



ATO Submission

to the House of Representatives Standing Committee on

Economics, Finance and Public Administration's

Inquiry into

The Management of the Tax File Number System

2 November 1999

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As the Committee’s Terms of Reference will address the full ANAO Report (No. 37, 1998-99), the ATO submission has been structured as far as possible to reflect the Report.

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1 Executive Summary

1. The submission outlines the history and operation of the Tax File Number (TFN) system as well as describing the Australian Taxation Office (ATO) Planning and Risk Management approach which is a context for TFN strategies. The submission highlights significant issues and initiatives, and then provides an updated status report against each of the Australian National Audit Office (ANAO) recommendations.
2. The TFN system has achieved most of what was originally intended in terms of improved compliance in the taxation and government payments systems, and improved service and administrative efficiency, whilst maintaining privacy.
3. The system has been significantly and progressively extended over the last 10 years, with clear additional benefits.
4. The ATO has, with other stakeholders, developed and implemented TFN initiatives in the context of its overall risk management approach. It has targeted higher risk areas and does not aim to cover all risk areas equally. There is a need to balance how finite resources are applied, and to balance risks against perceived or actual costs, and intrusiveness, to the community.
5. Risk assessment is a continuing process. As community behaviours, transactions and technologies change, so we adjust those risk assessments. As an example, such risk assessment processes were responsible for identifying the problems concerning TFN misuse in the clothing industry (as raised by an ATO staff member in a submission to your Committee). The behaviours identified have been addressed through a variety of strategic responses, including referrals to AFP and NCA. ASC and AUSTRAC have also been involved.
6. In the context of ongoing risk assessment, we are actively reviewing the appropriate balance in several areas discussed in the ANAO report, including:
 - Proof of Identity (PoI) and identity risk;
 - rental income reporting;
 - Australian Transaction Reports and Analysis Centre's (AUSTRAC) reporting;
 - Investments and Royalties Withholding Taxes Branch (IRW) systems integrity;
 - TFN data quality; and
 - continued development of how we deliver TFN services.

These reviews involve many other stakeholders.

7. The ATO has initiated discussions with other agencies to improve the PoI and client identification system, and has established a hierarchy of possible improvements that are now being evaluated for cost-benefit. Some could be implemented administratively, whilst others would require legislative change. Some could be contentious.
8. Of the areas of possible extension of TFN withholding and/or reporting, two of the most prospective relate to real estate property income and AUSTRAC transactions. However, in both cases there is significant work to be done to assess the cost benefit and practicality. We are continuing this work in consultation with other stakeholders.

9. The deficiencies of the IRW system are acknowledged but need to be balanced against the relatively small compliance and revenue risks. We are planning to enhance related systems in the context of tax reform initiatives including replacement and transfer of some of the IRW functionalities into our core systems.
10. It should be noted in this respect, that the ATO has for some time invested considerable effort in achieving a high degree of interconnectivity and integration across its core systems and data bases.
11. In respect of TFN data quality, we have a wide range of improvement initiatives in hand. In two specific areas:
 - we are actively analysing duplicate TFNs, though our work to date indicates that the extent and risk of the issue is less than initially indicated; and
 - for treatment of redundant records, we have several initiatives under way, though the cost benefit of full archiving at this stage appears doubtful.
12. We are continuing to develop leading practices in client identification and registration strategies, eg.
 - investing in the Australian Business Number (ABN) and adopting any related good practices for TFN; and
 - a comprehensive and ongoing TFN Improvement Project (TFNIP).
13. The most appropriate timing of investment in improving the TFN and related systems also needs to be considered realistically in the context of demands on resources and systems for implementing tax reform initiatives.

2 History and Benefits of the TFN System

2.1 Origins of the TFN System

(1) Pre 'TFN' arrangements

The Australian Taxation Office (ATO) has used a taxpayer identification file numbering system since 1936, although the arrangements were converted from an alphanumeric range to the current 9-digit numbers for individuals in 1976. The primary purpose of the previous file numbering arrangement was for ATO administrative efficiency, enabling a client to have their income tax affairs managed or to be used by the client in dealings with the ATO.

As an administrative tool, the allocation of a new identifier generally occurred through the lodgment of a client's first income tax return. Little or no requirement was placed on the individual to prove their identity.

In the mid 1980s the debate commenced about the introduction of a mechanism that would enable the Government to combat increasing community concern over tax, social welfare, Medicare and other fraud on the Commonwealth. This led to the introduction of the *Australia Card Bill 1986*. After considerable debate this Bill was set aside by the Senate on 8 October 1987 and the Government decided not to proceed with the legislation.

In a press release on 29 September 1987 the then Prime Minister referred to the decision not to proceed with the Australia Card Bill. He went on to announce that the Government had decided *'as a matter of priority, to examine the use of the existing tax file numbering system administered by the Australian Taxation Office, as part of a package of measures to crack down on tax cheating and welfare fraud'*. At the same time he announced the Government's intention to establish a Fraud Control Committee to monitor the development and implementation of fraud control mechanisms within Government agencies, and to introduce legislation providing for the reporting of large cash transactions.

(2) May (1988) Economic Statement

Following the Cabinet Decision (No 1115) of 18 May 1988, the then Treasurer formally announced the Government decision to proceed with the ATO proposal to enhance the existing 'Tax File Number' system. The essential purpose of the extended TFN system was to improve the efficiency and effectiveness of the ATO's income matching system under which reports supplied to the ATO are matched to details disclosed in the client's income tax returns.

(3) The Extended TFN System that took effect from 1 January 1989

The intention of the new TFN arrangements was to build a high integrity, unique identifier that would enable improved controls over the ATO's income matching system. The TFN system was designed to apply to Australian residents. (Non-residents could also apply for a TFN if they were authorised to work in Australia or had a requirement to lodge an Australian income tax return for income earned through investments.)

For individuals, the TFN consists of a 9-digit number, with an algorithm used to apply a 'check digit' as the last digit of the number. Within a range of 1000 numbers, the check digit formula will only provide approximately 100 valid numbers. The remaining 900 will not be recognised as valid TFNs by the ATO client identification system.

ATO clients who had an existing file number when the new arrangements took effect, continued to use that unique number. The ATO undertook an extensive program to advise existing taxpayers of their TFN and of the necessity to quote this number in all future dealings with the ATO. In addition, taxpayers were invited to advise ATO of any discrepancies or inaccuracies in the information held. The feedback from this exercise was used to review the taxpayers' records, thereby building on the integrity of the client identification system.

Where clients needed to obtain a TFN, from the commencement of the new arrangements, a TFN registration process was designed that required the provision of specific, original, source documentation to give a high degree of confidence about the identity of that TFN applicant.

(4) Income types initially impacted by the TFN arrangements, and the sanctions

The first phase of the new TFN arrangements had an impact on clients receiving salary and wage income from employment. From April 1989 employees were asked to quote their TFN on an Employment Declaration form so that the relevant rate of tax could be deducted under the appropriate schedule. Although under the TFN arrangements there was no compulsion for an employee to quote the TFN to an employer, failure to do so (in most instances) meant that the employer was obliged to deduct the highest marginal rate of tax, plus Medicare Levy.

As a result of the TFN legislation, group employers were obliged to record the employee's TFN on the Group Certificate, if it had been quoted on the Employment Declaration. The duplicate group certificate details were then provided to the ATO to facilitate the income matching system.

The second phase of implementation of the TFN arrangements related to 'investment' income. The arrangements were phased in from 1 July 1990, allowing for a one-year period for clients to either quote their TFN to their financial institution or investment body, or have tax withheld at the highest marginal rate, plus Medicare Levy. Development of these arrangements occurred through significant consultation and involvement from the *Interest and Dividend Payers Consultative Forum*.

In the circumstances where tax had been withheld because of the failure to quote the TFN, that amount of tax credit was available through the lodgment of the relevant year's income tax return.

Again, the investment bodies had an obligation to report to the ATO quarterly about the quotation of TFNs and an annual requirement to send an Annual Investment Income Report about the details of investment income paid to the client.

(5) Certain exemptions from the need to quote a TFN

The TFN legislation originally made provision for various categories of clients that were able to claim exemption from the requirement to quote a TFN for investment purposes. Some examples of those categories are:

- most pensioners (though TFN quotation required by paying agencies);
- entities not required to lodge income tax returns;
- non-residents;
- children whose income is below a certain threshold; and
- genuine Norfolk Island residents.

In respect of 'Employment' income, children under 16 who claim the general exemption on an Employment Declaration form and who do not earn enough to have tax taken out of their pay need not quote a TFN.

(6) Privacy Act 1988

The *Privacy Act 1988* came into effect on 1 January 1989, in conjunction with the introduction of the TFN arrangements. Enactment of that TFN legislation was delayed to allow for consideration of the Privacy Bill.

The effect on the ATO of the introduction of the Privacy Act was to reinforce the secrecy aspects of taxation law and to extend the ATO's responsibility to include safeguards in the collection and use of taxpayers' information. The TFN arrangements are protected by strict guidelines that are binding on the ATO as well as employers, financial institutions and other persons/organisations that have access to TFN information, or as a result of their responsibility to report information to the ATO.

