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New dimensions in regulatory compliance – building the bridge to better compliance

Stuart Hamilton[1]

generalization for the purposes of this article, I will work on the basis that most people comply because it is the accepted thing to do, a societal or peer norm, rather than through deliberate calculation, compulsion or fear.

Without such a broad level of voluntary compliance any regulatory system would be swamped with cases that called for intervention - which would quickly outstrip the resources and remedies available.[11] That's not to say it is all smooth sailing. Norms can clearly change over time - sometimes rapidly - and from a tax compliance viewpoint, breakouts of mass marketed arrangements have at times severely strained the Australian system.[12]

The compliance framework or model that a regulatory authority adopts is like a 'lens' it uses to view its clients and it appears to become part of a shared value set that inevitably permeates its strategies, systems, and style of interactions with clients.[13]

Allingham, M G & Sandmo, A 1972, 'Income tax evasion: a theoretical analysis', Journal of Public Economics 1, pp 323–338. While this was the initial ground breaking paper on the economics of tax evasion and the effect of penalties, it predicted a far higher rate of non compliance than was in fact observed given actual audit rates and penalties. https://darp.lse.ac.uk/papersdb/allingham-sandmo_(jpube72).pdf; Sandmo, A 2006, 'The theory of tax evasion: A retrospective view', National Tax Journal 58, pp 643 – 663 at http://old.nhh.no/sam/stabssem/2004/sandmo.pdf; Fischer, C M, Wartick, M & Mark M 1992, 'Detection Probability and Taxpayer Compliance: A Review of the Literature', Journal of Accounting Literature 11, pp 1-46, brings a richer conceptual compliance framework taking into account: demographic factors (e.g. age, gender and education); non-compliance opportunity (e.g. income level, income source and occupation); attitudes and perceptions (e.g. fairness of the tax system and peer influence) and tax system structure (e.g. complexity of the tax system, probability of detection, penalthi6a50026 and ce es2.7(2.1(r)hau,ing.4(10026 Tce L-6.6(gend6 scn 19.1067 0 TD

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("You are what you do" said Aristotle.) It becomes a key facet in shaping the compliance 'culture' of the organisation and can even influence its structure, since structure often follows strategy, as Alfred Chandler noted in 1962.[14]

Such frameworks or models are more useful if they provide logical guidance or direction, allow for improvements on previous approaches, add insight by explaining

Regulatory systems where the only answer is, for example, a prosecution, tend to view the solution set to a compliance issue as 'prosecuting the right clients' – even though a prosecution might not be the most effective treatment to engender long term compliant behaviour.[15]

It's a rather limited tactical response for an increasingly complex regulatory world.

Figure 3
A linear compliance continuum – introducing shades of grey

This more nuanced view is one of the conclusions of the OECD Forum of Tax Administration (2010):

- The disengaged clients who have decided not to comply,
- The resistant clients who don't want to comply,
- The captured clients who try to comply, but don't always succeed, and
- The accommodating clients who are willing to do the right thing.

To work the Braithwaite model requires compliance staff to make reliably informed and accurate judgments not merely about whether non-compliance has occurred but also in respect of the 'motivation' for that non-compliance – a challenging ask as it goes beyond observed behaviours to making inferences about a client's state of mind. There is a real risk that staff focus on the perceived client attitude rather than on the actual client behaviour.

It should also be noted that some commentators[25] have raised questions regarding the applicability of the compliance pyramid in situations where the determination of compliance itself is uncertain – where legitimate differences of views exist regarding what compliant behaviour is. This situation, not uncommon with large complex transactions, magnifies the danger of asking staff to reliably form views as to the apparent motivation for perceived non-compliance. 'Difficult' tax minimisers may be inappropriately viewed as 'aggressive' tax avoiders. This aspect is discussed further later in this article.

As noted earlier, the compliance pyramid posits an escalating choice of remedy matched to observed client behaviours and the perceived motivation. For example:

- For those perceived as doing the "right thing" – the majority of clients – compliance is made as simple as possible. Information reporting requirements are reduced and interactions are made as cheap and easy as is practical.[26]
- For those perceived as trying, but not succeeding, in doing the right thing, education and advice is provided to enable compliance. This can be general, or aimed at a specific client segment – an industry or occupation group or some other discernable client grouping.[27]
- Some clients may be selected for a review where the output is advice on how to comply in the future, rather than an adjustment that punishes the past. For example, 'record keeping reviews' where the output is often advice on how to better record transactions. These interventions are generally relatively quick,

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the client rather than indicating a level of concern (a view of risk) at that point in time that suggests follow up action to ascertain the relevant salient facts and circumstances. A more appropriate regulatory approach therefore is to describe the level of 'risk' or 'concern' associated with evidenced behaviours.

