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Tax Complexity and its Impact on Tax Compliance and Tax Administration in Australia

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The Australian federal tax system is widely regarded as one of the most complex tax systems in the world and has enjoyed this reputation since at least the 1970s. That is, in spite of the considerable attention given to tax complexity in Australia by policymakers, administrators, businesses, lobby groups, voters, and other interested parties over a number of decades, the tax system remains at least as complex as ever.

The ramifications of the complexities of the Australian tax system are profound and impact on every aspect of our way of life, including the way we do business, work, invest, retire, plan for the future, grow the economy, educate our children, and care for others. Tax policy is a subject close to the hearts of voters, and elections have been won and lost on the basis of proposed reforms. While taxes affect the whole of society in some form or other, it is the taxpayers, the tax practitioners (or tax agents), and the tax administrators who are most directly affected by the complexities of taxation. In a self-assessment tax system, such as operates in Australia at the federal level, these three parties by necessity have a close and dynamic working relationship. They may not always be working together, but they are working side by side, observing what they can of each other, and adjusting and readjusting their behaviors and strategies according to their assessment of the risks they face. It is reasonable to expect that tax complexity will have some impact on these risk assessments. The tax administration will be seeking to maximize voluntary compliance, the tax practitioner will be advising the taxpayer on paying the least amount of tax as required under the law, and the taxpayer will ultimately be making the compliance-related decisions. It follows that understanding how taxpayers make these decisions and the roles played by tax practitioners is of critical importance to the tax administration. The purpose of this paper is to provide an overview of recent compliance research in Australia on the impact of tax complexity on taxpayers and tax practitioners, and, in turn, to consider the consequences for the Australian Taxation Office (ATO) and the way in which it is responding. While the focus of the paper is on the Australian federal tax system, it is expected that the content and findings will have relevance to other jurisdictions.

The paper is presented in four parts. It begins with an overview of the Australian tax system and its reforms and provides the context for the balance of the paper. The second part reviews recent compliance research undertaken in Australia, particularly on the impact of complexity, and includes an analysis of the findings of the various studies and their varied methodological designs. The third part discusses the impact of complexity on tax administration and includes an overview of the strategies and practices that have been adopted by the ATO and how taxpayers and tax practitioners have responded to these. The concluding part of the paper draws together the preceding analysis, considers strategies that could be considered in seeking to address complexity, and identifies areas where further research is needed.

Overview of the Australian Tax System

Reform of Australia's federal tax system has been an important item on the political agenda since the Commonwealth of Australia was first formed in 1901. At the time of federation and under the Australian Constitution, the states (or former colonies) had a concurrent general taxation power with the Federal Parliament (i.e. Commonwealth, (Cth)), with the latter having the exclusive power to levy customs and excise duties. The states continued to raise income taxes (which they had been doing since 1880), with the Federal Parliament first introducing an income tax in 1915 under the auspices of funding the war effort in WW1. The Income Tax Assessment Act (Cth) 1915, modeled on state legislation that existed at the time, was 65 pages in length and consisted of 22 sections. Another Act followed in 1922, and this was superseded by the Income Tax Assessment Act (Cth) 1936 which was some 250 pages in length. From 1915 until 1942, Australians paid income tax separately to both the state and federal governments. In 1942, the Federal Parliament passed a Uniform Tax Scheme, whereby the federal government raised a higher level of income tax and passed on grants to the states (and territories) on the condition that they did not levy income tax themselves (Coleman and McKerchar, 2004). Basically, the same situation exists today. Although the states have the power under the Australian Constitution to levy income tax, they have not exercised this power since 1942. Instead, the states and territories rely on other forms of local taxation such as payroll tax, land tax, and stamp duties to supplement the funds (including the revenue raised under the Goods and Services Tax (GST) first introduced in 2000) received from the federal government.

Nationally, the ATO operates as a unified, semiautonomous body, administering a range of Commonwealth legislation and collecting revenue on

behalf of the federal government (OECD, 2006). Almost everyone in receipt of income has to lodge an annual tax return (around 11 million individuals currently lodge income tax returns). The states and territories each have their own revenue authorities, and these are independent of each other and of the ATO. Federal-state fiscal relations have long been strained, and there has been much criticism (generally by the more populated states) of the so-called vertical imbalance and of the lack of horizontal equity in the way in which the GST collections are redistributed by the federal government (for example, see Warren, 2006).

