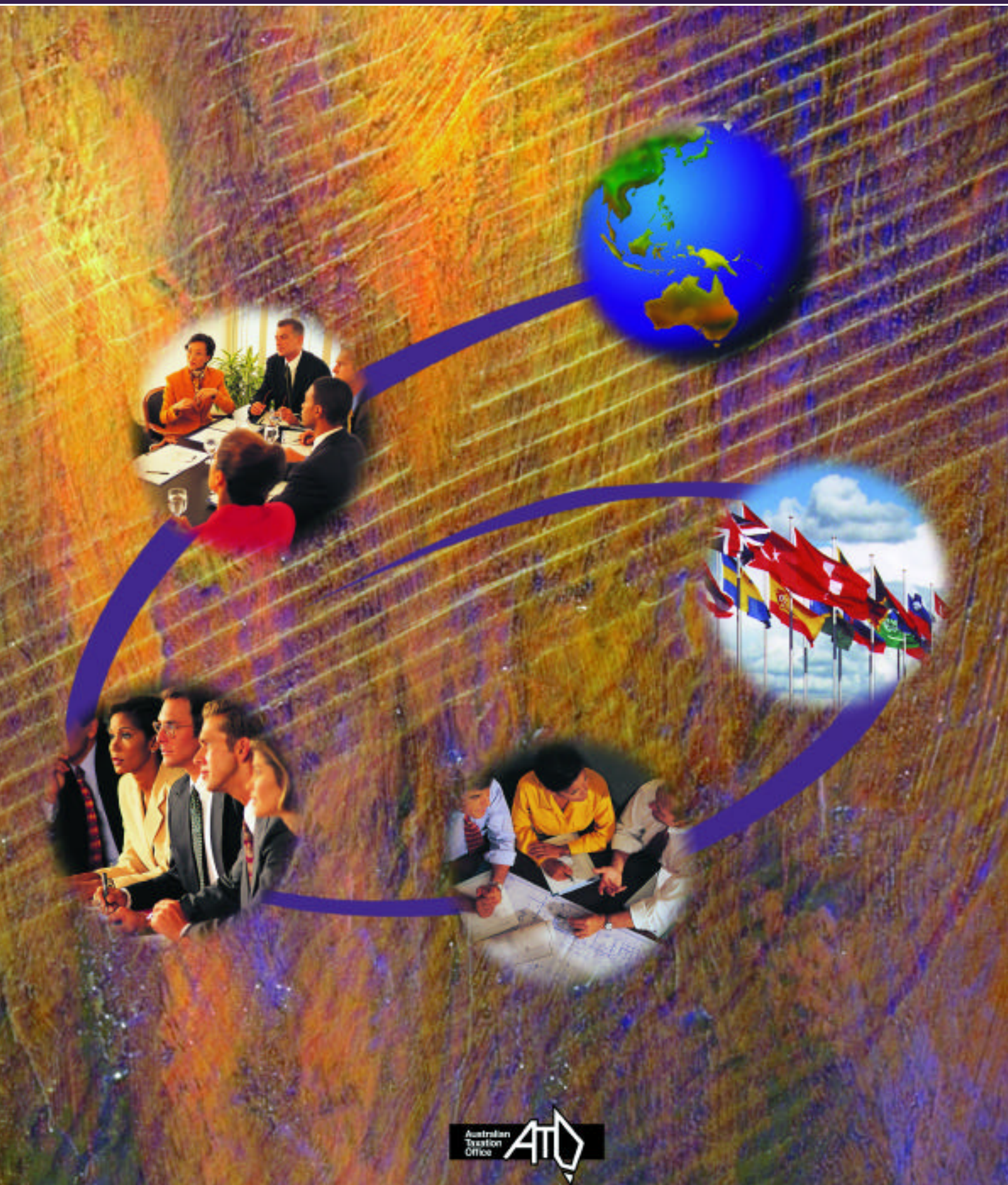


Cooperative Compliance

WORKING WITH LARGE BUSINESS IN THE NEW TAX SYSTEM



Foreword

The Cooperative Compliance Model outlines the relationship we seek with large business and the wider community — a cooperative relationship based on mutual respect and responsibility.

By working together, we can maximise our contribution to the Australian economy and maintain the community's confidence in the tax system.

The Model complements the Taxpayers' Charter and reflects our commitment to greater openness and better relationships with people in large business and the community.

Jim Killaly

Deputy Commissioner
Large Business and International
Australian Taxation Office

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About cooperative compliance

Cooperative compliance represents a new relationship between large business and the Australian Taxation Office (ATO) in the new tax system. The Cooperative Compliance Model opens the way to a better understanding between business, tax administrators and the community. The Model will improve the legitimacy, fairness, viability and functionality of the tax system.

The purpose of this publication is to outline how the Cooperative Compliance Model works and to set out its underlying principles and obligations. These principles provide a basis upon which the ATO and large business can develop and maintain an open working relationship that ensures that the taxation compliance process is both fair and effective.

This publication was developed in close consultation with the Commissioner of Taxation's Corporate Consultative Committee, comprising the following members:

The Commissioner of Taxation
Deputy Commissioner of Taxation, Large Business and International
Australian Bankers' Association
Australian Chamber of Commerce and Industry
Australian Industry Group
Australian Retailers' Association
Business Council of Australia
Corporate Tax Association
Insurance Council of Australia
Investment and Financial Services Association
National Tax Liaison Group
Minerals Council of Australia
Property Council of Australia

These members are committed to the principles of cooperative compliance.

This publication also draws on the views and experience of Second Commissioners, Deputy Commissioners and staff working in the tax compliance field, the Australian National Audit Office and the Centre for Tax System Integrity of the Australian National University.

Objectives

Cooperative Compliance

Optimising economic growth:

Improving Australia's international competitiveness and economic growth depends on several factors, one of which is maintaining the integrity and transparency of the tax system. This provides confidence for those investing in Australia. At the same time, if compliance and administrative costs are high, economic growth will be hindered. For instance, compliance activity that reduces tax avoidance helps to keep general rates of taxation lower.

Generating community confidence:

Any perception that the ATO is not fully committed to ensuring corporate compliance makes the wider administration of the tax system more difficult. Perceptions of the compliance levels of large business influence the wider community's confidence in the integrity and equity of the system. More than ever before, the community expects large business to contribute their fair share to the community via the tax system. A system that is widely perceived as fair will be better supported and more effective.

Building cooperative relationships with business:

Compliance strategies that are understood by business, and take into account the 'real world' concerns of business, will encourage voluntary compliance. A conscious effort by the ATO and business to co-design compliance solutions in problem areas will produce greater certainty, reduce compliance costs and provide improvements in the law and tax administration.



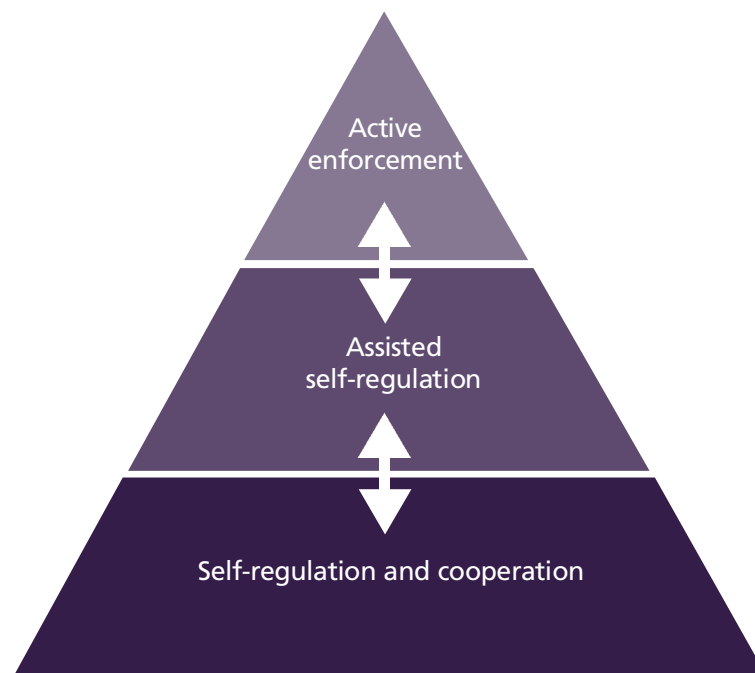
Principles

What is the Cooperative Compliance Model?

