Australian Government
Australian Taxation Office

Findings report top 100 program

Income tax and GST, 30 June 2021

Contents

This is the third year we are publishing our findings report for the top 100 assurance program for income tax. This year for the first time we are also including insights from the top 100 Goods and Services Tax (GST) assurance program.

For income tax and GST assurance reviews completed to 30 June 2021, this report:

- outlines our key findings and observations
- explains how we apply the justified trust methodology to
  - obtain greater assurance that large public and multinational taxpayers are paying the right amount of income tax or GST, or
  - identify areas of tax risk for further action.

Top 100 engagement

The top 100 population:

- consists of public and multinational businesses and superfunds that have substantial economic activity related to Australia
- consists of the largest contributors to corporate income tax, excise, and petroleum resource rent tax (PRRT) collections
- is also some of the largest remitters of GST.

As top 100 taxpayers can have a significant impact on the health of our tax system, we engage with them on an ongoing basis to manage their compliance and assure their tax performance.

Top 100 taxpayers are initially identified based on the size of their Australian operations. Other factors we consider include income tax, GST or excise paid, and the influence the taxpayer may have on their market segment. We review and moderate the top 100 population annually.

Our engagement with top 100 taxpayers is tailored based on our understanding of the complexity of their affairs. Our understanding is informed by their size, the transparency of their engagement with us, the choices and behaviours evidenced in their tax affairs, the level of risk they exhibit, and the level of assurance we have obtained.

Note: There were 77 economic groups in the top 100 population in 2020. This number varies year-on-year and some groups have more than one taxpayer in the top 100. Accordingly, the annual number of assurance reviews in the justified trust program does not equal 100.

The justified trust program benefits top 100 taxpayers, their shareholders, other key stakeholders and the wider community.

The program:

- provides certainty about their tax outcomes and the effectiveness of their tax governance processes
- ensures boards can be confident they are aware of, and understand, the ATO’s assessment of the tax profile of their organisations, and
- provides an objective mechanism to understand how the ATO’s assessment of the tax profile of their organisation compares to their peers and others in the market.

Over the past 2 years, we have seen a significant shift in the number of taxpayers attaining justified trust (or overall high assurance) for income tax. We have also seen a positive shift in the market's perception of justified trust and the 'currency' associated with the ATO's assurance ratings is becoming highly regarded.

We cannot disclose the assurance ratings of individual taxpayers, however a number of taxpayers are now publicly disclosing their ratings in their tax transparency reports. By disclosing their assurance ratings, shareholders and the community can gain insights and confidence about the Australian tax outcomes and tax contribution of the organisation.

Feedback from taxpayers show that they are seeing the benefits of investing in the justified trust program, in particular by those achieving overall high assurance. The program has resulted in the ATO acquiring a holistic understanding of the taxpayer's business operations and financial performance, which has ongoing benefits for future reviews. Taxpayers who attained overall high assurance are generally able to experience a tangible change in the intensity of reviews under the 'Monitoring and Maintenance' approach, leading to quantifiable savings in time and compliance costs, to the benefit of both the taxpayer and the ATO.

Under the 'Monitoring and Maintenance' approach, new significant transactions and significant business changes generally continue to attract a level of intensity consistent with the justified trust principles. However, where appropriate, the ATO will tailor the engagement approach by seeking to leverage from the assurance already obtained and the ATO's high level of confidence.

Our approach

Justified trust is a concept from the Organisation for Economic Cooperation and Development (OECD).

We introduced the justified trust concept starting with the income tax affairs of the top 100 population in 2016.

The justified trust program has now reached maturity in relation to the assurance reviews of the income tax affairs for top 100 taxpayers.

Over the past few years, we have worked closely with the top 100 taxpayers with the greatest impact on the tax system to detail:

- the criticality of a good, lived, tax governance framework, and encouraging self-assessment against the ATO's 'better practices'
- the areas of their economic and tax affairs over which we have a high level of assurance
- areas where we have concerns, and how a higher level of assurance can be obtained
- how the effective tax borne (ETB) of the Australian channel is critical to the ATO's understanding of their tax risk profile (in particular, transfer pricing matters)
- our future engagement approach in their tax assurance reports (TARs).

In 2019 we expanded the justified trust program to include GST for the top 100 population.

We apply the justified trust methodology and seek to obtain assurance of four focus areas:

1. That appropriate tax risk and governance frameworks exist, and are applied in practice. This includes the design of business systems to create, capture and report transactions correctly for GST purposes.

2. That none of the specific income tax or GST risks we have flagged to the market are present.
3. That tax outcomes of atypical, new or large transactions are appropriate.
4. That we understand why the accounting and tax results vary. We analyse the various streams of economic activity and how they are treated for taxation purposes. For example, we analyse the ETB to understand whether the right amount of tax on profit from Australian-linked businesses is being recognised in Australia. We also analyse the sales, acquisitions and other data, and compare this to net GST paid.

We continue to work towards integrating our reviews, where appropriate, for income tax and GST.

This report outlines our findings for the four justified trust focus areas for income tax and GST, as well as insights from our approaches once a top 100 taxpayer attains overall high assurance for income tax.

Top 100 income tax assurance program

Overall levels of assurance

As of 30 June 2021, almost half (49%) of top 100 taxpayers have attained overall high assurance (justified trust)[1]. This means that we have obtained assurance that these taxpayers have paid the right amount of Australian income tax for the year reviewed.

The overall level of assurance is based on an objective view (having regard to objective evidence) of whether the taxpayer is considered to have paid the right amount of tax.

Ratings

We apply consistent rating categories when considering our overall level of assurance.

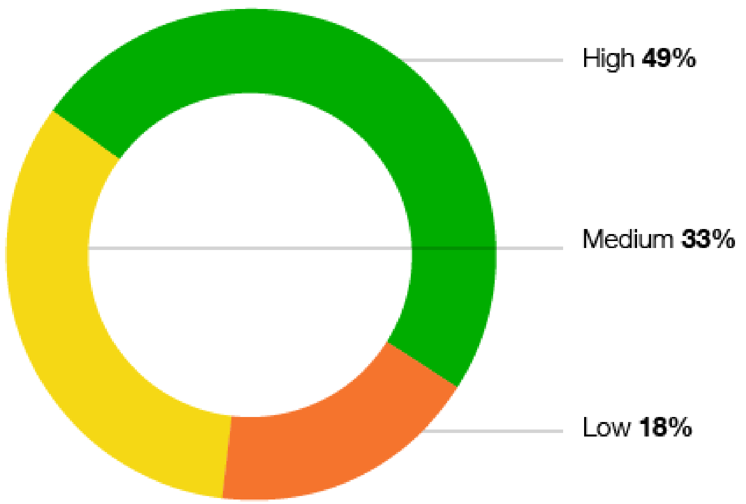
🟢	High	We obtained assurance that you paid the right amount of Australian income tax for the income year(s) reviewed. This means we are unlikely to contact you again in relation to the income year(s) reviewed unless something new comes to our attention.
🟡	Medium	We obtained assurance in relation to some but not all areas reviewed. For those areas not yet assured, further evidence and/or analysis will be required before we obtain assurance that you paid the right amount of Australian income tax for the income year(s) reviewed.

[1] This includes 3 taxpayers who attained overall high assurance prior to 30 June 2021 but the TARs were not issued prior to 30 June 2021.

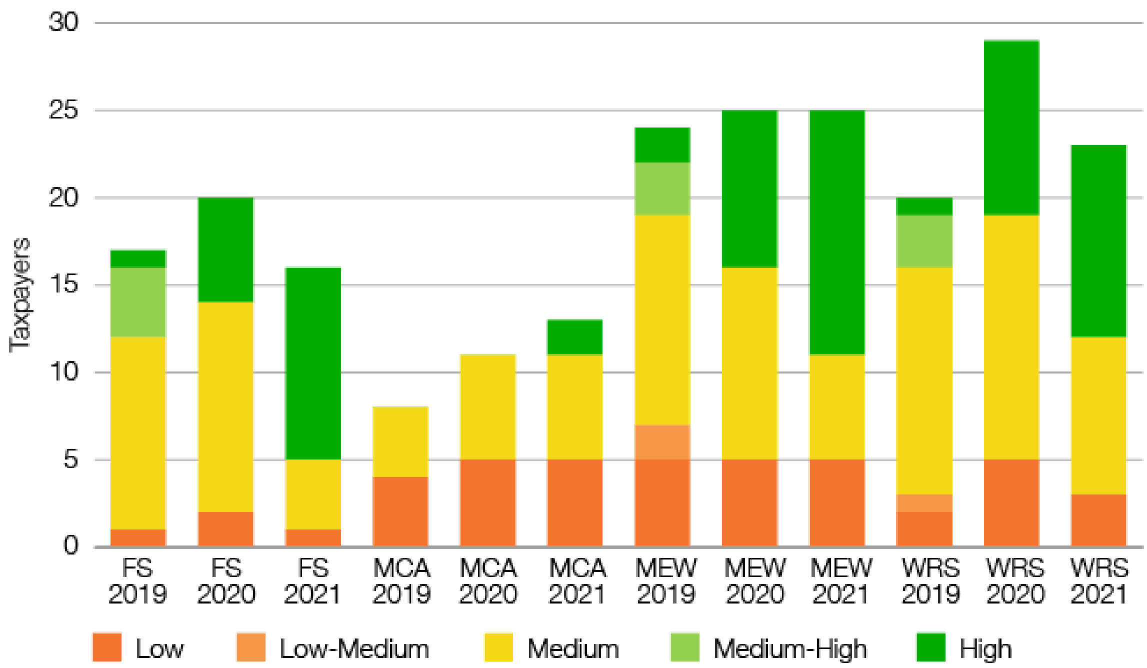
🟠	Low	We have specific concerns around your compliance with the Australian income tax laws and the amount of Australian income tax paid for the income year(s) reviewed.