Another feature of the Australian political landscape that needs to be appreciated is that parliaments at both state and federal levels have two chambers. This feature has had enormous influence (and at times been a constraint) on government policy and ensuing legislation, particularly at the federal level and when the government of the day has not held the balance of power in the upper chamber. Much complexity in the Australian federal tax system can be directly attributed to the political compromises that are made from time to time to get legislation passed. In contrast, New Zealand has one national unicameral parliament, and this has been a major factor in its much more successful track record in achieving tax reform (McKerchar, Meyer, and Karlinsky, 2006).

Given the politics of taxation in Australia, it is perhaps understandable that, since the 1930s onwards, there has been a series of reviews, inquiries, and Royal Commissions into the federal tax system. The first full-scale review of tax policy was the Asprey Committee which commenced in 1972. The Asprey Committee was formed in response to widespread and lively criticism of the tax system at that time and, possibly of more concern, the view that public attitudes to paying taxes were regarded as becoming less positive over time (though this was thought to be due in part to the rapid rate of inflation and increases in overall government spending that had occurred). The Asprey Committee (1975) made many far reaching recommendations, including greater reliance on indirect taxes, but they were largely ignored by the federal government at that time. Other major milestones in terms of reviews that have shaped tax policy in Australia included the government's Draft White Paper in 1985, the Liberal party's (while in opposition) 1993 "Fightback" tax reform platform of which a GST was the major feature (and was rejected at that time), the simplification of tax legislation (Tax Law Improvement Project) in 1993, the Review of Business Taxation (the Ralph Review) in 1998, and the Review of Self Assessment (ROSA) in 2004.

More recently, and as a result of a recommendation by the Ralph Review, a Board of Taxation was established in 2000 to advise the government on the formulation and development of tax policy and has undertaken a num-

ber of reviews and published reports on a range of issues. Its work program currently includes a scoping study on small business compliance costs and a review of the application of consistent self-assessment principles, www.taxboard.gov.au. Further, an Office of the Inspector General of Taxation was established in 2003 as an independent statutory office to review systematic tax administration issues and to report to government, in the interests of taxpayers, on recommendations that would improve the fairness, efficiency, and integrity of the tax system. At the time of establishing the Office of the Inspector General of Taxation (which also was based on a recommendation by the Ralph Review), some 60 potential review topics were identified based on taxpayers' concerns. The main categories of concerns included the risk and uncertainty associated with self-assessment; the ATO's law enforcement responsibilities and governance arrangements; and the range of complaints about the way in which the ATO relates to, and communicates with, taxpayers and their tax advisers. Its work program is published and currently includes a review into the administration of GST audits; a review of the potential revenue bias in Private Binding Rulings involving large complex matters; and a review into the ATO's ability to identify and deal with major, complex issues within reasonable timeframes, www.igt.gov.au.

These watchdog roles of the Inspector General and, to a lesser extent, the Board of Taxation are in addition to those fulfilled by the Ombudsman (to whom individual taxpayers can take their complaints about the ATO) and the Auditor General, whose role is to undertake performance audits examining the economy, efficiency, and administrative effectiveness of the ATO's administration of the tax system. In contrast to the Board of Taxation and the Inspector General who both report to the Federal Treasurer, the Ombudsman and the Auditor General report to Federal Parliament. Both the Board of Taxation and the Inspector General consult widely in the course of their work, regularly inviting taxpayers and tax practitioners to provide input to matters under review. Clearly, the history of reviews and watchdogs as described herein are evidence of the considerable and sustained interest in tax policy and tax administration by not just politicians and policymakers, but by the broader Australian community.

However, even under all these watchful eyes, it seems that the complexity of the Australian tax system has not yet been reduced. The Asprey Committee considered Australia's tax system of the 1970s to be complex. The Committee noted the number of amending Acts, the size of practitioner textbooks, the number of cases transmitted to Boards of Review, the number of appeals, and the size of the publication of sales tax rulings and felt that these were all indicators of increasing complexity. In the 1970s, the Income Tax Assessment Act was some 750 pages in length. The 1980s heralded a

period of rapid tax reform. New federal taxes introduced included capital gain tax, fringe benefit tax, training guarantee levy (this proved to be short-lived), gun buy-back levy (also short-lived), medicare levy, and the superannuation guarantee levy. A whole range of measures were introduced to improve farmers' financial self-reliance, offer tax concessions to small businesses, and promote investment in a range of endeavors including drought mitigation measures, the Australian film industry, mining, and research and development. By 1990, the Income Tax Assessment Act was some 4,000 pages in length.

