

Australian Taxation Office Justified Trust Reviews

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Deputy Commissioner Jeremy Hirschhorn described the ATOs justified trust initiative as being framed around the following core question:

“If we were to tell a citizen jury what we have done to assure the tax paid by an individual company, would they be satisfied that we had done enough to make sure that the tax they have paid is correct?”

J Hirschhorn, “Towards *justified trust* between the ATO and the Infrastructure industry’ paper presented to the 2016 National Infrastructure Conference, 26 May 2016, Melbourne, 4.

Justified Trust regime – overview

- What is Justified Trust?

- Four pillars:

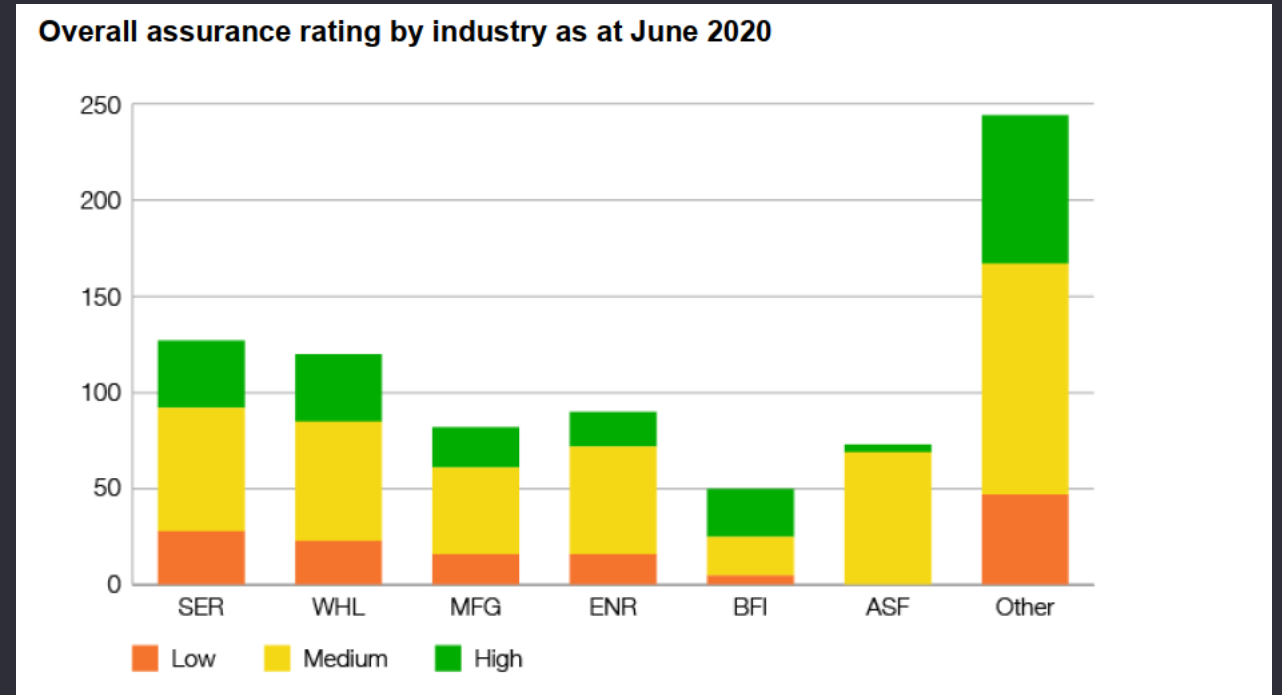
- Tax governance framework
 - Tax risks flagged to market
 - Significant/new transactions
 - Variance between accounting and tax results

- Why is Justified Trust important?

- Confidence
 - Transparency
 - Tax gap

- ATO Programs

- Top 100 Tax Assurance Review and Top 1000 Streamlined Assurance Reviews (income tax or GST)
 - Top 1,000 combined assurance program



Source: ATO Top 1,000 (income) tax performance program – Findings Report (30 June 2020), available at www.ato.gov.au

Understanding the tax governance framework - outcomes

- ATO guidance

- [Tax Risk Management and Governance Review Guide](#)
- [GST Governance, Data Testing and Transaction Testing Guide](#)

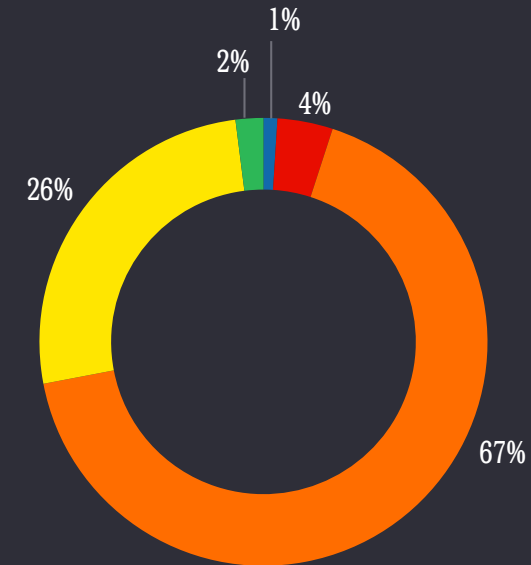
- Board-level and managerial-level controls