The reviews completed to the end of June 2021 resulted in the following ratings:

Graph 1 – Overall assurance ratings for the last review completed[2] as of 30 June 2021



Graph 2 – Overall assurance rating for the last review completed by industry as of 30 June 2019, 30 June 2020 and 30 June 2021



[2] All outcomes data used in this report in relation to income tax is based on the last review completed which can include a standard justified trust review, 'Monitoring and Maintenance' review, Annual Compliance Arrangement (ACA) review or refreshed year review.

Note:

- These groupings align with the industry segments used by the ATO as part of the Corporate Tax Transparency Reporting except where we have amalgamated the Banking, Finance and Investment (BFI), Insurance (ISR) and Superannuation (SUP) segments into a Financial Services (FS) segment. The groupings are
  - Banking, Finance and Investment, Superfunds and Insurance (FS)
  - Manufacturing, Construction and Agriculture (MCA)
  - Mining, Energy and Water (MEW)
  - Wholesale, Retail and Services (WRS).
- The population depicted in Graph 2 comprises fewer taxpayers in the top 100 population this year relative to the prior year. This is because for the 2020-21 year we are presenting information based on the current top 100 population, whereas for prior years our figures also included taxpayers who have since exited the population.
- The medium-high and low-medium ratings are unique to the top 100 program. These ratings are not used in the top 1000 program and were only used as interim ratings in the top 100 program prior to 2020. That is, where taxpayers were close to transitioning to a higher rating. From 2020 we reverted to the three main rating categories of 'low', 'medium' and 'high' in the top 100 program, and mid-point ratings are only used in very limited circumstances.

Observations

During 2021 we saw a marked increase in the number of taxpayers achieving overall high assurance with a shift from 29% to 49%. The number of taxpayers at overall low assurance has remained relatively consistent over the past 3 years. We observed continued improvement in ratings across all industries.

We have continued to see the same two key drivers for improvement this year. Firstly, despite the impacts of COVID-19, taxpayers continued to pro-actively engage with us during the year to progress and finalise the assurance reviews. Secondly, in more cases, we saw taxpayers having a better understanding of the justified trust principles and making efforts to provide objective evidence to support a higher rating for governance. In addition, by clearly outlining in the TARs our areas of concern and how taxpayers can attain justified trust, taxpayers worked with us to address those areas of concern resulting in improvements in tax outcomes and the overall assurance ratings.

For top 100 taxpayers who have had more than one TAR issued, over 50% have increased their overall assurance rating between the first and last TAR issued.

82% of taxpayers reviewed obtained either an overall high assurance rating (49%) or an overall medium assurance rating (33%). A medium assurance rating means we obtained assurance in relation to the majority of areas reviewed but not all areas. This reflects, to some degree, the complexity of large businesses and also signals there is still more to do in some cases. Further work could include improvements by taxpayers and also further assurance activities to be completed by the ATO.

Acknowledging the complexities of tax law, taxpayers may achieve overall high assurance notwithstanding they are in dispute with the Commissioner about a particular matter, provided all other areas have achieved an appropriate assurance rating. However, if the matter being disputed relates to a material systemic issue and features elements of profit shifting or tax avoidance, or we have concerns about taxpayer behaviour, the taxpayer may not be able to achieve overall high assurance.

The top 100 population comprises our largest and most complex taxpayers, and we expected that it would take more than one year to review the entire business and attain overall high assurance. We now have almost half of top 100 taxpayers who have now attained overall high assurance (justified trust). This is a 20% increase from our last findings report in 2020 and reflects a marked increase from our first findings report in 2019 (with 6% at overall high assurance).

We continually monitor the tax affairs of the top 100 population. However, in recognition of the level of trust we have in the tax infrastructure of these high assurance taxpayers, we tailor our engagement approach to focus on maintaining our high level of confidence where possible. The nature of our engagement for the two income years following an overall high assurance rating is the ‘Monitoring and Maintenance’ approach. Under the ‘Monitoring and Maintenance’ approach, we expect taxpayers to proactively engage with us to disclose new or changed arrangements. We continue to engage regularly with taxpayers in this phase and we use our data and analytics capability to safeguard against non-disclosure.

This year, we completed 23 ‘Monitoring and Maintenance’ reviews.

To reaffirm our confidence that a taxpayer continues to pay the right amount of tax, we will conduct a refreshed justified trust review. A refreshed justified trust review involves a reassessment of the four pillars of justified trust. This year, we conducted our first refreshed justified trust review where the taxpayer was able to retain its overall high assurance rating.

We expect that we will continue to have more taxpayers attain overall high assurance and our current forecast indicates that this will increase by 8% in the coming year as more taxpayers transition from overall medium to high assurance in the 2021-22 year. This assumes that these top 100 taxpayers provide the required objective evidence to support the high assurance outcome, and we do not identify any new or further issues in the review. These improvements will primarily come from the cooperation of both the ATO and taxpayers to achieve timely completion of the planned assurance reviews for the year, and taxpayers actively addressing the areas of concern set out in the future assurance plans contained in the TARs.

For top 100 taxpayers that are not at overall high assurance, we are continuing to work closely with them to attain a higher level of assurance as part of the yearly PCR and ACA processes. However, we do not expect the number of taxpayers to achieve high assurance to ever reach 100%.

There are 18% of top 100 taxpayers at an overall low level of overall assurance, which is a slight decrease from last year (20%). This is representative of top 100 taxpayers with a higher risk profile who are typically involved in complex and numerous disputes, or where we have significant concerns around the taxpayer’s compliance with the Australian income tax laws. We will comprehensively and intensively review low assurance taxpayers, and are more likely to use audits to progress issues.

Tax risk management and governance

Tax governance framework

Tax governance is a key focus area under the justified trust methodology for large public and multinational businesses.

We consider the existence, design and operation of a tax control framework for income tax and GST focusing on the 8 controls set out in the Tax risk management and governance review guide and the GST Governance, Data testing and Transaction Testing Guide (collectively, the Guides).

1. Board-level control 1: Formalised tax control framework
2. Board-level control 3: The board is appropriately informed
3. Board-level control 4: Periodic internal control testing
4. Managerial-level control 1: Roles and responsibilities are clearly understood
5. Managerial-level control 3: Significant transactions are identified
6. Managerial-level control 4: Controls in place for data[3]
7. Managerial-level control 6: Documented control frameworks
8. Managerial-level control 7: Procedures to explain significant differences.

The Guides:

- set out principles for board-level and managerial-level responsibilities, with examples of evidence that demonstrates the design and operational effectiveness of tax control frameworks, and
- focus on the processes and controls in place, and may not necessarily reflect the tax risk appetite or capabilities and experience of the tax or finance team, or their advisers.