[24] Braithwaite, V 2003, 'Dancing with Tax Authorities: Motivational Postures and Non-compliant Actions' in Braithwaite, V (ed) Taxing Democracy: understanding tax avoidance and evasion, Ashgate, Aldershot. 5 postures suggested: Commitment, Capitulation, Resistance, Disengagement, Game-playing: at http://demgov.anu.edu.au/papers/Braithwaite2003TD(2).pdf

[25] Burton, M 2007, 'Responsive Regulation and the Uncertainty of Tax Law – Time to Reconsider the Commissioner's Model of Cooperative Compliance?' eJournal of Tax Research, Volume 5, No1 at http://www.atax.unsw.edu.au/ejtr/content/issues/previous/paper4_v5n1.pdf

[26] See for example the direction of the ATO 'Easier, Cheaper, More Personalised Change Program' at http://www.ato.gov.au/content/downloads/Making_it_easier_to_comply_2005_06.pdf

[27] See http://ato.gov.au/corporate/content.asp?doc=/content/42628.htm on marketing aspects to particular groupings.

5. EXPLICITLY BRINGING RISK INTO THE PICTURE

As noted earlier, before a regulator can determine whether a client is compliant or not decisions have to generally be made about 'who' to review. Aspects concerning likelihood of non-compliance, the potential consequences of that non-compliance and the degree of certainty of these need to be guided by risk based case selection (who the regulator reviews to determine whether or not they are, in the regulators view, compliant) and client engagement approaches in a practical sense, where it is both evidence based, repeatable and scalable across markets. Making it reality rather than mere organizational rhetoric.

At their most basic level, risks are simply things that can threaten our success in achieving our intent or vision. Risk events have both a likelihood of occurrence and a consequence of occurrence and it is critically important to understand the difference between these two aspects, 'how likely' and 'how much', in order to consciously manage and treat risk.

My experience is that it isn't uncommon for people to talk about risk just in terms of likelihood and not calculate the relative and absolute consequence aspects. That tends to fuel 'one size fits all' approaches that may work well when all are of one size – but most aren't (eg A hundred dollar consequence is ten thousand times smaller than a million dollar consequence and ten million times smaller than a billion dollars... if you just use likelihoods you effectively loose the significance of the dimension of consequence.)

A risk with a lower likelihood, but higher consequence is generally a very different thing to a risk with a higher likelihood, but lower consequence – even though the risk event and overall risk rating may be the same, you usually need to approach them very differently to be effective.[33]

[33] The standard 4 'Ts' of risk management (ie Tolerate, Treat, Transfer, or Terminate the risk) play out differently by the combination of likelihood and consequence. See for example HM Treasury 2004, The Orange Book - Management of Risk - Principles and Concepts at http://www.hm-treasury.gov.uk/d/orange_book.pdf (Eg 'Tolerate' is appropriate for Lower risk, Terminate the process for Higher risk etc.).

In its approach to risk management the ATO follows the standard for risk management – ISO31000[34] - derived from ASNZS 4360.

Figure 7
The AS NZS 4360 Risk Management Steps

We should note that risk management frameworks bring with them relatively mature and robust approaches to the prioritisation of very different risks for treatment – a key facet in considering compliance interventions.

Like most organisations, the ATO has utilised a risk matrix as a conceptual aid for displaying and considering relative risk levels of various, and often very different, risks.

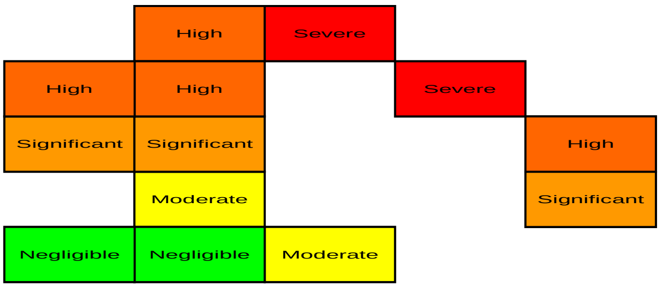

Figure 8
Example Risk Matrix

[34] Available at http://www.riskmanagement.com.au/

An issue was how compliance 'view' of risk might best fit with these broader risk management approaches. For example, if we have two clients with the same likelihood of potential non-compliance, but significantly different relative and absolute consequences of non-compliance, who should we prioritise for review and how should we map[35] them onto a risk matrix?

