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Small business income tax gap

How we estimate and reduce the small business income tax gap for 2022–23.

Published 3 November 2025

Latest estimate and trends for small business income gap



Compare the 2022–23 small business income gap with trends from previous years.

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Latest estimate and trends for small business income gap

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The 2022–23 small business income tax gap

For 2022–23 we estimate a net small business income tax gap of \$27.2 billion or 17.4%. This means we estimate around 83% of the total theoretical tax will be paid. This gap forms part of our overall tax performance program. This estimate is preliminary and will be revised when further data is available.

Small business population

The small business population comprises a diverse range of structures and operations. It covers businesses with a turnover of up to \$10 million.

Small business operating structures include:

- companies
- sole traders (individuals carrying on business in their own name)
- trusts
- partnerships.

The taxation of small business differs depending on the structure of the business. For example, the profit made by trusts and partnerships will generally be taxed in the hands of the beneficiary or partner, rather than the entity.

When calculating the income tax gap, our primary focus is on entities that have an income tax obligation. To estimate this tax gap, we estimate separate tax gaps for:

- small companies: companies with a turnover up to \$10 million
- individuals in business: individuals associated with small business entities including partnerships, trusts and companies AND sole traders earning business income up to \$10 million.

The published tax gap estimate is a combination of these two components. The small business income tax gap forms part of our overall tax performance program. Find out more about the **concept of tax gaps and the latest gap available**.

About the estimate

The estimate for the 2022–23 small business income tax gap is preliminary and will be revised when further data is available.

This estimate is based on a partially completed sample of 1,380 randomly selected cases. The estimate will be updated next year when the remaining cases are completed, which will give us a more informed and reliable estimate based on approximately 2,000 case outcomes.

We have also revised the estimate for 2021–22 (first published in the 2024 Annual Report as a preliminary estimate) using additional case outcomes. The revised estimate has increased when compared to the preliminary estimate, up from 12.6% to 15.9%. Table 1 shows the latest series of estimates.

As the small business population grows, the dollar value of the tax gap will generally increase, even if levels of compliance remains steady. The net tax gap as a percentage is a most meaningful measure of tax performance as it accounts for growth in the population.

Table 1 shows:

- We are seeing the small business income tax gap increase in both 2020-21 and again in 2021-22. Our preliminary estimate for 2022–23 suggests that this trend will continue.
- Growth in the small business taxpayer population and economic growth contribute to the increase in the theoretical income tax liability for small businesses.

- The expected tax collections have not kept pace with the amount owed (theoretical liability), reflecting higher levels of non-compliance, which has resulted in an increase in the net gap percentage.


More detailed information is available to explain the behaviours contributing to the tax gap as observed in the small business random enquiry program.

Table 1: Income tax gap – small business income tax group 2022–23

Element	2017–18	2018–19	2019–20	2020–21
Population (m)	4.94	5.10	5.20	5.44
Gross gap (\$m)	13,336	16,229	15,420	19,314
Amendments (\$m)	970	962	793	931
Net gap (\$m)	12,365	15,267	14,626	18,383
Expected Collections (\$m)	85,869	88,262	90,372	103,904
Theoretical liability (\$m)	98,235	103,529	104,998	122,288
Gross gap (%)	13.6%	15.7%	14.7%	15.8%
Net gap (%)	12.6%	14.7%	13.9%	15.0%

Figure 1 displays the gross and net gap for small businesses as a percentage over the same period, the dotted line between 2021–22 and 2022–23 reflects the fact that this estimate is preliminary.

Figure 1: Gross and net tax gap percentages, 2017–18 to 2022–23

 The gross and net gap in percentage terms as outlined in Table 1.

Note: The estimate for 2022–23 is preliminary and subject to revision.

Tax gap components


The main components driving the small business income tax gap are:

- omitted income
- over-claimed deductions
- people outside the tax system, for example, cash-only businesses operating without an Australian business number (ABN)
- non-pursuable debt, such as debt that is uneconomic for us to pursue. This is most "self-acknowledged" amounts owing, for example, amounts of tax disclosed on a BAS, which the taxpayer is unable to pay. Only a relatively small component represents non-pursuable Commissioner-raised debt, i.e., from an amended assessment.