The TFN Guidelines also apply to anyone who has possession and control of an individual's TFN information and provides that adequate security is afforded to that information. Severe penalties can result from improper use or disclosure of that information.

The Privacy Commissioner is empowered to award compensation for breaches of privacy and to instruct agencies to alter or cease practices held to be in breach. For continued community confidence it is important that the ATO has effective arrangements in place to safeguard privacy, and a commitment to maintain these.

2.2 Extensions to the TFN System

The table at Appendix 1 charts the emergence of the TFN arrangement and the progressive extension of its use, both for taxation and broader Government policy purposes. It demonstrates that the system has been significantly and progressively extended over the last 10 years, with clear additional benefits.

2.3 Benefits gained from the TFN System

Appendix 2 summarises examples of the benefits gained from the TFN system. The TFN system has achieved most of what was originally intended in terms of improved compliance in the taxation and government payments systems, and improved service and administrative efficiency, whilst maintaining privacy.

3 ATO Planning and Risk Management Approach

The TFN administration and development strategies need to be seen in the context of the overall approach to planning and risk management.

3.1 ATO Integrated Planning System and Strategic Directions

The Integrated Planning System is a rigorous system of corporate governance and a key element of the ATO's Strategic Management approach. It enables the ATO to continuously monitor and review the effectiveness of its strategies so decisions about allocation of resources can be made based on shifting priorities. It is an evolving process, adapting to deal with emerging issues.

While the ATO is clearly focused on its purpose and guiding principles, the organisation continuously revises its strategic direction to reflect changes occurring in the environment. For example, in 1998-99 the organisation:

- directed resources to implement tax reform;
- directed resources to key compliance initiatives, such as targeted 'hot spots', to protect revenue;
- increased its emphasis on improving community confidence and service;
- built stronger alliances with key stakeholders;
- increased strategic intelligence activities at the corporate and business line levels, based on an integrated approach to identifying, gathering, analysing and acting on intelligence; and
- adopted technologies to streamline work practices.

The organisation's strategic directions and relative risks are reflected in decisions on planning and resourcing and are made in the context of the Government's new accrual budgeting framework.

3.2 Assurance

It is in this dynamic environment that the ATO's assurance and performance reporting processes are reviewed and streamlined. In 1998-99, four reporting sub-systems were operating and corporate assurers were appointed to provide overview reports on aspects such as finance, security, information technology, internal audit and human resources.

The four reporting sub-systems are:

- a corporate governance system to ensure the ATO's operations meet expectations;
- a business and service line governance system to ensure each line's operations meet expectations;
- a corporate performance reporting system to ensure the ATO's outcomes and outputs are being achieved within budget; and
- a line performance reporting system to ensure each line's performance is on-track and within budget.

This financial year, monthly performance reports will reflect performance against ATO Outputs as articulated in the ATO Outcomes and Outputs Framework, and detailed in the ATO Corporate Plan (1999-2002).

Twice a year, the monthly process is supplemented by governance reports from all lines, and reports from corporate assurers. These reports deal with more systemic issues, patterns and trends.

End-of-financial-year reports must include assurances and representations about the internal control processes and the veracity of financial balances. These are further supported by audit and fraud control planning and programs.

3.3 Risk Management

Risk management is central to the planning, resourcing and assurance processes. The ATO's operations are generally conducted within a risk management framework derived from standards such as:

- the MAB-MIAC Guidelines for Managing Risk;
- the Australia/New Zealand Standard for Risk Management; and
- the ANAO's Better Practice Guide to Controlling Performance and Outcomes.

The framework recognises that there are limited resources available. Risk management helps the ATO to apply its finite resources to achieve objectives in the most efficient and effective way.

This risk management framework is the tool ATO managers use when assessing risk. The framework assists with decision making regarding whether or not the identified risk is acceptable or requires treatment. The risk assessments focus on the ATO's objectives, identifying risks and analysing them for likelihood and consequences, assessing priority and treatment where the risk is considered unacceptable.

The acceptability, or otherwise, of a risk will hinge on judgements as to impact on:

- revenue
- compliance
- cost of compliance to the community
- community confidence
- internal capability and resources

Once a risk profile has been identified and assessed, it is then necessary to manage that risk through the implementation of an effective strategy and monitoring framework.

The ATO has been acknowledged by the ANAO (report no. 37, 1996/97 into ATO Risk Management) as being among the first agencies in the Australian Public Service (APS) to introduce a formal risk management process as part of its strategic planning framework. It also recognised the ATO's increasing commitment to risk management principles and the potential this had to 'significantly improve the economy, efficiency and administrative effectiveness of the tax processes, together with the ATO's equity and accountability in its handling of the processes.'

3.4 Risk Management and TFN

The ATO has, with other stakeholders, developed and implemented TFN initiatives in the context of its overall risk management approach. It has targeted higher risk areas and cannot (and should not) attempt to cover all risk areas equally. There is a need to balance how finite resources are applied, and to also balance risks against perceived or actual costs, and intrusiveness, to the community.

Risk assessment is a continuing process. As community behaviours, transactions and technologies change, so we adjust those risk assessments.

In this context we are actively reviewing the appropriate balance in several areas discussed in the ANAO report, including:

- Proof of Identity (PoI) and identity risk;
- rental income reporting;
- AUSTRAC reporting;
- IRW systems integrity;
- TFN data quality, and
- continued development of how we deliver TFN services.

These reviews involve many other stakeholders. Each is discussed in the relevant sections of this report.

4 The Tax File Number Improvement Project

Internally the ATO is undertaking a range of activities designed to re-engineer the current TFN system. At another level, the ATO is actively pursuing whole of government opportunities with other agencies. These are discussed below.

4.1 Outline of the Project

The Tax File Number Improvement Project (TFNIP) is an ATO corporate investment project which aims to improve compliance, service and efficiency by having better individual client identification and registration processes. In addition, the ATO is also aiming to provide increased confidence in the integrity and the use of the TFN for its stakeholders within the taxation and social welfare systems. More specifically, the project seeks to:

- improve the current system such that it supports the tax reform agenda;
- capitalise on the strengths of the current system while recognising that there are areas of weakness which can be improved; and
- contribute to a system which enables the whole of government agenda to be taken forward.

The TFNIP started in late 1998 within the Individual Non-Business Line (INB) of ATO. The main focus of the project is improving registration of new applicants and improving the data quality of the individual TFN database. As such, sub-projects dealing with PoI, extension of data matching on identity, the format and accessibility of the TFN advice, the potential for electronic delivery (within available ATO resources), and data quality have been the primary focus of the project.

The ANAO audit also made a number of additional suggestions and these have been incorporated into the TFNIP.

The current status of the TFNIP and the various sub-projects is outlined in Appendix 3. In addition, Chapter 5, which addresses specific recommendations, provides further details.

The next sub-sections provide more detail on the issues which have cross agency implications, in particular PoI and data matching on identity.

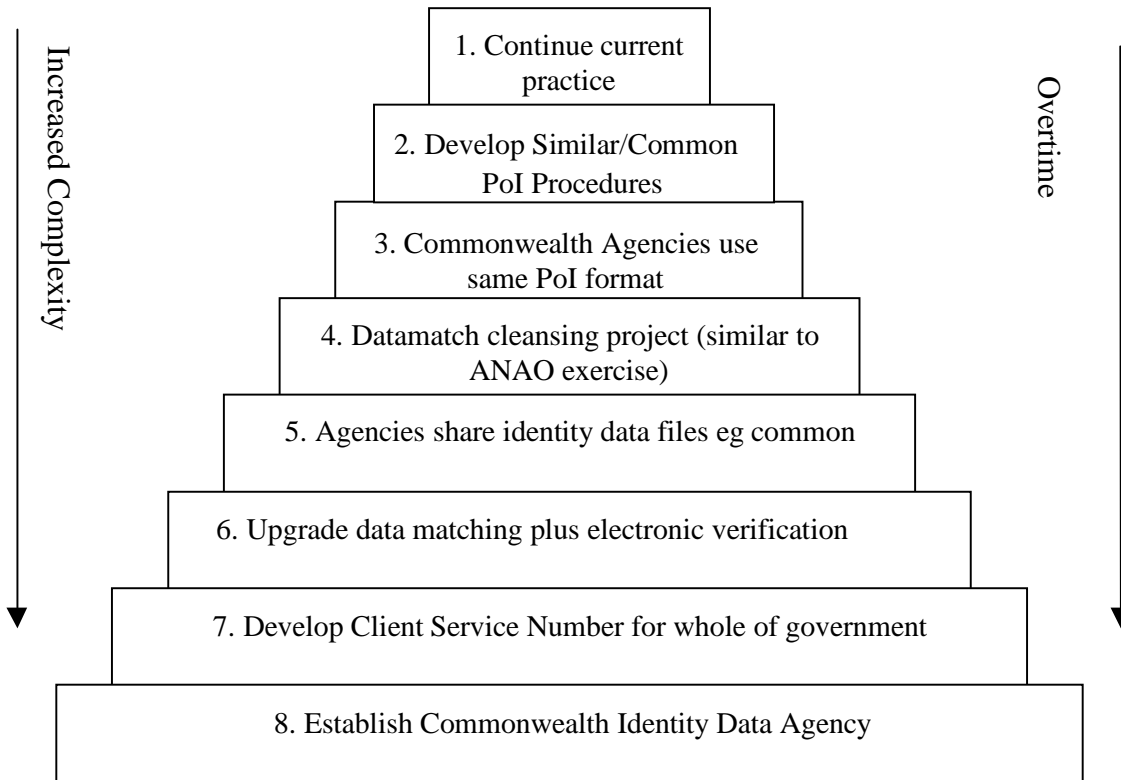
4.2 Whole of Government Liaison – Hierarchy of Options

The ATO has convened several meetings with Centrelink, the Health Insurance Commission (HIC) and other agencies to discuss:

- improving the integrity of current PoI documents and processes;
- the development of a common PoI policy across Commonwealth agencies;
- potential for extension of data matching of identity information (name, address and date of birth) between agencies; and
- potential for a whole of government client service number.