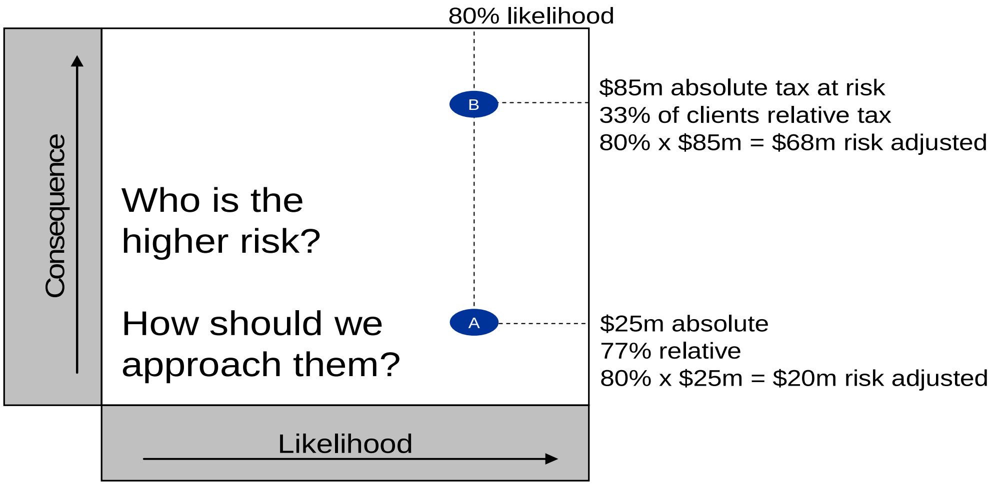

Figure 9
Differing absolute ($) or relative (%) risk positions[36]

- How should we best combine or take into account in our risk prioritisation, concepts such as relative non-compliance (eg client A evaded 77% of their tax – a view of severity of offence) and absolute non-compliance (eg client B evaded $85 million of tax)?
- How should leverage aspects, such as the influence or impact over clusters of clients that a market leader or an advisor might have, come into the picture?
- Can we find features associated with 'attitude' towards compliance (however that might be effectively and consistently estimated beforehand) or are we in practice largely limited to identifying potential non-compliance before client contact is made?

A further, and very important, consideration for a tax administration is how should possible avoidance[37] (bending the rules or having a tax position the Commissioner regards as contentious) figure relative to possible evasion (breaking the rules)?

[35] The scaling of the likelihood and consequence dimensions of a risk matrix is an 'informed judgment' by the organisation. Eg Logarithmic scales (eg by factors of ten) may be used for plots of absolute consequence and likelihood. The choice between say linear or logarithmic scales depends on the nature of the risks being plotted, what the tolerance for risk is and how many risk levels it wants to identify. A risk matrix is essentially a prioritisation tool for sorting risks, and hence scales that best suit the organisations decision-making on risk should be used.

[36] See Hamilton, S 2006, Optimising Compliance – the role of analytic techniques, available at http://www.itdweb.org/documents/Optimising%20Compliance%20-%20Role%20of%20Analytic%20Techniques.pdf for a deeper discussion.

As previously noted, we need to be able to effectively approach the compliance pyramid, with its responsive regulation concepts, in situations where compliance itself is uncertain, for example where the law's application to a set of facts and circumstances may be unclear and a reasonable contention exists.

This 'zone of uncertainty' in the operation of the law may range from facts and circumstances that appear to be legitimate tax minimisation, through to arrangements that appear to have little commercial purpose other than to obtain a tax benefit[38] not otherwise available.

It should be noted that, for large corporate clients involved in complex transactions this uncertainty of 'what is compliant' is associated with most of the risk of being viewed by the regulator as being potentially non compliant.[39]

[37] See the discussion in Chapter 1 "Tax Avoidance" of Pagone, G. T. "Tax Avoidance in Australia", The Federation Press, 2010.