The extent to which these components impact the tax gap varies depending on the segment of the population.


The following figures split the gross gap by population and the main drivers of non-compliance for each of them.

Figure 2: Small companies

 As a proportion of the small companies gross gap, 49% is from omitted income, 48% is from overclaimed deductions, and 3% is from non-pursuable debt.


For the companies component of the gap, omission of income accounts for about half of the overall gap (49%). Over-claimed business deductions represent nearly all the remainder of the gap (48%).

Figure 3: Individuals in small business

 As a proportion of the individuals in business gross gap, 71% is from omitted income, 20% is from overclaimed deductions, 8% is from people outside the system, and 1% is from non-pursuable debt.

For the individuals in small business component, the main driver of the gross gap is the omission of income (71%). Over-claimed deductions form 20% of the individuals in business gap (20%). 8% of the individuals in small business gap relates to people operating outside of the tax system. Non-pursuable debt forms a negligible part of the gap.

Figure 4: Combined small business

 As a proportion of the combined small business gross gap, 67% is from omitted income, 25% is from overclaimed deductions, 7% is from people outside the system, and 1% is from non-pursuable debt.

The final combined view shows the overall influence of omitted income on the gross gap (67%). 25% of the gap is caused by over-claimed deductions and 7% coming from people operating outside the tax system. These findings are similar to those published in 2024.

Findings from the random enquiry program

Through the **small business random enquiry program**, we check the income tax affairs of randomly selected taxpayers for the relevant year. This helps us calculate the tax gap estimate and identify the most common issues and behaviours driving the gap.

Our refreshed 2021–22 estimate is based on the examination of 1,928 taxpayer lodgments, conducted across a sample representative of the 2019–20, 2020–21 and 2021–22 small business populations.

As the 2022–23 random enquiry program is still underway, the preliminary estimate for 2022–23 is based on the examinations from the 2020–21 and 2021–22 years, used in conjunction with lodgment data from 2022–23. This estimate will be updated with outcomes from 2022–23 when this data is available.

Our observations highlight 4 key areas that require ongoing attention:

- continuing to address **shadow economy** behaviour (deliberate attempts to avoid paying the right tax)
- continuing to provide education and support to ensure small businesses are '**getting it right**'

- providing clear guidance to help small businesses correctly apply the law to their circumstances
- digitalising the small business tax experience to reduce compliance costs, improve certainty, and make it easier to meet tax obligations.

Small business behaviours observed

Most taxpayers reviewed in the sample reported correctly or were considered to have genuinely attempted to do so – however there has been a decrease in small business taxpayers getting it right in our most recent random sample.

In our sample, we broadly observed small businesses getting it wrong in one of 4 ways:

- making mistakes due to misunderstanding tax obligations
- making errors because of poor record keeping
- not declaring all business income
- making incorrect claims, such as claiming private expenses as a business expense.

Our sample includes individuals in business who may also have income and expenses from sources outside their business activities.

Errors in reporting these non-business items contribute to the small business income tax gap. Common examples include:

- underreporting salary and wages from an unrelated entity
- underreporting passive income from rental properties, gross interest and dividends
- miscalculating and underreporting capital gains
- claiming personal expenses as work-related deductions, including car, clothing, travel and gifts or donations.

Shadow economy behaviour observed

In 2022–23, the shadow economy contributed an estimated \$17.1 billion to the small business income tax gap, or over 60% of the gross gap. \$14.2 billion of this is associated with deliberate underreporting of income and over-claiming of deductions as observed through the random enquiry program. The remainder is

made up of an additional uplift to fully capture the effect of hidden wages and people operating outside the tax system.

This significant impact of shadow economy behaviour is largely attributable to around 6% of taxpayers in our random sample, who made deliberate attempts to avoid paying the right amount of tax.

For more information see [accounting for the shadow economy](#).


