *Client Service*, Australian Taxation Office, Audit Report No. 22, 1996–97

**4.19** The private sector's credit reference databases could also be of value to the ATO, particularly in relation to the assessment of risk of a tax debtor not paying their debt. Issues associated with the use of private sector databases are addressed in paragraphs 4.46 to 4.60.

**4.20** ANAO found that some ATO Branch Offices made some use of most of the above mentioned databases that are accessible to the ATO within existing law. ANAO considers that the more systemic use of relevant data sets on a national basis would improve efficiency, effectiveness and equity and enable the ATO to achieve a higher standard of debt collection. Use of some or all of the databases may be warranted for the collection of debt in some instances of continuing non-compliance. In such circumstances, we can see merit in national batch data-matching projects for classes of like tax debtors.

**4.21** We consider that, where possible, automated data matching of debtor cases with some or all of the above databases should be used. We noted that much time and other resources could be wasted in Branch Offices because such matching is done manually by a handful of staff trained to access particular databases on a commercial basis. This is inefficient and tends to discourage staff from using such necessary facilities. Ultimately, debt may not be recovered and additional expense may be incurred in reaching such an unsatisfactory outcome.

**4.22** State government agencies charge a fee to access their databases. There is, therefore, a cost to the ATO from the more extensive use of these databases. As the ATO will now collect the GST for State and Territory governments on a fee for service basis, State and Territory governments might now be more willing to negotiate national fees (with associated economies of scale) with the ATO. The national, systemic use of these databases would incur a national cost, but would yield national benefits. We consider that the ATO should research these issues as a step towards the preparation of a business case about the national, systemic use of these databases in tax debt collection. As the potential use of these databases would be widespread throughout tax administration, adding the total cost of their acquisition exclusively to receivables management would not be appropriate.

**4.23** A characteristic of contemporary tax administration is that the increasingly intelligent use of data and systems can yield dramatic benefits. The use of sophisticated information technology systems and high quality data can transform data into information and knowledge resulting in reduced cost of services, improved taxpayer compliance and additional revenue. In the private sector there are firms that provide some services that could be regarded as being in competition with some of the ATO's receivables management functions. A competitive advantage

of the better firms is the intelligent use of data and systems. We consider that the ATO has some way to go in the achievement of industry best practice in its use of data and systems to achieve the one outcome set by Government.

**4.24** We have found that those private sector counterparts to ATO's debt collection function aim to achieve a competitive advantage by their skill and inventiveness in the use of databases. We consider that if the ATO aimed to achieve best practice in the use of databases to collect debt it would need to make considerably better use of the databases it now uses. It would also need to make systemic use of all relevant databases. It would need to access more databases than it does now. It may need additional software capability. It would also need to automate processes that might now be carried out manually. As a first step in this direction, a number of research projects might have to be completed. The main purpose of these would be to evaluate the cost effectiveness of various approaches.

### **ANAO data matching studies**

**4.25** We undertook several quantitative analyses to explore the potential for improved debt collection from matching taxpayer records amongst various ATO databases. We matched COMPACT records against the Annual Investment and Income Returns (AIIR) database. We did this to explore the potential use of this database to indicate whether tax debtors had some financial resources available to meet their debt obligations. We undertook another analysis to examine the links between tax debtors who were company directors and the tax debts of the companies of which they were directors.

**4.26** Commonwealth law requires financial institutions to provide the ATO with the AIIR database. The AIIR database contains information about a taxpayer's investments and transactions with financial institutions. This information is of relevance to the collection of tax debt. This information could be most useful in determining a taxpayer's capacity to pay in those cases where there is an unwillingness to pay. This information is already used to a limited extent, but there are likely to be revenue benefits from its systems use.

**4.27** The ATO can match COMPACT records and AIIR records for those debtors who have not responded positively to ATO's actions. In some cases the match would show that the tax debtor does have the resources to pay the debt. The ATO could take appropriate action to recover the debt directly, or through communication with the debtor. We found that some branches have undertaken limited data matching between AIIR and COMPACT. We understand that accessing the AIIR information by ATO is often done only for specific cases.

**4.28** In order to obtain an overview of the potential benefits of the AIIR data, we obtained tabulations showing the extent to which income tax debtors have interest bearing accounts. As this information is relevant to the timely collection of debt, we also obtained separate tabulations of those income tax debtors with aged debts. The target data set was limited to individual taxpayers and to income tax debt. Appendix 7 describes how the tabulations were produced.

**4.29** Our study does not provide an exact picture of the investment holdings of the matched income tax debtors. This is because there is a difference between the dates to which the financial transactions on AIIR, and the debts on COMPACT, relate. The AIIR data, which is compiled by financial institutions, relates to transactions carried out during the financial year 1997–98. These transactions include the establishment of various types of accounts, deposits into them and the receipt of dividend and interest into accounts. Most of the COMPACT records relate to income tax assessed for income earned in the same financial year, 1997–98. However, the AIIR record may indicate an investment that may not necessarily exist at the time the match was undertaken. Nevertheless, the AIIR information relates to transactions that did take place while the debt was active. We consider that the ATO could arrange to match COMPACT and the AIIR data so that the records are more contemporaneous.

**4.30** The result of various rules of matching and data simplification produced 42 059 unique individual income tax debtors. There were 132 077 AIIR reports associated with these individual tax debtors. These reports were matched against 252 758 COMPACT debtors who had a total debt of some \$1.88 billion. This resulted in a match of 56 912 TFN AIIR records. This means that we found 56 912 AIIR records that matched with COMPACT records using the TFN as the matching key. There was a total debt of about \$778 million associated with these records. That is, we found a 23 per cent match responsible for 41 per cent of tax debt. We suggest that this alone indicates the value of the systematic matching of COMPACT records against AIIR transactions.

**4.31** Some (just under 2000) of the 56 912 records had entered into arrangements with the ATO to pay and in some cases the ATO had written off the debt as irrecoverable at law. These were removed from the analysis. About 55 000 cases remained. These were estimated to have about \$100 million invested in AIIR accounts. They had tax debts to the Commonwealth totalling approximately \$764 million. The analysis tabulated numbers of debtors with particular amounts of debt in relation to an estimate of the amount of money invested. By this means it was

possible to assess the extent to which the matched debtors might have an amount of money invested that was commensurate to the amount of debt. The analysis shows that an estimated maximum of \$100 million was available for ATO collection action.<sup>65</sup>

**4.32** This indicates that many income tax debtors have sizeable amounts of money in accounts with financial institutions. If this were true, the ATO could access these accounts to pay some or all of the debtors' debts. The analysis indicated that over 80 per cent of the income tax debtors who have AIIR records might have sufficient funds invested to pay their debt. Furthermore, just over half of the income tax debtors who have AIIR records had debts that were more than 90 days old and that about half of these debtors might have sufficient funds invested to pay their debt. It is possible that in those cases where a tax debtor had funds invested which could be used to pay all or some of a tax debt, the ATO could have accessed the AIIR accounts and obtained some or all of the funds available and reduced or eliminated the debt accordingly.

**4.33** This analysis shows that there are many debtors who appear to have the means to pay their tax debt straight away. This study is indicative, rather than definitive, of the value of the systematic use of the AIIR information in tax debt collection. It indicates that there would be merit in the ATO establishing computer systems that would automatically match the relevant subset of COMPACT debtors against AIIR records. This could enable automatic, or at least prompt, action to be taken against those who avoid paying their income tax. On the basis of ANAO's study alone, it indicates that there is potential to recover additional unpaid debt, an upper limit of about \$100 million is indicated.

**4.34** We examined the extent to which INB income tax debtors with other tax roles were associated with tax paying entities that were also tax debtors. Table 8 in Appendix 9 presents information about the income tax debt of some company directors. In June 1999, 27 232 company directors who were income tax debtors were also directors of companies that lodged income tax returns in 1997. This group of company directors owed the Commonwealth some \$509 million. This group comprised only six per cent of income tax debtors, but owed the Commonwealth nearly 18 per cent of income tax debt.

---

<sup>65</sup> This would only be available for collection if each of the 55 000 cases had funds invested in excess of their tax debt. The analysis indicates that about 25 per cent of the matched debtors were in this category. Moreover, the analysis indicated that about half of the matched debtors had investments that could make a substantial contribution to the acquittal of their tax debt, if the investment could be applied to that purpose.

**4.35** We analysed this group further to identify those company directors who were income tax debtors, whose companies were also income tax debtors (Table 9 in Appendix 9). There were 6860 tax debtors in this group. The income tax debt of this group of company directors comprised 41 per cent of the income tax debt owed by company directors whose companies had lodged income tax returns in 1997. More interestingly, those 140 debtors whose companies also had debts owed 51 per cent of all Level 6 debt (ie. that had tax debts greater than or equal to \$100 000). They owed an average of just over \$1 million each. The group of debtors who are directors of companies that have debts comprise just 0.01 per cent of income tax debtors, yet they have seven per cent of income tax debt.

**4.36** The above analyses are indicative of the benefits of matching the tax compliance behaviour of taxpayers and the entities associated with them. We conducted further analyses for a range of other roles. These included trusts, partnerships and superannuation funds, especially the excluded funds. Unfortunately, the results of these studies were inconclusive, in part because of shortcomings in ATO's systems and data. The ATO advised that these problems might be overcome by the introduction of the ABN and new systems being implemented to support the new tax system. We suggest that the ATO rectify these weaknesses and establish the systems necessary to enable the matching of all of the entities associated with tax debtors. This would include national batch data matching projects based classes of like tax debtors. This is particularly so for those debtors with whom there are associated high risks of non-compliance and revenue loss.

## **Recommendation No.6**

**4.37** ANAO recommends that the ATO adopt research-based debt collection strategies appropriate for a whole class of high level debtors with complex arrangements involving associated entities that focus on the primary obligation compliance of entities and classes of entities sharing common business characteristics.

*ATO Response: Agreed*

This research has commenced.

## **Predictive compliance models**

**4.38** The flexibility of ATO's response to tax debtor behaviour would be improved as the ATO improved its capacity to predict the occurrence of a tax debt. We found that the ATO has initiated a range of projects designed to improve the understanding of the occurrence of tax debt as



recommended by the ANAO in the 1996 Report. This should enable the ATO to construct computer-based models of tax compliance behaviour. This could also enable the ATO to predict the likelihood of debtor behaviour in particular cases. If the ATO was able to predict tax debtor behaviour with sufficient accuracy, preventative action could be taken in relation to taxpayers that were most at risk of becoming debtors.

**4.39** We consider that ATO's use of reliable and valid predictive compliance models would be beneficial to the Commonwealth. The ATO has two projects underway designed to improve the capacity to identify taxpayers with a high risk of becoming tax debtors. One of these involves the ABS and the utilisation of demographic and taxation information. The other involves the further development of the profiling technology summarised in Chapter Two of this Report.

**4.40** The initial work undertaken with the ABS indicates the need for a closer study of the main determinants of tax debtor behaviour. The variables that relate to these determinants may be found in databases other than those used so far in the ABS project. In paragraphs 2.8 and 2.17, we reported the successful use of ATO's debt profiling technology. Phase two of that project is designed to adapt the technology to improve the operation of the Compliance Model.

**4.41** ANAO supports ATO's development of predictive compliance models. As the work becomes more successful, the ATO should be able to apply the framework of the Compliance Model earlier in the tax administration cycle. By doing this, the ATO could achieve improved compliance and increased revenue in a more timely way than previously. It may be that the variables of greatest predictive value are not amongst those normally retained on ATO's databases. We suggest that the ATO explore the use of additional data sets, such as those mentioned in paragraph 4.18, in order to find the variables of greatest relevance.