A modified form of self-assessment (whereby the ATO calculated and advised the net tax payable) was introduced for individuals from July 1, 1986, and an imputation system for the taxation of corporate profits from July 1, 1987. Full self-assessment was introduced for companies and superannuation funds from July 1, 1989. Self-assessment underwent modification in 1992 to give the ATO legislative power to issue public and private rulings on tax law and thereby relieve some of the burden of self-assessment experienced by taxpayers. By 1993, the 1936 Act had grown into a “monster—a system out of control and getting progressively worse” (Spry, 1993). The government announced in December 1993 that the 1936 Act would be rewritten into more simple language to make it less complex, more understandable, and therefore easier and less costly to comply with. The rewrite was specifically directed not to address policy issues. The rewritten legislation was progressively enacted as the Income Tax Assessment Act 1997. However, the project was subsequently disbanded only one-third complete. Basically, the rewrite project was overtaken by the need for policy reforms, and, to this end, the Ralph Review was established.

Tax policy reform on a scale not seen before in Australia followed with the introduction on July 1, 2000, of A New Tax System (ANTS). Its features included a GST (and the repeal of the wholesale sales tax), pay-as-you-go withholding and installment systems, Australian Business Numbers (ABNs) (as a single business identifier), and a new penalty regime. From July 1, 2001, an optional Simplified Tax System (STS) was introduced for small business (based on a recommendation of the Ralph Review), with its intention being to address the compliance cost burden facing small business. However, the takeup rate of STS was initially very low (14 percent for the year ending 2002 in spite of over 95 percent of businesses meeting the eligibility criteria) and it has undergone further reforms effective from July 1, 2005, in a bid (though arguably misdirected) to improve its attractiveness (McKerchar, 2007).

By 2003, there were in excess of 7,000 pages of federal tax legislation (Dirkis and Bondfield, 2004). The Board of Taxation completed a major project to identify inoperative legislative provisions in 2005, and legislative changes were enacted in 2006 as a result. Even so, in 2007, there are some 8,000 pages in four volumes of tax legislation (with both the 1936 and 1997 Acts being operative), supplemented by over 2,300 pages of legislation in respect of superannuation and another 1,152 pages of GST legislation. While the volume of legislation may be only one aspect of tax complexity, it is certainly one aspect on which real progress is yet to be made.

Other measures of tax complexity are comprehensively discussed elsewhere in the literature (for example, see Cooper, 1993; Krever, 2003). Suffice to highlight here that while volume, language, and structure have attracted considerable attention, more recently attention has turned to functional responsibility and legislative style. Until 2002, the ATO had the function of developing tax law and policy in addition to implementation and administration of the law. This led to considerable criticism of the ATO and its inability to perform both functions in a period of extensive change (ANTS being the case in point). As a result, and on the recommendation of the Board of Taxation, those staff responsible for advising on policy and on legislative drafting were removed from the ATO to the Treasury. In 2004, as an outcome of ROSA, Treasury announced the adoption of a new legislative style of drafting referred to as “coherent principles drafting,” though its meaning still seems to be open to interpretation and its application to date has been limited. It is difficult to envisage that this new drafting style will make any real impact on reducing tax complexity. To be fair to the drafters, it is difficult to make simple law out of complex policy, and it is unclear and often unworkable policy (on which consultation, when it does take place, does so far too late) coupled with ongoing change that is the major cause of tax complexity in the Australian context.

To give taxpayers greater certainty in complying with the requirements of self-assessment, the ATO issues binding rulings which are its interpretation of the legislation. (By way of illustration, in 2006, the ATO issued over 11,000 Private Binding Rulings, 133 Class Rulings, 11 GST Rulings, and 15 Public Rulings.) However, even with simple legislation and a plethora of rulings to give greater certainty, the large majority of Australian taxpayers no longer lodge their own income tax returns. In 1980, 20 percent of personal taxpayers used a tax agent. By 1992, this figure had increased to around 75 percent and has since remained fairly consistent. Personal taxpayers feel that the system has become too complicated, and there have been too many changes for them to be able to confidently complete their own returns (McKerchar, 2003). Over 90 percent of business taxpayers use a tax agent

to prepare their returns, and this figure has remained consistent at least since the 1980s.

This need to engage a tax agent to ensure that taxpayers have met their tax compliance has consequences for compliance costs, particularly monetary and time costs, which have been an ongoing political thorn in the side of successive Australian governments. It also has consequences for the level of compliance itself, which is by and large brokered, and this in turn serves to emphasise the important role tax agents play in terms of taxpayer compliance.¹

The Inspector General recently described the Australian tax system as one where the balance of uncertainty and risk in the tax system is now weighted against taxpayers. Further, it was argued by the Inspector General that this imbalance, together with the adoption by the ATO of a “one size fits all” approach to the application of penalties and interest for noncompliance, has served to encourage taxpayer perceptions of unfairness and uncertainty in the system of self-assessment (Vos and Mihail, 2006). In spite of numerous reviews and watchdogs in place, the criticisms of the 1990s in respect to the growth of complexity in the Australian tax system and its compliance costs still remain. However, questioning the fairness of the system and its uncertainty, as perceived by taxpayers, must be of great concern for policy-makers and the tax administration. In the current environment as described, it is clear that the challenges for the tax administration in managing its risks and maximizing voluntary compliance in a self-assessment system are great and indeed many. This leads to the next section of the paper where a number of compliance research studies in the Australian context of tax complexity are reviewed.