The ATO has also met with a number of State and local government agencies to discuss their perceptions and views on similar issues and opportunities. These are discussed later in this section.

At a recent meeting of the ATO, Centrelink and HIC, it was proposed that a hierarchy of solutions be developed for consideration. This hierarchy, based on discussions with senior project officers from the above three Commonwealth agencies and others, is below.



The following table briefly canvasses the advantages and disadvantages of each of the above steps in the hierarchy above against a range of criteria, including:

- the need to maintain overall compliance and collect targeted revenue;
- the need to minimise compliance costs for clients;
- the need to maintain community confidence including addressing the privacy concerns;
- the need to build an efficient ATO and reduce administration costs; and
- the need to support a range of policy initiatives across other agencies and work towards a whole of government approach.

It should be noted that subsequent steps build on the advantages of the previous steps.

Step	Advantages	Disadvantages
1	<ul style="list-style-type: none"> ▪ Considered that 95% of population represent low or no risk ▪ No additional investment or cost 	<ul style="list-style-type: none"> ▪ ANAO criticisms remain ▪ Unknown cost of ID fraud ▪ Different PoI processes for community resulting in increased cost of compliance for individuals meeting different regimes
2	<ul style="list-style-type: none"> ▪ Simpler single regime ▪ Provides increased client service and certainty for clients in establishing identity across government agencies ▪ Simpler for agencies issuing identity documents to Commonwealth ▪ Discourages minor frauds 	<ul style="list-style-type: none"> ▪ Could involve some cost due to form and system changes ▪ Desired flexibilities for different programs could complicate process ▪ Individuals may still need to re-establish PoI with each agency
3	<ul style="list-style-type: none"> ▪ Better client service arising from a uniform regime ▪ Could be shared with financial institutions (or based on “100 point” system) and other tiers of government ▪ Common data problems may be resolved and fraud may be discouraged 	<ul style="list-style-type: none"> ▪ Costs for forms and IT changes ▪ Community and privacy considerations need to be addressed
4	<ul style="list-style-type: none"> ▪ Would identify inconsistencies in identity data between government databases ▪ Would identify potential fraud cases previously undetected ▪ Would update government identity records and make some cost savings ▪ Improve current data matching on identity where TFN not compulsory 	<ul style="list-style-type: none"> ▪ Community and privacy considerations need to be managed ▪ May require legislative changes ▪ If too many exclusions – some value may be lost ▪ Up front costs may be of concern to some agencies
5	<ul style="list-style-type: none"> ▪ Would enable a one-stop approach for the public changing address with government agencies ▪ Increased ease of community compliance ▪ Would allow up-to-date client details for all agencies ▪ Would entail no change for large percentage of community ▪ Opt-in system could increase level of acceptance by community 	<ul style="list-style-type: none"> ▪ Community and privacy considerations need to be managed ▪ May need to be opt-in system for community which would limit effectiveness ▪ Potential costs in setting up, maintaining and managing
6	<ul style="list-style-type: none"> ▪ Improves client service ▪ Considerable value in consolidation of data about births, deaths, arrivals and departures ▪ Helps to limit and detect identity fraud ▪ On-line verification assists speed of authentication ▪ Potential to authenticate PoI on the spot or electronically 	<ul style="list-style-type: none"> ▪ Potential high set-up costs ▪ Community and privacy considerations need to be managed ▪ May be difficult to manage real time verification

7	<ul style="list-style-type: none"> ▪ Could be used at all levels of government ▪ Could be initially an opt-in for individuals resulting in higher/quicker service levels ▪ May not need to be a “card” per se but a linking number for all agencies (ie similar to ABN) 	<ul style="list-style-type: none"> ▪ Significant start-up costs if a card issued ▪ Privacy concerns need to be managed ▪ Community concerns about ‘connectivity’ of information ▪ Would need support from majority of government agencies
8	<ul style="list-style-type: none"> ▪ Reduction in overall registration costs for government by having one registration point ▪ Minimise fraud and prevent duplications ▪ Single agency with uniform regime more accountable ▪ Would become single entry point to government for individuals 	<ul style="list-style-type: none"> ▪ Public concerns about Government intervention ▪ Privacy concerns ▪ Establishment cost

The ATO is currently working with these other agencies to further consider and develop options from steps 2-4. Providing that a balance between all of the above criteria can be sensibly achieved, it is our intention to progress with these.

We recognise that there are potentially sensitive political and community issues which would need to be considered in terms of actively progressing steps 5-8. In addition, detailed cost-benefit analyses have yet to be carried out for these latter options. Nevertheless, we believe it is appropriate, confirmed by the ANAO report, to progress evaluation of these proposals. We intend developing these options with other relevant stakeholders, with a view to advising to government.

4.3 Current negotiation with external agencies on Proof of Identity (PoI)

The ANAO report contains numerous references to PoI and suggests, in a number of places, that the ATO should consider the development of a Commonwealth single individual client service number. The ATO has instigated consultation across a number of Commonwealth agencies and other levels of government to canvass their views.

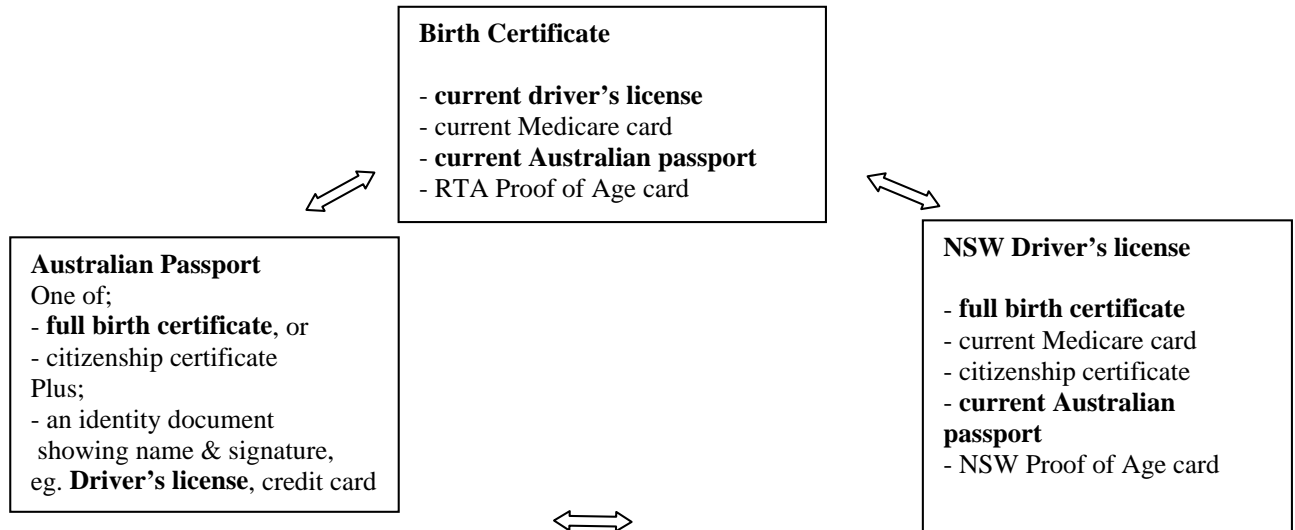
4.3.1 Background

Traditionally, Commonwealth agencies with PoI requirements for their individual registration processes have consulted with each other on a fairly informal basis to share current knowledge about identity document integrity. However, while the pool of identity documents is invariably the same, various preconditions and levels of importance have been placed on these documents. For instance, Centrelink ascribes a higher level of integrity to a birth certificate which was issued more than five years ago than to one more recently issued. The ATO does not differentiate.

Like most agencies, the ATO has, over time, adapted the range of identity documents which it accepts; adding new or additional forms and deleting those which have become redundant. For example, the latest reprint of the TFN application form removed the Tradesmen Certificate and the Nurses Registration Certificate because possession of such documents would ostensibly already presume that the individual is working and therefore has a TFN for taxation purposes.

An identified area of concern among agencies is the so-called 'circular path' of identity. The following diagram illustrates how a birth certificate, a driver's licence and an Australian passport can variously be used as suitable proof of identity to obtain one another.

Examples of 'Circular Path' for Identity documents.



NB: The PoI requirements for the above documents are more expansive, but the requirements would be satisfied in the above example.

This 'circular path' is a primary feature of a system where an identity can be created. Recognising this, the ATO has commenced an extensive liaison process with other agencies, including some at State and local government level. The intention of this liaison is primarily to establish a higher level of integrity and reliability for identity documents.