The Cooperative Compliance Model ('the Model') is an adaptation of the ATO Compliance Model, which was developed through extensive consultation with industry, government and community groups. It promotes the use of tailored responses to different taxpayer groups based on their compliance risk levels and histories. These responses range from support and assistance through to targeted enforcement measures, such as audits, sanctions and prosecutions. The Model is intrinsic to the policy, legislative and administrative processes of the new tax system. It provides a pathway to design and improve the law based on lessons learned from compliance activities.

The compliance pyramid (Figure 1) demonstrates how cooperative compliance works. The base of the pyramid – characterised by a cooperative, self-regulatory approach – is the most desirable area of operation for the ATO and for business. The diagram shows how cooperative compliance allows for movement both up and down the pyramid, from active enforcement measures at the top down to self-regulation and cooperation at the base.

Figure 1 The compliance pyramid



The Model relies on:

- Commitment from the ATO and large business to jointly build a positive professional relationship.
- Recognition that such a relationship builds understanding, but does not preclude disagreement or different views on the law and compliance.
- Self-regulation by large business, and ATO enforcement if self-regulation fails to work.
- Resolving the underlying causes of compliance problems by improving the quality and structure of the law.
- Assistance from large business to verify and demonstrate that community expectations of compliance are being met and that the business tax system is working effectively.

Principles

Why have a Cooperative Compliance Model?

There are several reasons for creating the Model.

The successful operation of Australia's tax system is a process in which the Government, the ATO, business and the community all have an important role to play. While the ATO has the responsibility for managing the tax system on behalf of the Federal Government, the system is based on taxpayers – whether they are individuals, small businesses or large corporations – voluntarily complying with their obligations under the law.

Taxes are a necessary part of community living, to fund roads, schools, hospitals and other community support. They also provide major infrastructure benefits for business, such as the rule of law, the protection of property and the facilitation of trade and investment.

The compliance of large business is important – for revenue, economic performance and the overall management of the tax system. For a tax system to work successfully, it needs the cooperation of business and the community. The behaviour of those at the top of the taxpayer scale impacts significantly on how the wider community views the tax system, and the level of confidence that community has in the system's integrity. Also, businesses who are paying their tax need assurance that others are not getting a competitive advantage through not paying their fair share. In recent years, the amount of tax paid by the largest businesses has increased at twice the rate of economic growth. Yet, in the community, the perception persists that corporate Australia is not paying its fair share.

The Cooperative Compliance Model is designed to clearly explain taxation compliance activities involving large business. It acknowledges that large business and the ATO have mutual obligations to ensure that the compliance process is working efficiently and effectively, and also to demonstrate to the wider community how it works. The challenge for the ATO and the business sector is to facilitate and support good corporate citizenship that will strengthen the Australian economy and promote the wellbeing of Australian society.

Who is this publication for?

This publication informs a range of interested people of the benefits of the Model. They are:

- The large business community.
- ATO executives.
- ATO managers and their staff.
- The wider community.
- Tax professionals.

What will success look like?

The Model will provide a range of benefits to Australians and deliver significant advantages across the tax system - for the ATO, for large business, for other taxpayers and for the community as a whole. The success of cooperative compliance will be demonstrated by:

Minimising compliance costs

Compliance costs will be reduced, improving business performance and encouraging large businesses to comply with their obligations voluntarily. The promotion of self-regulation reduces intrusion and provides greater focus on the tax issues most likely to cause problems.

Using ATO resources efficiently

It is in the interest of all that the resources of the ATO are used efficiently. Cooperative compliance frees staff to focus on the important compliance issues and work in a planned manner. Self-regulation, particularly for lower risk taxpayers, will increase the efficiency of ATO collection activities.

Sustainability

The approach of cooperative compliance can accommodate change and emerging risks in the legal and business environment, without disturbing its core principles.

Improving voluntary compliance

The Model will build appropriate relationships which are able to improve cooperation, and therefore self-regulation. Large businesses will be encouraged to approach the ATO to prevent non-compliance and improve the overall structure of the tax law. Demonstrating improvements in corporate voluntary compliance will, in turn, improve community confidence in the integrity of the tax system.

Using intelligence effectively

The Cooperative Compliance Model will promote access to up-to-the-minute intelligence and enable timely and appropriate responses to emerging threats to the integrity of the tax system.

Increased interaction between the ATO and large business will lead to the development of 'coalface' knowledge that will help the ATO and large business better understand each other's needs. Shared knowledge will lead to accurate risk assessment and improved ATO coverage and service.

Principles

Improving the law

Uncertainty in tax law is a major complaint of large business. Greater cooperation between large business and the ATO will help identify weaknesses in the law and difficulties in its administration. This information flow will ensure that the tax law and associated administrative processes correspond to policy intentions, and contribute to its improvement.

Addressing deficiencies in the tax system

Insights gained from cooperative approaches will promote understanding of the underlying causes and patterns in non-compliance and the implementation of appropriate responses.

Generating community confidence

The increased transparency of our compliance approach under the Model will demonstrate that taxpayers are treated equitably and that the ATO is addressing non-compliance. The image of both the ATO and large business will be improved by greater visibility of compliance activities, in particular the level of voluntary compliance.

Applying Taxpayers' Charter principles

Business will receive fair, professional and consistent treatment in their dealings with the ATO, as outlined in the Taxpayers' Charter. ATO service standards will be achieved and the ATO will work to ensure that its professionalism is recognised as high.

Building cooperative relationships

The ATO, large business and other interested parties will work together to design solutions that meet the needs of all without compromising the law and community interests. Transparency and cooperation demonstrate that all parties are committed to taxpayer rights and obligations.

Improved mutual understanding will assist the identification of win-win practices and approaches. The ATO will ensure high-risk taxpayers maintain regular contact, so that appropriate compliance responses can be applied.

Seven basic principles

Both the ATO and large business can give meaning to the Model by applying its seven basic principles. These are:

Understanding taxpayers

For the ATO, an economic group perspective is essential to understanding corporate behaviour. Taking such a perspective encourages examination of compliance from a number of viewpoints including industrial, economic, international, psychological and social. The ATO needs to understand not just individual taxpayers in isolation, but also the dynamic environment in which they operate and the administrative impact the ATO has on them.

Building partnerships

The community is a key participant in the tax system and can significantly influence the ATO-large business relationship. The community, the ultimate owner of the tax system, demands a fair and equitable application of the taxation law. A successful community partnership involves the ATO in co-designing its policies and approaches with the community, working together to identify and resolve problems. Having transparency in the partnership brings to light the best and worst compliance practices.

The willingness of the ATO and large business to work together to influence compliance is a key element in developing effective compliance partnerships. Conversely, aggressive and unresponsive behaviour from either party can undermine the integrity and legitimacy of the tax system in the eyes of the wider community.

Increasing flexibility to encourage and support compliance

Flexibility and responsiveness to change provide new opportunities for the ATO and large business to facilitate compliance. A range of options is required to support corporate compliance so that specific circumstances can be taken into account.

For example, the use of a negotiated Advance Pricing Arrangement between the ATO and a corporate taxpayer is easier to verify and provides greater certainty about future tax liabilities than do transfer pricing audits.

Principles

Escalating options to enforce compliance

The compliance pyramid spans the full range of ATO approaches to assure compliance, from self-regulatory mechanisms to active enforcement measures such as audits. The ATO's preference is to work with taxpayers using strategies at the lowest possible level first, escalating its approach only if these options fail to work. In some cases, the ATO's understanding of taxpayer behaviour will require the use of a higher level strategy much earlier; for example, where evidence exists that a crime has been committed or a pattern of tax avoidance is emerging.

Continuously improving the law

Uncertainty about tax law is a key issue. The laws that govern the taxation system are extensive and complex. The integrity of the tax system is improved by addressing the design of the law and by drawing attention to weaknesses in its operation. The development of policy and legislation is assisted by strengthening the communication between the policy, legislative and administrative processes.

Creating a dialogue with the judiciary

Judges are key participants in the tax system, as their interpretations of the law are important in influencing the tax system and business behaviour. A dialogue between the judiciary and tax administrators would help to improve understanding of how legal interpretations impact on corporate compliance.

Responding to the globalisation of business

The increasing globalisation of business strategies means that the ATO needs to be at the forefront in understanding and responding to the taxation implications of this globalisation. In particular, the cooperation of the corporate sector plays a vital role in increasing the ATO's understanding of the relationships between large corporations and foreign tax systems and administrations.

What are the practical steps to make the Model work?

The Model emphasises that large business and the ATO can work together to identify weaknesses in the tax system, develop streamlined cost-effective solutions and increase community confidence.

To give these ideas practical meaning, the Model is applied by bringing together five processes (see Figure 2) that explain the compliance relationship between the ATO and large business. These five processes are:

- Understanding business and the law.
- Assessing the risks.
- Planning strategies.
- Implementing strategies.
- Reviewing and improving.