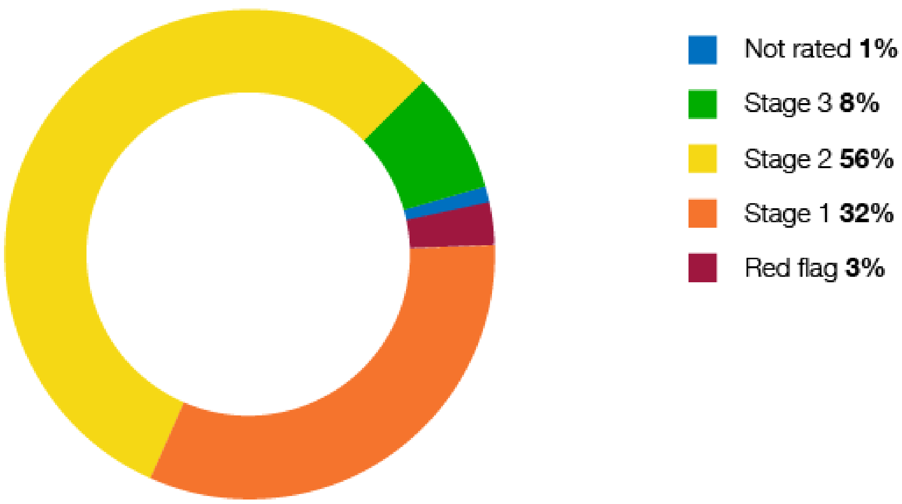
Ratings

We apply the following staged rating system when reviewing and assessing tax governance. Practical guidance about how we rate tax governance is available on ato.gov.au:

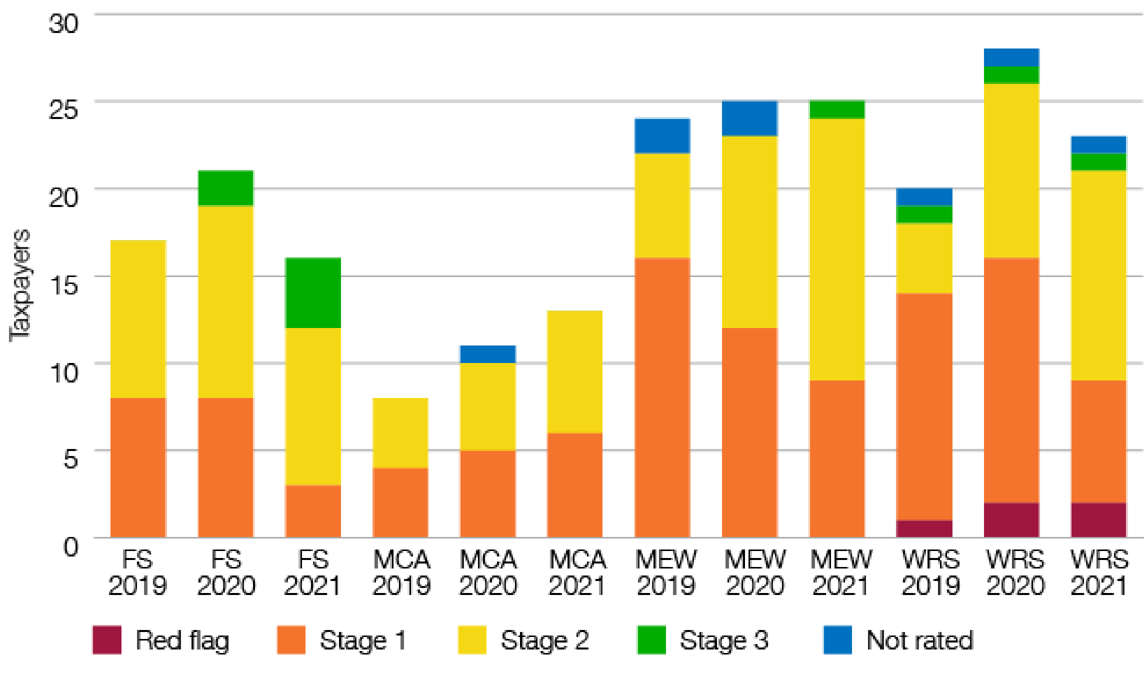
🟢	Stage 3	You provided evidence to demonstrate that a tax control framework exists, has been designed effectively and is operating effectively in practice.
🟡	Stage 2	You provided evidence to demonstrate that a tax control framework exists and has been designed effectively.
🟠	Stage 1	You provided evidence to demonstrate a tax control framework exists.
🔴	Not evidenced or concerns	You have not provided sufficient evidence to demonstrate a tax control framework exists or we have significant concerns with your tax risk management and governance.

The reviews completed to the end of June 2021 resulted in the following ratings which have been grouped by industry:

Graph 3 – Overall governance rating, 30 June 2021



Graph 4 – Overall governance rating for the last review, 30 June 2021



Observations

During 2021 we saw a marked increase in the number of taxpayers achieving Stage 2 and Stage 3 ratings for governance. We observed continued improvement in governance with these shifts reflecting the continuing efforts of many taxpayers to enhance their tax risk management frameworks and to provide objective evidence in support of their governance processes.

Stage 1

A Stage 1 rating recognises that a tax control framework exists but reflects that further work is needed to demonstrate that the framework is designed effectively.

For income tax, 32% of taxpayers were assigned a Stage 1 rating for the year ended 30 June 2021 compared to 46% for the year ended 30 June 2020. We have seen a decrease in the number of taxpayers at Stage 1, as these taxpayers have provided objective evidence addressing their design gaps and accordingly proceeded to a higher rating (Stage 2).

We continue to work with those top 100 taxpayers with a Stage 1 rating to progress to a Stage 2 rating as part of current and future reviews. In this regard, the process for reporting tax risks to the board and the periodic internal controls testing program remain the common areas with limited formal documentation.

Stage 2

A minimum Stage 2 rating is required to achieve an overall high assurance rating or justified trust. This means taxpayers have provided objective evidence to demonstrate that a tax control framework exists for income tax and has been designed effectively.

We have seen a further increase of taxpayers assigned an overall Stage 2 rating this year, including the majority of taxpayers whose tax control framework we did not rate during the year ended 30 June 2020. For income tax, 56% of taxpayers were assigned a Stage 2 rating for the year ended 30 June 2021 compared to 44% for the year ended 30 June 2020.

This result broadly aligns with the number of taxpayers who have achieved an overall high assurance rating for income tax this year, and who are now subject to the 'Monitoring and Maintenance' approach.

A number of top 100 taxpayers currently at Stage 2 are working with us to demonstrate that their tax control framework is not only designed effectively but also operating effectively in order to proceed to the next rating (Stage 3). However, for many taxpayers, a Stage 2 rating will be a satisfactory governance rating.

Stage 3

To obtain a Stage 3 rating, we look for evidence that the documented tax control framework is both designed and operating effectively in practice. This stage requires evidence in the form of a report of findings that taxpayers have independently tested the operation of their framework in practice and should conclude that the documented tax control framework is operating effectively.

Where the report of findings recommends improvements or enhancements, we will seek to understand whether these have been (or will be) implemented before assigning a Stage 3 rating. This currently applies to a number of taxpayers who are actively working on implementing recommendations stated in their reports of findings in order to achieve an overall Stage 3 rating.

We have seen an increase in taxpayers assigned an overall Stage 3 rating this year (8%). A Stage 3 rating is indicative of a good, lived, tax governance framework. The board, shareholders and other stakeholders can be confident that there is independent assessment on the operating effectiveness of the tax control framework. These top 100 taxpayers also benefit from our ability to be able to rely on good tax governance being embedded in positions taken, disclosures in returns and tax calculations, which can reduce the intensity of our enquiries where there might be system type error risks.

Red flag

A red flag rating is only applied after careful consideration if we have:

- no evidence demonstrating that a tax control framework exists
- significant concerns with the taxpayer's tax control framework as evidenced by the high level of errors identified, or
- fundamental concerns about the robustness of existing tax controls.

There is a very small percentage of top 100 taxpayers that have been assigned a red flag rating for income tax governance (3%).

Not rated

This rating is only applied in the top 100 program in a very small number of cases for income tax governance. The reasons for this vary but include taxpayers who have been involved with large scale mergers and acquisitions, and also where the tax control framework was being substantially redesigned (and the changes were so significant that it was appropriate to defer our assessment to the following review). In these circumstances, we typically review the governance framework in the following year.

Tax risks flagged to market / Significant and new transactions and specific tax risks

We seek to understand, and review, the income tax treatment of the taxpayer's business activities, particularly significant and new transactions. We also look for, and review, risks or concerns communicated to the market, and determine if they are present.

Ratings

We apply a consistent rating system when reviewing and assessing the income tax treatment of a taxpayer's business activities, including significant and new transactions, and tax risks communicated to the market.

🟢	High	We obtained a high level of assurance that the right Australian income tax outcomes were reported in your income tax return(s). This means we are unlikely to contact you again in relation these matters for the income year(s) reviewed unless something new comes to our attention.
🟡	Medium	More evidence and or analysis is required to establish a reasonable basis to obtain a high level of assurance.
🟠	Low	More evidence and or analysis is required to determine whether a tax risk is present.
🔴	Red flag	Likely non-compliance with the income tax law.
🔵	Out of scope	We have not evaluated this item and not expressed a rating.

Observations

Our assurance reviews cover a number of areas which range from significant transactions and items in the tax return, to specific risks either identified in the tax return or communicated to the market.

In our reviews, we consider all relevant Taxpayer Alerts, Practical Compliance Guidelines (PCGs) and Public Rulings to assess whether they apply to the taxpayer's particular circumstances. We also review Reportable Tax Position (RTP) Schedule disclosures for taxpayers who have a PCR.