4.3.2 Liaison with other agencies

The ATO commenced the extensive liaison process in March 1999 to ascertain current developments with identity documents, to understand the extent of the problem, and to start to work towards developing options for potential solutions.

The liaison has been in the following areas:

- (a) Other Commonwealth agencies;
- (b) AUSTRAC, the Australian Bankers Association (ABA) and some national banks; and
- (c) (a) above together with agencies from the Tasmanian State Government, and the City of Hobart.

(a) Discussions with other Commonwealth agencies

The ATO has convened meetings with Centrelink, the HIC, the Department of Immigration and Multicultural Affairs (DIMA), the Australian Electoral Commission (AEC), the Passports Office of the Department of Foreign Affairs and Trade and AUSTRAC.

The discussions have confirmed various problems with PoI, shared aggregated statistical information regarding PoI documents (see table below) and discussed potential solutions. Common problems identified between agencies include:

- the integrity of common identity documents (ie birth certificates, driver's licences, overseas sourced documents etc.) and fraudulent use of these;
- the potential for all documents to be forged or fraudulently manufactured with modern technology
- the lack of real time on-line verification of originating documentation from issuing agencies;
- the risk of obtaining benefits from a range of agencies following the establishment of a fraudulent; and
- the potential problems in introduction of electronic services given the current state of PoI processes.

(b) Discussions with AUSTRAC, the ABA and a number of banks

The ATO and Centrelink are represented on an AUSTRAC chaired steering group examining identity fraud. AUSTRAC chair this group of cash dealers who are also investigating identity fraud and PoI issues. The liaison with AUSTRAC and the banks is necessary because of the general community acceptance of the '100 point' system they use for establishing the identity of new applicants for financial sector purposes.

One output of this steering group was the joint presentation by ABA and AUSTRAC to a State Police Heads of Fraud Conference in August 1999 where PoI and the cost of identity fraud were discussed. This issue has now been escalated to the next Australasian Police Commissioners' Conference.

Further, a range of aggregated statistical data on current usage of identity documents for new 'registrants' has been compiled. A summary of this information follows:

ATO TFN ¹		Centrelink ²		Banks ³		Credit Unions	
Overseas Passport	34%	Credit card	16%	Driver's licence	31%	Driver's licence	49%
Australian or overseas birth certificate	20%	Driver's licence	15%	Passport	23%	Medicare card	24%
Current student ID card	13%	Centrelink previous record	12%	Medicare card	15%	Passport	23%
Bank account statement	11%	Birth certificate	8%	Credit card	11%	Birth certificate	13%
				Birth certificate	8%		

Notes

- 1 ATO TFN data includes 53% from non-Australian citizens that is, working holiday makers, students etc.
- 2 Data was from NSW only – national figures being developed.
- 3 Represents two of the major banks.

The above data highlight the major documents used to establish identity across a range of organisations. Although birth certificates are not as widely used in this sample, as shown in the 'circular path' diagram above, they are used to partially satisfy the PoI requirements for other PoI documents (driver's licences, bank accounts, passports and others). Ongoing liaison with Registrars-General will be carried out in order to determine a systemic of the reasons which are provided when individuals apply for birth certificate. This will add to general intelligence and understanding around the creation of identity issue.

ATO will continue to participate on this AUSTRAC committee to share research and discuss common problems, and develop, where possible, solutions beneficial to the broader community.

- (c) Discussions with Commonwealth agencies, Tasmanian government agencies and City of Hobart.

More recently, the ATO convened a joint Commonwealth/State/Local Government workshop to examine PoI and identity fraud across the different levels of government. Because the Tasmanian Registrar of Births, Deaths and Marriages is to convene the National Conference of Registrars-General, Tasmania was selected as a starting point for discussions with other levels of government.

Tasmanian agencies included the State Registrar-General, Services Tasmania, the Licensing and Gaming Branch of the Tasmanian State Revenue Office and the City of Hobart.

The workshop highlighted similar problems across State and local government with PoI and identity fraud. Services Tasmania advised that it is in the process of developing a common PoI process for its diverse client agencies.

Not surprisingly, there is a great amount of similarity in the issues of concerns, suggestions for solutions and development of options between the levels of government. There is strong support for increased communication between the three levels of government. The development of a common PoI policy across the government sector will ultimately provide benefits to both the government sector and the community.

4.4 Current consultations with other Agencies on data-matching identity data

The ANAO report (p83) suggests that the ATO pursue access to HIC data sets on identity related information. Also the report recommends (7c) accessing and using additional data sets such as those of the Registrars-General. Active efforts are currently underway in both areas.

The ANAO matched two HIC data sets against the ATO's main client data base. Ninety six per cent of Medicare records matched those of the ATO and ninety eight percent of the Commonwealth Childcare Cash Rebate claims were shown to have ATO records. The ANAO believes that there is scope for further benefits to be gained. The ATO is currently undertaking work to determine the value and justification of the additional effort required.

It should be noted that the ATO, until 1995, had access to HIC identity records for the purposes of cross referencing identity details. However, *The Data-matching Program(Assistance and Tax) Act 1990* was amended to remove both the HIC and the AEC from the program as they were not considered to benefit in the same way as the assistance agencies.

The ANAO recommendation 7 (c) has been adopted and National Fact of Death data sets have been purchased recently from the Registrars-General. This data set is currently being used to update the ATO database.

(a) Discussions with Commonwealth agencies

Centrelink, as a result of the ANAO study, has recently obtained Government endorsement (announced in the 1999 Budget) to use the TFN in its data matching. This means that the matching of the Centrelink customer records with the ATO's Employment Declaration Form, Prescribed Payments System and Reportable Payments System can be enhanced by use of the TFN as the primary matching key. Estimates of increased savings amounting to some \$24 million per year are expected by Centrelink.

Present ATO discussions with Commonwealth agencies such as HIC, Centrelink and DIMA have centred on the usefulness of sharing the personal identity details of individuals held in those databases (that is, name, address and date of birth). The purpose of these discussions is to develop a proposal to consider repeating the data matching exercise which the ANAO conducted (initially as a once-only exercise) to improve the quality of data bases held by the Commonwealth. Step 4 of the hierarchy of solutions at 4.2 above raises this possibility.

Discussions between the ATO and the Commonwealth Privacy Commissioner in October 1999 canvassed the idea of such a data cleansing exercise. Providing that the appropriate protocols and undertakings are agreed, the ATO believes that there may be scope to undertake a similar data cleansing exercise. Work is currently progressing on resolving how this may be done.

When firm proposals have been developed with other agencies, the ATO will formally approach the Privacy Commissioner for opinion and advice.

(b) Discussions with non-Commonwealth agencies

The NSW Registrar-General has recently developed an on-line verification proposal for its birth certificates. The Registrar-General has approached the ATO and other agencies with this proposal. In brief, an agency could check a suspicious or contentious birth certificate on-line to verify its validity.

The NSW proposal is presently limited to single transactions but the ATO understands that there is scope for batch processing to be developed. The ATO will continue to examine the usefulness of the proposal with other agencies and the NSW Registrar-General.

5 Addressing Specific ANAO Recommendations

The following sections include the specific ANAO Recommendation and the ATO's response to the ANAO in a box. An up-to-date status report then follows each box.

5.1 ANAO Recommendation 1

5.1.1 Electronic TFN Service to Schools

The ANAO recommends that

- a) the ATO examine the cost effectiveness of offering an electronic service to schools in regard to TFN applications;

ATO response: Agree. The ATO agrees that this option should be considered; in fact, there is a pilot underway in two schools in Victoria to test its viability. However, the ATO is conscious that it must not, nor must it be perceived to be transferring its costs to other organisations.

The ATO supports increasing electronic access for the public recognising that there is still a considerable need to maintain current paper based interactions to allow maximum access for the community.

The ATO presently offers a range of information and transactions through electronic means. Our current electronic service delivery policy accommodates high volume and low complexity interactions making the proposed TFN electronic schools pilot an ideal candidate for this service.

Since preliminary discussions with the schools, the proposed pilot has been somewhat delayed because of other priorities, but the ATO still intends to progress this initiative. Current timing would see the pilot commence early in 2000.

Part of the evaluation of the pilot will consider whether and what additional costs are incurred by the schools participating. Providing there are overall cost benefits, not just for Tax Office administration, this type of delivery mechanism for TFN applications could be extended in the future.

5.1.2 Maximising the Schools Education Program (SEP)

The ANAO recommends that:

- b) the ATO maximise the proportion of eligible 15 and 16 year olds enrolled at schools who choose to receive their TFN through the ATO's Students Education Program; and

ATO response: Agree. Given the debate when the ATO introduced the Schools Education Program (SEP) we are conscious that positive marketing is essential for this program. Accordingly the ATO notes that the objective of the TFN registration component of the SEP is to maximise the proportion of students who choose to apply for a TFN. However, the intention of Parliament in the TFN legislation is quite clear in that all taxpayers, including students, still have a choice whether to apply or not.

- c) and seek the support of the Department of Education, Training and Youth Affairs in preparing a submission for ministerial consideration about obtaining the cooperation of peak school bodies to the conduct of the ATO's Schools Education Program in Year 9 classes on an annual basis.