Represented as a scatter plot of compliance risk we are likely to have something like:

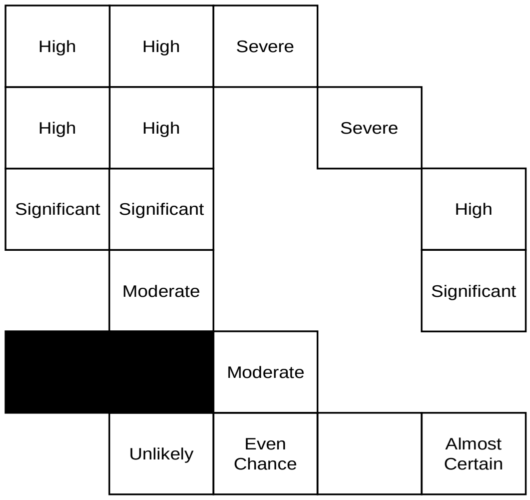

Figure 11
Most clients have a lower consequence and lower likelihood of non-compliance – most clients are compliant most of the time

There is a natural logic to this. In both cases the probability distribution of clients would generally follow a scale invariant[43] inverse power distribution[44], such as Pareto, of a few large consequence or higher likelihood clients and many lower likelihood/consequence ones. It is the way nature and regulatory systems generally work.

The reason for this in living systems is both obvious and subtle: viable systems adapt to reduce the impact and/or the likelihood of severe events, making them relatively 'rarer' over time. If they didn't the system wouldn't 'survive' long term (eg prohibition in the USA). This result will hold true whether our view of risk is event based or whole of client. A whole of client risk view is essentially a summation of the client's risk events.

[43] Essentially the shape of the distribution looks similar at all scales: eg the shape of cummulative tax paid by a hundred clients, a thousand, or a million etc.

[44] Eg one over x to the nth power ($1/x^n$) so small values of x are more probable than large values. In nature (many creeks few continent draining rivers) and in human systems (many towns few mega cities, many small taxpayers few billion paying taxpayers). See for example: Newman, M 2006 Power laws, Pareto distributions and Zipf's law at http://aps.arxiv.org/PS_cache/cond-mat/pdf/0412/0412004v3.pdf

It is not a simple ‘add and average’ since probabilities are involved, but the mathematics of forming a whole of client view is not really that complicated.[45] On the other hand how you form a view on the probabilities themselves can be quite complex; using either ‘decision rules’ from subject matter experts or, if sufficient data exists, from predictive data mining approaches – eg logistic regression, neural networks, decision trees etc.[46]

Having formed a risk based view of where a client sits relative to other clients we can then consider who we may want to, or can focus on – those who appear to present a higher relative risk. One way of thinking about this is to imagine that we are essentially zooming in on ‘who’ we might have compliance ‘concerns’ about and therefore may want to review.

We do this by considering the potential consequences of possible non-compliance as well as our view of the likelihood of non-compliance. (Eg A larger client generally warrants a different level of interaction and investment to a smaller client.) Clearly, from a risk management perspective, we will have a more significant interest in, and need for assurance with, higher consequence clients or events than lower consequence ones.

Equally we will be more interested in reviewing those clients or events that have a higher likelihood of being non-compliant (having a contestable position – one that we have concerns with) than those with lower likelihoods.[47]

---

[45] Overall likelihood for ‘n’ mutually exclusive ‘i’ risk events: $L_n = \Sigma(L_i \times C_i) / \Sigma(C_i)$. [Note this is not the average likelihood $\Sigma(L_i)/n$’ unless all risks have the same consequence.] The overall consequence is: $C_n = \Sigma(C_i)$ and the overall risk is: $R_n = L_n \times C_n = \Sigma(L_i \times C_i$

Figure 12
Timing and importance of detection efforts

If we then map a client engagement approach based on timing and frequency of the suggested detection effort - periodic to continuous (ie ~near real time) and the type and intensity of detection effort - passive monitoring to active review, the following risk differentiation framework emerges for the large market:[48]

Figure 13
Detection strategies/investment laid over a risk matrix

This framework is the basis of a risk differentiation framework now being used by the Australian Tax Office for its large corporate clients. Similar approaches are being used for advisors and intermediaries.

[48] For areas with much larger client numbers the engagement stances associated with the risk categorisations clearly need to be modified to match capability and cost effectiveness. The engagement stance should always be an appropriate and proportionate response to the risk posed.

Giving the quadrants broadly representative names[49] we derive the following:

Figure 14
Service, enforcement, leverage and client focus

This isn't really a radical change to the way the Australian Tax Office has been dealing with its clients in the large market in the past – it is very much a logical framework within which to set and guide what they have been doing day to day.

By taking into account consequence, it makes explicit that there is a set of clients in whom we may need to make an extra investment to keep them from moving 'up' the compliance model.