The assurance areas covered in the analysis for tax risks flagged to market, and significant and new transactions often have material tax consequences if they have been incorrectly treated or calculated for tax. Typically, other than governance, this is where most of our time during the review is spent to obtain higher levels of assurance. This also has a significant impact on the overall assurance ratings.

In the past 12 to 18 months we have issued more than 15 new Taxpayer Alerts, PCGs and relevant Public Rulings to address strategic tax risks and areas of concern for both income tax and GST. For all new Taxpayer Alerts, PCGs and relevant Public Rulings, refer to the Legal database.

Many top 100 taxpayers have arrangements that are covered by a guidance or advice product, and we have been working, and will continue to work, with these taxpayers to move away from any high-risk arrangements. In several cases, there is more evidence or work needed to be able to assure that the arrangement or transaction has been reported correctly and the right amount of tax has been paid, or alternatively determine that further compliance action (such as an audit) is required. It is therefore expected the ratings for these areas will improve over time as the assurance review is completed or, if there is a dispute underway, it is resolved.

The largest public and multinational companies are also required to disclose in the RTP Schedule information on uncertain tax positions, and arrangements that are considered to pose a systemic risk to the corporate tax base. These arrangements often involve tax avoidance or profit shifting (or both). We publish the results of reportable tax positions in an annual findings report.

As part of our top 100 assurance reviews, we check, on an annual basis, the accuracy and completeness of disclosures made by top 100 taxpayers in tax returns, accompanying schedules (including the RTP Schedules), country-by-country (CBC) reporting statements and financial statements.

The following sections outline specific areas of concerns and items that attract our attention. We do not see these in all cases.

We have also included, where applicable, information on the RTP Schedule disclosures made by top 100 taxpayers for the 2019-20 income year (and comparisons to the 2018-19 disclosures where available) under Category C in relation to these areas of concern or items that attract our attention.

The latest Findings report Reportable tax position schedule Category C disclosures provides the aggregated disclosures made by companies for the 2019-20 income year. The report provides insights to the types of arrangements large companies are entering into, including other arrangements which are not outlined below.

Transfer mis-pricing

Transfer pricing is a common assurance area with approximately 85% of top 100 taxpayers reporting related party dealings. This area encompasses a substantially large number of dealings and they can range from simple to very complex in nature.

The following is a breakdown of the typical transfer pricing areas reviewed across a range of dealings:

- adequacy of information available to support transfer pricing positions
- inbound and outbound supplies of goods and services
- international related party financing transactions including arm's length conditions, related party derivatives, interest free loans (outbound and inbound), cash pooling arrangements and guarantee fees
  - From 2018-19 to 2019-20, there has been an increase (62%) in Category C RTP Schedule disclosures for low risk related party financing transactions as self-assessed by top 100 taxpayers under Practical Compliance Guideline PCG 2017/4. Disclosures relating to high and medium risk transactions have remained relatively consistent.
  - Related party loans continue to be a key focus area and represent the highest proportion of unassured items that attract a red flag rating for the top 100 population.
- management and administrative services
- licence fees and royalties
- technical services
- insurance or reinsurance
- research and development (R&D) performed on behalf of overseas related party
- sale or use of Australian intangible assets overseas (including failure to adequately recognise use of Australian assets)

- offshore hubs (marketing/procurement) or service centres
  - Category C RTP Schedule disclosures for 2018-19 and 2019-20 by top 100 taxpayers relating to marketing hubs have remained consistent over the 2 years, with a high proportion disclosing low risk ratings pursuant to Practical Compliance Guideline PCG 2017/1. There was, however, an increase in high risk disclosures in relation to non-core procurement hubs.
  - The high proportion of disclosures of low risk ratings for marketing hub arrangements reflects the efforts that have been made by the ATO and top 100 taxpayers, who are responsible for the majority of Australian exports sold through marketing hub arrangements, to resolve our concerns through Advance Pricing Arrangements (APAs) or settlements. A small number of material arrangements are subject to ongoing compliance action. Marketing hub arrangements represent the second highest proportion of unassured items (after related party loans) that attract a red flag rating for the top 100 population
- inbound distribution arrangements
  - From 2018-19 to 2019-20, there has been a slight increase in Category C RTP Schedule disclosures for high risk inbound distribution transactions as self-assessed by top 100 taxpayers under Practical Compliance Guideline PCG 2019/1. Disclosures relating to medium and low risk transactions have remained relatively consistent.

Common issues which continue to arise in relation to transfer pricing matters include the following:

- The size and complexity of the global value chain in the top 100 population – top 100 taxpayers often have very complex businesses and Australia can be a significant part of the value chain. We are finding this takes time to source relevant information to support the transfer pricing analysis.
- Changes in transfer pricing policy or methodologies without an underlying change to the functional profile of a taxpayer, and inappropriate methodologies being selected given the taxpayer functional profile.
- Related party financing transactions – top 100 taxpayers often have at least one financing related issue that has been reviewed. Where applicable, we would expect to see evidence supporting a top 100 taxpayer's self-assessment of the risk indicators and risk zone rating pursuant to Practical Compliance Guideline PCG 2017/4. High quality documentation is also expected to be maintained to support transfer pricing positions and debt allocations with respect to financing related income or deductions.
- Services transactions – the beneficial nature of services and the appropriateness of allocation keys are not well documented or evidenced.
- Royalty, licensing or intellectual property arrangements – the performance of development, enhancement, maintenance, protection and exploitation activities is not well documented or evidenced.
- Transactions that are covered by an APA or Bilateral Advance Pricing Arrangement (BAPA) – we will review the agreements and the annual compliance report that is required to be submitted annually for APAs and BAPAs to ensure that taxpayers are

continuing to follow the terms of the agreement/s. Where transactions are subject to settlement agreements or private rulings, we also review these to confirm that taxpayers are adhering to the terms of the settlement agreement or implementing the relevant transactions in accordance with the ruling.

Structured arrangements designed to reduce Australian tax

In some cases, we see arrangements that are structured to reduce Australian tax. In those cases, the low assurance ratings and red flags are sometimes associated with related party transactions (including third party back-to-back transactions) promoted or designed to achieve Australian tax savings, including:

- contrived related party financing arrangements, including the use of financing transactions with special terms designed to
  - artificially defer or avoid interest withholding tax while obtaining annual Australian income tax deductions
  - avoid dividend withholding tax upon repayment/redemption of contrived related party financing arrangements, and/or
  - otherwise obtain deductions or avoid assessable income using arrangements designed to circumvent specific anti-avoidance rules such as thin capitalisation and the hybrid mismatch integrity rule, and debt/equity classification rules
- migration of Australian generated intangible assets to overseas related parties in order to reduce Australian taxable income or withholding tax
- arrangements of the kind described in Taxpayer Alert 2020/4 – Multiple Entry Consolidated (MEC) Groups avoiding capital gains tax through the transfer of assets to an Eligible Tier 1 (ET-1) company prior to divestment
- arrangements designed to avoid income being attributable to an Australian permanent establishment
- ‘inversion’ or ‘top-hatting’ arrangements, or the interposition of partnerships or other entities, designed to
  - shift recognition of income and/or change or mischaracterise the nature of income
  - facilitate related party transactions to obtain Australian tax deductions
  - reduce or eliminate withholding tax, and/or
  - avoid the application of targeted anti-avoidance measures.

Other common areas attracting our attention

Other areas that continue to commonly arise in reviews that attract our attention include the following:

- **Consolidation** – consolidation areas reviewed include the allocable cost amount process (we have seen some instances where the allocable cost amount has not been prepared at the time of the assurance review), asset recognition, valuation, reconsolidation events and MEC groups.

- **Research & Development (R&D) expenditure** – this area remains an ongoing focus for us. R&D expenditure represents the second highest proportion of unassured items (after uniform capital allowances) that attract a low assurance rating for the top 100 population. We are commonly asking for more detailed working papers for R&D expense allocations and overheads. In some instances, we have also referred R&D matters to AusIndustry for a review of the eligibility of R&D activities, particularly in relation to software development and digital transformation activities.

- **Thin capitalisation –** some of the issues we are seeing are asset revaluations and not including some arrangements as debt such as preference shares and notes. A small number of taxpayers have made Category C RTP Schedule disclosures for the 2019-20 income year which are covered by Taxation Determination TD 2020/2 which sets out our view of the operation of the law to these arrangements.

- **Losses** – we holistically focus on generation, carry forward, transfer and utilisation of any losses. Our reviews consider not only the technical tax analysis, but we also look to understand the origin of the losses and the commercial environment of the business at the time they were incurred. We also seek to understand when top 100 taxpayers will utilise any carry forward losses and move into a tax payable position. This involves consideration of the same/similar business test and continuity of ownership tests.

  On 6 October 2020, the government announced that it would target support to businesses and encourage new investment through a loss carry back tax offset. We will be reviewing taxpayers that have made a loss carry back claim. We will be looking to ensure that there is sufficient evidence to support that taxpayers meet the eligibility criteria, the provisions have been applied correctly, and the calculations are correct.