ATO response: Agree. The ANAO has acknowledged that the SEP was an initiative which the ATO instigated and which has proven to be very successful. The ATO realises that we are fortunate to be in a somewhat privileged position to have access to those schools who choose to take part in the SEP. While we continue to seek further access and co-operation in this regard, we recognise that there are other curriculum pressures and priorities for schools.

The ANAO were very complimentary about the ATO SEP in their report, considering it “ a low risk, low cost approach”.

In the 1998-99 year the SEP registered 115,000 - 25% of the total number of TFNs registered for individuals; this is in line with previous year results. The ANAO also estimated potential savings of \$2m by increasing the proportion of secondary school students applying for TFN through the SEP.

The ATO anticipates that the current SEP will continue to provide a low risk/cost option for obtaining a TFN and over time, possibly increased enrolments. However, relying on a purely cost-based approach which aims to maximise the numbers of students enrolling by way of the SEP, is not the sole consideration. The ATO is very conscious that it relies on community support for such an approach and would not wish to jeopardise its current good standing within the education system. Indications suggest that if the pilot of the electronic schools registration process is successful then we may well see an increased uptake overall.

The ATO, in line with the ANAO recommendation 1 (c), is negotiating with Department of Education, Training and Youth Affairs and State schools authorities to lift the profile of the SEP. However, as noted previously, the ATO is but one of a number of stakeholders and would need to negotiate carefully and with due regard for other educational priorities.

5.2 ANAO Recommendation 2

5.2.1 Proof of Identity - risk management approach

The ANAO recommends that the ATO in conjunction with other agencies research and report appropriately upon the policy considerations, client benefits and cost-effectiveness of:

- a) implementing an effective risk management process, including quantitative analyses of Proof of Identification (PoI) data;

ATO response: Agree. The ATO has been developing a framework for risk assessment which incorporates TFN registration and PoI issues. In addition, research has been underway for some time in an attempt to identify levels of risk in relation to different segments of the client population. The ATO intention is to continue to work closely with Centrelink and other agencies (who carry out similar PoI practices) especially in relation to known fraudulent registration cases.

The foregoing discussion at Part 4 above details the progress which is being made regarding this recommendation. Initial quantitative analysis of PoI data has occurred as a result of the current inter-agency discussion. As indicated, this will continue to be progressed.

In addition, the latest risk assessment, (see 5.7 below) has indicated that continuing risks associated with the current PoI regime have been identified and strategies are being developed as part of the TFNIP to address these.

The initial risk assessment focus was on fraudulent applications and the findings to date are in line with the PoI risks identified by the ANAO. However, given the minimal numbers of actual fraud cases identified over the years, the ATO believes that only the most sophisticated and deliberate attempts are still a risk. The actual cases which have been identified and prosecuted have shown that there has generally been a systemic and calculated effort expended in order to falsify and construct different identities. The lessons from these are to be developed into case studies for training purposes.

5.2.2 Delivering TFN services through additional avenues to the ATO

The ANAO recommends that the ATO in conjunction with other agencies research and report appropriately upon the policy considerations, client benefits and cost-effectiveness of:

- a) delivering TFN client services through appropriate alternative means additional to the ATO;

ATO response: Agree. The ATO has been for some time undertaking work with Centrelink on a range of initiatives, including electronic transfer of Centrelink client applications and POI certification by Centrelink for non-Centrelink clients. In relation to new arrivals into the country DIMA and the ATO are working together on a new system of automatic registration

The ATO already receives TFN applications via Centrelink, Department of Education and Youth Affairs (DETYA), Department of Veterans' Affairs (DVA) and secondary schools with PoI certified by those organisations. At this stage, these applications are paper-based.

Source	Number (98-99)
Secondary Schools	115482
Centrelink – Other Benefits	37140
Centrelink – unemployment and sickness benefits	15958
DETYA	6706
DVA	115
Received from Non ATO sources	175,401
Percentage of total TFN application via non-ATO sources	38.76%

Options currently being considered to extend these services include:

- (a) the Schools Education Program (see section 5.1).
- (b) extension to tertiary institutions

The ATO is currently investigating a proposal to involve tertiary institutions, especially for the large and growing number of overseas students, in a similar PoI verification process, and eventual electronic processing of TFN applications. On the basis that the student must provide identification information to the institution upon enrolment, there would be a reduction in double handling of such cases. Consultation with the International Student Advisors Network has recently commenced.

(c) Centrelink registrations

The ANAO made reference to the current process whereby Centrelink and DVA accept TFN applications and certify PoI from their clients. TFN applications are then sent to the ATO for processing and TFN allocation.

The ATO is building on this initiative in liaison with the other agencies, on the assumption that clients should continue to have this service available into the future in a more cost-effective and client friendly manner. This is particularly the case for those living in remote and rural communities.

To this end, a joint electronic service delivery proposal is presently being considered which would allow an automated forwarding of Centrelink applications to the ATO for processing (similar to the DIMA proposal below). Such improved processing would also address the occasional delays which occur in passing applications.

We would also consider whether it would be practical and appropriate for Centrelink to then accept POI and TFN applications from others – who may not be their clients and thus not known to them. Further work is required in this regard.

(d) DIMA registrations

The ANAO report referred to a proposed exchange of information that has been under discussion between the ATO and DIMA. The proposal has two components.

In the first phase DIMA would provide visa information to the ATO identifying visa holders who had been granted work rights in Australia. On the basis of the identification occurring at the visa grant stage, the ATO would be able to automate the TFN registration of these persons by creating and attaching a TFN to each visa number before they approach the ATO. This would greatly simplify TFN issues for these persons and the ATO. However, heavy commitment of IT resources in both the ATO and DIMA will probably defer implementation of this phase until at least late 2000.

The second phase would eliminate the unlawful use in Australia of TFNs issued to foreigners who have been recorded on DIMA's movements database as having departed Australia. Implementing this phase will take longer because the current DIMA legislation does not allow ATO access to movement records. Solutions to this are currently being considered.

In order to address the likely large influx of overseas visitors in the next year, as a result of the Olympics, the ATO is also currently examining other short-term options to streamline TFN processing. One possible option is for the ATO to have electronic access to visa number information to automatically confirm work rights. At present such confirmation occurs manually; the increased numbers of arrivals in 1999-2000 will require more efficient processes.

Another proposal to access DIMA visa grant information is being developed to enable newly arrived TFN applicants to simply write their visa number on the TFN application, rather than queue at ATO Public Assistance counters. This visa number would be verified with DIMA's visa grant information.

5.2.3 Generating TFNs - algorithm

The ANAO recommends that the ATO in conjunction with other agencies research and report appropriately upon the policy considerations, client benefits and cost-effectiveness of:

- c) providing a more secure, client focussed and cost effective means of generating/composing TFN's. The ATO should have regard to the widespread use of the TFN (by employers, investment bodies and other government agencies) and to Defence Signals Directorate's advice concerning secure algorithms;

ATO response: Agree. However, the ATO considers that the avenue for abuse through TFN generation using the algorithm is limited and that current TFN systems are an appropriate, cost effective response to the risk identified. This is an area where a balance needs to be struck between risk and cost from both a client and an ATO perspective. As we continue to improve our understanding of client needs through working closely with them we recognise that new and emerging risks may arise needing new and different solutions.

The ATO met with the Cryptomathematics Research Group of Defence Signals Directorate (DSD) in September 1999 to follow up the comments made in the ANAO report (paras 2.63 to 2.66). The discussion centred on the security offered by the TFN algorithm and the potential for more secure alternatives.

DSD technical advice suggests that a 100-digit number, which would prove very cumbersome for all stakeholders, would provide a very secure system. They also suggest that an 18-digit number, or a number including alpha and numeric characters - though not as secure - would increase the current level of security.

On balance, in terms of current level of risk weighed against convenience and costs of implementation and maintenance by the ATO and other stakeholders, the ATO does not believe that such options are currently justifiable given the level of risk involved. It is agreed, however, that there is a need to monitor aspects of current usage of the algorithm to ensure that risk does not increase.

If it becomes apparent that a more secure system is in fact needed in the future the ATO will seek the assistance of the DSD to develop a suitable alternative.

5.2.4 PoI audits

The ANAO recommends that the ATO in conjunction with other agencies research and report appropriately upon the policy considerations, client benefits and cost-effectiveness of:

- a) conducting PoI audits within and across government agencies; and

ATO response: Agree. This issue will be evaluated as part of the ATO risk assessment process.

The ANAO (para 2.38) raised a number of concerns about PoI fraud including the above recommendation. The initiatives discussed above (Section 4) cover many of the ANAO

suggestions. As indicated there, our preferred approach is to strengthen the whole PoI foundation across Commonwealth agencies in conjunction with the reliable issuing authorities.

The ANAO also commented that the ATO should apply 'the lessons learnt from PoI frauds' (para 2.40). We are currently analysing and mapping known fraud cases, to see what can be learnt from this. As the ANAO indicates, if a seemingly 'authentic' range of PoI documents is able to be readily manufactured, there is little chance of an ATO registration process uncovering this without some third party information or verification. We will, however, continue to monitor this aspect.