These are the 'Key clients', where the precautionary principle of risk management is of increased importance – where you don't want to wait for things to go wrong if they can be reasonably prevented and where it is important to be able to demonstrate to the broader community that the largest players are being appropriately monitored by a prudent regulator.

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In one sense this is a level of recursi

- For those clients with relatively higher consequences (often the largest clients or those with significant influence in the tax system) the logical strategy is that the regulator would invest more time and effort in trying to reduce the likelihood of non-compliance – of the client having a contentious tax arrangement.
- For those clients with lower conseque

The generally long lead times of legal processes don’t help in this regard and it

Successfully addressing clients in 'market time' who breach the 'dam wall' is clearly a priority for any effective compliance strategy otherwise more risk-neutral clients[55] will become involved.

Such breaches can be opportunistic constructs of advisors, devised for a particular business situations faced by a large client. The advisors or others associated with the transaction then may use the template of the approach and promote[56] its use with other clients, facilitating a break-out of avoidance activity that exhibits the classic "S" innovation growth curve.[57]

The risk differentiation framework provides for the needed higher level of focus on clients that are, based on past experience and current market intelligence, perceived as being more likely to be involved in such contentious approaches.

A key caveat with all of this is that frameworks are broad guides rather than absolutes and they do not mandate, nor sanction, the use of an inappropriate approach, given an understanding of a client's facts and circumstances. The framework should provide guidelines for engagement - rather than tramlines for action.

The framework does not suggest that a higher risk client has made an error or is non compliant. In the large market it is about coming to an informed professional judgement, using the limited amount of information available, of who is relatively more likely to have a significant contentious arrangement. Identifying and resolving those contentions, whether by agreement or by going to the Courts, is key to providing increased certainty of tax outcomes to the market.

In the framework, tax attitudes and behavioural indicators would be expected to differ between the left and right hand sides. However there is no sharp divide between the two sides, rather a spectrum of behaviours that change from left (lower likelihood) to right (higher likelihood).

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[55] "Saints, Swingers, and Sinners" is a simplistic, but useful, mnemonic of some broad groupings of a regulated population to be kept in mind. One can think of the 15% to 20% or so risk averse as being "Saints"- who won't cheat or bend the rules even when highly unlikely to be caught or punished, "Sinners" as the 15% to 20% or so risk takers who are more likely to defy the system and gamble on

For example, broadly speaking, higher and medium risk clients might be expected to have some aspects of the following behaviours,[58] none of which is definitive:

- Relatively low effective tax rates over time (compared to peers, partners, or the past) that often appears to be at odds with the economic outcomes being achieved.
- A history of relatively aggressive tax positions that the regulator has concerns about.
- Relied on non disclosure or limited disclosure of significant, potentially

One thing to keep in mind is the significant information asymmetries involved here:

- o The taxpayer will generally have a deep, detailed knowledge of themselves, the transactions they have entered into, and probably a reasonable degree of awareness about those of their immediate competitors, but little about their claims relative to the distribution for the entire business population.
- o The tax regulator, on the other hand, has a wide but very limited set of information about all taxpayers, primarily that which is on the tax returns and activity statements, but little specific information about the businesses transactions that go to make up the high level summary detail in those returns and statements.

The regulator's view of a client's risk, determined by the evidence and information they have about all clients at a point in time may well differ from a client's view of their risk. This is not unexpected given the significant information asymmetries that exist.

While in the majority of cases the regulators view of client risk and the client's view will in fact coincide, as most clients are viewed as lower risk or key, it is not surprising that views of relative risk for the much smaller number of 'higher risk' and

7. USING THE RISK DIFFERENTIATION APPROACH IN PRACTICE

In practice the ATO's Compliance Risk Differentiation Framework[59] serves several purposes:

- It provides an overarching framework for differentiating engagement stances with taxpayers according to an informed 'professional judgment'[60] of their likelihood and potential consequences of non-compliance.
- It enables a coherent, consistent and informed approach to form a view of a taxpayer's relative risk of non compliance, taking into account the multiple factors associated with likelihood and consequence, and the intensity of the response to that risk.
- It allows the communication of the approach, and view of a taxpayer's risk categorisation, to the taxpayer in an open and transparent manner so as to enable an informed discussion about their perceived risk of non-compliance.
- It facilitates resource and capability discussions and decisions regarding quite diverse compliance risks[61] (eg Transfer Pricing, Thin Capitalisation, Capital Gains Tax Reduction, Inappropriate use of losses etc) all within a consistent framework.