Compliance Research in Australia

The pursuit of simplicity has been a recurrent theme in many of the major reviews of the Australian tax system. The Asprey Committee considered the desirable features of a tax system to be efficiency, fairness, and simplicity, with fairness being the most universally desirable, followed by simplicity. However, it was recognized that policymakers had to repeatedly choose between these features and that there was considerable conflict. The Ralph Review described complexity as having three aspects: technical, structural, and compliance. Technical complexity arose where ascertaining the meaning of the legislation was less than straightforward. Structural complexity referred to the poor structuring of provisions and to the unintended or in-

¹ Note that tax agents in Australia must satisfy a range of requirements, including education and experience, before being registered. For further information, see www.tabd.gov.au.

consistent interaction of different provisions. Compliance complexity arose where there was an excessive burden of recordkeeping, tax form completion, or other compliance activity placed on the taxpayer.

It makes sense that, in order to be able to reduce complexity, the causes of complexity need to be identified and addressed. The Ralph Review identified a range of factors that interacted to produce tax law complexity including black letter law, grafting of legal meaning, tax reform, differentiated taxation of entities, policy framework, the progressivity of the personal tax system, and the desire to address equity concerns. Complex law has consequences for judicial interpretation, and this in turn has an impact on the costs of compliance and of administration. However, the complexity of the law is only one dimension of the systemic problem. For example, other dimensions that need to be considered include the choice of tax system, the nature of its base and the level of integration, and the way in which the system is implemented and then administered. But is reducing complexity the same as simplification? The concepts are both somewhat subjective and have tended to be used both loosely and interchangeably. To a large extent, this probably explains why improvements are difficult to identify and taxpayers' perceptions as to their compliance burden have remained largely unchanged. There is also the consideration that taxpayers are far from being a homogenous group.

Australia's dilemma regarding tax complexity is not unique. Blumenthal (2001) stated that the United States had stood at the crossroads for a decade in its initiative to rescue complexity, with virtually no one thinking that the Federal income tax was simple. Instead, simplicity had been compromised in the pursuit of equity and economic efficiency. However, there was a growing suspicion that increasing complexity was having a negative impact on compliance.

In the Australian context, given a reasonably comprehensive withholding system, personal taxpayers (i.e., those not engaged in a business, but in receipt of salary, pension, or investment income) have limited opportunities to not declare assessable income without detection. There is undoubtedly more scope for taxpayers to inflate their claims for deductions, or to exploit the ambiguity created by complex laws and instructional materials. However, Australian research into the impact of complexity on the compliance behaviors of personal taxpayers has been unable to support this proposition (McKerchar, 2003). This study, using a mixed method design (large-scale survey with the sample population drawn randomly from the ATO's taxpayer database, and a case study) and focusing on taxpayers who were self-lodgers, found that complexity gave rise to unintentional noncompliance and

intentional overcompliance: both of which appeared to favor the tax authority in terms of revenue collections. Clearly, this is unfair.

Other findings of importance derived from this study included that the effect of complexity was directly related to compliance costs and that this in turn had an effect on personal taxpayers' commitment to compliance (which was found to be high). That is, increasing complexity could make it more difficult for the ATO to take advantage of the high tax morale that was found to exist in Australia. Respondents expressed reluctance in seeking assistance from the ATO, due mainly to a lack of confidence in the ability of ATO staff and unease about being conspicuous. Respondents indicated that they relied heavily on tax agents because they wanted an accurate return of income (i.e., they wanted to be compliant) and that they regarded the system as too complex for them to ever understand (or just not worth their while spending the time to do so).

The burden of (or opportunity provided by) tax complexity in Australia falls primarily on tax agents who are at the coalface in advising their clients. Research conducted into the causes of complexity for tax agents, their relative importance, and impact on tax agents' practices was conducted late in 2004 with funding from CPA Australia (McKerchar, 2005). This multiparadigm research used an electronic survey and a case study protocol. Of the 24,000 agents registered in 2004, over 80 percent were in receipt of the ATO's electronic newsletter, and this means was used to promote the survey. The response rate was low, with some 220 respondents taking part in the survey. Followup contact indicated that many agents simply did not read the ATO's electronic newsletter (which is consistent with the findings of the research discussed below). The case study protocol was based on indepth interviews with volunteers—tax agents who were members of CPA Australia.