Figure 2 The five processes of cooperative compliance



Principles

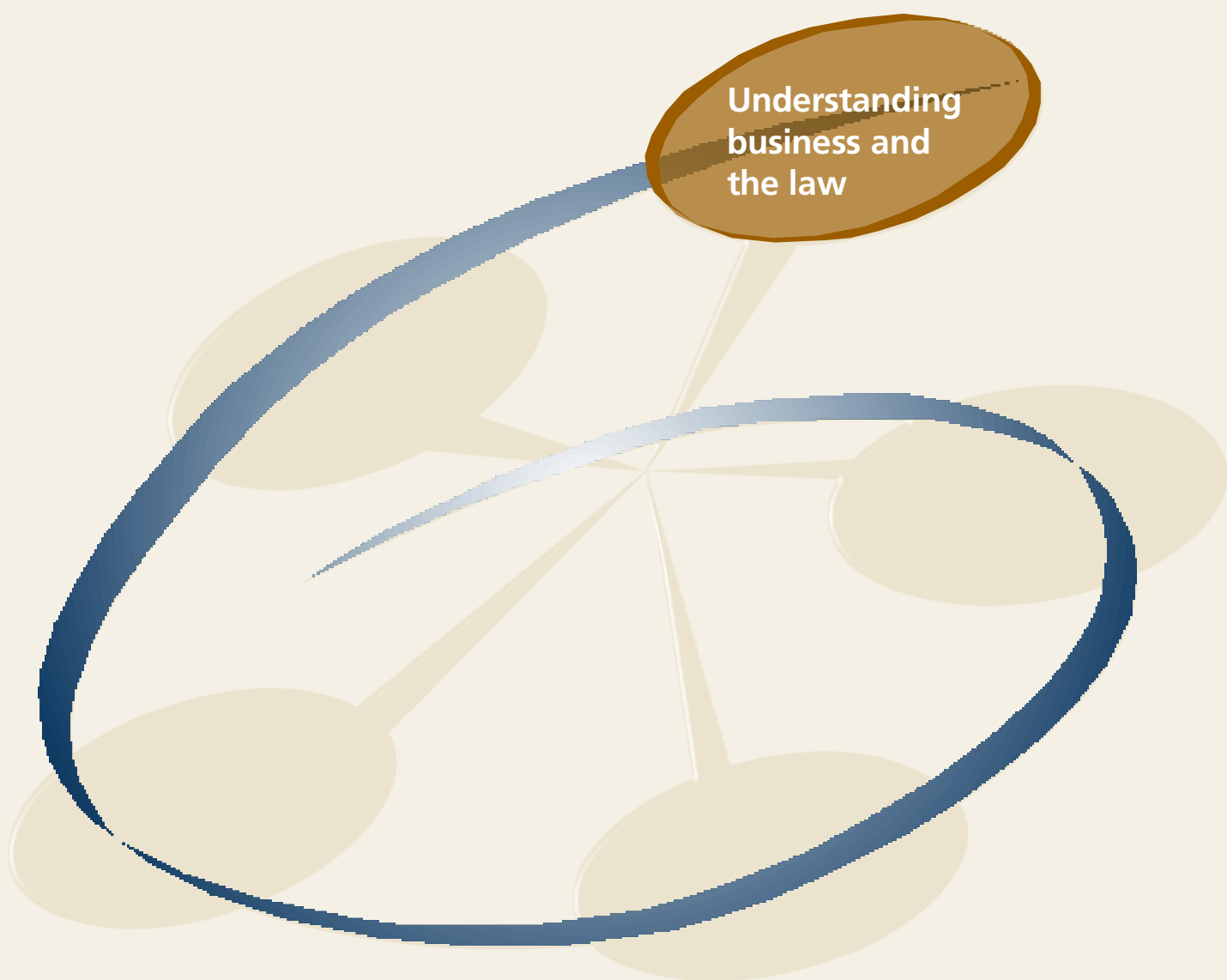
These five processes are not prescriptive, and will involve varying levels of collaboration between the ATO and large business. Business tax compliance is complex. Large business and the ATO seek both certainty and flexibility. Certainty can be achieved by making compliance expectations and actions more transparent, while allowing enough flexibility for good judgement and common sense to operate.

The Model is designed to apply at any level, from a single transaction by one entity to the entire market. These levels, outlined in Table 1, provide increasingly greater benefits for the ATO and large business to solve compliance problems and spread solutions quickly and cost-effectively. While the Model can be applied at any of the six levels, the higher levels enable the causes of compliance to be resolved, rather than just the symptoms. Therefore operating solely at the lower levels will not be an effective investment in time and resources for either the ATO or large business.

Table 1 The six levels of application

Application Level	Comments
Whole of market	<p>Dealing with compliance across industries and across the ATO. Can include issues relating to the wider community.</p> <p>Examples:</p> <ul style="list-style-type: none"> • High Wealth Individuals. • International issues. • E-commerce. • Aggressive Tax Planning. • Tax Reform implementation.
Tax issue	<p>Involves specific tax issues that relate to a cross section of large business. The issue is not industry specific.</p> <p>Example:</p> <ul style="list-style-type: none"> • Transfer Pricing.
Industry	<p>Involves compliance across a set of corporations which are industry related.</p> <p>The ATO's industry approach develops strategies to manage compliance risks.</p> <p>Examples:</p> <ul style="list-style-type: none"> • Industry forums. • Industry Watching Briefs.
Economic group	<p>Many large businesses are part of a corporate group structure. To be effective, the ATO needs to manage compliance in the context of the economic group.</p> <p>Example:</p> <ul style="list-style-type: none"> • Multi-national groups.
Entity	<p>This involves managing compliance for one business.</p>
Transaction	<p>This involves managing compliance for a specific transaction that a business has been involved in.</p>

Process 1



Understanding business and the law

For both the ATO and large business, it is vital that tax administrators have a thorough understanding of the world in which business operates and the realities of the commercial environment. This is the first step towards cooperative compliance. A well-developed understanding of business establishes a foundation for achieving effective compliance management.

Tax administrators need to recognise that large business operates within a large and changing social, political and economic environment that influences peoples' decisions and behaviours. They also need an understanding of the policy, legislative and administrative processes of the law and a capability to apply and improve that law to meet community needs. This knowledge enables better judgements to be made on large business behaviour and how this behaviour and the law impact on compliance.

The model uses the 'BISEPS' system (see Table 2) to assist the ATO's understanding of business behaviour. The six BISEPS factors are (B) business, (I) industry, (S) sociology, (E) economy, (P) psychology and (S) systems of compliance. These broad areas reflect the fact that taxpayer compliance decisions are affected by a wide set of factors that are related.

Process 1

Table 2 BISEPS of the Cooperative Compliance Model – factors and examples

B	Business	The extent and nature of the group’s business activities and transactions. Location and size of industry. Business plans and strategies. Entity and group structure. Capital structure, financial performance and ratios.
I	Industry	Conditions affecting the industry - region, size and participants. Industry associations. Industry profit margins and cost structures. Nature of the competition. Industry skill levels. Impact of technological and business change. Financial performance. Industry norms and regulatory environment.
S	Sociology	Knowledge and norms of the professional/business group, e.g. standard of record keeping and lodgement timeliness. Culture of the organisation and management. Business, professional networks and reputation. Approach to community and corporate citizenship. How the group deals with finances and paying tax. Linkages to gatekeepers and advisers.
E	Economy	Domestic, international environment and trade conditions. Key overseas developments. Government policies – interest rates, inflation, tax system and economic reforms.
P	Psychology	Management objectives and philosophy. Views and reactions of management to wider community. Approach to managing risk and drivers of the risk strategies. Attitude and relationship with the ATO.
S	Systems of compliance	Decision making systems, processes and organisational structure. Quality Assurance standards and records. The support and authority the corporate taxpayer’s tax compliance team receives from management. The degree of ease in accessing information. Nature and purpose of transactions e.g. value, type, conduct, methods, timing, costs and benefits. Compliance history. Tax analysis of issues and expected range of tax results.

Note: The list is not exhaustive. These and other examples can be found in Auditing Standard AUS 304 ‘*Knowledge of the Business*’, prepared by the Auditing Standards Board of the Australian Accounting Research Foundation.

Understanding large business and the environment is an ongoing activity which draws on the experience of ATO staff and large corporates. By working more closely with large business, the ATO can add the experience and views of business people to its own knowledge. The exchange of views between the ATO and large business provides an important source of information for understanding contemporary business behaviour, and for forecasting how this might change in the future. It is through this dialogue that all parties can make better sense of what is happening so that fair, accurate and timely action can be taken.