Tax practitioner behaviours observed

Most small businesses engage a tax professional to help prepare and lodge their returns, but the nature of these relationships vary significantly. We observed that small businesses who reported correctly had more regular contact with a tax professional.

We also identified instances where tax professionals:

- made mistakes because of bookkeeping and accounting system errors
- provided incorrect advice
- failed to show reasonable care.

In approximately 40% of cases where there was evidence of shadow economy behaviour, the tax agent contributed either directly through deliberate actions or indirectly by not taking reasonable care in checking claims made.

For previously published tax gap figures, see [Australian Tax Gaps - Data.gov.au](#) 

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ATO action to address the small business income gap

How we support our clients to meet their compliance obligations.

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Our strategies and approaches

In 2022-23 the year of our latest tax gap estimate, some of our key focus areas to improve small business tax performance included:

- providing continued support to small businesses and their trusted advisors to help them report correctly through public advice, letter campaigns and online learning
- firm compliance action to address a range of shadow economy activities such as omitted income, sales suppression, unexplained wealth, sham contracting, activities targeting high risk industries and behaviours
- strengthening our controls and protecting the system and community against fraud
- addressing growing collectable debt – for those who were unwilling to work with us, we took strong and deliberate action as we increased our debt collection activities
- developing and implementing a digitalised tax experience for small business where tax naturally follows business performance and processes – this work reflects our ambition to reduce compliance costs, improve certainty, and make it easier for small businesses to meet their tax obligations from the start.

Findings from the **Small business random enquiry program** continue to support the application of differentiated approaches to:

- help small businesses meet their tax and super obligations
- promote fairness across the system, and
- detect and address shadow economy activity.

Helping small businesses to report correctly

Most small business owners want to do the right thing – but navigating tax and super responsibilities while running a business can be challenging.

Through our 'getting it right' campaign, we support small businesses to get their tax and super obligations right by sharing what attracts our

attention and the consequences of operating outside the system.

To make managing tax and super easier, we have developed **tools and services** designed with small businesses in mind.

We want to keep pace with the rapid evolution of technology and the growing use of digital solutions in everyday business operations. As more businesses rely on digital tools to manage their finances, operations and interactions, we are evolving alongside to deliver smarter, more streamlined services.

By harnessing the increasing availability of data, focusing on digital-first interactions and co-designing solutions with the community, we work to:

- create a digitalised tax experience that better aligns with natural business processes and systems
- reduce compliance costs
- help prevent debt
- give small businesses the clarity and confidence to get it right from the start.

Taxpayers avoiding their obligations

We are seeing a concerning increase in the tax gap due to deliberate tax avoidance by some small business taxpayers. This behaviour – known as **shadow economy** activity – accounts for more than 60% of the gross small business income tax gap.

While most small businesses do the right thing, a minority deliberately do not comply with their obligations. That's why we maintain a strong and targeted focus on those who deliberately under-report income, overclaim expenses or operate outside the system.

To strengthen this effort, the government extended the **ATO Shadow Economy Compliance Program** through to 30 June 2028, ensuring continued action against those undermining the integrity of our tax system.

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Methodology for estimating small business income gap

What method we use to estimate the small business income tax gap.

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The bottom-up method

We use a random enquiry program bottom-up method to estimate the small business tax gap. This comprises an estimate of the income tax gap for individuals in business and an estimate for small companies. These are combined to give us the overall small business income tax gap.

We use the same overall steps, but because they have different characteristics, we calculate them separately. We step through the method below and combine the estimates in Table 1.

Step 1: Estimate unreported amounts

We calculate the average amendment and amendment rate for reviewed taxpayers for each population based on sample data from up to three years. These averages are then extrapolated to the relevant population to estimate the base unreported tax liability.

To estimate people outside the system, we compare Australian Bureau of Statistics (ABS) Census of Population and Housing (Census) data with tax return data. This provides an estimate of the number of non-lodging individuals in business.

We then estimate a dollar impact, drawing on the random sample data to determine the final unreported amount.