Briefly, the research found that agents were overwhelmed by the volume of tax material of which they needed to keep abreast, not just legislation, but rulings, determinations and practice statements issued by the ATO. To a lesser extent, the rate of change was an issue as was the complexity of the law. Agents' job satisfaction was suffering as was their confidence in their technical ability. They were coping in a variety of ways, including undertaking additional technical research without always passing on the costs to clients; narrowing the scope of their activities; or relying on the advice of higher-level technical experts (which has implications for compliance costs). Tax agents were frustrated with both government and the ATO. More simple, integrated, and efficient tax systems with less regulatory material and less ad hoc change were what was needed, and agents wanted to have more input into the process.

Much of the research into complexity and business taxpayers has focused on identifying and measuring compliance costs (for example, see Evans et al., 1997), rather than the study of compliance behavior, and this is understandable given the level of reliance on tax agents as previously explained. However, two recent and as yet unpublished studies will be relevant to this discussion once their findings are released. The first study (McKerchar, Hodgson, and Datt, 2006), commissioned by the Inspector General of Taxation in 2005, examined the perceptions held by taxpayers and their tax agents of revenue bias on the part of the ATO in dealing with Private Binding Rulings (PBRs) on large, complex matters. Telephone interviews (collecting both quantitative and qualitative data) were conducted with a random sample (of 50 percent) of ruling applicants who satisfied the set criteria in respect to annual turnover (>AU\$100 million) and who had lodged a PBR application within a given 2-year period. A response rate of over 85 percent was achieved. Specifically, the study was to report on:

- the role of the ATO in relation to PBRs that involve uncertainty in the application of the law or underlying policy intent, including the ATO's interaction with Treasury;
- the potential adverse effects of not following a PBR;
- the perceived cogency of reasons provided for ATO decisions in relation to PBRs;
- the transparency of the PBR process and technical issue resolution;
- the adequacy of ATO assurance measures and controls that are aimed at minimizing the potential for revenue bias;
- the timeliness in providing PBRs, in particular the effect that the ATO's Priority Ruling Process (PRP) has had on perceptions;
- the basis for any perceived revenue bias in the ATO's treatment of its particular PBR application; and
- the potential measures that will resolve perceptions of bias.

The study was focused on "perceptions," and, concurrently, the Inspector General conducted a technical review of the PBR applications in terms of their technical accuracy, time taken, and administrative systems. The

Inspector General is expected to report to the Treasurer in August 2007, and it is anticipated that the report will be released to the public shortly thereafter (and will be made available at www.igt.gov.au).

The second piece of recent research relates to a study which was commissioned by the Board of Taxation in 2006 (McKerchar, Hodgson, and Walpole, 2006). The Treasurer had asked the Board to undertake a scoping study of tax compliance costs facing the small business sector and to work closely with small business, particularly microbusiness (i.e., annual turnover <AU\$2 million), to identify the major areas where compliance costs might be reduced. The Board was asked to take into account:

- the purpose and object of the law;
- the relationship between taxpayer compliance costs and government administration costs;
- costs incurred by business for nontax reasons and any additional costs incurred by businesses or their advisors for tax reasons (tax compliance costs);
- transitional costs and ongoing tax compliance costs;
- taxpayer circumstances and commercial practices;
- other legislation; and
- any other matters the Board considers that may materially impact on small business tax compliance costs.

The Board of Taxation called for and received submissions from the public. In commissioning the scoping study, the requirement was that a qualitative methodology be used with the output presented in matrix form. A grounded theory strategy was employed, and convenience sampling was used. In-depth interviews and observations were conducted with small business owners and accountants, primarily at their places of work. The researchers' records of interviews were initially open-coded and then reconfigured using axial or pattern coding to provide more meaningful units of analysis. These units were then presented as conceptually ordered matrices and then as a refined metamatrix based on the design principles of Miles and Huberman (1994). The Board of Taxation is expected to report to the Treasurer in August 2007, and its report is expected to be made available to the public shortly thereafter at www.taxboard.gov.au.