**4.42** Another useful way of reducing the incidence of tax debt is for ATO staff to advise the debtor on how to reduce the likelihood of the debt occurring in the future. ANAO understands that the ATO has been trialling such work, eg. through letters to taxpayers with debit assessments who were overdue debtors in previous years.

**4.43** Staff are required to advise clients about the requirements of tax legislation. We understand that in practice this requirement means that the role of ATO staff is limited to advising clients of legal requirements; that is, ATO staff would not be involved in advising taxpayers in the same way as commercially engaged tax agents. We agree that ATO staff do not have the same responsibilities to clients as would commercially engaged tax agents.

**4.44** We have been advised that where taxpayers have had previous debts, and there is an indication that there will be future debts, ATO staff may provide advice to the taxpayer about how to reduce the likelihood of the debt recurring. If staff provide such advice, they are required to record the advice given in the narration segment of the debtor's COMPACT file. ATO research has shown that in a number of cases there was no indication that advice had been given to the debtor on how to reduce the likelihood of the debt occurring in the future. In raising this matter, we are mindful that it is not the job of the ATO to assist taxpayers to interpret the application of tax law to their individual circumstances, but to help taxpayers understand the requirements of tax law.

### **Recommendation No.7**

**4.45** ANAO recommends that the ATO evaluate the cost effectiveness of making more systemic use of relevant databases in tax administration on a national basis. Relevant databases include, but are not limited to AIIR, ASIC, AUSTRAC, HIC, land titles offices, valuers-general, and registrars of motor vehicles, births, deaths and marriages.

*ATO Response: Agreed*

The ATO currently makes use of the databases specifically mentioned, with the exception of the HIC database.

The ATO also acknowledges that, in the context of debt collection, most 'searches' currently done are on an ad hoc, rather than systemic or national basis.

### **The use of credit reference databases**

**4.46** ANAO was advised that a standard practice amongst credit providers in the private sector is the use of the databases of credit reference bureaux. Such firms generally use these databases in two ways, subject to statutory regulation. In some instances, the names and details of debtors with debts outstanding for greater than 90 days are listed with the databases. In other instances, private sector firms access the databases to obtain information about a prospective client's or a debtor's credit rating.

**4.47** The *Privacy Act 1988* regulates access to the databases and the listing of information. This legislation requires that an agency be a credit provider as defined in the *Privacy Act 1988* before it can list consumer credit information. In addition, if an agency proposes to list information of a personal, as distinct from a corporate, nature the permission of the person to be listed is required before listing can proceed.

**4.48** We raise for consideration the possibility of the ATO being able to utilise the databases of the credit reference bureaux in the same manner as do credit providers in the finance sector. Current legislation does not allow the ATO to use the credit reference databases. We understand that if the ATO were to use credit reference bureaux as do financial institutions that are credit providers, the *Privacy Act 1988*, the *Taxation Administration Act 1953* and the Income Tax Assessment Acts would require amendment. We have been advised that making the necessary amendments to enable the ATO to use the databases in the same manner as any other credit provider in the finance sector would raise significant issues for Government. There would be issues associated with the release of taxation information and with the status of the ATO in relation to the databases. Current legislation restricts access to credit providers and we have been advised that the ATO is not considered to be a credit provider. As the possible use of the databases of the credit reference bureaux raise a range of complex and sensitive issues, we have provided a review of them and it is on this that we base our recommendation.

**4.49** We have been advised that the use of the databases in these ways has had a significant impact on the expeditious recovery of debt. The effect of listing a debtor is to downgrade the debtor's credit rating. The result might be that the debtor is unable to obtain further credit until the debt referred to the database has been paid. The existence of a bad debt on a debtor's credit reference database record can act as a strong incentive to pay an outstanding debt, regardless of its age. We were advised that, subject to the dollar value, industry experience is that for the prompt payment of lower level debt, impending listing with the credit reference bureau generally has a greater impact on the debtor than the advice of an impending of legal action. We were informed that there is a significant improvement in the payment of outstanding debts once overdue debtors receive advice that listing might proceed.

**4.50** The credit reference bureaux, including debt collection firms, provide a range of services to assist firms to assess the credit worthiness of prospective clients and debtors. As a result, new and more sophisticated credit risk assessment services are being introduced to the market. Apart from the more advanced analytic services, firms routinely access the databases as the law permits information to be obtained to assist with the debt collection process. Such information might include: address data; debts owed to other creditors; public record court information; recent, and other, applications for credit that have been made by prospective clients and debtors. Other information might include debtors who are currently paying off other debts by installment and the involvement of company directors with other companies insolvent

or otherwise. We understand that the databases are a useful aid in locating debtors that are difficult to trace. We note that some of this information is only available to credit providers—it would not be available to debt collecting firms as such.

**4.51** We have been told that there is a general view in the finance industry that the listing of information about commercial and personal debtors is a key tool to maintaining the efficiency of the industry, including preventing the wider occurrence of bad debt. This can result in an overall improvement in transaction costs in the finance sector.

**4.52** In paragraph 3.58 we reported that the ATO has about \$2.2 billion collectable aged active debt on its ledgers and that 38 per cent of this (ie. about \$836 million) has been partially actioned. Private sector experience, as conveyed to ANAO, is that collectable aged debt is paid much more promptly when a firm advises a debtor that listing may soon take place. If the ATO had this facility, it could result in the quicker payment of a proportion of \$2.2 billion. We have not estimated the proportion nor the financial benefits that quicker payment would achieve. We consider that there would be merit in the ATO undertaking this research.

**4.53** The tasks of debt collection include the assessment of the credit worthiness of the debtor and the assessment of the debtor's total assets. This is an important part of tax debt collection as a sizeable amount of debt is recovered as a result of ATO agreement to accept payment by arrangement.

**4.54** In 1998–99 there were over 145 000 taxpayers who had established arrangements with the ATO to pay a total of about \$2 billion tax debts. Amongst these there were 50 194 individual income tax debtors who paid by installment, most of whom were on low incomes with an average debt of less than \$750.

**4.55** Debts owed by business taxpayers are, on the average, many times larger than these are. We estimate that business tax debtors would be paying a total debt of about \$1.7 billion by installment. The question arises whether the ATO was justified in accepting an installment arrangement for all of the business taxpayers that pay by installments. We were not able to resolve this issue, but note that in some cases the ATO might not have had sufficient information to assess whether the business taxpayer had the capacity to pay the debt in full.

**4.56** Given the magnitude of debt paid by installment by business debtors, and their number, a professional assessment of the risk that business debtors might default on debt payments and of the credit worthiness of the business could be helpful to the ATO. Access to the

databases of commercial credit reference bureaux, and the use of the analytic services they provide could help with the assessment of this credit risk. As a result of this additional information, a proportion of tax debtors that currently pay by installment might be required to pay the debt outright. We have not estimated this proportion nor the financial benefits that full payment would achieve. There would be merit in the ATO undertaking this research.

**4.57** Some of the debtors incurring tax debts associated with the payment of the recurring taxes such as PAYE might not be arranging their affairs so that tax can be paid at the time required. In some cases these debtors are corporate entities. In some cases they are individuals trading as businesses and employing others in the business. In response to demands from the ATO that the overdue tax be paid, such debtors will usually seek an extension from the ATO of time to pay the overdue tax. They may seek ATO's approval to enter into arrangements to pay the overdue tax by installments. In many cases, the ATO has no independent information about the financial situation of the debtor to draw upon when responding to the debtor's request.

**4.58** The payment of business taxes could be considered to be a normal business expense. Commercial entities ought to be managed in ways that enable such legitimate and readily measured costs of doing business to be paid as and when they fall due. An inability to pay business taxes might be properly regarded as important information about the financial condition of a business that financial markets should have. In this regard, information about the non-payment of a recurring tax debt of a business may be different from information about the non-payment of income tax by an individual. The non-payment of income tax by business might also be information of legitimate interest to financial markets. To the extent that information about the non-payment of tax is of legitimate interest to financial markets, the referral of such information to credit reference bureaux could be beneficial to the efficiency of markets. Such referral might, in any case, be justifiable if it assisted the Commonwealth to collect more cost-effectively the monies properly owing to it, and if it did not conflict with Government policy. The use of credit reference bureaux in the way indicated is routine practice in the private sector. Most banks and finance companies list most defaults at 90 days. Amongst other things, it gives warning to other institutions about the financial health of the debtor.

**4.59** The issues reviewed above are complex and significant. Some benefits that the Commonwealth could obtain if the ATO had use of the facility have been outlined. There may be scope for improving the cost

effectiveness of ATO's debt collection as a result of the ATO having access to the credit reference databases. The scope for improved taxpayer compliance and increased revenue would come from two main sources. These are the quicker payment of collectable aged debt and the reduced incidence of payment of debt by installment. There would be merit in the ATO completing a cost-effectiveness analysis of the issue. The analysis would need to have regard to the need that the privacy of clients would remain protected and that the standards of performance specified in the Taxpayers' Charter could continue to be achieved. There may be scope for improved efficiency of the finance sector if information about a business's difficulty in meeting tax obligations was as available to the market place as is other information crucial to the assessment of credit risk. This would be an industry-wide benefit, not one that would accrue direct benefit to the ATO. There may also be scope for the Commonwealth to negotiate a unique arrangement for ATO's access to and use of the relevant credit reference databases, that has regard to ATO's unique circumstances. The options for such arrangements should also be examined in the cost-effectiveness analysis.

## **Recommendation No.8**

**4.60** ANAO recommends that the ATO evaluate the cost effectiveness of accessing the databases of credit reference bureaux, with the view of putting options to Government where authority would be required.

*ATO Response: Agreed*

An evaluation of the issues and potential gains will be conducted. The ATO recognises the potential benefits, legislative and sensitive policy issues involved.

## **Quality Assurance (QA) programs**

**4.61** The ATO has implemented QA programs that focus on the actions of staff in relation to key aspects of debt collection process. These characteristics include security, timeliness, accuracy, appropriateness and completeness of the work of staff. The QA programs include Business Imperative Audits of the work of debt collection staff. The QA programs have improved the quality of decision making, compliance with ATO policy and procedures and the use of legal action, contributing to a reduction in the overall cost of legal services. ATO's QA programs may be able to improve administration further by a more concentrated focus on data quality and case sampling. We understand that the ATO plans to make such QA processes intrinsic to the new Receivables Management computer system that will replace COMPACT.

**4.62** QA can be a key process for providing stakeholders (such as the Commissioners, the Government and Parliament) with assurance that information, work processes and decisions are of a satisfactory quality. Current QA programs may not achieve this objective, even though they contribute to improved management. ATO's QA programs could be more securely connected to ABS statistical sampling methodology. There is also scope for the ATO to use QA on a more systemic basis along the lines of better practice in the finance sector. By these means, the ATO could provide an improved assurance that its systems and data were of industry better practice standard.

### Recommendation No.9

**4.63** ANAO recommends that the ATO align its QA programs more closely with ABS statistical sampling methodology and better practice in the finance sector so that it can provide an improved assurance that its systems and data are of industry better practice standard.

*ATO Response: Agreed*

The ATO's Receivables Management Quality Assurance Program will be making increased use of standard ABS Sampling guidelines.

Existing Quality Assurance processes will also continue to be developed, using ABS guidelines, for use as a strategic and quality measurement tool.