Step 2: Estimate for non-detection (including hidden wages)

We adjust for undetected non-compliance that our audit processes may miss, to avoid understating the true tax gap. To do so, we apply uplifts based on the midpoint of international benchmarks.

We also apply an uplift for hidden wages to the individuals in business population. This is consistent with our wider program for hidden wages.

Applying uniform non-detection uplifts to the estimate would exaggerate the size of the final gap. A different uplift is applied to the deduction labels of small business tax returns.

The impact of non-detection across the tax gap is also different across the 2 populations represented in this estimate:

- individuals in business
- small companies.

Individuals in business

Within the individuals in business population, the following 3 areas require an estimate to account for non-detection:

- business income
- deductions
- hidden wages.

The uplift for business income forms the largest component of non-detection. This recognises the limitations in detecting omitted income where little or no third-party reporting systems are available.

We apply uplifts to observed results based on the midpoint of international ranges.

Non-detection of deductions in the individuals in business population is applied differently. This is because there is no incentive for taxpayers to under-claim deductions on their tax return. So the uplift for non-detection for deductions is confined to the capacity to detect errors in tax returns where deductions have been claimed.

Actual wages received by individuals in business can be difficult to validate in a random enquiry program. We used a macro estimate based on the hidden wages element used in the pay as you go (PAYG) withholding and super guarantee gap estimates.

An estimate for wages not detected in the random enquiry program and for people operating outside the system was reconciled to the hidden wages analysis undertaken in the PAYG withholding gap estimate. The result provides an estimate for hidden wages in the individuals in small business population.

Small companies

The small companies element has only 2 areas that require an estimate to account for non-detection:

- business income
- deductions.

Like individuals in business, the income non-detection uplift for small companies forms the largest component of the non-detection estimate.

We recognise limitation with detecting omitted income for small companies. This is because no, or limited, third-party reporting systems are available to compare to. We apply uplifts to observed results based on the midpoint of international ranges.

Non-detection of deductions and other issues in the small companies population is applied in the same way as individuals in small business. There is also no incentive for these taxpayers to under-claim deductions on their tax return. So the uplift for deductions non-detection focuses on the capacity to detect errors in tax returns where deductions have been claimed.

Combined impact of non-detection

Table 2 shows a summary of the combined impact of non-detection on the small business income tax gap, for the 2022–23 estimate and revisions to prior years.

Table 2: Summary of the impact of non-detection on the g: million)

Source of non-detection	2017–18	2018–19	2019–20	2020–21	2021–22

Business income	4,025	4,953	4,658	5,662	7,302
Deductions and other issues	113	138	131	211	231
Hidden wages	606	607	692	783	894
Total non-detection	4,743	5,698	5,481	6,656	8,427

Step 3: Estimate for non-pursuable debt

We add in the value of non-pursuable debt. This is debt the Commissioner of Taxation has assessed as:

- not legally recoverable
- uneconomical to pursue, or
- unable to be pursued due to another Act.

Debt trends show that it takes more than 5 years for non-pursuable amounts to crystallise for any one income year. To account for this, we add a provisional amount of non-pursuable debt to the actual amount recorded, based on historical amounts. These figures are revised as we refresh and move these estimates forward.

A revised debt methodology is under development that considers external economic factors and internal changes to provide a realistic estimate of the amount of debt that will likely never be paid.

Table 3 shows a summary of the actual and provisional amounts of non-pursuable debt.

Table 3: Summary of non-pursuable debt for small businesses

Description	2017–18	2018–19	2019–20	2020–21	2021–22
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Actual non-pursuable debt	228	166	133	135	110
Provisional non-pursuable debt	153	215	248	246	27
Total non-pursuable debt	381	381	381	381	381

Step 4: Estimate gross gap

Next, we add the results of steps 1 to 3 to arrive at the gross gap estimate. The gross gap is equal to the sum of the base unreported tax liability, non-detection, and non-pursuable debt.

Step 5: Estimate net gap

We deduct compliance outcomes and voluntary disclosure amounts (amendments) from the gross gap in step 4 to arrive at the net gap.