- **Uniform capital allowances –** this area represents the highest proportion of unassured items that attract a low assurance rating for the top 100 population. When assuring capital allowances claims, we consider the systems and governance processes adopted, as well as the supporting evidence provided (including working papers). Common areas of focus include the use of project pools, balancing adjustment calculations, self-assessed effective lives and asset classification (particularly for composite assets and leasehold improvements). Where automated software tools are used to prepare claims, we also evaluate the level of ‘human intervention’ that confirmed revised claims satisfied the law. When taxpayers review past claims, we expect a ‘two way’ analysis – identifying capital items which could have been expensed, and also identifying where expensed items might be more appropriately capitalised.

  On 6 October 2020, the government announced that it would target support to businesses and encourage new investment through a temporary full expensing incentive (TFE). We will be reviewing taxpayers that have made a TFE claim. We will be looking to ensure that there is sufficient evidence to support that taxpayers meet the eligibility criteria, the provisions have been applied correctly, and the calculations are correct.

- **Deductions** – most of the general deductibility issues we are seeing relate to revenue or capital classification and the subsequent tax treatment of the expense. This includes capitalised labour, exploration expenses and repairs and maintenance.

- **Revenue –** we are seeing that in some cases we need more evidence and/or analysis of sales revenue and other material revenue amounts to establish a reasonable basis to obtain a high level of assurance where we have been unable to reconcile revenue figures reported in the tax return with audited financial accounts.

- **Controlled foreign companies**, **related party derivatives and attribution of profits to permanent establishments** – these are areas that commonly arise in our justified trust reviews.

- **Hybrid mismatch –** we have identified and reviewed circumstances where the hybrid mismatch rules apply, having regard to Law Companion Ruling LCR 2019/3 and accompanying Practical Compliance Guideline PCG 2019/6 and Practical Compliance Guideline PCG 2018/7. Consistent with this guidance, we expect top 100 taxpayers to engage with us if, having considered the risk of their arrangement taking into account our risk assessment framework, they conclude that there is a potential tax risk associated with the arrangement. Several taxpayers have made Category C RTP Schedule disclosures in the 2019-20 income year with regards to hybrid arrangements.

- **Diverted Profits Tax (DPT)** – in the course of our assurance reviews, we may consider the application of the DPT concurrently with other provisions of the income tax law, including the transfer pricing rules in Division 815 of the *Income Tax Assessment Act 1997*. We have considered, or are considering, the potential application of DPT in a small number of top 100 cases.

Ratings and engagement

For some issues or transactions, we require more evidence and/or analysis to obtain high assurance. We are working with top 100 taxpayers to articulate the areas that require further evidence or analysis. In some cases, medium assurance ratings on specific transactions may be satisfactory and, depending on the area and the significance of the transaction, it may still be possible to achieve overall high assurance.

For taxpayers to be able to achieve high assurance, we expect:

- high quality information
- relevant supporting documentation
- an open and transparent relationship with us.

Alignment of tax and accounting outcomes

We analyse the differences between the accounting and tax results. This includes understanding the effective tax rates and ETB. We seek to understand, and be able to explain, any variances between tax and accounting outcomes. This provides an objective basis to obtain greater assurance.

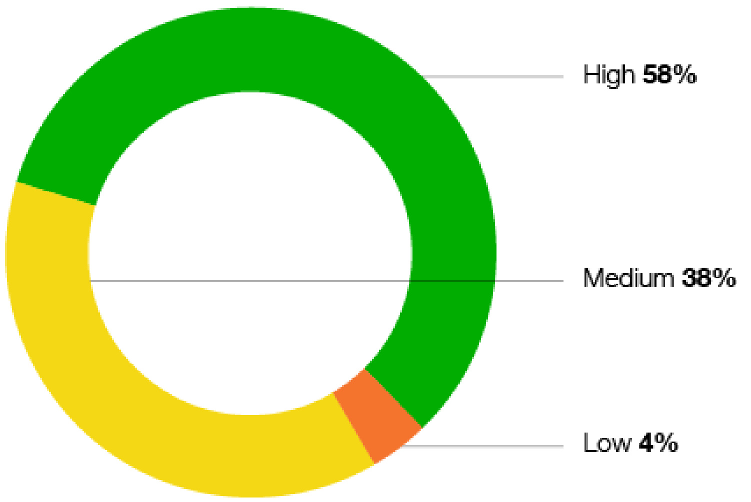
Ratings

We apply a consistent rating system when reviewing and assessing the alignment of tax and accounting outcomes, which is outlined below.

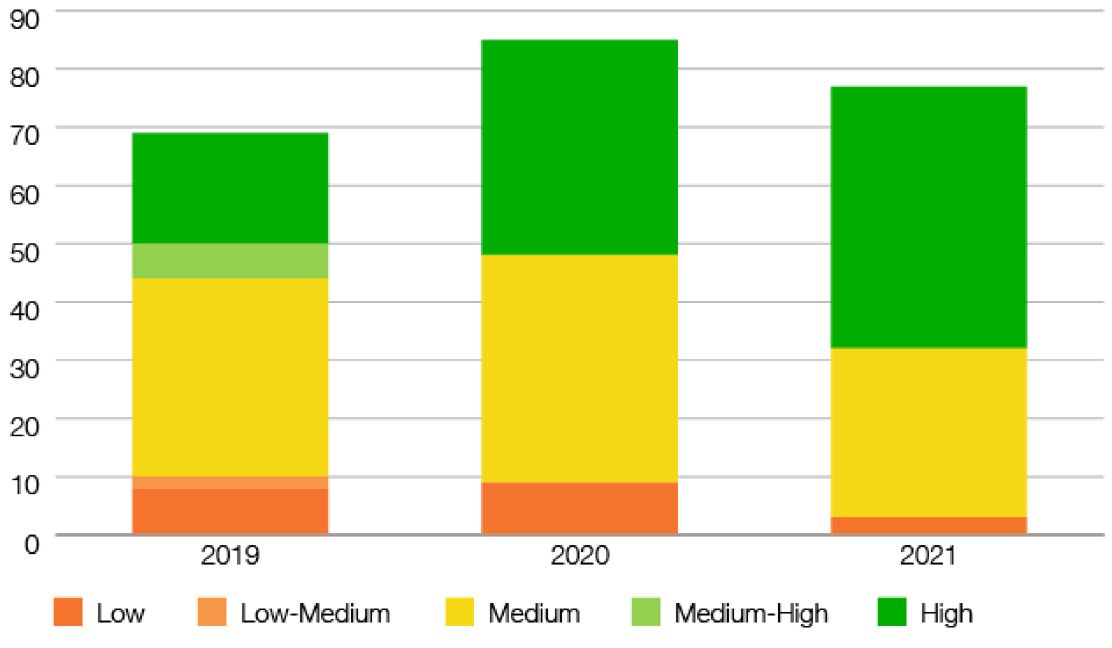
●	High	We understand and can explain the various streams of economic activity and why the accounting and income tax results vary.
●	Medium	Further analysis and explanation is required to understand the various streams of economic activity and/or why the accounting and tax results vary.
●	Low	We identified concerns from our analysis of the various streams of economic activity and/or why accounting and tax results vary.
●	Red flag	We do not understand and cannot explain the various streams of economic activity and/or why accounting and tax results vary.

The reviews completed to the end of June 2021 resulted in the following ratings:

Graph 5 – Alignment of tax and accounting ratings for the last review completed as of 30 June 2021



Graph 6 – Alignment of tax and accounting ratings for the last review completed as of 30 June 2019, 30 June 2020 and 30 June 2021



Observations

Most (96%) of the top 100 taxpayers have obtained a medium or high assurance rating with respect to the alignment of tax and accounting outcomes, with the proportion at high assurance increasing from 43% at the end of June 2020 to 58% at the end of June 2021.

We are generally able to obtain assurance over a significant proportion of reported income and expenses as most taxpayers have audited financial statements, supported by a book-to-book reconciliation between net profit or loss reported in the financial statements and the total profit or loss disclosed in the relevant tax return. This can be more challenging for taxpayers with MEC groups, foreign branches or stapled groups. However, in many cases we have now overcome these challenges through active collaboration with top 100 taxpayers with these structures to deepen our understanding of these taxpayer's various streams of economic activity, and why the accounting and income tax results vary.

We are also generally being provided with detailed book-to-tax reconciliations which allow us to obtain assurance over the key adjustments from the accounting results in order to calculate the taxable income (and tax payable) figures.

The number of medium ratings (38%) for this focus area demonstrates that further analysis is required, and underway, to understand the various streams of economic activity where the accounting and tax results vary for the top 100 population. It is also reflective of the significance and complexity of the transactions that are still being reviewed and have not yet been rated as high assurance.