Using a range of risk filters and factors,[62] the ATO formally profiles large businesses twice a year (when enough comparative data from Tax Returns exists and the timing allows for substituted accounting period taxpayers, late lodgers, self amendments to be appropriately considered) against previous results and data from other businesses, both domestic and international.

This 'past and peers' quantitative analysis is then supplemented with qualitative intelligence from other sources (media, external databases, observations by field staff, other tax administrations etc) regarding potential problem areas, to place large market taxpayers into one of the four risk categories of each tax type (Income Tax, GST etc).[63]

- Higher risk, (relatively higher likelihood and consequence)
- Key Taxpayer, (relatively lower likelihood and higher consequence)
- Medium risk, (relatively higher likelihood and lower consequence) and
- Lower risk, (relatively lower likelihood and consequence).

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[59] The Risk Differentiation Framework is available at: http://www.ato(e(ue0 Tb6 cs 0 0n,A/es,poetce-7m 26 Tw xpas 0.e6 r.2(m)t.asp.2(m)?ally9)3.2(m)o)(t)c=b6 rt

The risk categorisation in the large market is thus an informed professional judgement, using intelligence available at a point in time, rather than something produced at the push of a button. As the information set changes or is enhanced, the categorisation of a client's relative risk may change.

Importantly, the risk categorisation of a taxpayer does not in any way influence the outcome of a possible risk review of a client nor the choice of remedy – that of course depends on the facts and circumstances found regarding their compliance obligations. However it does influence the initial likelihood and initial intensity of a review.

The numbers of taxpayers placed in each category is informed by analysis of the Pareto-like distribution of taxpayers and their risk and the ability to resource responses to that risk:

- Relatively few taxpayers, about 2%, are considered higher risk,
- about 8% are considered key taxpayers and these account for the majority of income and other taxes paid,
- roughly 25% of large market taxpayers are categorised as medium risk (selected for a variety of risk themes such as compliance assurance of large claims, risk scoping of new arrangements, and some for potential enforcement), and
- the majority, about 65%, are considered relatively lower risk.

(These are indicative percentages only and may vary from year to year as risk themes change.)

8. ENGAGEMENT STANCE

For higher risk taxpayers, the suggested engagement stance is a real time/continuous risk review. These taxpayers matter a lot and often set the tone for the market. Accordingly, the ATO assigns sufficient resources to enable it to identify, review and understand any material transactions that have the potential for tax planning so that it can quickly form a view as to their appropriate treatment, ideally before that tax return has been lodged.

For key taxpayers, the framework is suggestive of a continuous monitoring stance. Most of Australia's largest businesses fall into this category, they pay most of the taxes and they have significant influence on the tax system.

As major 'payers and players' the actions of key taxpayers matter a great deal to the overall health of the tax system. Hence the ATO has a particularly keen interest in appropriately verifying that the key taxpayer's risk management and governance frameworks adequately identify and mitigate tax compliance risks.

Most taxpayers categorised as key taxpayers engage with the tax office to seek or understand the Commissioner's view on a potentially contentious matter, whereas our experience has been that higher risk taxpayers largely 'default to detection' by the Tax Office – hence the larger investment in detection effort by the Tax Office with these taxpayers.