The ANAO also mentions entering into service provisions arrangements with DIMA and the Australian Federal Police (AFP) to augment the ATO's capacity to detect and prevent high risk fraud. As indicated previously, we are currently continuing to work with a range of 'expert' advisers on a range of detection and prevention strategies. The cross Agency forums mentioned in Section 4 include compliance specialists from Centrelink, AFP and DIMA.

5.2.5 Provision of TFN advice to clients

The ANAO recommends that the ATO in conjunction with other agencies research and report appropriately upon the policy considerations, client benefits and cost-effectiveness of:

- e) providing the client service number in a format which is easy for clients to access, use and maintain, while protecting their individual privacy.

ATO response: Agree with qualification. The ATO believes that such consideration should include taking into account the preferences of a range of different clients and notes that certain formats have not, at least in the past, seemed palatable to the general public (as recognised during the Australia Card debate). In reviewing options, there will also be a question of balance between community compliance costs and the ATO's cost of administration.

The ANAO has, in its report, correctly reflected the expanded role of the TFN in implementing government social and other policy. The ATO has moved beyond simply dealing with tax administration issues and now has joint responsibility for an ever increasing variety of social and other government policy implementation (eg HECS, Private Health Insurance Incentive Scheme (PHIIS), Family Tax Initiative (FTI)).

This expanded role in many cases requires use of taxation data - either as a check to ensure that an entitlement exists or for the ATO to act as the delivery mechanism for a rebate, deduction or other benefit item. The Family Tax Initiative can, for example, be claimed in one of three different ways.

The TFN is also used more widely for other non taxation purposes (eg as a prerequisite to gaining Commonwealth benefits.). The expanded role of the TFN suggests that there may be an extra need for a wider range of delivery options to address user convenience and accessibility

There are several possible aspects in addressing a format that provides greater client convenience:

- 1) The ANAO posits that similar advantages to those which will accrue to business, as a result of the ABN being used as a single identifier with government, would also accrue if a single client service number (CSN) were used for individuals.

The ATO is in agreement with this principle, but clearly this is subject to a range of privacy and cost-benefit considerations. The ATO has a good track record in protecting privacy and is also responsible for developing cost effective ABN approaches. We will draw on this experience to progress CSN evaluations with other agencies; and

- 2) The ANAO report also suggested that the current paper-based advice format which is mailed to clients informing them of their new (or current) TFN should be reviewed. Such a review is presently occurring as part of the TFNIP.

At present all individual resident clients who apply are sent the same advice; non-residents have a different advice. The review has shown that in order for clients to retain, remember and maintain their TFN readily some more effective means of communication ought to be used. We recognise that with different style and frequency of TFN usage, 'one size does not fit all' and we are working to develop different formats and advices for different groups of applicants. (For example, students' advices may be simpler and brighter with design features and messages which will make more of an impact.)

Preliminary research has shown that approximately one in ten individual TFN applications already have an existing TFN. These are identified in the initial registration process and actioned accordingly with the taxpayer. This additional workflow is part of the reason why it is important to provide the original advice, and any subsequent advices in a more retainable format. Such messages as 'one TFN for life' and 'don't lose this – you'll need it' are being considered in this process as a form of early education.

Other possibilities include the use of 'cards' as advices, and provision of a 'tax folder' which may contain their TFN plus other basic tax advice information – with a pocket for collection of receipts and other tax information.

In developing alternate formats the TFNIP is also surveying recent TFN applicants to gauge their preferences. Work is continuing.

5.3 ANAO Recommendation 3

5.3.1 Information Technology issues to the Investment and Royalties Branch

The ANAO recommends that the ATO ascertain the cost-effectiveness of assigning appropriate information technology resources to Interest Royalties and Withholding Branch.

ATO response: Agree. The benefits of redevelopment of the Interest Royalties and Withholding system has been recognised and prioritised. However, delivery is subject to balancing all tax reform priorities.

The IRW system deficiencies are acknowledged. The IRW system is a legacy system with a limited planned life. As redevelopment for tax reform has the highest priority, and the risks are relatively low, the resources available for IRW redevelopment are limited.

The functions of the IRW system are being being moved across to the core ATO systems. This will be based on a generic withholding system designed to support both current and proposed

legislation for a number of taxes, and will have a greater capacity to for a wider range of compliance approaches including additional accounting controls.

We note that there is a high degree of integration of systems and data across core ATO systems.

5.4 ANAO Recommendation 4

5.4.1 Extensions of TFN Withholding

The ANAO recommends that the ATO examine the risks to the integrity of tax administration and to the collection of revenue arising from transactions [such as those listed in paragraph 3.24(sic)] being outside the TFN withholding arrangements and consider options for addressing these risks, such as the inclusion within the TFN withholding arrangements.

ATO response: Agree. The ATO has previously proposed and received legislative support for extension of TFN reporting arrangements in the clothing, fishing, smash repair and fruit and vegetable industries. Whether further extension is required in the areas detailed in the report needs further consideration in the context of balanced risk assessment and alternative strategies

The ANAO report makes specific reference to compliance research for non-resident property owners. The ATO is carrying out further research in relation to this group but notes that there is still significant uncertainty as to the extent of rental income and capital gains non-disclosure.

In particular, the figures used in the report for non-resident property owners rental and capital gains were taken from ATO research which was based on a very small and localised sample and then extrapolated nationally. There is some question as to the appropriateness of the methodology used for extrapolation purposes, and therefore on the overall level of risk.

Our findings in the general real estate area have highlighted a number of potential risks and we are assessing risk based strategies to address these as a matter of course. This research to date has indicated that the disclosure of rental income and net capital gains by resident landlords may not be as significant a risk as rental deduction claims.

When a risk area is identified the ATO considers a range of options to address that risk including education, awareness raising via publicity, increased reporting or enforcement action. Approval to seek legislative change is an option but is not our preference without first seeking other solutions.

The transaction types listed in the ANAO report (paragraph 3.30) have been considered and remain under consideration by the ATO. But cost effective solutions are not always close at hand. Some rely on legislative change, and in addition, the external cost of compliance (for example, organisations reporting large amounts of data to the ATO) is a major consideration. As ATO electronic delivery initiatives develop, the cost of compliance may fall and make some of these options more acceptable.

Taking these factors into account, the transaction areas which appear to most readily lend themselves to possible extension of the Tax File Number provisions are:

- (a) AUSTRAC financial transaction reports;
- (b) resident property income(rental and capital gain); and
- (c) non-resident property income(rental and capital gain).

(a) AUSTRAC reports

TFN matching of AUSTRAC financial transaction reports to ATO data holdings would significantly enhance the efficiency, accuracy and integrity of current ATO processes. It would enhance the value of AUSTRAC data holdings to the ATO and allow the ATO to be more effective in combating tax evasion and money laundering in the cash economy.

This proposal to include TFN details (if held by cash dealers) on financial transaction reports provided by cash dealers to AUSTRAC requires legislative change, the support of AUSTRAC, the support of the Privacy Commissioner and, preferably, the support of the financial institutions.

AUSTRAC provides access to its financial transaction reports information to the ATO, various Commonwealth law enforcement agencies and various State law and revenue agencies. If this proposal is successful, AUSTRAC must ensure that any TFN received from a cash dealer is quarantined to ensure that the TFN can only be accessed by the ATO.

Alternative considerations to including TFNs on financial transaction reports are:

- to have a unique identifier or coding of the TFN that is unintelligible to any users other than ATO officers.
- to include the proposed Australian Business Number (ABN) on financial transaction reports. The inclusion of an ABN on financial transaction reports would have limited success as an ABN is only available to enterprises. For financial transaction purposes, there is no compulsion or benefit available to an enterprise in providing an ABN to a cash dealer. An ABN (if held by a cash dealer) could be provided on financial transaction reports if a TFN was not available.

Attachment of a TFN (if held by a cash dealer) to financial transaction reports provided to AUSTRAC is not seen by the ATO to be an unreasonable burden to be placed on the cash dealers. Consideration should, however, be accompanied by extensive consultations with banking and industry groups and their representatives to test this proposition, and with any other groups within the Australian community, upon whom the proposal may impact.

See Appendix 4 for further background information on this proposal.

(b) Resident property income;

Currently TFN provisions do not apply to the reporting and recording of property transactions such as rental transactions and real estate sales and purchases. The current arrangements make it difficult for the ATO to readily match property income received by land against the income reported in annual tax returns; and difficult to reconcile taxpayer property deduction claims.

i) Resident rental income

The ATO carries out systematic risk assessment (referred to as the Compliance Management Strategy) for each of the items (labels) on income tax returns for the individuals taxpayers segment. In recent years, resulting from this work, we have initiated the Rental Compliance project.

In potential compliance risk terms – based on the field and benchmark audits that the ATO has undertaken - property transactions (income and deductions) clearly represent some risk to the revenue. This continues to be tested.

As evidence, benchmark audits undertaken in 1998/99, based on 1997 rental returns, estimated the net rental (income less deductions) compliance gap to be around \$266 million. This was against a background of a gross rental income for individuals totalling over \$10 billion.

In response to this, in 1998 a rental property schedule was introduced as part of the individual taxpayer tax return. This provided the ATO with details on the number of properties owned by taxpayers, the gross income derived from each property and a break up of the various expense claims for the property. This enabled better targeting of deduction claims considered to constitute a revenue risk.