### Persistent tax debtors

**4.64** The ATO regularly conducts investigations into the compliance behaviour of categories of taxpayers. Sometimes these categories relate to industry groups (eg. fruit and vegetable growers, wholesalers and retailers) in other cases the categories relate to occupational groups (eg. taxi drivers). ATO research shows that there are three professional groups (lawyers, accountants and medical practitioners) with an average level of tax debt that is nearly five times the national average (barristers nearly ten times the national average). Whilst the average level of debt per occupation is only 2.6 per cent, over 20 per cent of taxpayers in these professions are tax debtors.<sup>66</sup> In December 1997 the ATO established a project focussed on the legal profession in New South Wales. The project aimed to better understand the high level of debt established by the

<sup>66</sup> The figures reported in this paragraph are based on tax returns carrying the appropriate occupation code. Not all returns have the occupation code or have the correct occupation code. As a result, the percentages are, as it were, based on a fairly large sample (probably at least 50 per cent) of the total population. In the case of barristers in NSW every case was identified and so the percentages are correct. They will, however, vary during any given year between 19 per cent and 23 per cent.

legal profession, to examine other compliance issues and to seek best practice in the collection of the profession's debts. The ATO advise that that the majority of taxpayers in the legal profession comply fully with Commonwealth law and do not present any problem to the ATO in respect of the lodgement of tax returns, the payment of recurring taxes and the payment of tax debts. However, the ATO also point out that over 40 per cent of the solicitors and barristers in NSW have not lodged for last year and there is a pattern of the ATO regularly having to demand lodgement.

**4.65** In April 1997 legal professionals, in over 2000 cases Australia-wide, owed the Commonwealth some \$67 million in unpaid primary tax debt. The ATO advised that for many years the legal profession has been the occupational group with the highest proportion of tax debtors. The barristers' book debt scheme of the 1980s has been well documented, as has barristers' involvement in tax avoidance schemes. Some Queen's Counsellors had been quite prominent in the tax avoidance industry in the 1970s and 80s. This had been of such concern at the time that some judicial office holders had called for the legal profession to set standards. For example, Mr. Justice Davies, then President of the Administrative Appeals Tribunal, called upon groups representing the legal profession to set standards for barristers and solicitors who act as advisers in the tax field.<sup>67</sup>

**4.66** The ATO has found that a relatively small number of high-income debtors (with substantial tax debts) use bankruptcy as a means of avoiding tax. It is a device used almost exclusively by high-income professionals, whose source of income is largely fee for service. That a sizeable proportion of these individuals is in professions that can promote or undermine the integrity of the tax system is also noted.

**4.67** The ATO considers, given the current legal and administrative arrangements, that there seems to be no reason why the incidence of serial bankruptcy could not continue or, indeed, increase. In a major speech on 17 September 1999 about taxation administration the Commissioner of Taxation expressed his concern about the behaviour of these persons. The Commissioner stated:

*These people have had every opportunity to pay their debts. Their activities, in my view, have all the hallmarks of thumbing their nose at us and, more importantly, the community. This requires a tipping of the balance to a strong and unconventional response. The conventional response clearly is not working.*<sup>68</sup>

---

<sup>67</sup> "QCs Get Extra For Tax Scheme Views" by Gary Sturgess, Law Reporter, *The Age* 10 Aug 1981.

<sup>68</sup> "A Question of Balance" Michael Carmody, Commissioner of Taxation. Address to the American Club 17 September 1999, p. 15.



**4.68** The ATO advised that such individuals, as described above, do not pay their tax debts and, when asked to pay, indicate that they will bankrupt themselves rather than pay tax or any late payment penalty, including interest. In some instances, in order to get the primary tax, the ATO has remitted penalty and interest payments. The ATO has stressed that where, in some cases the ATO remits penalty and/or interest, the focus is primarily on balancing the taxpayer's circumstances against the revenue flow. These individuals are generally well prepared for bankruptcy and leave the ATO with little choice other than to accept the offer for settlement. ATO advise that bankruptcy has in the past yielded only 4–10 cents in the dollar where such debtors have been bankrupted rather than pay tax. The ATO advised that typically, after bankruptcy action has been taken, some might not pay tax contributions. If they do not, then once again the individual begins to establish new debts with the ATO.

**4.69** ATO found that some individuals are serial bankrupts who have entered bankruptcy in the past with little obvious impact on their business. The only detriment suffered by these professionals is that they are unable to operate a trust account, but this appears to be only a minor obstacle. If a person enters into bankruptcy, it is likely that a major part of the entire tax debt (not just the penalty and interest) would not be recoverable. Bankruptcy is a serious step for anyone in business to take and one that may have wider ramifications than the non-payment of tax.

**4.70** The ATO has documented over 300 cases of tax non-compliance behaviour, in which tax debt collection action is proceeding for the collection of relatively large income tax debts. This is despite six and seven digit taxable incomes that may be more than double the amount of tax due. In most cases, very little of this assessed tax has been paid, in some cases none at all for several (up to ten) years in a row. In most cases these taxpayers have not disputed the ATO's tax assessment. Tactics for avoiding tax include failing to lodge returns, failing to pay when arrangements are made, and declaring voluntary bankruptcy. Even though the ATO has obtained judgement in its favour, sometimes the taxpayer has still refused to pay.

**4.71** By entering into bankruptcy, the taxpayer avoids paying tax. In several cases where this tactic has been employed, the Commonwealth has foregone close to one million dollars. In general, when bankruptcy has been declared, creditors, including the ATO, often receive little or no dividend from the liquidated estate. In a number of the instances of this type of extreme non-compliant behaviour reviewed by the ANAO, the behaviour of the taxpayer has not changed. The behaviour continues,

notwithstanding the recurring cycle of non-lodgment of tax returns, income tax assessment, refusal to pay and lodge, prosecution, judgement, bankruptcy, payment arrangements (often with the Insolvency and Trustee Service) and so on. We understand that in some instances these people may be in receipt of income that has originated from the Commonwealth. The ATO advise that there are barristers with sizeable tax debts who represent the Commonwealth and in particular the ATO. Although the debts are slow to collect it is not necessarily the case that among this group there are people entering bankruptcy to avoid tax. We suggest that the ATO examine ways of more efficiently collecting debt in situations where the Commonwealth pays fees directly or through third parties to persons who have significant debts to the Commonwealth and a history of non-compliance.

**4.72** ATO advised that, as a generic group, legal professionals present the ATO with an Australia-wide tax compliance problem in respect of the size of debts, the number of debts, the deteriorating tax compliance behaviour of some barristers and solicitors, the time and cost of collection and their impact on other taxpayers. ATO research indicated that legal professionals, as a generic group, are typically at the centre of a small business structure. This usually consists of one or more service companies, a superannuation fund, a family trust and possibly a partnership. In addition, the taxpayer is usually a director of a company. ANAO considers that the ATO should establish whether the observed poor primary obligation behaviour in the taxpayer continues with entities connected to the taxpayer. The ATO advised that, as a generic group, medical practitioners, particularly specialists, also present tax compliance problems. Taxpayers associated with the Building and Construction industry are also prone to use bankruptcy as a means of avoiding tax.

**4.73** ANAO considers that the incidence and nature of the avoidance of tax liabilities by some taxpayers, such as those reviewed, may raise questions about tax law and administration that warrant closer attention by the legislature. The ability of some debtors to continue in their profession regardless of bankruptcy or conviction for breaches of tax law assists them avoid the payment of tax. We refer to the case published in the Disciplinary Reports No. 6 of the NSW Legal Services Tribunal 1997 that is relevant to the consideration of these concerns.<sup>69</sup> The ATO advised that it considers that such individuals refuse to pay, not because they cannot afford to pay, but because they can manipulate the system such that they do not have to pay. ANAO found that ATO's analysis of

---

<sup>69</sup> Legal Services Tribunal Disciplinary Reports No 6 1997 pp. 29–32.

tax minimisation techniques used by some tax debtors has resulted in the ATO being able to put to Government options for the closure of some legislative loopholes.<sup>70</sup>

**4.74** In the speech referred to in paragraph 4.67, the Commissioner of Taxation advised the following in respect of some of the tax debtors discussed above.

*I am giving advance notice that in fulfilling my responsibility under the law to advise the Parliament on the working of the Act I propose including in my 1999–2000 Annual Report details of those persons who have a substantial debt outstanding at 1 January 2000 and who have a history of playing hardball in the way I have outlined.<sup>71</sup>*

**4.75** The Commissioner also said that he

*... will be writing to the relevant professional bodies, associations, councils, etc., in the event that analysis shows significant participation by their members. I am doing that in the hope that they will agree that holding yourself out to the community as having professional standards extends to not playing the legal system to get around paying an acknowledged tax debt. My objective is to get relevant bodies to work with us to change this behaviour.<sup>72</sup>*

---

<sup>70</sup> An example is the following: The Government has established a General Interest Charge (GIC) that will be applied to overdue tax. Associated with this reform is a change to taxation legislation that removes an anomaly made use of by some high income tax debtors such as those reviewed above. This anomaly permitted a person to be allowed the interest component of an outstanding tax debt even if the ATO had remitted all penalties, including interest. In such cases the debtor had not paid the interest but was, nevertheless, allowed to deduct the amount of interest that would have been paid had it not been remitted as a legitimate deduction simply because it was incurred. ATO's advice to Government recommending the removal of the anomaly was based on the ATO's experience of the conduct of high income tax debtors in the use of the anomaly to reduce their tax payable. Even though some taxpayers were able to reduce the assessed tax payable by such devices, they nevertheless did not pay the tax.

<sup>71</sup> *A Question of Balance* Michael Carmody, Commissioner of Taxation. Address to the American Club 17 September 1999, p. 15.

<sup>72</sup> *Ibid*, p. 15.

## Recommendation No.10

**4.76** ANAO recommends that the ATO identify the best methods to address the compliance problems raised by its research into persistent tax debtors.

*ATO Response: Agreed*

The ATO will continue to implement strategies to enable it to better detect, analyse and respond to aggressive tax planning arrangements. A senior group has been established to provide organisational leadership and to better coordinate strategic responses.



Canberra ACT  
20 December 1999

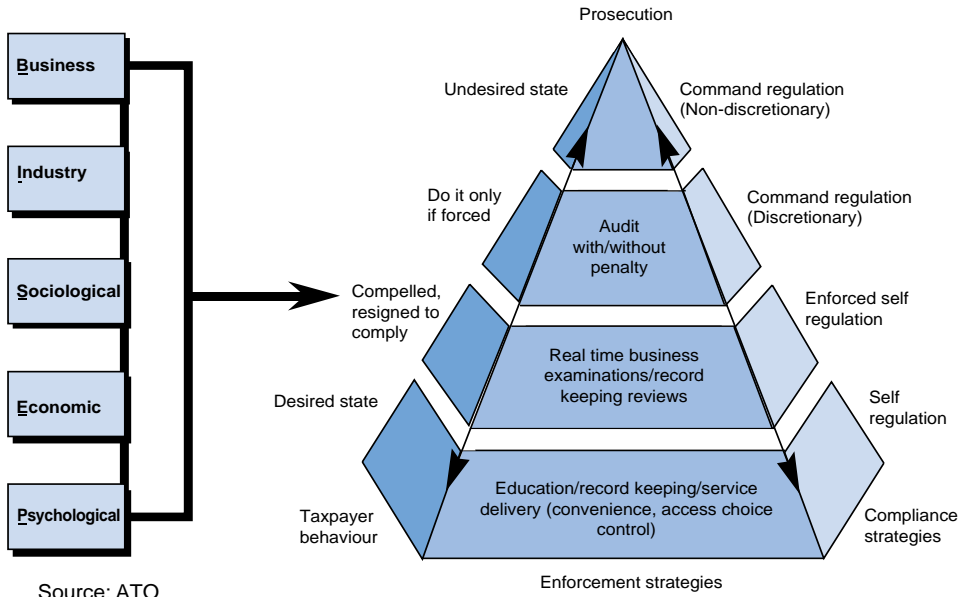
P. J. Barrett  
Auditor-General

# Appendices



## Appendix 1

### The Compliance Model



The Compliance Model shows a simple idea about how to select the best compliance strategy for a taxpayer or group of taxpayers. The better the understanding of the taxpayer's compliance behaviour, the greater the likelihood that the right strategy will be selected. In this context the right strategy is that which brings about the desired compliance behaviour.<sup>73</sup>

The left-hand side of the diagram lists five factors that summarise the determinants of compliance behaviour. The right-hand side of the diagram shows the compliance hierarchy. One side, labelled 'taxpayer behaviour' summarises the extremes of compliance between full voluntary compliance and total non-compliance. Full voluntary compliance is the most desired state and the one where most taxpayers fit. Total non-compliance is the most undesirable state and comprises a small minority of taxpayers.