Given ATO compliance actions can take many years to complete, an uplift is applied to amendment amounts in later years to reflect expected final outcomes. Where actual amendment outcomes exceed this estimate, the actual amendments are used instead.

Amendments of \$100 million and above are treated as outliers and excluded from the amendments estimate. These amendments may belong to entities in other tax gap populations, such as high wealth or medium business. We will reassess their allocation in future estimates.

Step 6: Estimate the theoretical liability

The expected collections amount is calculated by adding voluntary expected collections and amendments. The net gap is added to the expected collections amount to estimate the theoretical tax liability.

Summary of estimation process

Table 4 shows the dollar value (in millions) at steps 1 to 6.2 for the individuals in business element. Steps 6.3 and 6.4 show percentage figures for the gross and net gaps.

Table 4: Applying the methodology – individuals in business

Step	Description	2017–18	2018–19	2019–20	2020–21
1.1	Estimate unreported amounts for sample and extrapolate to population (\$m)	5,467	7,193	6,636	8,470
1.2	Apply estimate for people outside the system (\$m)	1,433	1,822	1,692	1,640
2.1	Apply estimate for non-detection (excluding hidden wages) (\$m)	3,675	4,736	4,385	5,100
2.2	Apply estimate for hidden wages (\$m)	606	607	692	780
3	Add non-pursuable debt (\$m)	237	237	237	237
4	Equals gross gap (\$m)	11,419	14,595	13,643	16,247
5.1	Subtract amendments	763	741	605	720

	(\$m)				
5.2	Equals net gap (\$m)	10,655	13,854	13,038	15,519
6.1	Add expected Collections (\$m)	71,023	73,528	75,450	85,706
6.2	Equals theoretical tax liability (\$m)	81,678	87,383	88,488	101,225
6.3	Gross gap (%)	14.0	16.7	15.4	16.0
6.4	Net gap (%)	13.0	15.9	14.7	15.3

Table 5 shows the dollar value (in millions) at steps 1 to 6.2 for the small companies element. Steps 6.3 and 6.4 show percentage figures for the gross and net gaps.

Table 5: Applying the methodology – small companies element

Step	Description	2017–18	2018–19	2019–20	2020–21
1.1	Estimate unreported amounts for sample and extrapolate to population (\$m)	1,311	1,135	1,229	2,155
1.2	Apply estimate for people outside the system (\$m)	n/a	n/a	n/a	n/a

2.1	Apply estimate for non-detection (excluding hidden wages) (\$m)	463	355	404	771
2.2	Apply estimate for hidden wages (\$m)	n/a	n/a	n/a	n/a
3	Add non-pursuable debt (\$m)	144	144	144	144
4	Equals Gross gap (\$m)	1,917	1,633	1,777	3,069
5.1	Subtract amendments (\$m)	207	221	188	205
5.2	Equals Net gap (\$m)	1,710	1,413	1,589	2,864
6.1	Add Expected Collections (\$m)	14,846	14,734	14,922	18,198
6.2	Equals Theoretical tax liability (\$m)	16,556	16,146	16,510	21,062
6.3	Gross gap (%)	11.6	10.1	10.8	14.6
6.4	Net gap (%)	10.3	8.7	9.6	13.6

For more information about our research methodology, data sources and analysis, see [creating our tax gap estimates](#).

Limitations

The following caveats and limitations apply when interpreting this tax gap estimate:

- The 2023 preliminary estimate uses outcomes finalised to date from the 2021 and 2022 random enquiry program samples. We will revise the 2023 estimates with additional outcomes from the 2022 and 2023 samples.
- The 2018, 2019 and 2020 sample years were reduced due to the need to support the community during natural disasters and COVID-19.
- The precision of our estimate is limited by the sample size of the random enquiry program. By using an ongoing bundled sample, we seek to maintain suitable confidence intervals over time.
- We are working to develop non-detection estimates for random enquiry programs in the Australian environment. In the interim, we use the midpoint estimate for credible international estimates used by the United Kingdom and United States.
- Estimates for the tax impact of people outside the system are difficult to estimate. This estimate will always be subject to significant uncertainty.
- There is no external data set that has the same view of the small business population that we have.