- BLC 1: Formalised tax control framework
- BLC 3: Board is appropriately informed
- BLC 4: Periodic internal controls testing
- MLC 1: Roles and responsibilities clearly understood
- MLC 3: Significant transactions are identified
- MLC 6: Documented control frameworks
- MLC 7: Procedures to explain significant differences

- Need for objective evidence

- Ratings system: Red flag, Stage 1, Stage 2, Stage 3

Tax Risk Management and Governance assurance ratings (June 2020)



■ Unrated ■ Red flag ■ Stage 1 ■ Stage 2 ■ Stage 3

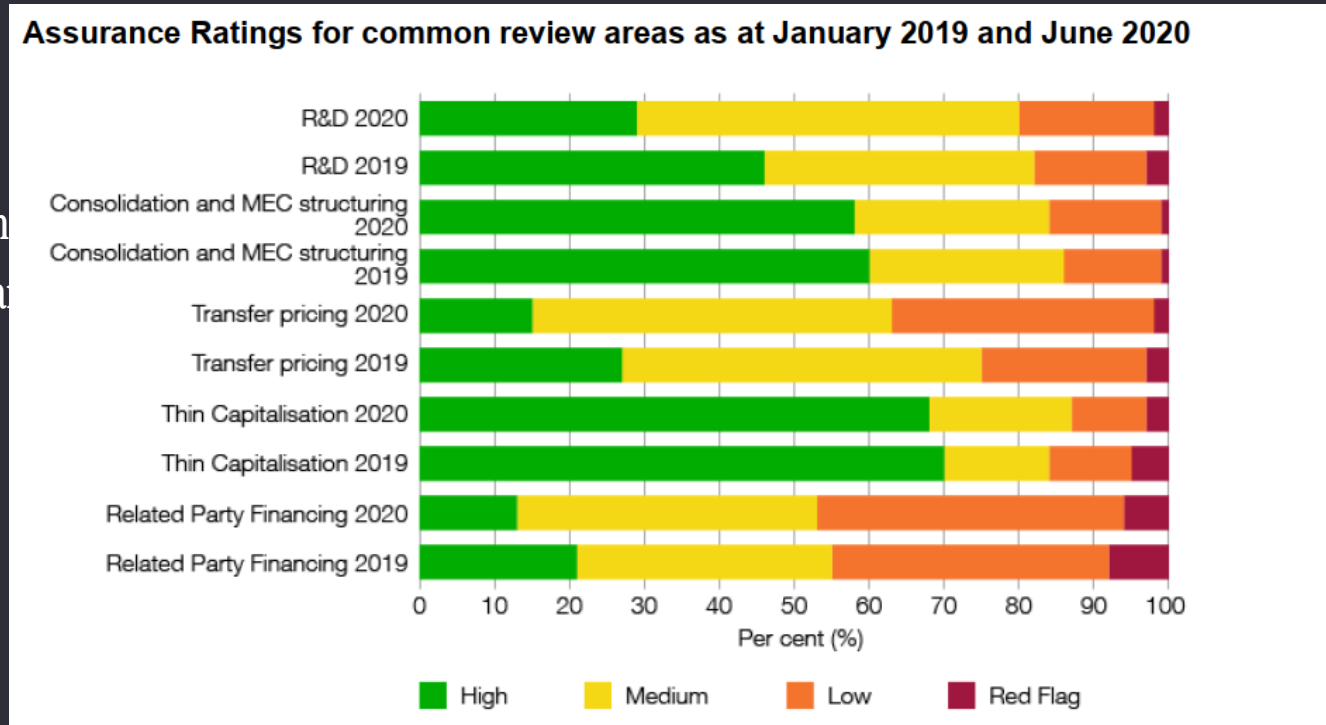
Source: ATO Top 1,000 (income) tax performance program – Findings Report (30 June 2020) available at www.ato.gov.au

Identifying tax risks flagged to the market

- ATO guidance has been published – current areas of focus:
 - Capital allowances
 - Research and development
 - Tax losses
 - Consolidation
- Other risks identified in the ATO's Findings Reports for the Top 1000 program:
 - Inbound and outbound holding structures
 - Structured arrangements designed to reduce Australian tax
 - Transfer pricing
 - Thin capitalisation

Understanding the importance of significant and new transactions

- Typical questions asked by the ATO:
 - Group structure, new businesses, restructures
 - Acquisition or disposal of interests in other entities
 - Controlled foreign entities
 - Branches or permanent establishments
 - Transfer pricing documentation and international agreements
 - Statutory accounts of ultimate/immediate holding companies
 - Tax losses
- Structured arrangements
- Transfer pricing