These examples of tax compliance research in Australia do illustrate that the impact of complexity and its impact on taxpayers and tax administration is a topic that is currently receiving attention at the highest levels. It is also of interest to note that, in the compliance costs scoping study for the Board of Taxation, the terms of reference were not limited to compliance with tax legislation. More recently, in March 2007, the Assistant Treasurer has asked the Board of Taxation to consult publically on the scope to apply consistent self-assessment principles across all federally administered taxes. This continued attention by government is indicative that the problem of tax complexity, at least from the perspective of taxpayers and tax practitioners, is not easing. It would be appropriate now to turn to tax administration and consider its role and strategies in dealing with the issue.

Impact of Complexity on Tax Administration

Michael D'Ascenzo, Commissioner of Taxation, has described tax administration in Australia as big business. The ATO has an annual budget of around \$2.6 billion and collects around AU\$230 billion annually which is about 90 percent of the Australian government's revenue. The ATO administers dozens of Acts and in 2006 implemented around 100 new legislative measures, including the 30-percent child care tax rebate, superannuation choice, and improvements to self-assessment systems. The ATO employs more than 21,000 staff and has more than 17 million taxpayers (D'Ascenzo, 2007a).

The ATO has long recognized the need to work with taxpayers and tax agents as part of improving voluntary compliance and managing risk. Based on the ATO's Strategic Statement 2006-2010 (ATO, 2006b), there has been a shift of emphasis from revenue collection, as the key role of the ATO, to optimizing voluntary compliance by creating the right environment for people to pay tax. An important part of this environment is the reputation of the ATO and the nature of its relationship with the community. To this end, the ATO has put considerable strategic effort into building a transparent relationship with taxpayers and tax practitioners.

The creation of this transparent relationship was evident when the Taxpayers' Charter (similar to a Bill of Rights, which is not provided for in the Australian Constitution) was first introduced in 1997 (and revised in 2003). The Charter sets out the rights of taxpayers to be treated fairly and courteously in their dealings with the ATO in an attempt to address the perceived imbalance of power, but it has no legal effect. A Compliance Model has also been developed that gives recognition to the different attitudes that taxpay-

ers have towards compliance and the need for the ATO to adopt appropriate and proportionate strategies of support and intervention. In 2002, the ATO began its Listening to the Community Program and currently has over 70 formal consultative forums where it consults with a range of taxpayers and tax practitioners about their needs and expectations in dealing with the tax administration.

In the spirit of transparency and with an underlying philosophy that prevention is better than cure, the forward publication of the ATO's Compliance Programs first began in 2003-04 with the aim of making it as simple as possible for taxpayers to comply with the law. A Compliance Program sets out in advance the tax risks that the ATO intends to focus its enforcement effort on for the coming year based on its risk assessment.² The ATO believes its approach to risk management is unique in its level of openness and accountability (D'Ascenzo, 2007a).

The key message from the Listening to the Community Program was to make dealing with the ATO easier, cut compliance costs, and provide a more individualized service. It was obvious that that the ATO needed to do better in designing its administrative systems and processes from a user rather than an administrator's perspective (Farr, 2006). In response, the ATO introduced the Change Program in 2004. In its preliminary stage, the Change Program included the introduction of e-portals for tax agents and business taxpayers for improved self-help service. In the 2006 financial year, there were 11.6 million logins to the tax agent portal supporting 3 million transactions; the business portal had about 1.2 million logins supporting 400,000 transactions. From July 1, 2006, the Tax Practitioner and Lodgment Strategy (TPaLS) business line assumed corporate responsibility (with 312 staff and AU \$24 million allocated in 2006-07) (ANAO, 2007) for managing the ATO's relationship with tax agents—clearly recognizing the important roles they play in taxpayer compliance.

From Listening to the Community, the ATO has more recently shifted its emphasis to the three Cs of Consultation, Collaboration, and Codesign. There is now a complex model of community consultation that includes 11 peak consultative groups and many subgroups, working parties, industry forums, and expert panels that advise, make recommendations to, and engage with the ATO. From the ATO's perspective, an important aim of the consultation is to align its administration and requirements more closely with accepted business and accounting procedures, transactions, and processes, to ensure that practical solutions are adopted that are consistent with the policy

² Compliance Programs and all other ATO reports and Commissioner's addresses referred to in this paper are available at www.ato.gov.au.

intent of the law without increasing compliance costs. From the perspective of taxpayers and tax practitioners, it appears (at least) that they have greater ownership of, and responsibility for, the tax system.

The 2005-2006 ATO Annual Report (ATO, 2006a) presents very positive findings about its relationship with taxpayers and tax agents based on recent surveys commissioned by the ATO. For example, it was reported that over 80 percent of tax agents felt that it was now easier to deal with the ATO, that the information received by the ATO was more tailored to meet their needs, and that they thought the ATO was improving its systems and business processes to make it easier for tax agents to deal with the ATO. Further, 85 percent of businesses felt that the ATO was doing a good job, and almost 75 percent of respondents from the general community were positive about the overall performance of the ATO. It is reported that, overall, there appears to have been a steady increase in positive perceptions about the ATO since 2000.