The middle face of the triangle, 'enforcement strategies' summarises the range of enforcement strategies appropriate to taxpayers' level of

<sup>73</sup> The Cash Economy Task Force developed the Compliance Model for the ATO. It drew on a considerable body of knowledge about the reasons why people function the way they do with the institutional arrangements of societies. The ATO advise that the Compliance Model has been adopted by the ATO as the guide to taking administrative action by all areas of the organisation. An account of the model was published in the Second Report of the Cash Economy Task Force, *Improving Tax Compliance in the Cash Economy*, ATO, April 1998.

compliance. By way of illustration, it says that as the attitude of most people is to comply with the law, the most appropriate strategy to achieve compliance with new tax legislation, for example, would be to inform and educate people about their compliance responsibilities. The third side of the triangle summarises the range of compliance strategies appropriate to taxpayers' attitudes towards compliance. It says, for example, that the severest of strategies should be used only on those who demonstrate an attitude of severe non-compliance. Examples of action at this level are prosecution, bankruptcy and publicity.

An important lesson from the diagram is that the strategy most appropriate to the behaviour of the taxpayer is likely to be the most effective. Information and education campaigns will have no impact on those with an attitude of total non-compliance. Similarly, prosecution action is the most inappropriate compliance strategy for someone who will comply in response to a letter that draws his or her attention to an incident of non-compliance. As the severest strategies are usually the most expensive ones, the use of the Compliance Model can improve the efficiency with which the ATO allocates resources.

The Compliance Model provides a sound knowledge-based framework for determining the most appropriate strategy to take in relation to a compliance problem, given what is known about taxpayers, their situation, circumstances and lines of business.



## Appendix 2

### Implementation of ANAO Recommendations

<b>Recommendation Number</b>	<b>Recommendation and ATO response in 1996</b>	<b>State of Progress at time of follow-up audit and ANAO comment</b>
Recommendation No.1	The ANAO <i>recommends</i> that the ATO conduct research into the outstanding debtors' population to identify causes of outstanding debt, high-risk taxpayer population segments and opportunities for improvements to compliance strategies.	<p><b>Full implementation in progress</b></p> <ul style="list-style-type: none"> <li>The ATO has initiated a wide range of research projects and strategies including specialised research projects into classes of like debtors, and other research into debtor population. This was conducted using the risk profiling neural net algorithms, predictive analytic research undertaken with the ABS, the use of specialised risk-focussed work analysis software such as the On-Line Analytic Processing (OLAP) facility, and the ATO's in-house research facility the Kdnet.</li> </ul>
Recommendation No.2	The ANAO <i>recommends</i> that the ATO conduct research into payment methods to identify additional cost-effective methods.	<p><b>Fully implemented</b></p> <ul style="list-style-type: none"> <li>ATO has introduced a range of payment options and has researched the use of credit cards. Payment by direct debit has been implemented.</li> </ul>
Recommendation No.3	The ANAO <i>recommends</i> that the ATO review its use of key publications to clarify the consequences of failure to pay tax debts on time. Clarification should include the taxpayer's payment responsibilities, the possibility of legal action, the extent of late payment penalty and the ATO's policy regarding special circumstances.	<p><b>Full implementation in progress</b></p> <ul style="list-style-type: none"> <li>New pamphlet publications on "Paying your taxes" and "So you have a tax debt" are sent out to debtors in conjunction with the Taxpayers' Charter.</li> <li>Electronic Publishing Infrastructure Project (EPIP) is improving Intranet presence.</li> <li>The RBA/GIC reforms will provide taxpayers with regular, up-to-date information about their debt and the interest charges associated with it.</li> <li>The ATO's internal and Atoassist facilities provide customer support.</li> <li>Rationalisation of automatic letters improved national correspondence standards.</li> </ul>

<b>Recommendation Number</b>	<b>Recommendation and ATO response in 1996</b>	<b>State of Progress at time of follow-up audit and ANAO comment</b>
Recommendation No.4	The ANAO <i>recommends</i> that the ATO review its use of DSS forms and publications to help taxpayers make the appropriate financial arrangements for future tax obligations arising from loss of employment.	<p><b>Reviewed, but not Implemented</b></p> <ul style="list-style-type: none"> <li>• Examination of the matter identified some key complexities that detract from the recommendation; eg. the potential for unnecessary tax instalments and lodgements from 'non taxable' beneficiaries; and the potential to aggravate hardship and increase end of year refunds. Further, few beneficiaries become overdue debtors. The matter will be kept under review.</li> </ul>
Recommendation No.5	The ANAO <i>recommends</i> that the ATO develop an automatic system of reminder letters and additional information on notices of assessments, encouraging taxpayers in particular risk groups to pay their tax in a timely manner. Such encouragement should state specific collection techniques that would apply for recurring non-compliance.	<p><b>Fully implemented</b></p> <ul style="list-style-type: none"> <li>• The RBA/GIC initiative will meet this recommendation.</li> <li>• Profiling will help the ATO make the most appropriate collection response to each debtor and to classes of debtors.</li> <li>• Implementation of the Receivables Management System (RMS) will allow greater automation of processes.</li> <li>• A better automatic letter system has been established.</li> <li>• ANAO has noted that the ATO has some initiatives underway for some classes of recurring non-compliance.</li> <li>• Interactive Voice Response (IVR) System can automatically deal with selected taxpayer transactions without direct human intervention.</li> </ul>
Recommendation No.6	<p>The ANAO <i>recommends</i> that the ATO develop the capacity of its debt collection business systems to:</p> <ul style="list-style-type: none"> <li>• identify all outstanding debts as soon they fall overdue and/or are established;</li> <li>• provide flexibility for targeting action based on risks of recovery action immediately after debts are identified as being overdue; and</li> <li>• monitor all outstanding debt and all recovery action.</li> </ul>	<p><b>Implementation in progress</b></p> <ul style="list-style-type: none"> <li>• Introduction of the RMS will allow greater automation of processes.</li> <li>• ATO has brought forward the referral to COMPACT of income tax debtors on the NTS database case referrals ahead to allow faster actioning.</li> <li>• Profiling will help the ATO make the most appropriate collection response to each debtor and to classes of debtors.</li> <li>• COMPACT has been enhanced to enable the establishment of a national case management capacity.</li> <li>• The OLAP facility enables the national monitoring of case management.</li> </ul>

<b>Recommendation Number</b>	<b>Recommendation and ATO response in 1996</b>	<b>State of Progress at time of follow-up audit and ANAO comment</b>
Recommendation No.7	The ANAO <i>recommends</i> that the ATO give higher priority to the implementation of proposed improvements to business systems to batch-produce large groups of statements as part of automated recovery processes.	<p><b>Implementation in progress</b></p> <ul style="list-style-type: none"> <li>• Implementation of RBA/GIC has resulted in the issue of statements in relation to all PAYE, PPS, RPS and Sales Tax clients.</li> <li>• The ATO expects to issue statements for income tax clients after 1 July 2000.</li> <li>• The implementation of BAS in July 2000 will allow the issue of a single account statement for all tax products other than legacy accounts.</li> </ul>
Recommendation No.8	The ANAO <i>recommends</i> that the ATO give higher priority to the implementation of proposed enhancements to business systems to produce cross-revenue line statements.	<p><b>Implementation in progress</b></p> <ul style="list-style-type: none"> <li>• The RBA/GIC initiative will help meet the requirements of this recommendation.</li> </ul>
Recommendation No.9	The ANAO <i>recommends</i> that the ATO develop the capacity of ATO business systems to separate disputed assessments into disputed and undisputed components to assist the recovery process.	<p><b>Implementation in progress</b></p> <ul style="list-style-type: none"> <li>• ATO advises that disputed debt will be separated and dealt with independently in the new RMS</li> </ul>
Recommendation No.10	The ANAO <i>recommends</i> that the ATO ensure that proposed improvements to the business systems' capacity to automatically impose ATLP are implemented as soon as possible.	<p><b>Problem will no longer arise</b></p> <ul style="list-style-type: none"> <li>• The RBA/GIC initiative allows fully automated imposition of the GIC to all PAYE, PPS, RPS and Sales Tax debts.</li> <li>• Tax Reform initiatives in July 2000 will allow automated imposition of GIC for income tax clients.</li> <li>• The ATO has implemented a limited automated ATLP function for income tax debts as an interim measure.</li> </ul>
Recommendation No.11	The ANAO <i>recommends</i> that the ATO enhance the business system's capacity to automatically segment the debtor population by risk characteristics of the debtor and characteristics of the debt, using data available on ATO business systems.	<p><b>Implementation in progress</b></p> <ul style="list-style-type: none"> <li>• The new RMS will allow greater automation of processes.</li> <li>• Profiling will help the ATO make the most appropriate collection response to each debtor and to classes of debtors.</li> </ul>

<b>Recommendation Number</b>	<b>Recommendation and ATO response in 1996</b>	<b>State of Progress at time of follow-up audit and ANAO comment</b>
Recommendation No.12	The ANAO <i>recommends</i> that the ATO increase the capacity of the business system to control and monitor the recovery process on a national basis.	<b>Implementation in progress</b> <ul style="list-style-type: none"> <li>• COMPACT has been enhanced to enable the establishment of a national case management capacity.</li> <li>• The new RMS will enable the ATO to better manage all debt on a national basis.</li> </ul>
Recommendation No.13	The ANAO <i>recommends</i> that the ATO ensure the systematic revision of debt collection policy and rulings in response to changes in the legislative framework and collection environment.	<b>Fully implemented</b> <ul style="list-style-type: none"> <li>• The Debt Collection Policy Committee has developed and updated debt collection policy in response to changes in legislation or to the collection environment.</li> <li>• The infrastructure has been established to maintain the currency of policy.</li> </ul>
Recommendation No.14	The ANAO <i>recommends</i> that the ATO develop and disseminate clear and comprehensive standards for debt collection activity.	<b>Partially implemented</b> <ul style="list-style-type: none"> <li>• The Debt Collection Policy Committee has developed and distributed debt collection administrative standards and procedures nationally. However, national standards for debt collection performance are still being developed.</li> </ul>
Recommendation No.15	The ANAO <i>recommends</i> that the ATO develop and implement a comprehensive debt collection Quality Assurance program. This program should take advantage of the efficiencies associated with business system automation of case selection, review and reporting, supplemented by an appropriate manual QA program.	<b>Partially implemented</b> <ul style="list-style-type: none"> <li>• Quality Assurance initiatives have been progressively implemented since 1997. However these fall short of the comprehensive program recommended by the ANAO. Poor quality data, systems rigidities and the variable priorities of operational management have impeded the full implementation of this recommendation.</li> <li>• ATO's QA initiatives have however improved the quality of administration in INB and case decision making in the former SBI and WHT business lines. The ANAO has made additional recommendations about QA initiatives in this Report.</li> </ul>