Another element of this section is the ETB calculation, which we use to analyse the tax and economic performance of corporate groups. We consider that ETB is a part of good governance. Boards and tax representatives of corporate groups should understand their ETB calculation and discuss the results (including underlying proxies and assumptions) with us. We particularly encourage taxpayers to provide information around their global value chains and foreign taxes paid on Australian linked activity, and continue to work with us to refine and enhance the ETB analysis.

Tailored high assurance engagement

Obtaining high assurance

In the top 100 program, we apply a principled approach to reaching overall high assurance (justified trust). This is based on 2 elements:

1. a quantitative threshold of more than 90% tax assured and economic activity correctly reported, and
2. an objective assessment of 7 qualifying factors.

The quantitative threshold of element 1 must be met before the qualifying factors in element 2 can be applied.

The 7 qualifying factors are outlined below:

1. Governance

Governance has been rated at least a Stage 2 in the TAR.

2. Tax risks flagged to market

Any tax risks flagged to market (PCGs, Taxpayer Alerts, Public Rulings, including those set out in the RTP Schedule Category C disclosures) have been rated at least a medium level of assurance in the TAR, and are not of immediate concern or identified as necessitating further action based on the information provided.

3. International related party dealings and CFCs

International related party dealings, profit attribution to permanent establishments and CFCs have received at least a medium level of assurance in the TAR, and are not identified as necessitating further action based on the information provided.

4. Losses

Losses, if applicable, have received at least a medium level of assurance in the TAR. This includes that the commerciality of tax losses has been verified and we understand when a taxpayer expects to utilise carried forward balances and move into a tax payable position.

5. Effective Tax Borne (ETB)

The ETB calculation in the TAR and any underlying assumptions or proxies have been verified with the taxpayer. The ETB calculation has not highlighted any new areas of concern that pose a potential tax risk, including, for example, holding overseas interests in jurisdictions where there is not a substantiated commercial purpose.

6. Reportable tax position schedule

There are no inconsistencies in RTP Schedule disclosures which are identified between lodgment of the tax return and finalisation of the review.

7. Cooperative and collaborative behaviour

It has been a cooperative and collaborative process and whilst working with a taxpayer we have not observed any non-cooperative behaviour.

An overall provisional high assurance (justified trust) rating may still be possible in limited circumstances. Such circumstances may include where the taxpayer has provided an undertaking and is actively working on addressing a specific design gap in their tax governance framework or there is ongoing compliance activity. Where there is ongoing compliance activity, provided the quantitative threshold is met (inclusive of that unassured issue), the availability of a provisional rating will depend on the nature and stage of the compliance activity.

‘Monitoring and maintenance’ approach

When a top 100 taxpayer attains an overall high assurance rating under our justified trust assurance program, this means that we have confidence that they have complied with Australian income tax laws. In recognition of the level of trust we have in the reported tax outcomes of these taxpayers, we tailor our engagement approach to focus on maintaining our high level of confidence.

The nature of our engagement with PCR taxpayers following an overall high assurance rating is known as the ‘Monitoring and Maintenance’ approach and we have recently published guidance on this approach for taxpayers and their advisers.

Under the ‘Monitoring and Maintenance’ approach, we will monitor the taxpayer’s disclosures and tax outcomes over the two income years following an overall high assurance rating to maintain the level of justified trust obtained. During this period, we will seek to leverage the high assurance already obtained in relation to ongoing business activities.

We will continue to meet with taxpayers on a regular basis throughout the year to maintain a contemporary understanding of business performance, key transactions and areas of focus. We may request supporting evidence to be provided throughout the year to assist our enquiries.

Taxpayers will be expected to proactively engage with us and make disclosures of significant or new transactions, or where there are material changes, before these occur. We expect the following to be disclosed on a real time basis or as part of the annual review (as relevant):

- significant or new transactions
- material business changes
- change of tax treatments or positions that have previously been assured as part of the current or prior review
- change of reporting of uncertain tax positions as reflected in current and deferred tax balances in the financial statements
- details of any new tax risks flagged to market (note these should align with disclosures in the RTP Schedule)
- disclosure issues or errors relating to information reported in the income tax return or accompanying schedules that should be corrected
- material changes to the design of the tax governance framework, and
- outcomes of independent operational effectiveness testing of the tax governance framework completed.

Where the taxpayer makes a disclosure or notifies us of any of the above circumstances, or where our review detects a significant change or potential tax risk, we will request further evidence from the taxpayer to determine if verification is required. Where an item requires verification, our assurance activities in relation to these transactions or events will generally be targeted to areas not previously assured. At the end of the review, the taxpayer will receive a 'Monitoring and Maintenance' Assurance Report.

A large number of taxpayers have completed a 'Monitoring and Maintenance' year review with a few also completing a second 'Monitoring and Maintenance' year review, and we have been able to rely on the assurance attained previously.

While most taxpayers should experience a tangible decrease in the intensity of their review under the 'Monitoring and Maintenance' approach, this is very much dependant on whether (and the extent to which) transactions need verification. In the 'Monitoring and Maintenance' reviews completed to date, there has been a need in a number of instances for further verification as part of the review. This further verification has been in relation to governance enhancements, unreviewed transactions that were flagged in the future assurance plans at the time they attained overall high assurance, and new significant transactions relating to the year being reviewed.

Annual Compliance Arrangement taxpayers

For top 100 ACA taxpayers who have obtained a high overall level of assurance, we will revert to an annual ACA review, including an ETB analysis, in accordance with the ACA terms of arrangement. Typically, an ACA will require greater review activity than proposed under a 'Monitoring and Maintenance' review. This is because ACAs include an ATO sign-off in relation to each income year under review.

A few taxpayers have completed reviews as per the terms of the ACA.

Refresh year

The ‘Monitoring and Maintenance’ reviews and ACA year reviews will be followed by a more comprehensive justified trust review to refresh our confidence in the taxpayer’s tax outcomes every third year.

The assurance activities for the refresh year will resume a whole-of-business approach, covering the tax outcomes of the entirety of the taxpayer's economic activities and applying the four pillars of justified trust.

We will seek to 'top up' our assurance where appropriate. In ordinary circumstances, it is expected that the refreshed review will require less resource investment by taxpayers and the ATO as existing information, evidence and knowledge are able to be leveraged. At the end of a refresh year, the taxpayer will receive a full TAR.

A few taxpayers have moved into a refreshed review with one refreshed review completed as at 30 June 2021.

There may be circumstances where a refresh year may also be required earlier than the third income year, for example where there has been a fundamental business change such that there is a new business operation we need to obtain assurance over, or where we have reason to consider that our trust should no longer be maintained.

Top 100 GST assurance program

The top 100 population is a significant contributor to total GST collections. The top 100 population contributed $7.6 billion in GST collections for 2019-20, which was almost 13% of total GST collections.

In 2019 we expanded the top 100 assurance program to include GST. The top 100 GST assurance program seeks greater assurance that top 100 taxpayers are reporting the right amount of GST. This supports and expands on existing compliance approaches, including justified trust reviews for income tax.

Under the top 100 GST assurance program, we will complete a GST assurance review for each top 100 taxpayer by 30 June 2023. The review will generally focus on the last complete financial year.

GST and income tax teams are working collaboratively to deliver justified trust assurance reviews and we continue to work towards integrating our approaches to implement the justified trust work program from a whole-of-client and multiple tax perspective.

During a top 100 GST assurance review, we review the four focus areas outlined above.

The program has a strong focus on tax control frameworks for GST purposes. Taxpayers are encouraged to self-review their GST tax control frameworks, and undertake robust and regular data and transaction testings to ensure that their business systems are creating, capturing and correctly reporting GST.

Overall levels of assurance

The overall level of assurance is based on an objective view (having regard to objective evidence) of whether the taxpayer is considered to have reported the right amount of GST.

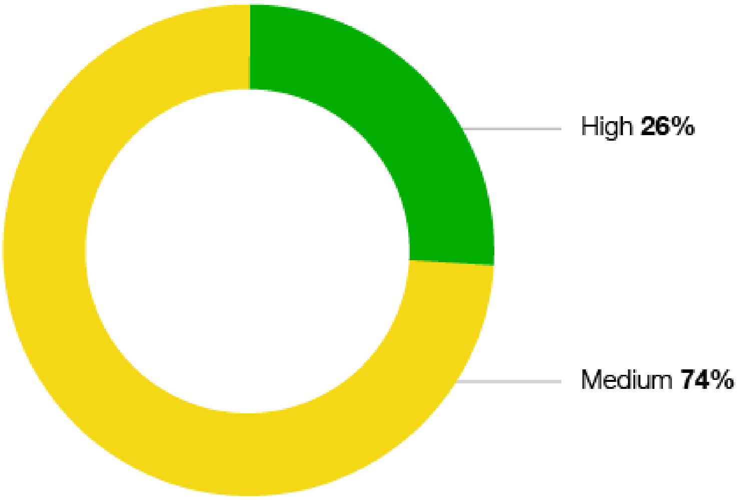
Ratings

We apply consistent rating categories when considering our overall level of assurance.