The revenue impact of the rental property schedule has been monitored. Additional net revenue attributable to the rental property schedule program is estimated at \$80 million, with contribution from increased income and reduced deductions.

This year we have extended use of the audit and property schedule strategy to partnerships and trusts , noting the gross rental income in this area (including companies) is around \$9 billion.

We are also looking at possible use of third party data (eg Rental Bonds Service Board) to assist our compliance effort, although quality and accessibility of data is an issue.

By way of illustration, as part of the Rental Compliance Project, data held by the NSW Rental Bond Services Board was requested and assessed to identify landlords not declaring rental income. The identity data captured and held by the Board was quite limited. It transpired that where a real estate agent number was present on a rental bond form then landlord details were not required, or if they were supplied on the form they were not captured. Nor were landlords required to provide their name in full or quote a date of birth. The Rental Bond Board indicated that at least 70% of bonds lodged with them came via real estate agents.

The above illustrates the ATO approach of properly assessing the compliance risk, and a range of alternatives to gain relatively low cost leverage in our compliance strategies. Extension of TFN withholding or reporting needs to be assessed in this context.

(ii) Resident real estate capital gain income

At present TFN reporting provisions do not apply to real estate sales or purchases.

In 1998, 42,782 individual taxpayers disclosed real estate capital gains income worth \$808 million. Based on results to date, it is estimated that in 1999 this will amount to 46,649 taxpayers disclosing capital gains of \$932 million. Taxation Statistics indicate that Trust and Company returns will increase the capital gain figure by a further \$2.7 billion. It is important to note that these figures reflect only the result from gains disclosed; there is no reporting mechanism in place to support the compliance measurement of non-disclosure.

Research that has been conducted in this area has been restricted to the sale of property by resident taxpayers. To date, no significant compliance risk has been identified on resident capital

gain income. We are investigating the use of State government land title data to support compliance activity in this area.

c) Non resident property income

As noted in our original response to the ANAO report, there is significant uncertainty as to the extent of rental and capital gains non disclosure for non residents. We have initiated a lodgment compliance research project to gain better insights into this issue.

The possible introduction of withholding arrangements for non-resident property owners is referred to, in a broader context, in the recent Ralph Report on business taxation, and is currently under consideration by the Government.

5.5 ANAO Recommendation 5

5.5.1 Data Specifications for Annual Investment and Interest Reports.

The ANAO recommends that the ATO:

- a) seek concurrence of relevant financial institutions regarding the data specification for Annual Investment and Interest Reports information that provides the ATO with accurate and valid data that minimises compliance costs;

ATO response: Agree. Recognising that there is a requirement for financial institutions to provide regular reports the ATO consults with a range of umbrella organisations of investment bodies in order to seek agreement to and improvement of the data specifications needed. These consultative forums allow early industry input into the ATO specifications recognising the time lags inherent in updating systems.

Consultation with a range of umbrella organisations occurs regularly. When the ATO requires new or different financial reporting information or amendment to formats and delivery mechanisms approaches are made to the relevant bodies. Issues are discussed and potential solutions proposed in partnership with the other stakeholders.

5.5.2 Disparity between TFN Withholding tax collected and remittances to taxpayers

The ANAO recommends that the ATO:

- b) investigate the disparity between the TFN withholding tax collected and the amounts remitted to taxpayers; and

ATO response: Agree. The ATO agrees that this matter should be investigated and prioritised in the ATO's risk assessment process

As we do not have the clients of the financial institutions TFNs or identification details, we cannot be sure if we can unambiguously identify the account holders. The strategy we have adopted is to urge the financial institutions to be active in notifying their clients how they can recover their withheld tax and to educate their clients.

5.5.3 Reconciliation of Payments

The ANAO recommends that the ATO:

- c) reconcile remitter/investment body payments as appropriate and ascertain the level of tax payable having regard to the quality and timeliness of available data.

ATO response: Agree. The ATO agrees that this matter should be investigated and prioritised in the ATO's risk assessment process

The ANAO commented on the quality of the AIIR data received (see 5.5.1 above). The quality of received data directly affects the ATO's ability to fully reconcile remitter/investment body payments. However, IRW regard the matter as having a low risk to ATO and the community.

5.6 ANAO Recommendation 6

5.6.1 Opportunities to simplify refund process for exempt investors

The ANAO recommends that the ATO:

- a) examine opportunities for simplifying the refund process for exempt investors who have incurred the TFN withholding tax; and

ATO response: Agree. The ATO agrees that this matter should be considered. Any proposed action will need to be evaluated in the light of tax reform and other priorities.

The issuing of refunds is automated, however is dependant on supporting documentary evidence which is paper based. The process of refunding investors has been reviewed and streamlining has occurred to some extent, at least to improve turnaround times. However, it is acknowledged that the system of direct refunds and substantiation is of concern to some of our clients.

Consequently, a legislative proposal is included in a bill currently before parliament to enable exempt investors to claim refunds directly from financial institutions. This will considerably simplify the refund process for exempt investors. In addition, via the joint consultative forum, the ATO has liaised with financial institutions and recommended steps to minimise refund claims by encouraging investors to notify their exempt status to the financial institution when opening accounts.

It is important to note that there has been a significant decline in the level of direct refunds to exempt investors over the past four years as a result of the increased education activities directed at remitters.

5.6.2 Opportunities to simplify refund process for exempt investors

The ANAO recommends that the ATO:

- b) examine the cost-effectiveness of establishing suitable arrangements to ensure the automatic identification of exempt investors.

ATO response: Agree. The ATO agrees that this matter should be considered. Any proposed action will need to be evaluated in the light of tax reform and other priorities.

The ATO has conducted initial enquiries. It has determined that an extremely high cost would be attached to any automatic identification system, both from a government agency perspective (ATO, Centrelink, Veterans Affairs) and from a financial institutions perspective. Financial institutions consulted through the joint forum, expressed concern over the high cost of systems changes, account changes and staff education associated with implementing a system of automatic identification.

5.7 ANAO Recommendation 7

5.7.1 Client data quality

The ANAO recommends that the ATO:

- a) improve client data quality throughout its business lines;

ATO response: Agree. However the ATO notes that major elements of the Corporate Data Management Plan have already been put in place across Business and Service Lines by means of the Client Identity Integration Project including implementation of the ATO Data Standard. This standard imposes corporate client information business rules, data formats and edit rules across all ATO business systems. The ATO is also contributing to the development of an Australian Standard for “Interchange of Client Information” and the ATO Data Standard is being used as the base document for this exercise.

Several initiatives have commenced, or are planned, to address client data integrity. These include, but are not restricted to:

- 1) reviewing client data integrity risk approaches;
- 2) commissioning a project to determine the cost of bad data,;
- 3) purchasing Fact of Death data from Births, Deaths and Marriages;
- 4) updating records that have incomplete, or invalid, dates of birth;
- 5) investigating the use of data scrubbing tools; and,
- 6) identifying system enhancements.

(1) Client Data Integrity Risk Management

Since October 1998 new TFN risk management practices aimed at improving the level of client data integrity have been developed and, from April 1998, implemented nationally as part of a Client Data Integrity (CDI) project.

This project commenced with the following objectives in relation to TFN:

- reduction in TFN duplications;
- reduction in applications for a second TFN (non-fraudulent applications);
- reduction in TFN Enquiries; and
- gathering of strategic intelligence.

To meet these objectives the Project team:

- established a model for identifying clients who posed a risk of already having a TFN and procedures to deal with applications from these clients;
- derived new performance measures for TFN to encourage a quality culture in the area of TFN processing; and
- created a new TFN advice letter to educate clients about their number and to check the information transcribed onto the ATO mainframe (AIS) system at registration.

The wide use of TFNs for employment, income assistance, education and investment means that most people, once they have reached a certain age, should have their own tax file number. People past this age who lodge an application for a new tax file number would represent high risk in terms of creating a duplicate.

The project team decided that applicants over 20 years who were residents, and new arrivals who had been in Australia over one year, would be considered high risk and would be contacted by telephone prior to registration. The telephone call would be used to find out if the client had an existing TFN that we had been unable to find using our search techniques and if there was no TFN, the reasons why they had not needed one up until now. The information gathered on these clients would enable the high risk criteria to be refined by identifying those clients who have demonstrated a low risk of creating a duplicate.

The information captured has told us the extent to which certain clients pose a risk of having an existing TFN, the common reasons why people have not needed a TFN until now and characteristics of the people who apply for a second TFN. In addition, we have a reliable source of data to perform further analyses on our initial findings which have implications outside of the TFN environment, such as taxpayer compliance.

Summary results to date include:

- Over 10% of high risk clients were found to already have a TFN;
- There are several recurring reasons why people in the high risk segment did not have a TFN;
- Where a TFN already existed, it was predominantly more than five years old; and
- Overseas arrivals who already had a TFN obtained their first TFN either within three months of arrival or more than two years from arrival, with few exceptions.

These risk management practices are currently being further reviewed to ensure that risk categories have been properly identified, and to refine the process.

(2) Cost of Bad Data

INB has undertaken a two-phased project to determine the cost of bad data.