The nature and extent of the information needed will increase with the size and complexity of the large business or the issues involved. For large businesses with straightforward tax issues, the information needed may be minimal. Much of the information illustrating BISEPS in Table 2 is already recorded in the ordinary course of business.

Key principles for the ATO and large business in Process 1 are:

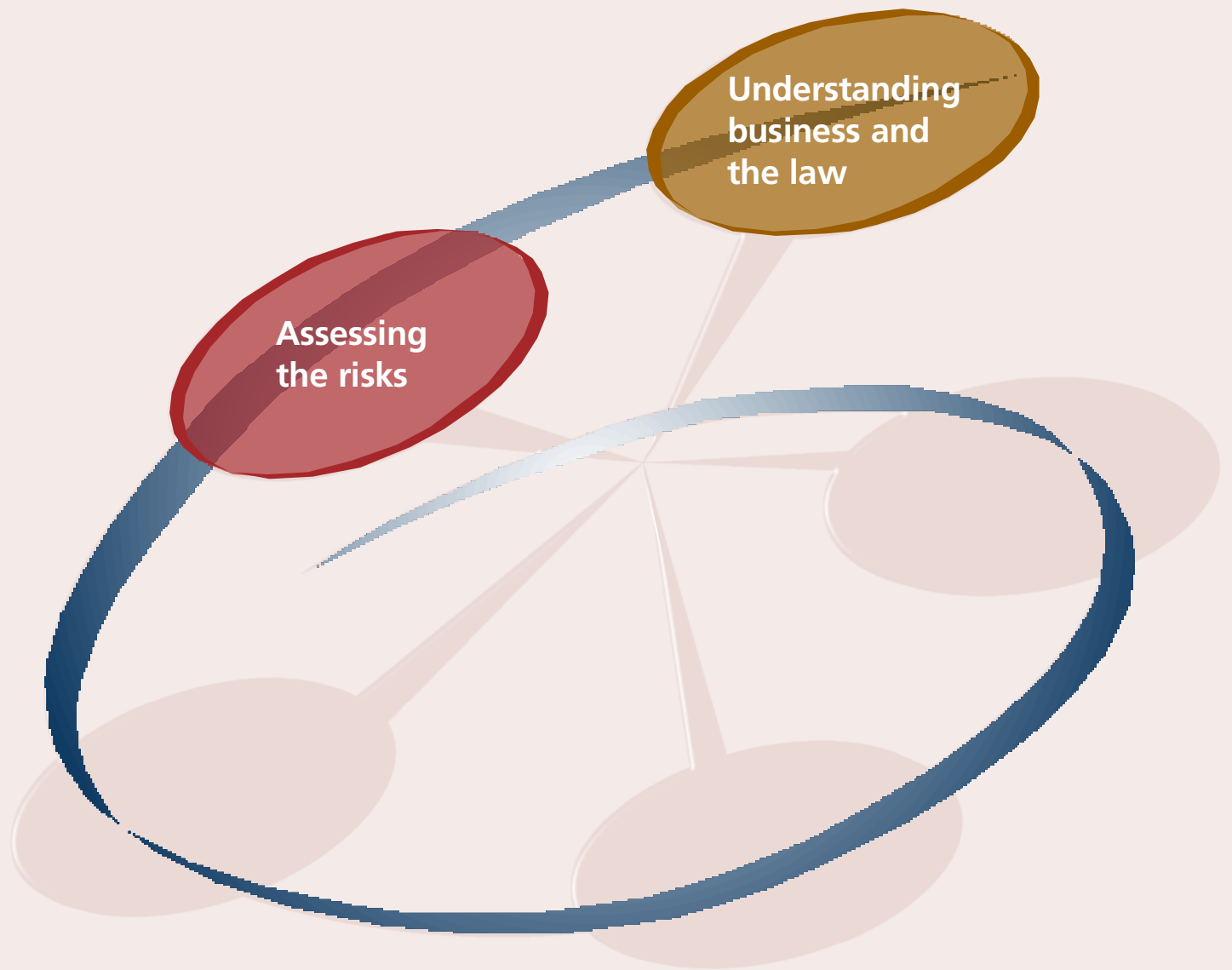
- Working together to improve understanding of business, the environment and the law.
- Understanding large business behaviour through examining the economic group that the business is a part of.
- Operating in a current, real-time manner, keeping pace with business and market developments as they occur rather than focusing solely on activity from past years.
- Resolving the underlying causes, rather than the symptoms, of compliance problems, and sharing the benefits and knowledge with as many businesses as possible.

What does this mean for large business?

An understanding by the ATO of the environment and a more cooperative relationship offers large business the following advantages:

- Consultation about developments in the environment and how these might impact commercially and on tax compliance.
- A more effective approach to the design of tax law and structure.
- Better interpretations and more focused compliance activities by the ATO.

Process 2



Process 2

Assessing the risks

Risk assessment provides an opportunity for the ATO and large business to move away from an enforcement regime towards more cooperative, self-regulatory approaches.

The ATO believes that business should be involved early in the risk assessment process. While the initial risk assessment is undertaken by the ATO, input from business is needed to prevent misinterpretations and to allow misunderstandings to be resolved quickly. This avoids unnecessary compliance interventions by the ATO.

It is important for large business to understand how the ATO operates in terms of its compliance activities. Such activities are generally undertaken on the basis of assessing identified risks. Identified risks are analysed and assessed to develop an overall risk profile of a taxpayer and the tax issues that need to be dealt with. Process 1 contributes to this. This risk management approach allows the ATO to tailor its strategies in a manner that is appropriate for all identified risks.

Seven criteria are considered by the ATO when assessing risks:

- business and transactions.
- globalisation.
- attitude.
- systems of compliance.
- perceptions of stakeholders.
- materiality.
- application of the law.

They are outlined in the risk matrix in Table 3. An overall risk ranking that varies from 'extreme' to 'trivial' is made after considering all seven risk criteria. The risk matrix can be used for particular parts of a market, or for an entire industry group, to assess business risks and determine the actions the ATO might take to eliminate or reduce those risks to a manageable level.

Table 3 Risk matrix Each risk criterion includes examples of what compliance looks like for the extreme and trivial levels of risk.

Criteria	Extreme	High	Major	Significant
Business and transactions	Complex business group structure and transactions. Volatile industry/business activity. Non-commercial business arrangements.			
Globalisation	Considerable international activity and extensive non-commercial transactions involving preferential tax regimes/tax havens. International aggressive tax planning activities.			
Attitude	Uncooperative/confrontational approaches adopted. ATO contacts generally not constructive. Pattern of aggressive tax planning. Little commitment to compliance. No use of self-regulatory approaches.			
Systems of compliance	Low integrity compliance system in place. No effective quality assurance or risk management processes. Little or no corporate governance. No supporting documentation. Low professionalism of corporate staff and tax advisors.			
Perceptions of stakeholders	Considerable impact on community confidence. Potential for serious damage to tax system integrity.			
Materiality	Very significant impact on revenue. Significant difference in tax revenue between ATO view and the taxpayer's. Unpredictable pattern of revenue to government.			
Application of the law	Uncertain, ambiguous law. No effort in helping to develop certainty and clarity in the law. Numerous linkages to domestic and international laws producing complexity. Novel applications of the law.			

Process 2

	Moderate	Low	Trivial	Criteria
		→	<p>Straightforward business group structure and transactions.</p> <p>Low volatility of industry/business activity.</p> <p>Commercially realistic business arrangements.</p>	Business and transactions
		→	<p>Limited international activity. No use of tax havens or activity in preferential tax regimes.</p> <p>No international aggressive tax planning activities.</p>	Globalisation
		→	<p>Highly cooperative approach. ATO contacts constructive.</p> <p>No pattern of aggressive tax planning.</p> <p>Strong commitment to compliance.</p> <p>Presence of self-regulatory approaches (e.g. APA).</p>	Attitude
		→	<p>High integrity compliance system in place.</p> <p>Quality assurance and risk management processes working.</p> <p>Good governance.</p> <p>Documentation accurate, contemporaneous, complete and reliable.</p> <p>High professionalism of corporate tax staff and advisors.</p>	Systems of compliance
		→	<p>Little impact on community confidence.</p> <p>Little potential for damage to tax system integrity.</p>	Perceptions of stakeholders
		→	<p>Low impact on revenue.</p> <p>Small difference in tax revenue between ATO view and the taxpayer's.</p> <p>Predictable pattern of revenue to government.</p>	Materiality
		→	<p>Clear, unambiguous law.</p> <p>Feedback to ATO where flaws in the law are identified.</p> <p>Few linkages to other domestic or international law that, combined, produce complexity.</p> <p>No novel applications of the law.</p>	Application of the law

Each risk criterion in Table 3 includes examples of what compliance looks like for the extreme and trivial levels of risk. These examples also illustrate what are referred to as the structural and behavioural drivers of risk.