	High	We obtained assurance that the taxpayer reported the right amount of Australian GST for the period reviewed. This means we are unlikely to contact you again in relation to the tax periods reviewed unless something new comes to our attention.
	Medium	We obtained assurance in relation to some but not all areas reviewed. For those areas not yet assured, further evidence and/or analysis will be required before we obtain assurance that the taxpayer reported the right amount of Australian GST.
	Low	We have specific concerns around the taxpayer's compliance with the Australian GST law and the amount of Australian GST paid and GST refunds claimed for the period reviewed.

The GST assurance reviews completed to the end of June 2021 resulted in the following ratings:

Graph 7 – Overall assurance rating for all GST assurance reviews completed as of 30 June 2021



Observations

COVID-19 caused delays in the top 100 GST assurance program last year with several GST assurance reviews deferred and delayed for top 100 taxpayers. Accordingly, the number of GST assurance reviews finalised to date represents a small proportion (23.5%) of the top 100 population.

The majority of top 100 taxpayers who have had a GST assurance review finalised have attained an overall medium level of assurance. This means we obtained assurance in relation to the majority of areas reviewed but not all areas. Around a quarter of taxpayers reviewed have attained an overall high level of assurance meaning that we have assurance these taxpayers have reported the right amount of GST for the period reviewed.

The GST assurance reviews completed as of 30 June 2021 related to taxpayers from a range of industries; the majority of which do not present the highest GST risks impacting the large market. Therefore, it is unsurprising that all taxpayers reviewed to date have achieved an overall medium or high assurance rating.

There are several reasons why taxpayers did not attain an overall high assurance rating.

The primary reasons include:

- the inability to attain a Stage 2 rating for governance due to the absence of objective evidence to demonstrate that a tax control framework exists and has been designed effectively with respect to GST
- due to the size of the GST economic group, a divisional or business segment approach was undertaken which meant that there was insufficient coverage over the whole group and a further review is required to obtain sufficient coverage.

Tax risk management and governance

Tax governance framework

Tax governance is a key focus area under the justified trust methodology. As outlined previously, we review governance by requesting objective evidence of the design of tax controls. We review the design of controls based on documentation given to us and look for evidence in the form of approved policies and procedures demonstrating the existence and design of a tax control framework (for example, work instructions, templates and process maps).

The GST Governance, Data Testing and Transaction Testing Guide outlines how we apply the justified trust methodology in our top 100 GST assurance reviews when reviewing the existence, design and operation of a taxpayer's GST controls as part of an effective tax control framework.

We consider the 8 controls outlined previously. There are 3 controls that are fundamental because the design of these controls directly influences the way in which GST is reported. These fundamental controls are:

1. Board-level control 4: Periodic internal control testing
2. Managerial-level control 4: Controls in place for data[4]
3. Managerial-level control 6: Documented control frameworks.

We also consider the other 5 controls as these are common controls and the design is equally as critical for both income tax and GST. There are also common features in the way these controls are evidenced for both taxes.

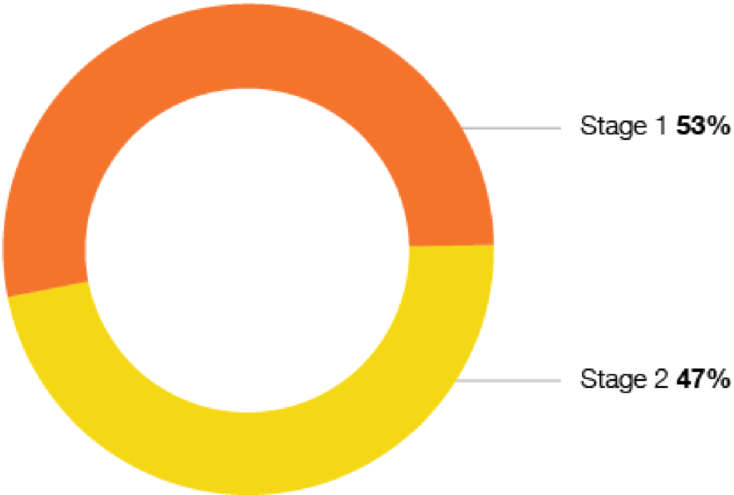
Ratings

We apply the same standard ratings system as outlined previously for income tax when considering the existence, design and operation of a tax control framework for GST purposes.

[4] We only apply this control in relation to GST.

The GST assurance reviews completed to 30 June 2021 resulted in the following ratings:

Graph 8 – Overall GST governance rating for all GST assurance reviews completed as of 30 June 2021



Observations

During 2021, we saw a number of taxpayers who have had a GST assurance review finalised achieving a Stage 2 rating for GST governance. This reflects the efforts of these taxpayers to build on the design of their tax risk management frameworks to incorporate GST.

Incorrect reporting from inadvertent errors is one of the main GST risks identified through the top 100 assurance reviews. Most GST amended assessments in the large market are often the result of voluntary disclosures arising from processing or system type errors primarily due to governance issues (e.g. design gaps, missing systems controls, manual data processing, systems errors and gaps in BAS review procedures).

Through improved governance, and taxpayers undertaking more regular and robust data and transaction testings, we expect to see fewer inadvertent positions being taken in the form of system type errors in a pre-lodgment context.

We have identified links between GST errors made in applying the GST special rules and the design of GST controls. The most common example is in relation to the application of the financial acquisitions threshold. We have observed manual data processing procedures and BAS review procedures are missing the detailed steps to be undertaken to identify, quantify and report GST claimable when applying the financial acquisitions threshold.

We continue to see that periodic independent governance control testing continues to be the control that top 100 taxpayers find most challenging for both income tax and GST.

Systems and BAS walkthroughs performed in top 100 assurance reviews help inform us of particular aspects of our governance review, however, we require source documents to evidence the tax control framework. Therefore, teams will leverage from the walkthroughs to identify systems and BAS controls, and request evidence during the meeting, to help to generate overall efficiencies with our governance reviews.

Based on the small number of reviews completed to date, the overall GST governance ratings generally aligned with the overall income tax governance ratings assigned to top 100 taxpayers. In the very few instances where the overall assurance ratings did not align, the taxpayers did not achieve Stage 2 ratings for the 3 fundamental GST controls (relating to controls in place for data for GST purposes, documented GST control frameworks, and periodic controls testing program covering the testing of GST controls).

We have also observed that a number of top 100 taxpayers have not yet designed and implemented a procedure to explain significant differences between financial statements and GST clearing account balances, and the BAS. We will follow this up with taxpayers in future governance reviews.

Stage 1

A Stage 1 rating recognises that a GST control framework exists but reflects that further work is needed to demonstrate that it is designed effectively.

Stage 2

A Stage 2 rating is required to achieve overall high assurance or justified trust for GST. This means taxpayers have provided objective evidence to demonstrate that a tax control framework exists and has been designed effectively.

Top 100 taxpayers are investing in GST governance, and this is reflected in our findings to date.

We are expecting to work with some top 100 taxpayers currently at Stage 2 to proceed to a Stage 3 rating. However, for many taxpayers, a Stage 2 rating will be a satisfactory governance rating.

Stage 3

To obtain a Stage 3 rating for GST, we look for evidence that the documented tax control framework is both designed and operating effectively in practice.

This stage requires evidence in the form of a report of findings that taxpayers have independently tested the operation of the framework in practice across all of the GST controls.

Although we did not assign any Stage 3 ratings during 2021, some top 100 taxpayers currently at Stage 2 are working with us to demonstrate that their tax control frameworks are operating effectively in order to achieve a Stage 3 rating. Some taxpayers have the testing of their GST control framework for operating effectiveness scheduled for next year.

GST risks flagged to market / significant and/or new transactions / specific tax risks

We seek to understand that the GST outcomes of atypical, new or large transactions are appropriate. We also review GST risks or concerns we communicated to the market, and determine whether these risks may be present.

Ratings

We apply a consistent rating system when reviewing and assessing the GST reporting and GST treatment of a taxpayer’s business activities, particularly significant and new transactions, and GST risks or concerns communicated to the market.

🟢	High	We obtained a high level of assurance that the right Australian GST outcomes were reported in your Business Activity Statements. This means we are unlikely to contact you again in relation these matters for the income year(s) reviewed unless something new comes to our attention.
🟡	Medium	More evidence and/or analysis is required to establish a reasonable basis to obtain a high level of assurance.
🟠	Low	More evidence and/or analysis is required to determine whether a tax risk is present.
🔴	Red flag	We have concerns there is non-compliance with the GST law.
🔵	Out of scope	We have not evaluated this item and not expressed a rating.