<b>Recommendation Number</b>	<b>Recommendation and ATO response in 1996</b>	<b>State of Progress at time of follow-up audit and ANAO comment</b>
Recommendation No.16	The ANAO <i>recommends</i> that the ATO develop national procedural documentation to provide clear and consistent guidelines on collection processes.	<p><b>Fully implemented</b></p> <ul style="list-style-type: none"> <li>• The Debt Collection Policy Committee developed and distributed debt collection standards and procedures nationally.</li> <li>• Procedures also developed for Debtassist and SBI debt collection procedures.</li> <li>• ATO has maintained a substantial professional development and technical training program for staff.</li> </ul>
Recommendation No.17	The ANAO <i>recommends</i> that the ATO review existing debt collection delegations and authorisations with a view to national consistency and increase the ATO's business systems' capacity to control and monitor delegations and authorisations.	<p><b>Fully implemented</b></p> <ul style="list-style-type: none"> <li>• National set of delegations implemented.</li> <li>• Next review scheduled for November 1999.</li> </ul>
Recommendation No.18	The ANAO <i>recommends</i> that the ATO improve its debt collection business systems to provide a greater degree of automated recovery action throughout the collection process.	<p><b>Implementation in progress</b></p> <ul style="list-style-type: none"> <li>• The new RMS will allow greater automation of processes.</li> <li>• Profiling will allow the ATO make the most appropriate collection response to each debtor and to classes of debtors. Once established, this is an automated process.</li> </ul>
Recommendation No.19	The ANAO <i>recommends</i> that the ATO improve the capacity of its business systems to structure key risk data associated with outstanding debt, and provide interpretative data, such as financial ratios and risks indices, to assist efficient and effective decision-making by recovery staff.	<p><b>Implementation in progress</b></p> <ul style="list-style-type: none"> <li>• The new RMS will allow greater automation of processes.</li> <li>• Profiling has assisted in the development of appropriate automated action for debtors.</li> <li>• ATO systems do not have the capacity to produce the nominated interpretive data.</li> <li>• ANAO has made additional recommendations in this Report about the acquisition and use of such data.</li> </ul>

<b>Recommendation Number</b>	<b>Recommendation and ATO response in 1996</b>	<b>State of Progress at time of follow-up audit and ANAO comment</b>
Recommendation No.20	The ANAO <i>recommends</i> that the ATO implement a program for evaluating and improving debt collection procedures, training and business systems.	<b>Implementation in progress</b> <ul style="list-style-type: none"> <li>• ATO has maintained a substantial professional development and technical training program for staff.</li> <li>• The QA programs provide feedback on a regular basis about opportunities to improve debt collection procedures, training and business systems.</li> </ul>
Recommendation No.21	The ANAO <i>recommends</i> that the ATO report debt collection performance information by the following segments: <ul style="list-style-type: none"> <li>• primary debt outstanding;</li> <li>• additional debt applied as late payment tax;</li> <li>• additional debt paid on time while an outstanding debt is on account; and</li> <li>• debt arising from system errors.</li> </ul>	<b>Implementation in progress</b> <ul style="list-style-type: none"> <li>• The ATO regularly compiles performance information on a range of categories and segments, but not against all of the segments recommended.</li> <li>• The ATO has stated that the new RMS will facilitate easier collation of performance information.</li> <li>• No performance information on ATLP—it is being substituted by the General Interest Charge.</li> </ul>
Recommendation No.22	The ANAO <i>recommends</i> that the ATO's performance reports age outstanding debt with reference to the date that the debt becomes outstanding.	<b>Implementation in progress</b> <ul style="list-style-type: none"> <li>• The COMPACT system requires that the age of a debt is calculated from the date that the debt is entered onto COMPACT. This date is always later than the date on which the debt becomes outstanding.</li> <li>• The ATO has stated that the capacity to report on outstanding debts will be increased with the new RMS.</li> <li>• The ATO has also stated that the RMS will also enable the ATO to date debt from the correct date, namely the date on which the debt becomes outstanding.</li> </ul>

<b>Recommendation Number</b>	<b>Recommendation and ATO response in 1996</b>	<b>State of Progress at time of follow-up audit and ANAO comment</b>
Recommendation No.23	The ANAO <i>recommends</i> that the ATO develop and implement performance information that reflects the effectiveness of recovering outstanding debt (in terms of finalisation by collection and finalisation by other means) and the associated costs within an aged profile of debt. This performance information would provide the means for improving internal and external benchmarking and the selection of the most cost-effective options for recovery.	<p><b>Partially implemented</b></p> <ul style="list-style-type: none"> <li>• The ATO compiles this information, but as yet to a limited degree.</li> <li>• Ongoing work with the Australian Quality Council will enable the ATO to improve the quality and range of performance information.</li> <li>• With the introduction of accrual budgeting, the ATO now compiles information about the net cost of debt collection services. It is planned that the new RMS will facilitate more detailed reporting of costs.</li> </ul>
Recommendation No.24	The ANAO <i>recommends</i> that the ATO develop the ability to report performance on client segments of the outstanding debtor population.	<p><b>Implementation in progress</b></p> <ul style="list-style-type: none"> <li>• The ATO is developing this ability.</li> </ul>
Recommendation No.25	The ANAO <i>recommends</i> that the ATO establish a framework for coordinating debt collection research across business lines.	<p><b>Implementation in progress</b></p> <ul style="list-style-type: none"> <li>• The ATO has improved the cost effectiveness of legal collection strategies by carefully researching their cost and benefits.</li> <li>• The Kdnet research facility has improved ATO's capacity to coordinate debt collection research across business lines.</li> </ul>
Recommendation No.26	The ANAO <i>recommends</i> that the ATO conduct research to estimate the costs incurred by both the ATO and the Commonwealth for each collection technique, and that it implement a system that automatically assigns estimated costs to collection cases.	<p><b>Partially implemented</b></p> <ul style="list-style-type: none"> <li>• ATO has achieved the capacity to automatically cost collection for some classes of techniques or cases. The ATO has specified this capacity for the new RMS.</li> </ul>
Recommendation No.27	The ANAO <i>recommends</i> that the ATO ensure that the debt collection case management system has the capacity to isolate groups of outstanding debtors nationally to control test the cost-effectiveness of new collection strategies with reference to a control group.	<p><b>Partially implemented</b></p> <ul style="list-style-type: none"> <li>• The enhanced COMPACT system enables the isolation of cases on a national basis, but current ATO systems do not permit the control testing specified by this recommendation.</li> </ul>

<b>Recommendation Number</b>	<b>Recommendation and ATO response in 1996</b>	<b>State of Progress at time of follow-up audit and ANAO comment</b>
Recommendation No.28	The ANAO <i>recommends</i> that the ATO review its overall coverage of plans to ensure that all debt collection units have plans in place, thereby promoting a degree of consistency across the whole of Debt Collection on a branch, region, business line and national level.	<p><b>Fully implemented</b></p> <p>The ATO established a Receivables Management function within the new Small Business line on 1 March 1999. Strategic and operational planning for that group has progressed since then. Close liaison continues with INB debt collection.</p>
Recommendation No.29	The ANAO <i>recommends</i> that the ATO examine the development of more user-friendly and consistent approaches of providing access to debt collection reference materials for debt collection staff.	<p><b>Fully implemented</b></p> <ul style="list-style-type: none"> <li>• Better approach to internal communications with staff.</li> <li>• ATOconnect, ATO law, ATO practice statements, Debt Assist.</li> <li>• Newsletters with debt collection updates.</li> <li>• Debt Collection Policy Committee developed policy and procedures for easier reference.</li> </ul>



## Appendix 3

### Staff reductions as a result of changed Withholding Tax Arrangements

In 1997 the ATO presented Government with a review of tax penalty arrangements and their administration that identified that the revised penalty payment thresholds would yield savings of:

- 1998–99 \$9 million (180 Average Staffing Level (ASL))
- 1999–00 \$11 million (225 ASL);
- 2000–01 \$11 million (225 ASL).

These savings were made forthwith and the ATO's budget was adjusted downwards so as to achieve these ASL savings in the years indicated.

The ATO advised Government that the major share of these savings (estimated at between 80 per cent and 90 per cent) were predicated on the then ATO recommendations for a more cost effective penalty regime being adopted. The implementation of it required new legislation.

As a result of the election in 1998 and changes to Government tax policy, the new legislation did not become operational until 1 July 1999.<sup>74</sup> ATO has advised that it will not become fully operational until 1 July 2001.

ANAO notes that the savings to tax administration were embodied into the 1997–98 Budget some two years before the savings could be realistically achieved.

---

<sup>74</sup> This is the RBA/GIC package.

## Appendix 4

### The Ancient Debt Project<sup>75</sup>

During financial year 1997–98 the ATO undertook a project to collect ancient debt on ATO's books in one region. The project consisted of up to ten staff and had an estimated cost of about \$600 000. The project functioned for about 15 months. Although accurate records of the project were not kept, the ATO estimated that the project examined about 1400 ancient debt cases that had a total of approximately \$25 million overdue tax debt owing.

The team managed to finalise about 500 cases resulting in additional revenue of about \$3 million. The ATO negotiated arrangements to pay off the overdue tax debt for a further 218 cases. The expected revenue from these payments is estimated to be about \$3.5 million. Negotiations were underway with a further 329 cases and the ATO expected to collect additional revenue from them, perhaps as much as \$5 million. The team was satisfied that the overdue tax debt of about \$4 million could not be recovered from 332 cases. These were written off. The ATO advised that the likely revenue that accrue from this project when all negotiations and arrangements were settled would be about \$12 million.

The ATO advises that all of the debt would have been written off had the project not been initiated. The project shows that the ATO can collect at least half of ancient debt that would have otherwise have been written off. It indicates that an investment of \$600 000 on ATO debt collection activity directed at debts more than two years old can generate \$12 million in Commonwealth revenue.

ANAO noted that no action has been taken on the debts during the two years that they were on COMPACT. This meant that the management of the cases was labour intensive. ATO staff had a major task establishing the correct value of the overdue tax debt. ANAO also noted that most of the cases actioned by the project team were for debt levels 4, 5 and 6. Very few of the cases actioned were for debt levels 1, 2 and 3.

---

<sup>75</sup> Ancient debt is debt that has been on ATO's books for two years or more.

## Appendix 5

### Outsourcing the collection of tax debts

<b>Characteristics</b>	<b>Income Tax</b>	<b>Recurring Taxes</b>
<i>Entity</i>	Person or Business	Business
<i>Balance Calculated</i>	According to ITAA and specific case law eg. Kinny <sup>76</sup>	According to a simple arithmetic formula
<i>Dispute Rights</i>	Available	Not available (except Sales Tax)
<i>Amendment Provisions</i>	Yes	No
<i>Release Provisions</i>	Yes	No
<i>Write Off</i>	Can be re-raised	Can be re-raised
<i>Association with ATO</i>	Lifelong	For period of registration
<i>Complications of hardship eg. Sickness, divorce, unemployment</i>	Yes	Not to the same extent as the entity is a business
<i>Corporate Veil</i>	Can't be lifted, no access to Directors	Can be lifted as there is access to Directors through Director Penalty notices
<i>Non-lodgment</i>	Must have lodgment to collect the debt (except s168 to raise default assessment)	Non lodgment can be overcome by an estimate
<i>Non-payment</i>	Simply collect as any other creditor in the State courts	Offence against the Commonwealth, a relatively simple process to collect
<i>Fines</i>	No	Yes and jail sentence
<i>Obligations and Payment</i>	May be years apart	Close
<i>Community acceptance Accurate Account Balance</i>	Lower because debt often a personal one Will require checking before outsourcing and will be on an annual basis or quarterly for provisional tax	Higher because the debt belongs to a business May not require as much checking before outsourcing. May be younger because recurring, probably monthly.
<i>Frequency of tax debt assessment</i>	Remote as assessment and collection of tax is generally annual; collection quarterly for companies	Likely of same type of debt arising, as tax is quarterly, but may also be monthly
<i>Legislative amendment required to outsource</i>	Likely	Likely

<sup>76</sup> This refers to the impact of a 1988 Supreme Court of New South Wales decision regarding the calculation of the tax outstanding and the additional tax for late payment on that tax. The impact of the decision is that for relevant cases, the ATO is required to manually reconstruct a taxpayer's account. This arises only in certain cases. These concern instances where an income tax assessment includes a provisional tax debt and that debt remains unpaid after the due date of the next year's assessment. In these instances, the ATO is required to calculate the additional amounts for late payment on the provisional tax separately to that of the prime tax in the actual assessment.