Structural drivers impact on the large business environment and have an influence which those businesses cannot control, for example a change in interest rates. Behavioural drivers influence the decision-making processes, affecting how a business might change its activities to take advantage of changes in the business or regulatory environment.

Risks can be assessed on the basis of their likelihood of occurring and the consequences to the tax system if they did occur. The assessments are then brought together through the overall risk rating.

The importance of the risk criteria will vary. Each criterion fits together as part of a network that provides an accurate basis on which to build sound hypotheses about taxpayer behaviour. Professional judgement is needed by tax administrators in carrying out an assessment and developing a hypothesis that fits the pattern of the preliminary risk assessment. This risk assessment and hypothesis will be discussed and tested with the taxpayer as part of the process of refining the hypothesis (as the basis of further compliance activity).

The ATO's aim is to focus its risk management approach more toward the management of strategic risks rather than individual risk issues. In this way it can identify and apply solutions to the underlying causes of risks rather than treating the symptoms in an isolated manner.

Large business can play a key role in this process. Outcomes need to be identified as part of producing a compliance strategy that has a clear purpose and direction, and meets the needs of both the ATO and large business.

It is important that there is a focus on the most relevant, material tax issues. In practical terms, the ATO will use hypotheses to focus thinking on the most significant issues. An hypothesis is an assertion proposing an explanation for particular facts, events or issues. It helps make sense of any information gained and provides a focal point for discussion and testing. The testing of the hypothesis provides the foundation for designing and implementing further activity.

The hypothesis is tested through a preliminary review which seeks to determine the scope of any problems, helping to refine the hypothesis and determine the extent and nature of future actions. The preliminary review is not an audit. It involves a quick, limited review with a business. In some cases, it might use small samples as a means of testing the accuracy and refining the hypothesis. In other cases, a discussion or interview might be sufficient to test and refine the hypothesis. The extent of verification will depend on the issues involved and the risk profile of the business. Verifying the hypothesis will help identify issues that require further action, and what that action might be, before committing more taxpayer or ATO resources. The ATO will ensure that the level of verification fits with the business' overall risk level. This keeps intrusion to a minimum and encourages the business to assist with the verification process.

Process 2

It is critical that an effective relationship develops between the ATO and large business. An effective relationship is the best basis on which to build the cooperation needed to test the hypothesis, and develop the desired outcomes that will drive further compliance activities.

Key principles for Process 2 are:

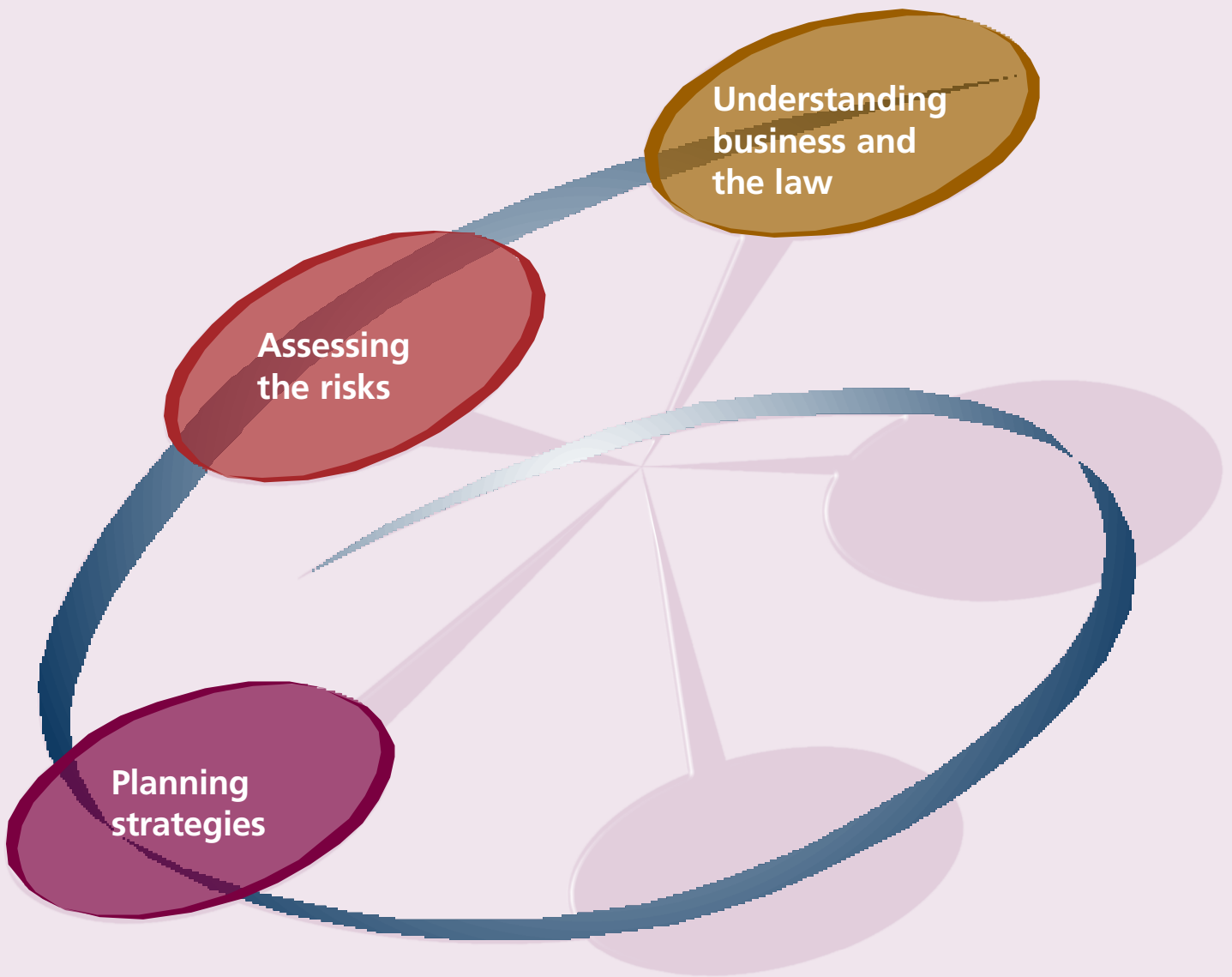
- Understanding and managing the relationship between the ATO and large business provides the most effective environment in which to assess risks, to develop desired outcomes and to test hypotheses.
- Using up-to-date, real-time information allows both parties to identify and communicate timely solutions.
- Risk assessment provides a pathway to encourage the ATO and large business to move from enforcement activities to cooperative, self-regulatory approaches.
- Having diverse strategies to monitor and treat the risks across the taxpayer spectrum provides the most appropriate, cost-effective means of managing those risks.

What does this mean for large business?

Involving large business early in the risk assessment process allows large business to:

- Profile their own compliance risk from the seven risk criteria.
- Review and refine a hypothesis before compliance action is taken.
- Develop desired outcomes that will help focus future compliance activity.

Process 3



Planning strategies

Good planning builds the most appropriate strategies for large business and the ATO to meet compliance objectives. Compliance strategies must be appropriate for the risk profile from Processes 1 and 2, and must focus on desired outcomes.

Good strategies:

- Increase the ATO's understanding of large business behaviour, the market and the environment.
- Reflect the risk assessment, the desired outcomes and the tested hypothesis.
- Identify opportunities to address deficiencies in the tax system where they have been found, and seek to apply solutions across wider groups of businesses.
- Are cost-effective for the ATO and minimise costs for large business.

The Cooperative Compliance Model draws on the notion of movement between a range of compliance activities, shifting from cooperation and self-regulation to active enforcement as required. The ATO's preference is to work cooperatively, but cooperation is not a rule. Although the ATO believes there are few benefits for a large business to escalate to enforcement options, such an escalation will occur where lower-level self-regulatory options have not been implemented. Generally, these movements will be proportional to the compliance issues involved. In some cases, escalation could be more rapid, for example, where there is evidence of a criminal offence or aggressive tax planning.

Planning the best mix of compliance strategies allows the ATO to consider the range of options available along the compliance pyramid, and to co-design with a taxpayer the best strategies for moving towards self-regulation. Taxpayers can, and should, be given the opportunity to return to the lower levels of the compliance pyramid as their willingness to work in a self-regulatory manner increases or their risk level decreases.