compliance

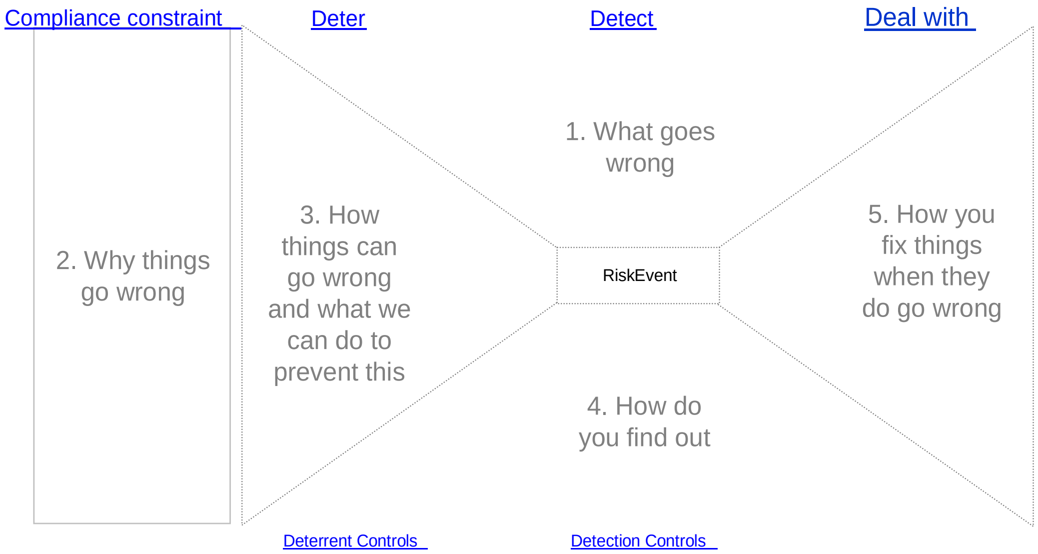

Figure 22
Risk bow-tie concepts

Now if we begin to populate a regulatory risk bow-tie with the compliance constraints:

- (why things go wrong – knowing what compliance is, wanting to comply, and, being able to comply), and the
- compliance strategies (eg for the knowledge deficiency compliance constraint, what we do to address that deficiency by use of targeted or marketing campaign education programmes, and ensuring that we have appropriate and influential exemplars of what 'good' compliance is, etc),

we start to flesh out a much more complete and nuanced 'end to end' deter, detect and deal with risk management narrative.

the regulator should consider ‘who’ needs this knowledge and ‘how’ important are

Both the risk differentiation framework and the compliance model are explicitly encapsulated in this more holistic risk management approach to regulatory compliance:

- Input from intelligence sources is used to form a view of where taxpayers sit in the risk differentiation framework – which guides engagement and detection efforts – so the risk categorisation of a taxpayer is a key output of

> "Any risk based framework is only as good as those who implement it, and risk based frameworks may not be implemented in such a way as to deliver on their promise of producing dynamic, risk sensitive regulation.
>
> Whilst senior management in each regulatory agency are clearly committed to the principles of risk based regulation, in any organisation, bridging the gap between senior management and those at the front line is a core challenge, and regulators are no exception. Re-skilling is always hard to achieve. It is particularly hard in the case of risk based approaches because, as senior officials in each regulatory agency recognised, the frameworks are requiring officials to operate 'outside their comfort zones'.
>
> Ensuring that front line officials move from a compliance or comparatively passive supervisory mentality to the more reflective and dynamic approach that risk based regulation is meant to introduce will take time, and some organisations and some parts of an organisation will move faster than others."

It is a difficult cultural change to progress and refine over time and there is a danger of an undue initial focus on the risk process activities and outputs rather than on the broader systemic, longer term outcomes. In particular those few categorised as higher risk are likely to strongly disagree with the regulators viewpoint and complain about the approach to the regulator, the media and ministers.

There is no getting around the fact that using any risk management approach to verify compliance requires the regulator to have a process to form a reasonably robust view of a client's risk of non compliance and how that risk sits relative to other clients – their priority for action. This risk prioritisation process is quite fundamental to risk management and will exist for any regulatory risk assessment system. (For example the Australian Prudential Regulatory Authority's "Probability and Impact Rating System" and "Supervisory Oversight and Response System"[80] shows a very similar coupling of risk and regulatory response.)

11. DEVELOPMENTS IN THE UK REGARDING REGULATORY APPROACHES

Looking further a field, an analysis of other countries regulatory best practices indicates that in some ways the UK has moved past Australia in modernising its approach to risk based regulatory guidance, enforcement and sanctioning.

For example, the UK Hampton Review "Reducing administrative burdens – effective inspection and enforcement"[81] which culminated in the UK Statutory Code of Practice for Regulators[82].

to regulatory work that, crucially, included explicit consideration of the likelihood and

These UK reports effectively took forward the earlier good work contained in the Australian Law Reform Commission's 2003 report "Principled Regulation: Federal Civil and Administrative Penalties in Australia"[87].

In my view there are real and significant opportunities for Australia to learn from the UK experience in setting up a consistent code of conduct for regulators as well as bringing non criminal regulatory compliance sanctions within a single coherent framework.

Rather than being faced with a large and bewildering array of differing regulatory

Those administering regulatory compliance systems need to have a clear strategy that sets out how they intend to encourage voluntary compliance - with a key risk to that intent being that clients don't voluntarily comply for a variety of reasons.

The Ayres and Braithwaite regulatory pyramid sets out a model for a choice of compliance remedy for administrators - and it is by differentiating our regulatory strategies by likelihood and consequences of non-compliance that we can more appropriately position ourselves to bring that model to life.