These conclusions in the 2005-06 ATO Annual Report have been more recently supported by the findings of the Australian National Audit Office (ANAO) (ANAO, 2007) in its followup report on March 14, 2007, on The Australian Taxation Office's Management of its Relationship with Tax Practitioners. The ANAO reported that the relationship had improved significantly since the first audit in 2002-03 (at which time, the relationship was described as "strained and tense").

However, in building transparent relationships, it appears that the ATO still has some way to go in respect to large corporate taxpayers. Both the former and current Tax Commissioners have been vocal in recent years in emphasizing the need for improved standards of corporate governance and the requirement under corporate law for the formalization of tax risk management policies at board level (D'Ascenzo, 2006). This dialogue has been followed up with audit activity—in the 2005-06 Compliance Program, it was revealed that 89 percent of Australia's top 100 companies and 83 percent of the top 200 were subject to a tax audit in 2004-05. This activity generated a 25-percent increase in revenue from the previous year.

It appears that the preference of boards by and large has been to maintain a civil relationship with the ATO and to keep a more respectable distance with less transparency. An example of this distance is the reaction by the top 100 corporations to the ATO's Forward Compliance Agreements (FCAs) which the ATO regards as the cornerstone of its vision for a capable and well-regulated tax profession (D'Ascenzo, 2007a). Under a FCA, the taxpayer allows the ATO to undertake a due diligence review of its systems and records and then commits to continuous disclosure to the ATO of the company's actual and potential tax and governance risks. The advantage

to the taxpayer is access to a lesser likelihood of audit, reduced penalties on errors, discounted interest rates on unpaid tax, and streamlined access to advice. However, the concept has not been warmly embraced by the top 100 companies, many preferring to maintain the business as usual approach and apply for Private Binding Rulings on a needs basis. So far, only two FCAs have been reached, and neither was apparently in respect of income tax. As for being a cornerstone, it is difficult to envisage FCAs ever living up to the ATO's expectations.

The much bigger challenge of the Change Program has been for the ATO to move to an integrated IT environment with enterprisewide processes focused on meeting the needs of taxpayers. The program, estimated to cost AU\$720 million, has been described by the Commissioner as ambitious (D'Ascenzo, 2007a). It is to be delivered in stages focused on improving taxpayer and tax practitioner products and services while transforming internal capabilities—people, processes, and technology—and providing a sound platform for the future.

In the first stage, a new Client Relationship Management (CRM) was introduced in 2006, collecting and centralizing all information about a particular taxpayer. In Stage 2, which is currently underway, the existing 180 case management systems are being replaced with a single Case Management System, and a new Work Management System is also being introduced. Stage 3 involves the delivery of a new Integrated Core Processing (ICP) system to replace 75 existing systems and manage all of the processing work undertaken by the ATO for all types of taxes. Significantly, the taxpayer (and his or her agent) will see exactly the same screen as the ATO when engaged in discussion with each other. The final release in Stage 3 is expected to be rolled out in July 2009 (D'Ascenzo, 2007b).

The technological changes to be undertaken are on an enormous scale but are expected to provide richer information about taxpayers' compliance histories and a better understanding of their likely behaviors. Contingent on the successful implementation of the Change Program, the ATO expect to be able to develop more refined risk models with wider data warehousing, analytics and data mining, and matching capabilities with progressively higher degrees of reliability (D'Ascenzo, 2007a). Indeed, given the enforcement capacity that these technological innovations will provide, the need for a transparent relationship seems somewhat diminished.

The major (and unanticipated) changes to superannuation announced in the 2006 Federal Budget have delayed the Change Program to some extent as the ATO has had to incorporate the implementation of the related policy and system changes. So, even the best laid plans by tax administrators have to adapt to change and increasing complexity that are beyond their control.

Clearly, tax complexity is a challenge for the tax administrator. In this section, we have examined how the ATO has responded and where it is positioning itself in the foreseeable future. In summary, its role as administrator and not policymaker or legislative drafter has been reaffirmed. This shift of function and greater focus on its service role (more so than its revenue collection role) appear to have given tax agents greater confidence in the ATO. It distances the ATO from sharing the blame for poor or inequitable policy or for inappropriate policy. The ATO has been very strategic in building a transparent relationship with taxpayers and tax agents in listening to the community—almost giving the appearance of changing sides. By consultation, collaboration, and codesign, taxpayers, tax agents, and the tax administrator appear to be united. Tax complexity may not have reduced, but the burden of responsibility for it seems to be inexorably shared. Can this approach work? Again, it is emphasized that much of what is at stake here in terms of maximizing voluntary compliance is the perceptions held by taxpayers and tax agents, not necessarily the reality. Time will tell. Given the investment in technology by the ATO and its enhanced enforcement capability, it is not being complacent nor relying entirely on trust and transparency.