The compliance pyramid implicitly asks practical questions: What actions would lead to an escalation to more enforcement related options? What actions would return a taxpayer to lower levels of the compliance pyramid?

Just where to start on the compliance pyramid is determined through the understanding of business and the law. This is emphasised in the earlier processes. The ATO and large business need to ensure a strong cooperative relationship exists, so that misinterpretations and missing information does not lead to inappropriate strategies or compliance methods being used.

Examples of some compliance products or options are given in Table 4. This list is not exhaustive and is likely to expand as the Cooperative Compliance Model is more widely implemented and best practices are developed. Large business can work with the ATO to develop and implement new products which expand the cooperative approach, meeting the needs of the ATO and large business.

Process 3

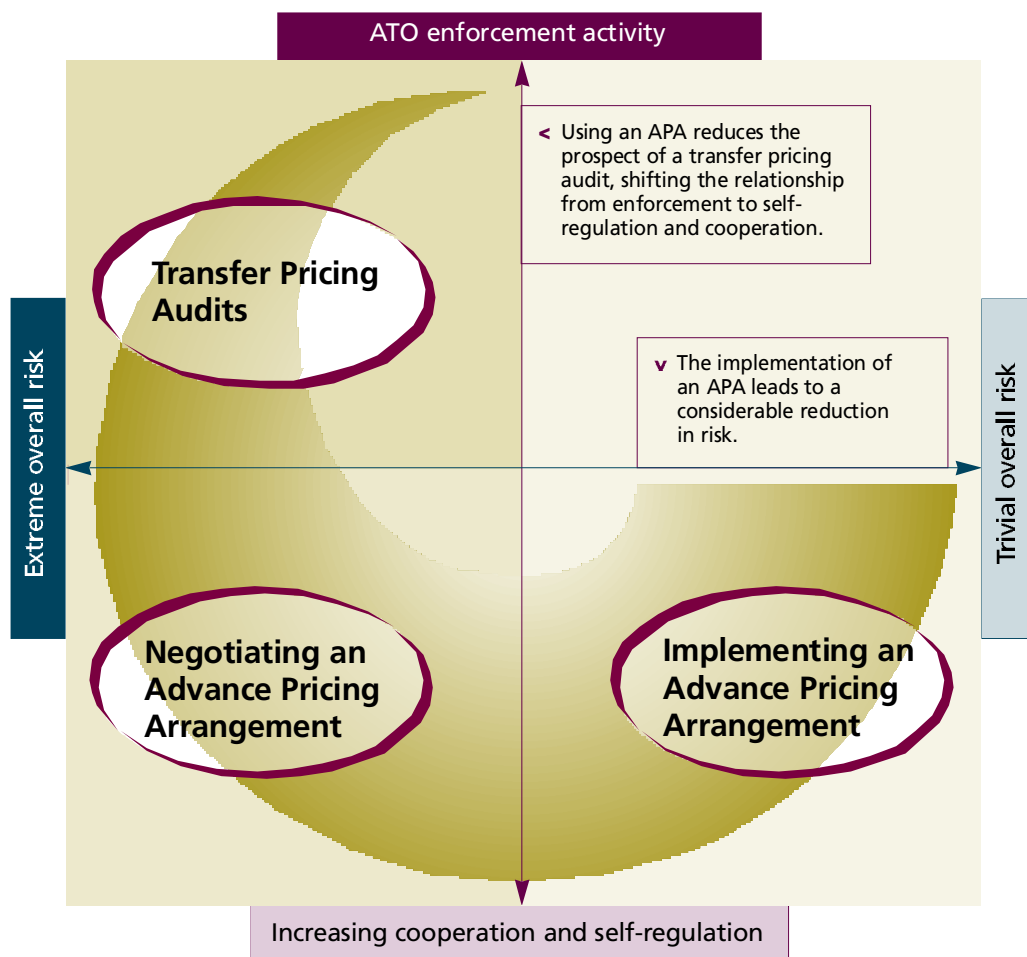
Table 4 Examples of ATO business compliance products

Compliance Product	Comment
Enforcement options	
Full audit	Comprehensive examination to ensure substantial compliance by major entrepreneurial groups, by major large corporations, in specialised industries, or in identified revenue risk areas. Limited to those businesses posing the greatest risk.
Specific issue audit	An examination of a limited number of specific issues for one business, for a group of businesses, or as part of a project which is focussing on a specific issue.
Roll-over audit	A follow-up on issues that emerged during a previous audit.
Assisted self-regulation	
Pre-lodgement audit	An examination of a taxpayer's affairs for the period in which the next tax return is to be lodged.
Advance Pricing Arrangement (APA)	Business has an agreement with the ATO on the future application of the arm's length principle in their international dealings with related parties. The ATO and the business agree on a transfer pricing methodology which results in an appropriate allocation of income and expenses between related parties.
New legislation/ ruling review	A review to determine the level of understanding and compliance with new legislation and rulings.
Test case	Litigation undertaken by the ATO where the interpretation of the law can be tested and clarified in the courts for the benefit of business in the wider taxation system.
Key Client Manager	ATO officer assigned to a large corporation to provide a direct link to resolve administrative issues that arise during the relationship.
Self-regulation	
Public/Private Rulings	Technical advice program to clarify and communicate the law. Private rulings relate to circumstances raised by business. Public rulings impact on a wider group of businesses in the community.
New/amended legislation	Designing and improving the legal structure to give effect to government policy or remove deficiencies in the law and strengthen its operation.
Industry Watching Briefs	Surveying an industry where risk assessment indicates a need for intelligence.
Tax Strategy Review	A short risk assessment review of a business' current tax policies, strategies and procedures. It is designed to indicate the likely level of substantial compliance, and has a more strategic rather than transactional focus.
Corporate Managed Review	A direct mail exercise where a business reviews its systems and processes against given parameters and expectations on a pro-forma, and identifies deficiencies and how they are being resolved.

The preference of the ATO and large business is to minimise confrontation and create a working relationship that minimises costs, resolves compliance problems quickly and demonstrates to the community the contribution that large business makes.

To make this preference a reality, it is necessary to shift away from enforcement activities to self-regulation options that produce and maintain lower tax compliance risks. For example, an Advance Pricing Arrangement (APA) decreases the need for a transfer pricing audit, thus shifting the activity from enforcement to self-regulation. The successful implementation of the APA reduces risk considerably (see Figure 3). Similar outcomes are achieved by developing and improving the law through such means as tax rulings, test cases and changes to legislation.

Figure 3 A transfer pricing example of shifting from enforcement to self-regulation and reducing risk.



Process 3

If further action is taken at the end of a preliminary review, as outlined in Process 2, a business should be given the opportunity to improve their compliance by taking corrective action themselves through self-regulation, with appropriate verification by the ATO. This involvement will differ depending on the nature of the corrective action needed and the number of taxpayers involved.

If, for example, a whole-of-market level is used, a business might contribute through membership of a project team. If the corrective action involves deficiencies in the law, a business could assist in developing options for improving that law.

There is a relationship between the escalation approach and risk levels. At lower risk levels, the use of self-regulation with verification will become a routine part of the ATO's compliance strategies. At higher risk levels, the ATO will consider opportunities to use self-regulation with verification before selecting enforcement activities. The ATO and corporate taxpayers can consider how a move down to self-regulatory activities can be achieved.

Useful assisted self-regulatory products for domestic compliance could include a domestic version of the Advance Pricing Arrangement (APA) and the Corporate Managed Review (CMR).

Advance Pricing Arrangements have been used to reduce risks significantly in relation to transfer pricing issues. The APA takes a cooperative approach to transfer pricing, working with a taxpayer to reduce the prospect of intensive and time-consuming audits. The APA achieves agreement on the operating relationship and practice at the start, unlike many other products where the relationship and practices are examined after conflict has occurred. The APA locks in compliance benefits over a longer period. The APA provides a practical framework to develop a domestic version where an economic group approach is preferred and a significant reduction in risk levels is needed.

Corporate Managed Reviews are a direct-mail self-regulatory device. Corporate managers self manage their compliance on particular tax issues by reviewing their systems and processes against parameters and expectations that relate to those issues. Verification is through a pro-forma indicating that the review has been undertaken, identifying deficiencies and outlining how these are being resolved. A small sample of field assurance visits can also be used for verification purposes. The CMR might be used where the client's risk level is at a moderate level, or a focus on a few specific issues is warranted as a result of the knowledge gained in Processes 1 and 2.