Observations

The following sections outline areas of concern and items that attract our attention. We do not see these in all cases.

Incorrect reporting

The prevailing risk we are seeing for top 100 taxpayers is incorrect reporting due to inadvertent errors that arise from governance issues and system type errors.

We have seen a material number of voluntary disclosures primarily due to governance issues and incorrect reporting (identified through data and transaction testings), however disclosures are typically not material in dollar terms.

Data and transaction testings are critical to assess correct reporting. Data testing involves running a number of pre-determined tests against a defined data set to identify reporting errors and exceptions for further investigation and/or correction. Transaction testing involves tracing an identified transaction from its source documentation through to the financial reports to confirm the accuracy of the GST treatment, calculation and reporting of the transaction. Where errors and exceptions are identified, further investigation will be necessary and/or correction may be required.

For top 100 GST assurance reviews, we consider a data set of at least 3 consecutive months as being a good representative sample of a full 12 month period for business operations that involve a stable supply and acquisitions base.

In assessing the correct reporting of a taxpayer's GST obligations, the ATO expects that taxpayers undertake robust and regular assurance and verification procedures that align with their business, and that are tailored to their own operating environment. We are seeing instances of taxpayers embedding the data and transaction testings or aspects of the testings into their own systems. Our expectations on data and transaction testings are set out in the GST Governance, Data Testing and Transaction Testing Guide.

We are seeing an increasing number of taxpayers engaging the services of a third-party adviser to undertake independent data testing with respect to a notified top 100 GST assurance review. In some cases involving third-party adviser data testing, we have seen some delays due to a number of different reasons, including setting the scope, instances of misalignment between the agreed scope and the findings report, requests for extension of time to complete the testing and finalise the report, and ATO concerns about the quality data and testings.

We are continuing to work closely with taxpayers and their advisers on the data testing to ensure that the outcomes are sufficiently robust so as to provide relevant stakeholders with the intended degree of confidence with respect to correct reporting. We have published the Guide to Independent Data Testing by Third Party Advisors. This guide will assist taxpayers by providing practical guidance on the ATO's expectations and the conditions that must be met for a taxpayer's third-party adviser to undertake the independent data testing that can be relied upon in a GST assurance review.

Other critical GST risks

We have also seen other critical GST risks in the small number of reviews completed and existing reviews that can be grouped broadly as follows:

- **GST food classification –** GST classification of food supplies is a well-known and very prominent risk.
  - We are seeing classification of products by suppliers/wholesalers and retailers that are not consistent with the ATO view.
  - Errors are generally attributable to gaps in governance controls.
- **Financial services and investment –** We have seen specific issues relating to the following:
  - The most common error we have identified in this area has been the failure to identify cross-border acquisitions subject to the application of the reverse charge provisions.
  - Our reviews consider risks that input tax credits are not appropriately denied on acquisitions that only relate to input taxed financial supplies (e.g. mortgage brokerage costs) or where apportionment methods used do not appropriately apportion input tax credits between input taxed and taxable or GST-free supplies. We have observed errors where inappropriate cost allocation drivers are used or changes in cost allocation systems made by finance have not been appropriately escalated for the tax team to consider the impacts.
  - Taxpayers have generally transitioned their arrangements in line with recent ATO public guidance on GST apportionment of credit cards, transaction accounts and home loans, such as Practical Compliance Guideline PCG 2019/8. We have seen instances where reduced input tax credits are not claimed consistently with ATO public guidance, specifically in relation to acquisitions made by account providers under complex IT outsourcing arrangements.
  - Errors have arisen where taxpayers do not have adequate controls in place for the review of agreements under which recipient-created tax invoice are issued (for instance, ensuring that the supplier continues to be GST-registered, such as in relation to trail commissions paid to brokers who may no longer be registered for GST).
  - For general insurers, we have observed some instances of errors in the calculation of increasing and decreasing adjustments under the relevant specific provisions.
  - We have observed non-financial services businesses making errors in monitoring the financial acquisitions threshold when making financial supplies as part of a

significant or unusual transaction (for instance, an IPO or M&A activity), or as part of an in-house treasury function.

We encourage taxpayers in the industry preparing for a review to refer to the GST Financial Services and Insurance Strategy for FY22 which sets out the ATO's areas of focus. Industry-specific bespoke data tests have also been provided which can be used to identify potential errors.

- **Property** – The property risk concerns the incorrect claiming of GST credits and the failure by taxpayers to correctly report the sale, transfer or acquisition of real property leading to reduced collection of GST. Key risk areas for real property include:
  - eligibility and application of the margin scheme where taxpayers have chosen to use this methodology, and
  - other issues, including supplies of a going concern, unreported sales of real property, and failure to take into account adjustments due to adjustment events.
- **International and cross border issues** – These issues primarily relate to cross-border GST obligations of non-residents who make supplies connected with Australia. This includes offshore supplies to Australian consumers, such as digital products and services, and low value imported goods.

Other common areas attracting our attention

Other areas that commonly arise in reviews that attract our attention include the following:

- ABN registration/ unregistered vendors
- relying on recipient created tax invoice arrangements without having the underlying agreements in place
- sharing economy (platforms)
- incorrectly treating an acquisition as creditable (e.g. non-deductible entertainment expenses)
- incorrectly treating supplies with related parties that are not part of the GST group
- attribution errors (e.g. periodic/progressive supplies, non-standard tax periods)
- GST joint ventures and the incorrect GST treatment on transactions between and within joint ventures
- absence of Subdivision 153-B (principal and agent) agreements but treating supplies and acquisitions as if there is a (valid) Subdivision 153-B agreement in place.

Understanding the alignment between accounting and GST

We seek to understand and explain the various streams of economic activity and how they are treated for GST, which may include applying the GST analytical tool (GAT).

Ratings

We apply a consistent rating system when reviewing and assessing the alignment of accounting figures to amounts reported on the BAS. This includes also understanding the reasons for any variances.

	Stage 3	We understand and can explain the variance between accounting figures and the amounts reported on the BAS. As a result of applying the GAT, we understand why accounting and GST results vary and this understanding is sufficiently supported by objective evidence.
	Stage 2	Further analysis and explanation is required to understand the variances between accounting figures and the amounts reported on the BAS. As a result of applying the GAT, we do not fully understand why accounting and GST results vary and/or this understanding is not sufficiently supported by objective evidence.
	Stage 1	We do not understand and cannot explain the variances between accounting figures and the amounts reported on the BAS.
	Red flag	We identified concerns from our analysis of the variances between accounting figures and the amounts reported on the BAS.
	Not rated	We have not assessed the various streams of economic activity and/or why accounting and GST results vary using the GST analytical tool.

Observations

The GAT tool is applied under this focus area. We apply the GAT in each top 100 GST assurance review except for taxpayers who are predominately input taxed.

The GAT uses a standard method statement applying a 'top down' approach to identify and understand variances between accounting figures reported in audited financial statements and GST reported on BAS'. The GAT is an important tool for taxpayers to check how their various streams of economic activity are treated for GST purposes.

We are seeing an increasing number of taxpayers embedding the GAT into their processes. There is an expectation as part of good GST governance that a taxpayer has a process in place to explain BAS reporting of GST payable and receivable compared to business outcomes, and to explain variances in comparison to financial statements.

Where the GAT has been applied, 60% of taxpayers have attained Stage 3 and 40% of taxpayers have attained Stage 2.

We recently published the GST Analytical tool (GAT) FAQ, and top 100 example and top 1000 examples to support top 100 taxpayers and their advisers with their top 100 GST assurance reviews.

We have initially been working closely with taxpayers to apply the GAT as part of their top 100 GST assurance review to demonstrate how understanding the variances between accounting and tax can be practically achieved.

We are encouraging taxpayers to prepare the GAT calculations themselves using the top down methodology proposed in the GAT guidance material. Where taxpayers need assistance in understanding the methodology or applying it, or making assumptions towards the GAT calculation, we are working collaboratively with them to finalise the GAT.

So far, we have observed that in most cases the information required in relation to adjustments from the profit and loss statements to the BAS has largely been available. Revenue analysis has been relatively straightforward to undertake in most industries and balance sheet movements on the whole appropriately reflected the majority of timing differences between GST and accounting. Good notes to the profit and loss statements including the cash flow statement have also been useful in assuring revenue and expense GAT adjustments.

We have also observed some challenges, including reconciling complex grouping variances, and the quantification of some differences (i.e. long-term construction contracts or mixed accounts where GST-bearing or non-GST bearing amounts are difficult to separate and quantify). In these cases, we work with the taxpayer to find other forms of objective evidence or alternative methods to assure the key GAT line adjustments.

We are currently working on developing a methodology to understand why accounting and tax results vary for general insurers.