Phase 1 was completed in May this year and developed a methodology that will enable the cost of a bad data item to be measured. Phase 2 has commenced and will attempt to apply the methodology to specific data items starting with duplicates. The aim of this phase is to prove the methodology, determine the cost of bad data for that data item and then recommend an improvement program.

(3) Purchasing Fact of Death data

The ATO recognised that many client records were not being updated where the client was deceased. Following discussions with State Registrars for Births, Deaths & Marriages it was agreed that they would develop a national database of Fact of Death data. This would be done through the Australian Institute of Health and Welfare and agencies, such as the ATO, would be able to purchase copies of that data. The data relates to all years since 1992.

The agreement was completed in March this year with the first data sets being provided in April. Quarterly updates will continue to be provided. This data will be progressively run through the Client Identification and Compliance (CIDC) system to identify and attach TFN's to the records. It will then be used to update client records on the ATO system.

(4) Updating records that have incomplete, or invalid, dates of birth

Analysis of ATO data bases revealed that there are a number of records where the date of birth was either incomplete,(ie. day, month or year of birth missing) or invalid (ie. day of birth not in the range 1 to 31, month of birth not in the range 1 to 12, or year of birth invalid). Having an invalid or incomplete date of birth inhibits matching process for new registrations, data matching with Centrelink and DVA, as well as complicating data matching for omitted/understated income.

AEC, Centrelink, Tax Return and Employment Declarations data will be used to update our records. It is expected that over 620 000 client records will be updated/corrected by this exercise.

(5) Investigating the use of data scrubbing tools

Data scrubbing tools provide a means for automatically cleansing data fields that contain non-acceptable characters, according to pre-determined business rules. In addition, there is provision for exception reports to be produced where the business rules can not be applied. Manual correction of such errors is required and can require substantial staff resources.

A data scrubbing tool has been used to prepare for ABN registrations. We are investigating the broader use of such an approach to the TFN database.

(6) System enhancements

Determining the need for system enhancements to support TFN registrations is an integral part of business as usual. Due to priority given to tax reform, some system enhancements have been deferred. However, these enhancements are progressively reviewed and re-prioritised.

5.7.2 Resolution of duplicate TFN's, archival of redundant records and access to additional sets

The ANAO recommends that the ATO:

- b) progress strategies for the resolution of duplicate, and the archival of inactive records;

ATO response: Agree with qualification. The ATO is investigating these issues, but also notes that the effort required in cleansing duplicate and archival records raises priority issues, with the need to balance this effort with the evaluation of risks posed and the systems efforts required for other work including tax reform.

- c) assess the cost-effectiveness of accessing and using additional data sets, such as those from the State Registrars-General;

ATO response Agree. The ATO is currently negotiating the cost of accessing additional data sets.

(1) Duplicate TFN's

Prior to the commencement of the ANAO audit, duplicate TFNs had been identified by the ATO as an area of concern. Some of the issues identified included:

- quantifying the number of duplications;
- attempting to determine the cost of duplications; and
- attempting to determine the potential for misuse or fraud of duplicate TFN's.

Criteria to identify potential duplications were developed and run through the ATO's Data Warehouse, an information and research data base with internally and externally sourced information. Cases were sampled to determine the validity of the matching criteria which were then further refined.

As a result, initially approximately 185,000 potential duplications were identified. From these, less than 24,000 were considered to be potential risks requiring resolution. This aspect of the project is in the final stages and a report on the findings is currently being drafted. While final figures have not been received, it is likely that, of the initial figure of 185,000 potential duplications, fewer than 2,500 will be confirmed as actual duplications. In summary, the project found that there were far fewer duplications in the cases reviewed than expected and there were very limited numbers of suspected fraud cases.

This indicates that our overall processes are generally able to identify and resolve those cases as they are initially registered and accordingly, do not seem to be a significant risk. In the vast majority of cases where a duplicate was identified, there was no activity recorded against one of the records, indicating that perhaps some individuals had inadvertently applied for a second TFN without realising that they may have already had one allocated.

Findings from the project will also be used in the review of client data integrity approaches discussed at 5.7.1 (1) and will also impact on system enhancements, 5.7.1 (6).

The project will continue with a focus on three different areas. The first of these will examine recently created duplications and will provide feedback to registration units in order that preventative measures can be put in place.

The second approach will review the criteria used to date to determine whether it is possible to refine our approach to improve the confidence level of cases reported as a result of running the program.

The final approach will look at other ways of identifying duplicate TFN's. As an example, one of the constants in the matching criteria used to date has been an exact match on surname. Amongst other changes, future criteria will look at variations, such as spelling errors, in the surname.

(2) Archival of inactive records and access to additional data sets

It is clear that the ATO data bases include a significant number of inactive records. Where we are clear about the status, we "flag" the record as inactive.

Factors that contribute include those clients who:

- have left the country and whose record has not been flagged (up to 100,000 per year over a 10 year period);
- have died and whose record has not been flagged (data has been purchased from Births, Deaths & Marriages in order to update these records);
- have duplicate TFN's, and where only one TFN is active.
- no longer have a requirement to lodge but who have not notified the ATO; and
- have registered to facilitate lodgment of a tax return but who have yet to lodge (876,106 were registered before 30/6/98 but have not lodged returns).

To the extent possible, and especially if flagged as inactive, such records are excluded by the use of specific selection criteria when the ATO undertakes particular educational or compliance programs.

In adopting the ATO Compliance Model across the ATO recognition has been given to the need to have accurate and up to date data on both client registrations and about obligations under the law – to lodge for example. With the additional focus on client profiling in order to better target communication, education and other strategies, identification of inactive records becomes more important.

Therefore, records have continued to be flagged as "inactive" on the system. For example, almost 2.5m records are known to be no longer needed for current ATO activities, i.e. the record has been flagged as deceased (541,984) or has an Further Return Not Necessary (FRNN) indicator (1,936,894) present.

In addition to those flagged as Deceased or FRNN, there are records held on ATO systems that are very likely of little use to the ATO, or that pose minimal risk to revenue. Typically these cases are inactive, i.e. there have been no lodgments, or other activity such as payments, etc, for some years (or never) and, due to age or other circumstances, it is unlikely that a requirement to lodge returns exists. Note also that this category will include deceased or FRNN cases where, for whatever reason, the record has not been appropriately updated.

There are three possible aspects to more accurately identifying an active database. These are:

- a) Archival - where records known to be no longer required are moved to a secondary storage medium.

Provided inactive records are flagged, the ATO does not consider that there is sufficient justification in terms of system storage or system performance in developing and implementing an archiving system. . When such archival occurs the whole individual record with all of its attached history is stored. Archiving such records is not of itself a costly exercise but the development of current systems to retrieve an archived record is quite considerable.

- b) Deletion - where records known to be no longer required are deleted from NTS.

As an alternative to archival, it is possible that selected records may be deleted from some ATO systems as part of annual maintenance. However, such a strategy, while it retains the individual record, does not enable retention of history detail. Naturally, the record would need to be flagged in some way, eg. 'Record deleted from NTS - Reason X, Y, Z'. Therefore, if for some reason, a record has been incorrectly deleted, and further activity is required, the ATO database can be reconstructed to an extent.

All records currently flagged as Deceased or FRNN could be deleted, subject to certain other conditions also being met (for example, the record would be free of debt or other indicators, such as Child Support, HECS, etc), Draft criteria for such deletion activity for records have been developed. Further work is progressing on this aspect.

Also, the recently acquired Fact of Death data will be uploaded before any systemic deletion activity occurs.

- c) Access to additional data sets

As discussed above access to additional data sets would allow the ATO to flag and/or delete inactive records which are not currently identified as such.

Fact of Death data is one example of this and, as stated in 5.7.1, the ATO has recently reached an agreement with Births, Deaths and Marriages to purchase this data.

As noted above in part 5.2.2, current DIMA legislation prevents access by the ATO to arrival and departure information from Immigration movements records. Solutions to this are currently being considered as the ATO believes that a significant number of its inactive TFN records relate to this category of client.

AEC data has also been previously utilised (see 5.7.1) to update previously incomplete data of birth details on the ATO database.

As noted previously (in Chapter 4 above) an amendment to existing HIC legislation would be necessary to allow the release of HIC data to the ATO for Client Data Register cleansing

Access to ASIC (Australian Securities & Investments Commission) information on liquidated companies and dissolved partnerships is currently being negotiated.

5.7.3 Quality of external data sets provided.

The ANAO recommends that the ATO:

- d) work with strategic partners to ensure that data sets conform to ATO standards before they are provided to the ATO

ATO response: Agree. The ATO treats this as part of its business as usual and has regular meetings of the Data Matching Programs Working Group. See also the response to recommendation 5(a) above.

Where there is a legislative requirement for the supply of information, the specifications impose the ATO data standards on all reporters. However, where there is no formal obligation in place, the specifications for data supply to the ATO are developed in conjunction with the organisations providing the data. Preliminary discussions regarding format, content, editing, etc., enables the ATO to maximise the quality of data received. In addition, data takeon editing and follow-up liaison with data suppliers occurs on an ongoing basis.

The ATO pursues these data sets and negotiates continuously with third parties as required and will continue to do so.