## Appendix 6

### COMPACT Problems: Data quality and other deficiencies

ANAO observed a number of weaknesses in the COMPACT system and in the quality of data used by the ATO for debt collection purposes. This is the consequence of several design features of COMPACT.

#### Quality of data

During the audit the ATO initiated a major clean up of data. Poor quality data has been a significant impediment to improved debt collection performance. The shortcomings in the quality of data on all relevant databases are of concern.

We have other concerns about data quality on COMPACT. These have to do with the origins of COMPACT and the numerous special-purpose extensions and re-developments that have been undertaken over the years. Data entry problems, unreliability in the COMPACT status codes, and the absence of quality assurance routines are other reasons for poor quality data. The following is an overview of several examples noted by the audit.

When a case is finalised, for example, the system over-writes previous case history data. It increases or reduces outstanding debt balances, in accordance with additional debt incurred or payments made, without maintaining a full payments and/or account history. As there is a high unreliability in the use of case status codes, especially the code for finalisation of cases, this problem is of concern. There are additional difficulties in matching debt referred or payments to the appropriate period.

The calculation of debt on COMPACT may also be affected by the inclusion of other means of collection such downloading, other credits, write offs, transfers and adjustments. The overall impact is that COMPACT financial data is not maintained on a consistent accounting basis. ANAO also noted instances where records have negative balances, where there is a status date that pre-dates the referral date and where there are records with a nil original balance. This makes the accurate analysis of trends in debtors very difficult. The introduction of the RBA/GIC arrangements with consequent history of entries and payments may alleviate this problem if adequate support systems are designed.

## **COMPACT and the ATO data warehouse**

The figures on reports derived from COMPACT and those derived from the data warehouse do not correlate. There are a number of reasons for this, including:

- Multiple referrals of a client. If a taxpayer is referred to COMPACT a number of times, each occurrence of referral for this client will be counted. By contrast the warehouse report will only include the most recent occurrence of referral which creates a discrepancy.
- Timing difference. Data is downloaded daily to COMPACT from NTS, AIS, FBT and CSA. The formal COMPACT reports are built on the 28th day of each month and each system is refreshed at varied times. This means that the reports are not going to be run on the same data.
- Deletion of cases created within same financial year. COMPACT allows the deletion of a case in the same year in which it was created. This means that a case may exist at the time of a COMPACT report but no longer exist when a warehouse report is created.
- Change of business line. There seems to be many instances of debtor cases being exchanged between INB, LB&I and SB. As the reports are a snapshot of what cases belong to a particular business line at a particular time, discrepancies are inevitable.

## **NTS/AIS Release 3 problems**

ANAO finds that there have been serious adverse consequences for debt collection performance from the introduction of NTS/AIS Release 3 (referred to as R3 in the following), since its implementation in January 1999. There were instances where notification of tax debt was sent with incorrect charges and amounts and to the wrong person. ANAO was advised that one of the main reasons that problems occurred was because the incorrect code for the type of tax being demanded (eg. Income Tax, FBT, Canning Fruit Charge etc) was input in the preparation of the Final Notice run.

In some circumstances, NTS did not finalise certain cases that had nil balance. The result was that cases are remaining 'live' on COMPACT despite there being no debt. Changes to the procedure for imposition of penalty and costs may have resulted in more than \$1 billion of penalty and costs being incorrectly debited where tax file numbers have been incorrectly keyed as the amount of assessed debt. Inadequate correction procedures exist resulting in the need to remit rather than cancel these errors. Considerable time has been required to add 'filters' to COMPACT reporting to excise these errors.

Another reason for the faults was that large numbers of cases with provisional tax or Quarterly Provisional Tax components had been incorrectly referred as new cases prior to the due date. This has resulted in the incorrect referral of more than \$1 billion worth of cases. These downloads caused major delays in processing, network congestion, problems with disk space in six offices. This in turn required the upgrading of hard drives, major problems with Debt Collection reporting and the use of many hours of COMPACT staff time to try to minimise the problems.

## Appendix 7

### Income tax debtors with investment accounts

#### 1. Introduction

The ANAO initiated a project to explore the potential value of AIIR information for the collection of tax debt. The project was conducted to determine the amount of investment capital that some taxpayers had, which could improve the ATO's ability to collect debt from these debtors. AIIR reports show interest earned for various account types. The amount of investment capital was inferred from the amount of interest that was recorded on AIIR.

#### 2. Data sources

The ATO's debt cases are managed through the COMPACT system. Cases are referred to the system once a tax debit becomes overdue and usually remain on the system until all outstanding amounts are cleared and finalised.

Data is copied periodically (usually at a two-week interval) from the COMPACT system onto the ATO Data Warehouse (DWH), which allows for better information orientated analysis. For this analysis, data was extracted from the DWH on the 8 June 1999. This included data that was transferred into COMPACT until 4 June 1999. Investment Income data (AIIR) is processed on a yearly cycle. The latest data available from the system is for investment income paid until 30 June 1998. Thus, there is a discrepancy between the dates of the two data sets used in this analysis.

#### 3. Selecting the population for analysis

The target data set was limited to individual taxpayers and to income tax debt. This means that we did not attempt to match the AIIR transactions of, for example, recurring tax debts or business debtors. Matching the AIIR data requires matching using the tax file number (TFN).

It was decided, therefore, to extract from COMPACT only individual taxpayers with TFNs who were also income tax debtors.

As a result, from a total of 256 822 Individual type clients, 252 745 unique cases were extracted for the project. We note that, as matching was TFN based, an unknown proportion of AIIR transactions were not matched because some investors do not quote their TFN.

The TFNs from the selected cases were obtained through the standard CIDC TFN Search Facility (TSF). They were matched against 185 270 AIIR reports from 1998. The result of various rules of matching and

data simplification produced 56 912 individual records. They consisted of individual income tax debtors and the AIIR data sets associated with them. Further analysis indicated that these represent 42 059 unique individual income tax debtors.

## **4. Analysis**

### **Status codes**

The debt cases from COMPACT are at various stages in the debt handling process. The stage is partially represented by a status code. Cases where status codes showed that recovery action was completed or on hold (ie. in dispute) were excluded.

### **Investment types**

The AIIR reports include several fields indicating the type of investor and account concerned. Only those reports that related to individual investors were retained for the match. This reduced the data set to 132 077 AIIR reports representing 42 059 unique clients.

### **Interest rates**

In order to match the AIIR information to the outstanding debt record it was decided that the amount of interest income received should be converted back to a notional amount of invested capital. Clearly there are risks in doing this as we have no information on the interest rate received and the absence of detailed account-type coding added a second degree of approximation in the use of industry averages.



## Appendix 8

### Payment of debt by instalments

All categories of taxpayers may enter into an arrangement with the ATO to pay their tax debt by instalment rather than in one lump sum payment. In 1998–99 there were over 145 000 taxpayers who had established arrangements with the ATO to pay a total of about \$2 billion in tax debts. As analysis of the repayment rates for business taxpayers who were paying their tax debts by instalment was problematic, we only analysed the payment of income tax debt by instalment of individual taxpayers.

There were 50 194 individual taxpayers who were paying their income tax debt by instalments. Research undertaken by the ATO on 1996 individual income tax debts showed that the median debt was \$678. We examined the rates of repayment for these individual income tax debtors. We expected to find a relationship between a debtor's taxable income and the rate of repayment of a debt. We also expected that those on higher incomes would repay their debt using a higher proportion of their income to those on lower incomes. We examined whether the ATO determines a rate of payment that maximised the Commonwealth's interest, but was within the means of, and without harsh detriment to, taxpayers.

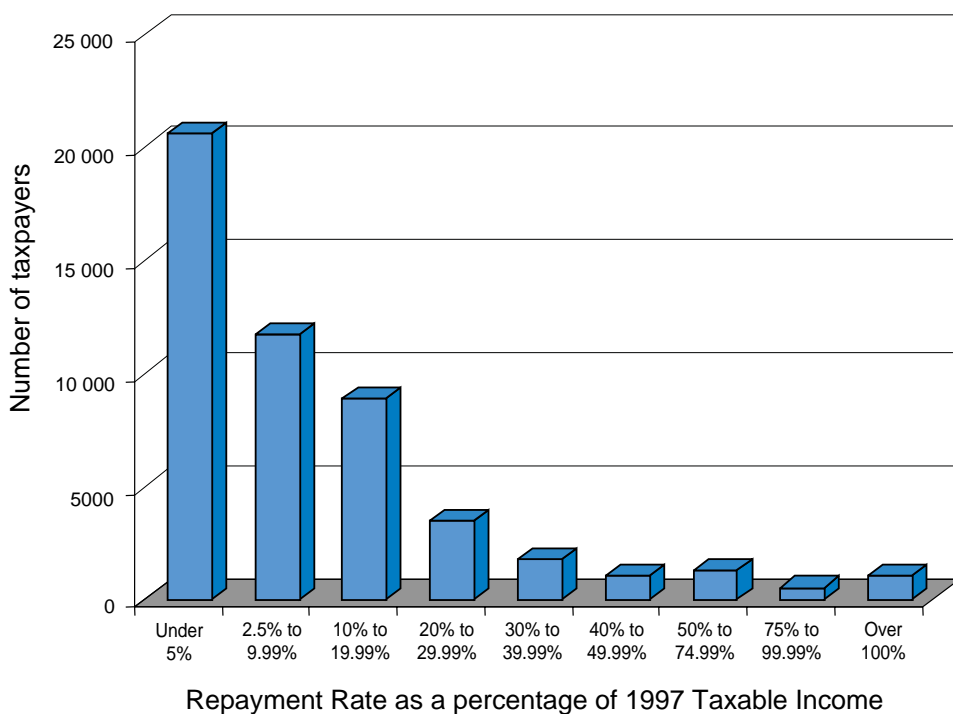
Figure 8 and Table 7 of this Appendix show the monthly repayment rates as a percentage of taxable income. This shows that 41 per cent of individual income tax debtors pay their income tax debt at a rate that is less than five per cent of their taxable income. ATO research shows that 60 per cent of income tax debtors had taxable incomes less than \$26 000. This suggests that those with repayment rates of less than five per cent were mostly individual income tax debtors on low incomes. However, we also have ATO research which shows that about five per cent, or almost 2400, individual income tax debtors with taxable incomes of \$50 000 or more pay their income tax debt at a rate that is less than five per cent of their taxable income.

The analysis does not lead to clear-cut conclusions, but indicates that the research of particular cases is warranted. The analysis thus far might suggest that two types of individual income tax debtors pay their tax debt by instalments. One large group consists mainly of low-income earners who may also be in receipt of income support. The other, relatively small group consists of persons on higher incomes and whose source of income may include non-wage and salary sources such as rent, interest, dividends, allowances, distributions from partnerships and trusts and other business income. The ATO's agreement to allow

repayment by arrangement at a low level for this group might not be in the Commonwealth's best interests. There may, of course, be good reason in any individual case that a high-income taxpayer cannot allocate more than five per cent of their taxable income to pay off an income tax debt. As we did not review individual cases, we are not in a position to comment on this.

Although our analysis did not lead to clear-cut conclusions, it would appear worthwhile for the ATO to consider the guidelines by which arrangements for repayment are made, and perhaps to set higher repayment rates for some of the income tax debtors on higher incomes.