Source: ATO Top 1,000 (income) tax performance program – Findings Report (30 June 2020) available at www.ato.gov.au

Book to tax reconciliations

- Understanding key book to tax differences – permanent / temporary
- Calculating the effective tax borne (ETB) and global value chain to understand why accounting and income tax results vary
- Goods and Services Tax (GST) Analytical Tool: sales, acquisitions and other data and compare this to net GST paid; reconciliation between Business Activity Statement and Financial Statements

Developing a framework and procedures to identify tax risk

- Board-level controls as published in the Tax Risk Management and Governance Review Guide
- Is there a formalised tax control framework?
- Is the board or sub-committee appropriately informed of tax risks?
- Is periodic internal control testing conducted?

Developing a framework and procedures to identify tax risk

- Managerial level controls – typically in the form of an operations manual that sets out guidelines on identifying, assessing, managing and monitoring tax risks.
- Key areas:
 - Ensuring sufficient capacity and capability
 - Ensuring information technology controls are in place
 - Assuring the flow of information from accounting records
 - Dealing with law and administrative updates

The role of internal audit in providing assurance

- **Design effectiveness – Gap Analysis**

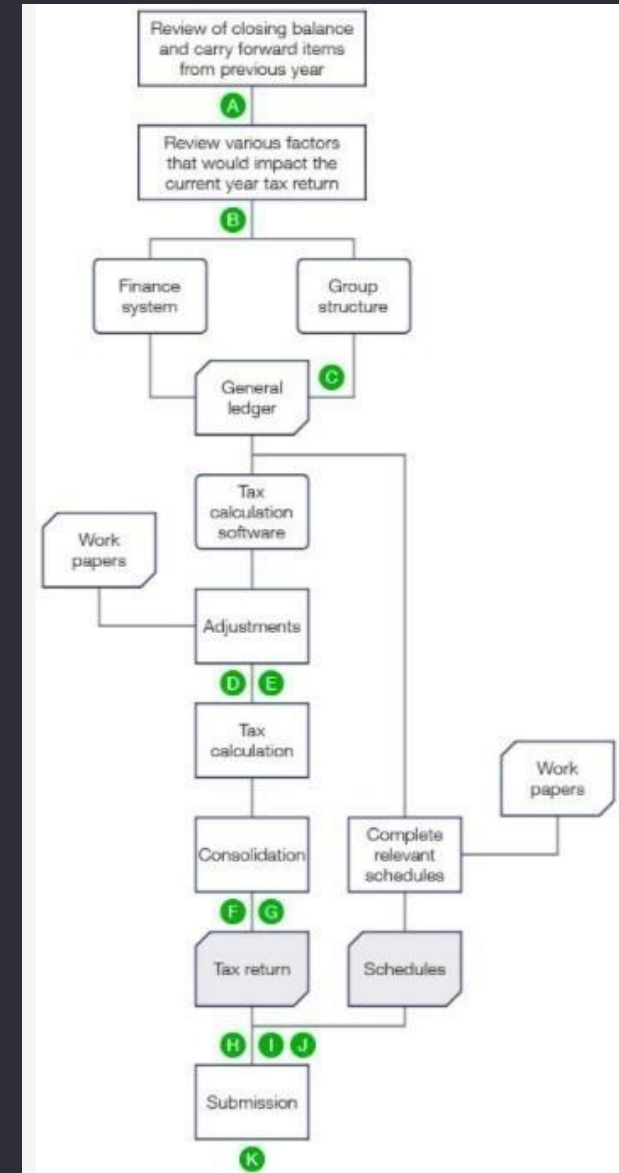
- Considers the *design* of a TCG framework
- Involves a comparison of your current state TCG against the ATO's 'better practices' in the ATO Tax Risk Management and Governance Review Guide
- If the controls are not met, are there any compensating processes?
- Output is typically a schedule with detail of precisely how the framework meets the ATO's controls
- Distinct from considering the *operation* of a TCG framework

The role of internal audit in providing assurance

- **Operational effectiveness – Self-Assessment Procedures (SAPs)**
 - Tests *operation* of TCG framework
 - Comprehensive set of procedures; instructions outlined in the ATO Tax Risk Management and Governance Review Guide
 - ‘Self assessment’ and independent controls testing of governance processes
 - Assesses board-level controls (BLCs) and managerial-level controls (MLCs) in an agreed upon procedures style review
 - SAP report documents evidence reviewed and testing of operation

The role of internal audit in providing assurance

- **End-to-end income tax return and Business Activity Statement preparation process**
 - Walkthrough: Identification of the risks, description of controls, type of control, control owners.
 - Testing: Testing methods, Assessment procedure, Sample size
 - Output: Report and issuing to Board / Board Sub-Committee.
 - ATO expectations



Source: ATO Tax Risk Management and Governance Review Guide available at www.ato.gov.au



Questions?



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