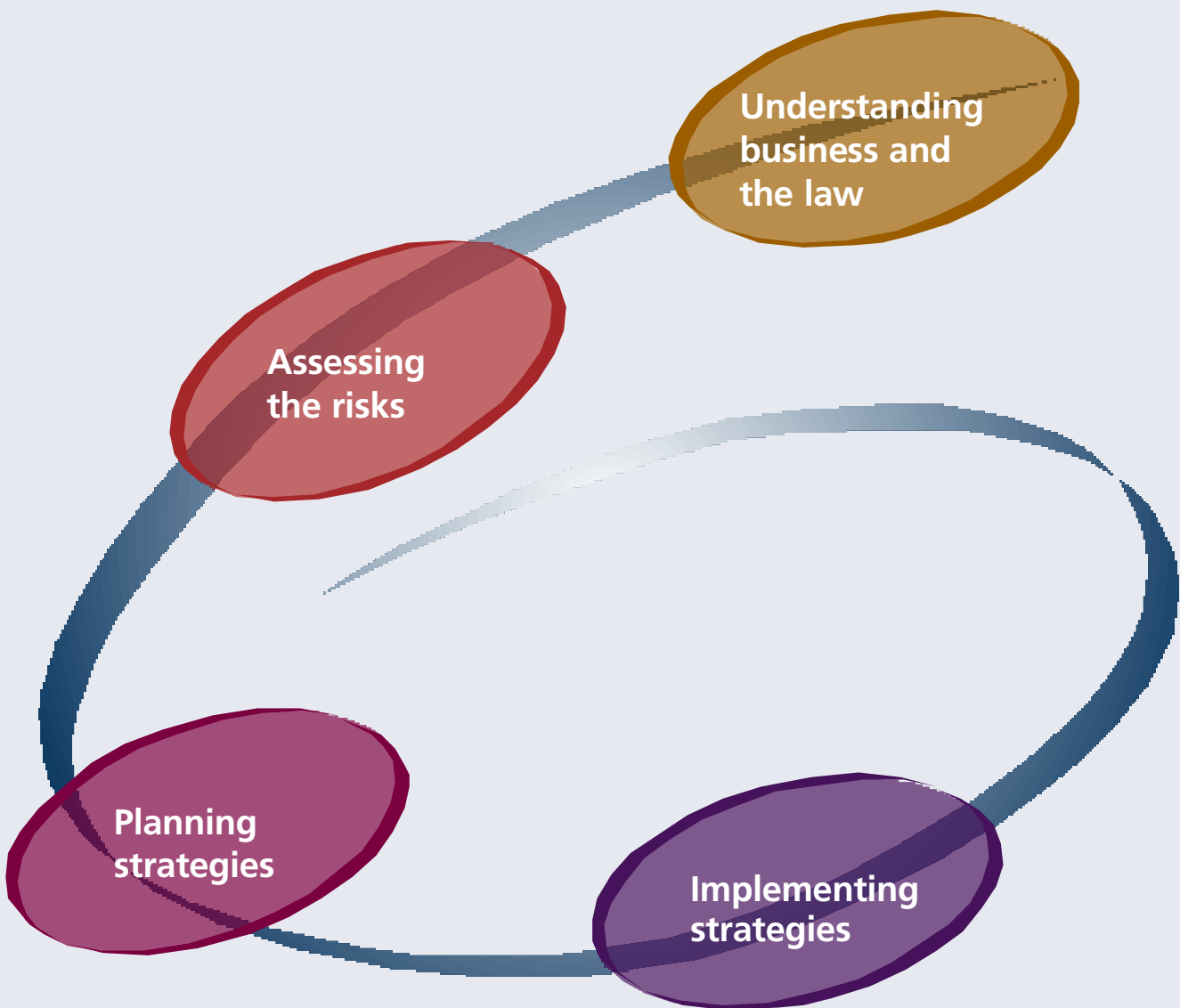
Key principles for Process 3 are:

- Building cooperation with large business as a means of assuring compliance and encouraging self-regulatory approaches, with appropriate verification, in preference to enforcement options.
- Achieving up to date, real-time compliance and drawing from a wide range of methods.
- Focussing on outcomes that provide a coherent path to assuring compliance.
- Devising strategies with the versatility to either escalate to more active enforcement options, or to adopt cooperative and self-regulatory options as risk levels decline and behaviour changes.

What does this mean for large business?

Planning strategies within the Model provides large business with an opportunity to work up front with the ATO to agree on the desired compliance relationship.

Process 4



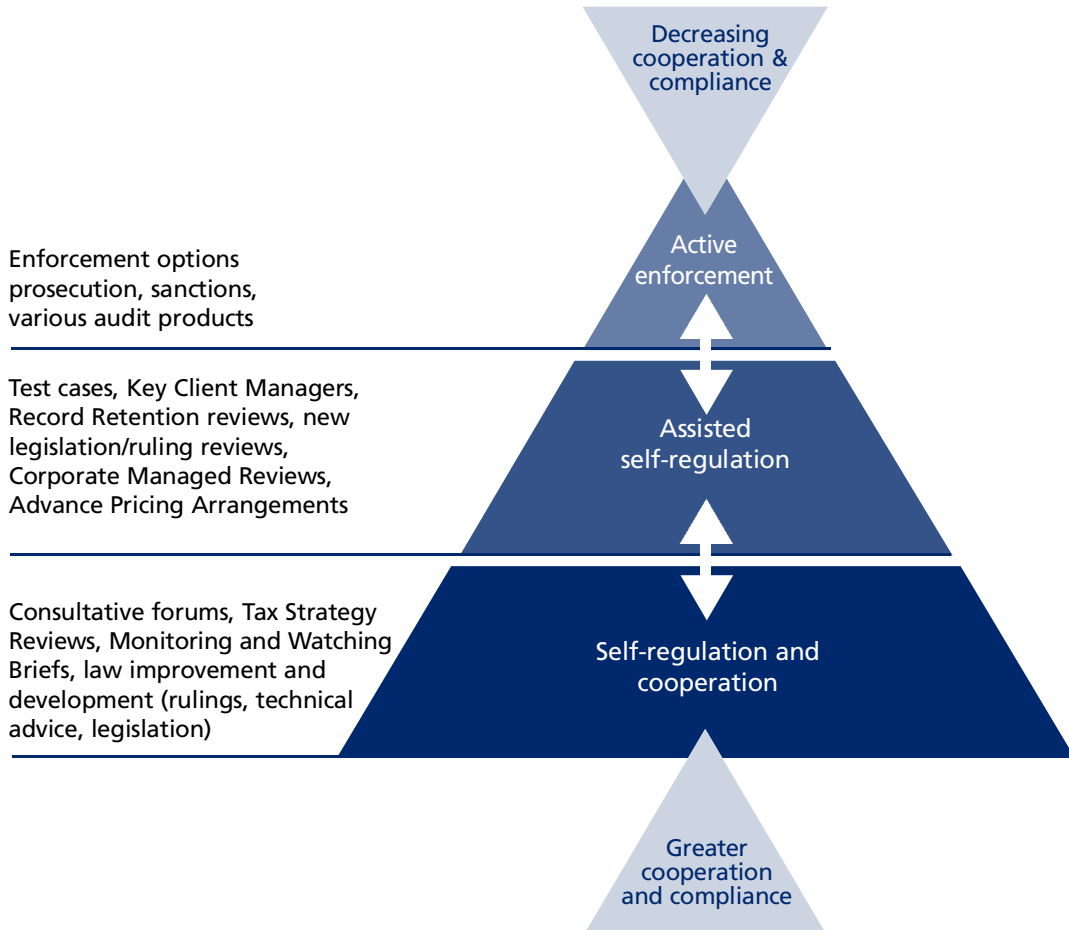
Implementing strategies

Implementation is a core component of the Cooperative Compliance Model and represents the culmination of the ATO's understanding of large business, risk assessment and strategy development. It is the most visible and direct means of the ATO managing its relationship with large business and demonstrating its professionalism and effectiveness in ensuring compliance.

What is learnt from our implementation activities increases our understanding of large business and the law. Recognition of the importance of the experiences of people underscores the need to have both formal and informal feedback throughout the processes of the Model.

Figure 4 illustrates a hierarchy of methods based on the Cooperative Compliance Model categories.

Figure 4 Using the compliance pyramid – examples of products within the Compliance Model hierarchy



Process 4

There are a wide range of possible compliance methods that can be used to manage corporate compliance. These include litigation, technical advice, field work, business intelligence and business analysis.