**Figure 8**  
**Monthly Arrangement Repayment Rates as percentage of 1997 Taxable Income**



**Table 7****Monthly repayment rates as a percentage of 1997 taxable income**

<i>Repayment Rate</i>	<i>Number</i>	<i>Percent</i>
Under 5%	20556	41
2.5% to 9.99%	11714	23
10% to 19.99%	8833	18
20% to 29.99%	3456	7
30% to 39.99%	1745	3
40% to 49.99%	1025	2
50% to 74.99%	1299	3
75% to 99.99%	503	1
100%	1063	2
<b>Total</b>	<b>50194</b>	<b>100</b>

## Appendix 9

### Tax Debtors who are Company Directors

**Table 8**

**Individual Debtors who are Company Directors of Companies that have lodged a 1997 return**

<i>Debt Level</i>	<i>Number of Debtors</i>	<i>% of Debtors<sup>1</sup></i>	<i>Amount of Debt \$</i>	<i>% of Debt<sup>2</sup></i>
1	11 775	4.48	11 394 614	4.89
2	7371	7.72	33 797 804	7.34
3	5437	10.12	73 836 914	9.54
4	1493	15.88	51 985 788	14.86
5	697	24.17	48 180 125	22.97
6	459	29.22	289 886 213	35.34
<b>Total</b>	<b>27 232</b>	<b>6.39<sup>3</sup></b>	<b>509 081 458</b>	<b>17.87<sup>3</sup></b>

1 Percentage of total number of individual debtors that have a debt in that range.

2 Percentage of total debt owed by individual debtors for that level of debt.

3 This means that the total number (ie. 27 232) of individual debtors who are company directors of companies that have lodged a 1997 return comprises 6.39 per cent of the total number of individual debtors, that they owe collectively tax debts totaling \$509 081 458 which comprises about 18 per cent of total individual debt. ATO advise that the total amount of individual debt is about \$2.8 billion.

Table 8 shows the number of individual debtors who are company directors of companies that lodged a 1997 income tax return in relation to the total number of individual debtors classified by the level of the tax debt.

Table 8 shows, for example, that there were 459 individual debtors in this category who had a tax debt in excess of \$100 000, that these 459 tax debtors comprised 29.22 per cent of individual debtors with such tax debts and that the total tax debt owed by these 459 tax debtors comprised 35.34 per cent of total level 6 debt owed by individual tax debtors.

**Table 9****Individual Debtors who are Company Directors of Companies that have active debts**

<i>Debt Level</i>	<i>Number of Debtors</i>	<i>% of Debtors<sup>4</sup></i>	<i>Amount of Debt \$</i>	<i>% of Debt<sup>5</sup></i>
1	2553	21.68	2 605 404	22.87
2	1959	26.58	9 047 170	26.77
3	1589	29.23	21 522 562	29.15
4	437	29.27	15 301 250	29.43
5	182	26.11	12 357 689	25.65
6	140	30.50	148 304 439	51.16
<b>Total</b>	<b>6860</b>	<b>25.19<sup>6</sup></b>	<b>209 138 514</b>	<b>41.08<sup>6</sup></b>

4 Percentage of total number of individual debtors who are company directors that have a debt in that range.

5 Percentage of total debt owed by individual debtors who are company directors for that level of debt.

6 This means that the total number (ie. 6860) of individual debtors who are company directors of companies that have active debts comprises 25.19 per cent of the total number of individual debtors who are company directors of companies that have lodged a 1997 return, that they owe collectively tax debts totalling \$209 138 514 which comprises 41.08 per cent of the total debt of individual debtors who are company directors of companies that have lodged a 1997 return.

Table 9 shows the number of individual debtors who are company directors of companies that have active tax debts in relation to the total number of individual debtors who are company directors of companies that lodged a 1997 income tax return, classified by the level of the tax debt.

Table 9 shows, for example, that there were 140 individual debtors in this category who had a tax debt in excess of \$100 000, that these 140 tax debtors comprised 30.5 per cent of the 459 individual debtors (Debt Level 6 of Table 8) who are company directors of companies that lodged a 1997 income tax return with such tax debts and that the total tax debt owed by these 140 tax debtors comprised 51.16 per cent of total level 6 debt owed by individual tax debtors who are company directors of companies that lodged a 1997 income tax return.

## Appendix 10

### Individuals (Non-business) Income Tax Debtors: Untraceable Cases 30 June 1999

**Table 10**

**Individuals (Non-business) Income Tax Debtors: Untraceable Cases  
30 June 1999**

<i>Debt Level</i>	<i>Number of Debtors</i>	<i>Value of Debt (\$m)</i>
1	5197	4.40
2	1068	4.56
3	590	7.82
4	86	3.00
5	36	2.41
6	12	5.42
<b>Total</b>	<b>6989</b>	<b>27.61</b>

# Index

---

1996 Report 13, 19, 39, 51, 57, 60,  
79, 98, 105

## A

accountabilities 15, 19, 53, 62, 95,  
97, 98

accountants 25, 111

accrual 23, 61, 67, 91

active 11, 17, 22, 45, 47, 50, 59,  
73-75, 77, 83, 89, 97, 102, 108,  
122, 141

active tax debtors 17, 50

Additional Tax for Late Payment  
(ATLP) 57, 59, 122, 126

aged debt 15, 17, 19, 22, 45, 50, 62,  
71, 74, 84, 88, 89, 102, 108, 110

aggressive tax planning 14, 19, 67,  
116

Annual Income and Investment  
Reports (AIIR) 101-103, 135, 136

ambiguous 21, 67

analytic 8, 55, 99, 107, 109, 120

ancient 45, 49, 50, 71, 74, 77, 130

annual report 11, 20-22, 27, 34, 48,  
49, 64, 66, 69, 70, 72, 73, 115

"A New Tax System" (ANTS) 97, 98,  
99

appropriations 21, 23, 39, 66, 67, 91,  
98

Australian Quality Council (AQC)  
68

Australian Securities and  
Investments Commission (ASIC)  
28, 99, 106

Average Staffing Levels (ASL) 129

assets 23, 38, 99, 108

ATO Integrated System (AIS) 50, 133

Australian Bureau of Statistics (ABS)  
25, 29, 83, 95, 105, 111, 115, 116

Australian Tax Office (ATO) 11-29,  
33-38, 40-43, 45-75, 77-115, 119,  
120, 122, 124, 126, 128-133, 135,  
137-141

Australian Transactions Reports and  
Analysis Centre (AUSTRAC) 28,  
99, 106

Australian Business Number (ABN)  
39

automated 23, 65, 100

avoidance 14, 19, 26, 67, 112, 114

## B

bankruptcy 25, 112-114, 120

barristers 25, 111, 112, 114

benchmarking 11, 20, 47, 56, 63, 69,  
126

budget 20, 21, 23, 27, 40, 66, 67, 69,  
73, 91, 98, 126, 129, 147

budget estimates 21, 69

Building and Construction industry  
114

bureaux 24, 28, 106, 107, 109, 110

Business Activity Statement (BAS)  
97, 122

business lines 11, 22, 34-36, 72, 92,  
124, 126

business systems 11, 14, 18, 47, 49,  
50, 54, 55, 59, 122, 124, 126

## C

call centres 58, 59, 65, 80, 97

cash economy 14, 19, 46, 67, 119

cash flow 42, 89

category 22, 49, 73, 77, 103, 140, 141

Centrelink 22, 28, 60, 87-90, 145, 146

collectable 15, 17, 20, 22, 45, 46, 48,  
50, 51, 61, 62, 64, 68-71, 73-75,  
77, 78, 84, 108, 110

commercial 12, 13, 22, 41, 52, 62, 63,  
72, 85-91, 100, 105, 108, 109

Commissioner of Taxation 14, 15,  
25, 36, 63, 66, 85, 112, 115

Computer Assistance for the  
Collection of Taxes (COMPACT)  
17, 20, 45, 48-50, 55, 59, 64, 70,  
72, 77, 79, 80, 82-84, 93, 101-103,  
106, 110, 122, 126, 130, 132,  
133-136

company directors 101-104, 107, 140, 141  
 competitive market 62  
 compliance 12, 16, 24-29, 40-42, 46, 54, 56, 57, 62, 63, 65, 67, 71, 79, 81, 83, 84, 93, 95, 96, 100, 104, 105, 110-114, 116, 119, 120, 122  
 compliance model 12, 16, 41, 42, 56, 104, 105, 119, 120  
 computer system 15, 93, 99, 103, 110  
 Consolidated Revenue Fund 23, 91  
 consumer 106  
 contestable 20, 52, 60, 65  
 costing 61, 72, 73  
 credit 18, 24, 28, 38, 40, 41, 50-52, 62, 74, 86, 87, 93, 97, 99, 100, 106-110, 113, 120, 130, 132  
 credit cards 86, 87, 120  
 credit providers 24, 86, 106-108  
 credit rating 24, 106, 107  
 credit reference 24, 28, 100, 106, 107, 109, 110  
 credit worthiness 99, 107, 108  
 culture 71, 93, 94  
 custodian 63  
 cycle 12, 40, 105, 114, 135

**D**

data mining 58, 99  
 database 14, 15, 23, 24, 28, 45, 51-53, 59, 95, 96, 98-101, 105-110, 122, 132  
 Data Warehouse (DWH) 135  
 debt collection 11-15, 18-24, 27, 28, 33, 34, 36, 37, 39, 40, 41, 47, 48, 51-54, 56-58, 60-66, 68-73, 75, 77, 80, 82-93, 95-101, 103, 104, 106-108, 110, 113, 122, 124, 126, 128, 130, 132, 133  
 debt level 19, 45, 61, 62, 80, 82, 130  
 debt on hand 12, 17, 35, 45, 46, 48, 49, 77  
 default 37, 108, 109, 130  
 demographic 105  
 Department of Finance and Administration (DoFA) 20, 68  
 directors 101, 103, 104, 107, 130, 140, 141

disciplinary reports 114  
 dispute 12, 17-19, 35, 38, 41, 45-48, 50, 51, 77, 78, 89, 113, 122, 130, 136  
 disputed debt 12, 1-19, 35, 46-48, 51, 77, 122  
 dollar value 17, 45, 49, 107  
 duplication 90

## E

effectiveness 13, 14, 16, 18-21, 23, 24, 28, 34, 40, 58, 60, 61, 63, 64, 67, 69, 70, 75, 85, 88-90, 92, 98, 100, 101, 106, 110, 126  
 efficiency 13, 14, 18-21, 23, 34, 40, 58, 60, 61, 64, 68, 70, 85, 92, 98, 100, 108-110, 120  
 equity 13, 14, 18-20, 33, 34, 54, 58-61, 64, 69, 70, 92, 98, 100  
 establishment 36, 39, 55, 57, 58, 62, 72, 97, 102  
 evasion 14, 19, 67

## F

family trust 114  
 fee 25, 98, 100, 112  
 fieldwork 51  
 final notices 81  
 finance sector 20, 25, 29, 65, 68, 87, 95, 107, 108, 110, 111  
 financial institutions 16, 24, 52, 63, 80, 85, 86, 101-103, 107  
*Financial Management and Accountability Act 1997 (FMAA)* 22, 37, 73, 78  
 financial year 17, 36, 50, 83, 102, 130, 133, 145  
 flexibility 15, 19, 21, 23, 61, 62, 65, 69, 71, 85, 91, 104, 122  
 Fringe Benefits Tax (FBT) 50, 78, 133  
*Fringe Benefits Tax Assessment Act 1986 (FBTAA)* 78  
 fruit and vegetable growers 111  
 Full Time Equivalent (FTE) 14, 47, 61, 96  
 funding 60, 66, 87, 91, 92



**G**

gainsharing 23, 90, 91, 92  
 General Interest Charge (GIC) 38, 39, 57, 83, 97, 115, 122  
 Goods and Services Tax (GST) 39, 97, 98, 100  
 Government 13, 14, 20, 21, 23, 24, 26, 34, 36, 38-40, 47, 57, 60, 61, 64-68, 77, 85, 87, 90-92, 98-101, 107, 109-111, 115, 129