Conclusions

While investment in technology and the capacity of staff and systems is now more than ever a major weapon in the ATO's armory, the extent to which it is a worthwhile investment remains to be seen. There is a concern that such investment may stop other policy options from being explored, particularly in respect to complexity and compliance. For example, at a recent Symposium on Personal Income Tax Reform held at UNSW in Sydney and sponsored by CPA Australia, the need to have salary and wage earners lodging returns at all was discussed (i.e., a shift to prepopulated returns as adopted by Nordic countries), as was the possibility of not allowing work-related deductions (i.e., the New Zealand approach) or of reintroducing a state-based income tax.³ Work-related deductions are claimed by around 7 million individuals and accounted for AU\$11.5 billion in 2004-05, which was over 50 percent of all deductions claimed by individuals (ATO, 2006c). Other possibilities include greater withholding of tax from source, taxing income and capital in the same manner (or applying a *de minimus* provision in the case of small capital gains that would effectively remove the compliance burden for share investors), and removing the tax structure differentials in the current income tax rates. Basically, these academic questions drive at the very heart

³ Symposium papers are available at www.atax.unsw.edu.au.

of policy reform, and the one thing we have learned in Australia is that the underlying policy issues cannot be ignored, or at least not indefinitely.

However, with initiatives such as the Change Program, e-lodgments by taxpayers (first launched by the ATO in 1999 as a world first and growing in popularity), and another project currently underway to prefill electronic returns (to a limited extent) for downloading by tax agents and taxpayers, there seems to be acceptance of the fact that transformational policy changes to reduce complexity are unlikely to happen in the foreseeable future. Undoubtedly, there will be further reviews, consultations, and federal elections.

The ATO has made a real commitment to understanding its taxpayers and working with them. It has put considerable effort into understanding its various types of taxpayers and their tax agents and building relationships over time. In the long run, these strategies should be very effective in maintaining the high levels of voluntary compliance that do already exist in Australia, provided that tax complexity (in every sense of the word) is not allowed to go unchecked. Similarly, this may give some measure of confidence to administrators in other regimes facing comparable circumstances.

Simple policy is a precondition to having laws that are simple to understand, to implement, and to administer. This is a golden rule of which policymakers and legislators should not lose sight. Consultation throughout the process can be effective, but not if left entirely to the later stages (i.e., implementation) in the process. More consultation at the policy stage in Australia could have saved a great deal of unnecessary subsequent changes when the policy was found to be unworkable or ineffective, such as has been the case with the Simplified Tax system for small businesses. However, consultation can also delay the process and be taken advantage of by self-interested parties (e.g., in May 2007, draft legislation to regulate tax agents was released, some 15 years in the making).

In respect to tax complexity, the Australian experience has been that less volume and less ad hoc changes are highly desired by both agents and taxpayers. While taxpayers and agents appreciate the support of and service provided by the ATO, they still have quite onerous compliance obligations placed on them by the various systems and legislative requirements. There is considerable scope for improvement, and it may be that taxpayers are willing to sacrifice some fairness for greater efficiency and/or certainty.

This does lead itself to avenues for further research. The extent to which different types of taxpayers are willing to accept tradeoffs between these ideals may help inform government, policymakers, and the tax administration. It may be that other ideals need to be considered in the mix, such as global competitiveness and/or economic development. The extent to

which tax complexity provides an opportunity or causes (groups of) taxpayers to overcomply and the various relationships based on distinguishing attributes may also help determine appropriate reform targeted at specific taxpayer types and/or types of complexity. The focus herein has been on tax complexity at the federal level, but it is clear that the regulatory burden is not just a tax issue, nor a federal government issue, and that there is considerable scope for better coordination and integration of information needs and systems across the board so that people (and in particular in Australia, small businesses) are productively supported by the systems rather than driven by them. Finally, qualitative and mixed method research approaches do offer researchers access to much richer data and deeper understandings of taxpayer behaviors. The important questions are not what people think, or how many agree or disagree, but why people believe what they do. Understanding what drives people's perceptions is the first step to changing perceptions and ultimately their compliance behaviors.

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