Bringing this more holistic view of compliance and risk mitigation together effectively adds another dimension to regulatory compliance approaches and enables a richer and more nuanced discussion to take place regarding compliance strategies and their targeting and timing.

The approach that has been outlined in this article provides a way of looking at the risk end to end, answering:

- o the strategic question of what risks are important (credible threat agents intersecting with critical system vulnerabilities),
- o the operational question of who may have or exhibit those risks, and
- o the tactical question one of how to best deter, detect and deal with the instance:

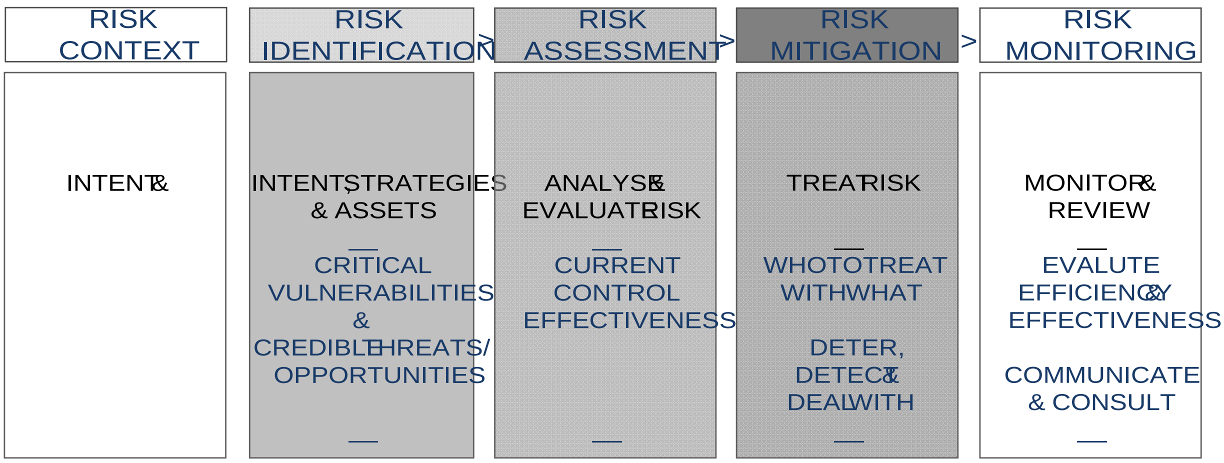

Figure 25 Bringing it together – End to end risk management

It provides a way of looking at managing a risk from discovery of a 'matter of interest' through to ongoing activities to systemically deter, detect and deal with 'matters of concern' - an approach for appropriately considering and dealing with both emerging

ANNEX 1: VARIATIONS ON THE COMPLIANCE PYRAMID THEME

The concept of the compliance pyramid has been taken up by others and, though remaining broadly consistent to the Ayres and Braithwaite model, there are some subtle variations:

Figure 27 A more recent representation of the compliance pyramid at the Australian Taxation Office
http://atogovau/corporate/content.asp?doc=/content/5704.htm
Australian Taxation Office, Australia

Figure 28 The 2004 UK's Inland Revenue version
http://www.hm-treasury.gov.uk/media/2/0/odonnell_ch2_497.pdf
Chapter 2, page 31, in Financing Britain's Future, Review of the Revenue Departments by Gus O'Donnell, March 2004, HM Treasury, United Kingdom

Figure 29
The 2006 European Union Fiscalis Risk Analysis Project
http://ec.europa.eu/taxation_customs/resources/documents/taxation/tax_cooperation/gen_overview/Risk_Management_Guide_for_tax_administrations_en.pdf
Risk Management Guide for Tax Administrations, Fiscalis Risk Analysis Project Group, FINANCIAL CODE: FPG/11, Version 1.02, February 2006, Page 33

Figure 30
The New Zealand Inland Revenue Compliance Pyramid
http://www.ird.govt.nz/aboutir/reports/annual-report/annual-report-2004/part3/annual-report-2004-part03-02.html New Zealand Inland Revenue, 2004

Figure 33
Australian Medicare Compliance
http://www.medicareaustralia.gov.au/resources/national_compliance/national_compliance_program_2007-08.pdf National Compliance Program, 2007–08, Medicare Australia

Figure 34
Australian Communications and Media Authority
http://www.acma.gov.au/WEB/STANDARD/pc=PC_312247
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