For all options and strategies, the expectations from both the ATO and large business are:

- Professionalism in all ATO compliance work, and in its responsibilities under the law and to the community, including integrity and excellence in knowing, applying and improving tax law.
- Project and case management methodologies which articulate the issues and actions to achieve satisfactory and timely completion, including milestones, risk assessment details and hypotheses, and escalatory and de-escalatory options.
- Responsiveness to new risks, new information and better ways of managing business compliance.
- Deficiencies in the system being addressed where opportunities are identified, and the solutions are applied across wider groups of businesses.
- Processes that assure the quality of all ATO compliance work, and demonstrate that quality.

The cultures of the ATO and large business will influence the success of the Cooperative Compliance Model. The ATO's aim is to identify cultural gaps and develop strategies to close those gaps. These strategies will maximise the potential for both parties to move their practices and behaviour toward cooperation and self-regulation.

Key principles for Process 4 are:

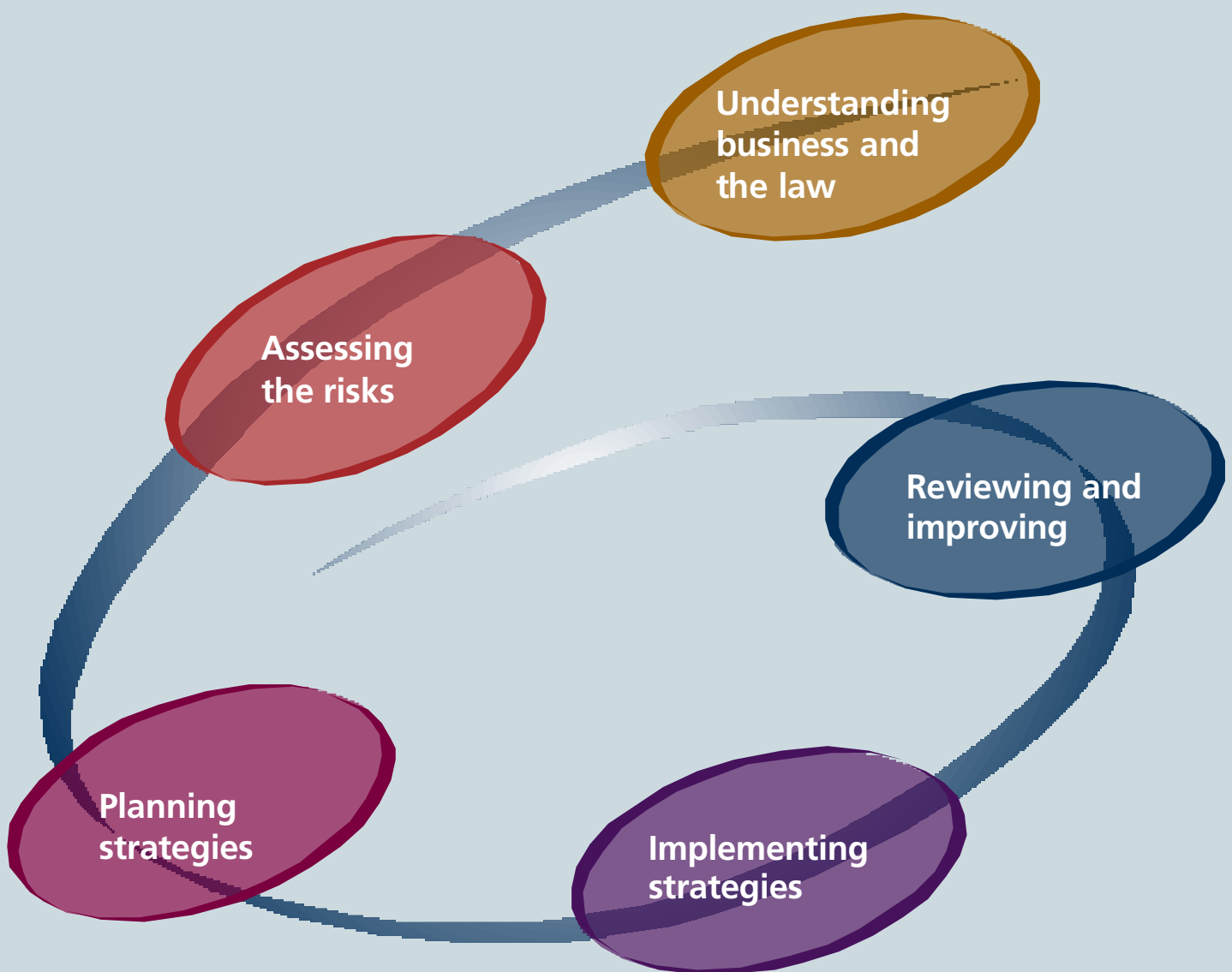
- Knowing the desired outcomes and the likely impacts of the compliance strategies and methods used.
- Applying the law professionally.
- Adapting to new issues and improving implementation on an on-going basis.
- Building relationships to manage compliance, valuing cooperation and being able to move up or down the compliance pyramid as needed.
- Addressing the underlying causes of compliance problems and applying cost-effective solutions to benefit large business, the ATO and the community.

What does this mean for large business?

Implementing cooperative compliance strategies offers large business the following advantages:

- A greater likelihood that self-regulatory options will be used or offered to improve and manage compliance.
- Where compliance is improving, business can anticipate a movement down the compliance pyramid to self-regulatory options (either with or without the assistance of the ATO).
- Where compliance is not improving, escalation up the compliance pyramid to other compliance options will occur.
- Movements up or down the compliance pyramid will be proportional to the changing risk level.

Process 5



Reviewing and improving

It is essential that the impact of compliance strategies, the methods used and the Cooperative Compliance Model's operation and performance are monitored effectively. What the ATO and business learns will provide a foundation to build better compliance processes and strategies, and adapt the Model to meet changes in business and the wider environment.

Key elements of Process 5 include:

- Measuring and managing performance

Table 5 lists ten performance areas. These are sound criteria which should be used as a guide to developing measures of how well the Cooperative Compliance Model is being applied at particular application levels.

- Communicating what is learnt

The impact of compliance activities needs to be understood by the ATO and large business. A dialogue with the business community and others involved in the tax system will provide different perspectives and test assumptions about the Model. This may not always produce consensus, but it should assist in understanding the diversity of views and the positions taken.

- Addressing deficiencies

Effective monitoring will reveal deficiencies in the system that need to be addressed and provide insights that improve the law as well as ATO strategies and methods. Such insights will enable the ATO to adapt the model and its compliance practices to changing conditions.

Process 5

Table 5 Cooperative Compliance Model performance areas

<p>Efficient</p> <ol style="list-style-type: none"> 1. Minimising compliance costs 2. Using ATO resources efficiently 3. Sustainability 	<p>Compliance costs are minimised to help large business voluntarily comply with their obligations.</p> <p>ATO resources are efficiently used – the right people in the right jobs at the right time. Focusing on the important issues and working in a planned manner.</p> <p>The Model is able to accommodate successive change and emerging risks within its main operations, key elements and strategic priorities.</p>
<p>Effective</p> <ol style="list-style-type: none"> 4. Improving voluntary compliance 5. Using intelligence effectively 6. Improving the law 7. Addressing deficiencies in the tax system 	<p>Activities facilitate and lock in compliance behaviour for the future and build appropriate relationships that enhance cooperation and self-regulatory approaches.</p> <p>The Model ensures access to real time strategic intelligence and timely and appropriate responses to modified new risks.</p> <p>The Model improves legislation and policy development, strengthening the feedback loops between policy, legislative and administrative processes.</p> <p>Strategic insights gained enable the ATO to address systemic deficiencies in the tax system.</p>
<p>Quality</p> <ol style="list-style-type: none"> 8. Generating community confidence 9. Applying Taxpayers' Charter principles 10. Building cooperative relationships 	<p>The increased transparency of our compliance approaches demonstrates that businesses are treated equitably and that the ATO is addressing non-compliance.</p> <p>Businesses receive fair, professional and consistent treatment in their dealings with the ATO.</p> <p>The ATO works with large business and other stakeholders to co-design solutions that meet their needs without compromising the law and community.</p>

Achieving good quality measurement systems is not easy, as traditional measurement and evaluation approaches do not often reflect emerging knowledge and strategic perspectives.

The key principles for an effective ATO measurement system to fit the Cooperative Compliance Model are:

- Using the insights gained to encourage learning, improve performance and maintain a dialogue with large business and other stakeholders.
- Having a contemporary and flexible focus that monitors performance from different perspectives.
- Identifying the most cost-effective approaches.

What does this mean for large business?

Large businesses can participate in testing the compliance methods, developing better approaches to compliance and improving the Model's practical application.