**H**

hardship 37, 63, 78, 84, 89, 122, 130  
 Health Insurance Commission (HIC) 28, 99, 106  
 high wealth individuals 46  
 higher level 19, 80, 81, 93

**I**

inactive 45  
 Individual Non Business (INB) 35, 36, 47, 72, 79, 82, 83, 90, 96, 98, 103, 124, 128, 133  
 incentive 23, 61, 85, 90, 91, 107  
 income tax 11, 12, 22, 24, 34-40, 50, 53, 55, 60, 65, 74, 77-80, 82-84, 88, 89, 92, 96, 97, 102-104, 107-109, 113-115, 122, 130, 131, 133, 135-138, 140, 141  
 Income Tax (IT) 34, 36-38, 55, 78, 130  
 Income Tax Assessment Acts (ITAA) 36-38, 78, 130  
 industry standard 50  
 initial action 17, 18, 50, 77  
 insolvency 42, 45, 50, 51, 114  
 integrity 12, 25, 40, 41, 69, 96, 112  
 interest bearing accounts 102  
 intergovernmental agreements 39, 98  
 interlocutory 38  
 internal audit 87, 88

**J**

Joint Committee of Public Accounts (now JCPAA) (JCPA) 13-15, 18, 19, 33, 41, 51, 52, 54, 59  
 Joint Committee of Public Accounts and Audit (JCPAA) 13, 33  
 judicial 112

**K**

Kdnet 57, 99, 120, 126

**L**

late lodgers 81  
 lawyers 25, 52, 111  
 legal profession 25, 111, 112, 114  
 legislative framework 15, 33, 36, 60, 78, 85  
 leverage 96  
 liquidity 89  
 listing 24, 106-108  
 location 22, 23, 60, 66, 77, 79, 81, 88, 93, 99

**M**

mareva 38  
 medical practitioners 25, 111, 114  
 mercantile agents 22, 80, 87-89  
 monopoly 66  
 monopsony 66

**N**

narration segment 106  
 new 11, 15, 17, 20, 38, 39, 45, 47, 49, 51, 53, 55-60, 64-68, 71, 77, 80, 82, 88, 95-98, 104, 107, 110, 113, 120, 122, 124, 126, 128, 129, 134  
 new tax system 39, 96, 97, 104  
 New Zealand Government 20, 64, 68  
 New Zealand Internal Revenue Department 20  
 no action 17, 50, 77, 80, 130  
 notice serving 89

## O

objection 38  
old 38, 41, 45, 49, 50, 71, 74, 84, 103,  
108, 130, 136  
opportunity cost 71, 81, 89, 91  
outcomes 20, 21, 23, 27, 40, 65-68,  
73, 91, 95, 100, 101  
outsourcing 14, 22, 27, 52, 60, 77,  
85-89, 130

## P

Pareto 61, 62  
Parliament 12, 13, 21, 23, 33, 34, 39,  
40, 67, 91, 111, 115  
partnership 22, 28, 60, 90, 104, 114,  
137  
Pay-As-You-Earn (PAYE) 35, 39, 50,  
80, 82, 109, 122  
penalties 14, 18, 39, 54, 57, 59, 115  
performance information 13, 14, 18,  
20, 21, 34, 52, 54, 56, 60, 66, 68,  
72, 126  
performance measures 20, 27, 56, 63,  
64, 70, 73  
Portfolio Budget Statements 20, 21,  
40, 66, 67  
predictive 105, 120  
pricing agreement 66  
private sector 15, 16, 23, 24, 41, 52,  
55, 60, 61, 70-72, 74, 79, 81,  
85-91, 93, 98, 100, 101, 106, 109  
profile 61, 75, 76, 84, 99  
profiling 55, 56, 58, 80, 99, 105, 120,  
122, 124  
Public Debt Interest (PDI) 83  
public policy 78

## Q

quality assurance 14, 15, 17, 24, 34,  
52-54, 57, 77, 95, 110, 111, 124,  
132  
quantitative 26, 45, 51, 70, 101

## R

receivables management 11-15,  
18-23, 27, 35, 36, 47, 52, 55, 56,  
58-61, 63, 65, 68-74, 77, 81, 85,  
91-96, 98, 100, 110, 111, 122, 128  
recommendations 11, 13-16, 18, 27,  
29, 33, 34, 36, 51, 52, 54, 55,  
57-61, 82, 120, 124, 129  
recovery rates 18, 77  
recurring 11, 12, 25, 35-37, 40, 55,  
72, 85, 88, 89, 92, 97, 106, 109,  
112, 114, 122, 130, 135  
reduction 21, 55, 58, 61, 67, 68, 70,  
71, 82, 83, 110, 129  
resource management 21, 23, 66, 67,  
91  
resources 12, 14, 15, 19, 22, 23, 38,  
40, 47, 60, 61, 66, 69, 71, 77, 80,  
81, 84, 85, 91, 96, 98, 100, 101,  
120  
retailers 111  
revenue 11, 15, 20, 22, 23, 34, 35, 37,  
39, 41, 47, 60-62, 64, 65, 68, 72,  
74, 77, 81, 84-86, 91, 98, 100,  
101, 104, 105, 110, 113, 122, 130  
revenue collection 11, 34, 35, 37, 41,  
62, 68, 72  
reverse workflows 96  
risk management 19, 25, 33, 34, 53,  
81, 95  
risks 15, 16, 53, 95, 98, 104, 122,  
124, 136  
Running Balance Accounts (RBA)  
39, 97

**S**

saleable asset 85  
 Sales Tax 12, 34, 35, 39, 50, 80, 122,  
 130  
 schemes 46, 112  
 Senate Committee 21, 69  
 serial bankruptcy 112  
 solicitors 112, 114  
 solvency 42, 45, 50, 51, 89, 114  
 strategic plan 69  
 strategy 19, 21, 22, 44, 61, 69, 80, 87,  
 88, 119, 120  
 streaming 99  
 superannuation 35, 50, 66, 104, 114  
 systemic risks 53, 95

**T**

tabulations 45, 69, 102  
 targeting 14, 19, 67  
 tax agents 83, 105  
 tax avoidance 14, 19, 67, 112  
 tax returns 25, 40, 64, 80, 8-84, 103,  
 104, 111, 112, 114  
 taxable incomes 113, 137  
 taxation legislation 18, 19, 115  
 taxation policy 12  
 taxi drivers 111  
 telephone 80  
 time frame 53, 65, 74, 84  
 time taken 15, 22, 52, 58, 65, 73, 74,  
 82  
 timeframes 75, 82, 84  
 transparency 20, 63, 68

**U**

unactioned 15, 17, 18, 22, 53, 62, 65,  
 73, 77, 84, 88, 89  
 uneconomic 15, 22, 53, 56, 65, 71,  
 78-80, 84, 87-89  
 unpaid 40, 82, 103, 112, 131  
 unsecured creditor 51  
 untraceable 15, 79, 88  
 untraceable debtors 15, 79, 88

**V**

variables 58, 70, 71, 105

**W**

welfare 86  
 wholesalers 111  
 withhold 35, 38, 39, 41, 74, 129  
 workloads 15, 53, 65, 95, 96  
 written off 14, 15, 17-19, 22, 37, 45,  
 49, 53, 65, 67-69, 71, 73, 74,  
 77-80, 84, 8-89, 102, 130

# Series Titles

---

## Titles published during the financial year 1999–2000

Audit Report No.1 Performance Audit  
*Implementing Purchaser/Provider Arrangements between Department of Health and Aged Care and Centrelink*  
Department of Health and Aged Care  
Centrelink

Audit Report No.2 Financial Control and Administration Audit  
*Use of Financial Information in Management Reports*

Audit Report No.3 Performance Audit  
*Electronic Travel Authority*  
Department of Immigration and Multicultural Affairs

Audit Report No.4 Performance Audit  
*Fraud Control Arrangements in Education, Employment, Training and Youth Affairs*

Audit Report No.5 Performance Audit  
*IP Australia—Productivity and Client Service*  
IP Australia

Audit Report No.6 Audit Activity Report  
*Audit Activity Report January–June 1999*  
—Summary of Outcomes

Audit Report No.7 Financial Control and Administration Audit  
*Operation of the Classification System for Protecting Sensitive Information*

Audit Report No.8 Performance Audit  
*Managing Data Privacy in Centrelink*  
Centrelink

Audit Report No.9 Performance Audit  
*Managing Pest and Disease Emergencies*  
Agriculture, Fisheries and Forestry—Australia

Audit Report No.10 Financial Statement Audit  
*Control Structures as Part of Audits of Financial Statements of Major Commonwealth Agencies for the Period Ended 30 June 1999*

Audit Report No.11 Performance Audit  
*Financial Aspects of the Conversion to Digital Broadcasting*  
Australian Broadcasting Corporation  
Special Broadcasting Service Corporation

Audit Report No.12 Financial Control and Administration Audit  
*Management of Contracted Business Support Processes*

Audit Report No.13 Performance Audit  
*Management of Major Equipment Acquisition Projects*  
Department of Defence

Audit Report No.14 Performance Audit  
*Commonwealth Debt Management*

Audit Report No.15 Performance Audit  
*Management of Australian Development Scholarships Scheme*  
Australian Agency for International Development (AusAID)

Audit Report No.16 Performance Audit  
*Superannuation Guarantee*  
Australian Taxation Office

Audit Report No.17 Performance Audit  
*Commonwealth/State Housing Agreement*  
Department of Family and Community Services

Audit Report No.18 Performance Audit  
*Electronic Service Delivery, including Internet Use, by Commonwealth Government Agencies*

Audit Report No.19 Performance Audit  
*Aviation Safety Compliance*  
Civil Aviation Safety Authority

Audit Report No.20 Performance Audit  
*Special Benefits*  
Department of Family and Community Services  
Centrelink

Audit Report No.21 Performance Audit  
*Audits of the Financial Statements of Commonwealth Entities for the Period Ended 30 June 1999*  
Summary of Results

# Better Practice Guides

---

Administration of Grants	May 1997
AMODEL Illustrative Financial Statements 1999	Jul 1998
Asset Management	Jun 1996
Asset Management Handbook	Jun 1996
Audit Committees	Jul 1997
Building a Better Financial Management Framework	Nov 1999
Building a Better Financial Management Support	Nov 1999
Cash Management	Mar 1999
Commonwealth Agency Energy Management	Jun 1999
Controlling Performance and Outcomes	Dec 1997
Core Public Sector Corporate Governance, Principles for (includes Applying Principles and Practice of Corporate Governance in Budget Funded Agencies)	Jun 1997
Corporate Governance in Commonwealth Authorities and Companies—Principles and Better Practices	Jun 1999
Life-cycle Costing (in Audit Report No.43 1997–98)	May 1998
Management of Accounts Receivable	Dec 1997
Management of Corporate Sponsorship	Apr 1997
Management of Occupational Stress in Commonwealth Agencies	Dec 1998
Managing APS Staff Reductions —supplementary Better Practice Principles in Audit Report No.49 1998–99)	Jun 1996 Jun 1999
Managing Parliamentary Workflow	Jun 1999
New Directions in Internal Audit	Jul 1998
Paying Accounts	Nov 1996
Performance Information Principles	Nov 1996
Protective Security Principles (in Audit Report No.21 1997–98)	Dec 1997
Public Sector Travel	Dec 1997
Return to Work: Workers Compensation Case Management	Dec 1996
Security and Control for SAP R/3	Oct 1998
Selecting Suppliers: Managing the Risk	Oct 1998
Telephone Call Centres	Dec 1996
Telephone Call Centres Handbook	Dec 1996