Accounting for the shadow economy

For tax gap purposes we focus on the shadow economy definition covers activities that are productive and legal but are deliberately concealed to avoid paying taxes or complying with regulations (or both).

The shadow economy estimate within the small business income tax gap is also separated into the calculations for individuals in business, and companies. Within these 2 broad categories, there are 3 main elements:

- deliberate non-disclosure of business income and deliberate over-claiming of business deductions
- hidden wages, predominantly individuals in the population receiving cash-in-hand wages – we estimate this using a top-down model

approach drawing on random enquiry observations

- people outside the system – where we use an ABS Census comparison approach.

When analysing the reasons for non-compliance, we sought to identify aspects of behaviour that indicated a deliberate intention to hide business activity.

We added a component to the individuals in business population gap estimate that is not included in non-detection, which is to account for people outside the tax system. This element seeks to estimate the amount of omitted income from these people. To quantify this element, we assumed that the incidence and relative magnitude of income non-compliance in the random enquiry sample is also representative of people outside the system.

The tax effect of the shadow economy for small business in 2022–23 is estimated to be \$17.1 billion. The majority of this, \$14.2 billion, is associated with under-reported business income and over-claimed business deductions.

We outline the impacts of the shadow economy on the community and how we address them in **tax and small business**.

Table 6 shows a summary of the shadow economy impact on the gross tax gap. This amount has increased from 51% of the overall gross gap in 2017–18 to 61% in 2022–23. For this estimate we assume the same percentage applies to the net gap.

Element	2017–18	2018–19	2019–20	2020–21	2021–22
Hidden wages	606	607	692	783	894
People outside the system	1,433	1,822	1,692	1,646	1,563
Undisclosed business income and over-claimed	4,732	6,637	7,452	9,255	11,737

business deductions					
Total shadow economy impact	6,771	9,065	9,836	11,684	14,188

Updates to previous estimates

Each year we refresh our estimates in line with the annual report. Changes from previously published estimates occur for many reasons, including:


- improvements in methodology
- revisions to data
- additional information becoming available.

We refreshed our previous estimate to consider updates in underlying data and refinements to the methodology, so the results between years remain comparable.

The increase in the updated estimates for 2020–21 and 2021–22 is mainly due to additional completed sample cases since the previous publication.

Figure 5 shows the net gap from our current model compared to the previous estimate, done in 2024.

Figure 5: Current and previous small business net tax gap estimates, 2015–16 to 2022–23

 Our previous and current net small business income gap as outlined in Table 7.

The data is set out as a percentage in Table 7.

Table 7: Current and previous small business net tax gap estimates, 2017–18 to 2022–23

Program	2017–	2018–	2019–	2020–	2021–

year	18	19	20	21	22
2025	12.6%	14.7%	13.9%	15.0%	15.9%
2024	12.6%	14.5%	14.0%	14.6%	12.6%
2023	12.4%	14.4%	13.1%	12.8%	n/a
2022	12.6%	12.7%	11.6%	n/a	n/a
2021	11.7%	12.7%	n/a	n/a	n/a
2020	11.5%	n/a	n/a	n/a	n/a
2019	n/a	n/a	n/a	n/a	n/a

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Reliability of small business income gap estimate

How we make sure the small business income gap estimate is reliable.


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We seek feedback and advice about how we estimate the gap from our external and internal subject matter experts. Based on the advice and assessment, the reliability rating for this estimate is **medium** with a score of 17, which is unchanged from the score published in 2024.

We have stratified the sampling process to ensure it is representative of the wider population.

We engage former Deputy President of the Administrative Appeals Tribunal, Mr Stephen Frost, for further assurance. He verifies the accuracy and quality of a sample of the audit results that underpin our tax gap estimate.

Figure 6: Reliability rating scale from very low to very high – small business income tax gap

The latest small business income gap estimate is rated as Medium at 17. The rating scale is from very low (1–10), low (11–15), medium (16–20), high (21–25) to very high (26–30).

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