ISSUE 30

TAX TRIBUNE

Magazine of the Intra-European Organisation of Tax Administrations

12 Technical Articles

In Focus...

IOTA Technical Activities Programme 2013

Dear Readers,

Mr. Miklós KOK
Executive Secretary of IOTA

It is with a great deal of pleasure that I introduce our 30th issue of the Tax Tribune, the annual magazine of the Intra-European Organisation of Tax Administrations (IOTA), which reflects on our 2013 Work Programme.

IOTA events in 2013 attracted well over 850 participants from 45 member tax administrations. As in previous years, several IOTA technical events were attended and supported by highly qualified speakers from the Organisation for Economic Co-operation and Development (OECD). The annual programme covered a wide variety of topics which addressed the most important and urgent problems modern tax administrations are facing. In our magazine, we would like to reflect this diversity of challenges by including articles from the widest field of practical tax administration issues possible. The range goes from the role of administrations to stimulate voluntary compliance through actual practices of exchanging tax information, managing the challenges posed by e-services to fighting tax evasion and avoidance.

In this issue, you can read articles which are based on presentations delivered at different IOTA workshops. Some tax professionals felt it important as a direct consequence of their participation in an IOTA technical event to share their thoughts with the readers based on their first hand impressions and experiences. Articles such as "Improving Compliance by Education", "Providing Assistance to Start Up Business" and "Engaging and Involving SME's in Tax Administration Processes" all build on the experiences gained from the interaction with representatives of other tax administrations.

This year IOTA continues to focus on the practical aspects of tax administration operations through the delivery of its technical work programme, hoping to generate a great deal of interest and attract more and more participants from IOTA members. The Organisation itself also faces many challenges in a constantly changing environment and the IOTA management aims to support the evolving demands of the membership. The current development efforts might sometimes result in a temporary fallback in delivery outcome, but the quality of our events are of utmost importance for us to facilitate the exchange of best practices between tax administrations regardless of any structural differences.

Unlike previous editions of the Tax Tribune, the 30th issue will only be published digitally on the IOTA Website, as we have to adopt new communication channels and also strive for a "paperless" administration. Moreover, at a time of considerable resource constraints, efficiency and innovation is becoming more and more important also in this field. The content, however, still remains similar to the previous paper versions. Another slight change is that we have reconsidered the frequency of the magazine. We thought it would be helpful for the reader to be informed about current practices of the tax administrations in the magazine in each quarter of the year.

I would like to express my sincere thanks to all authors of articles and to you all for your active interest in IOTA. I hope that all of you will find something of interest in this edition of Tax Tribune and I would like to invite you to also participate in our events in the second half year of 2014.

Miklós Kok
Executive Secretary

Articles

Improving Compliance by Education in Austria

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By Manfred ELMECKER

AUSTRIA

The contribution of the Austrian Tax & Customs Administration started with the idea of citizenship. We see an important mission to engage with future taxpayer (e.g. young people at school, students at the university) to make sure that they understand the role that taxes, social welfare contributions or other public fees play in their own lives and in helping society to function.

Several years ago, the Ministry of Finance launched the revenue strategy "Ensuring revenues through strengthening the economic place of Austria". For operationalizing this strategy, we developed the "Fair Play"-Initiative.

Fair Play is a package of support, control and anti-fraud measures devised to increase tax & customs compliance, with the following objectives:

- Increasing tax & customs morale (tax & customs compliance) through proactive involvement of businesses and citizens;
- Developing and discussing (im)possible ideas, methods, instruments, etc. for the interaction with different stakeholders;

- Ensuring the financial interests of the Republic;
- Ensuring fair competition for the honest economy.

The Austrian fiscal authority is not only interested in international developments but also assumes an active role of enhancements itself. The offensive examination of tax & customs compliance in that sense seems a good idea as a further development of the administration itself and also in terms of educational measurements. Institutional and interactive arrangements, interrelations between special interest groups and a selective management network build up the background for the methodology, which is based on the strategy and the fair play initiative.

In the present article the focus rests on the following selected examples of educational activities (it's an incomplete list):

- Education and training are determining factors in tax & customs compliance. As we talk about a paradigm shift (the "Fair Play"-Initiative) we are aware of the fact that, first of all, it is necessary to raise awareness amongst the employees of the tax administration. The topic of tax & customs compliance is nowadays an integrated part of the internal basic training courses.

- In parallel, education in tax matters is taught in certain schools to explain why taxes are levied, on what they are spent and what this means for the youngsters. We have produced special documents, brochures and videos, which are used in the classroom. Furthermore we have developed our own "educational homepage" for the young generation (www.finanzvifzack.at)

Beside a lot of information about taxes & duties, basic knowledge in business matters, etc., we offer on this website, Mobile Apps, e-Learning tools and the access to the Facebook site and Twitter account of the Austrian Tax & Customs Administration.

Tax & Customs matters are taught within regular lessons. We made a co-operation with the Austrian School Administration. Our "offer" is on a voluntary basis; which means that the teachers can demand the input from the Tax & Customs Administration. The request for "Tax & Customs-Gigs" by the different schools is very high. Every School has its own contact person from the tax or customs side. Our employees, who are going into the classrooms, were trained for these "challenges" and they get regular support.

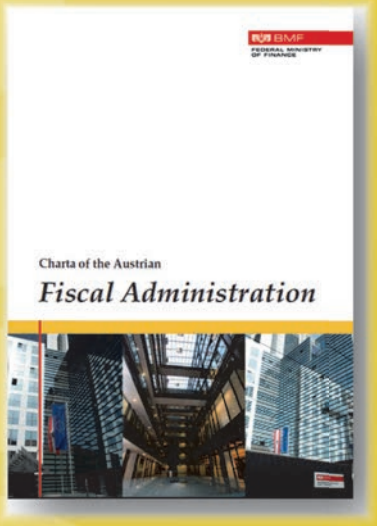
- During the last few years the Austrian tax administration has advanced the development of training and schooling with the co-operation of the Chamber of Tax Advisers. In 2011 a teaching profession called "Assistant in Taxes" started. Every year 60 teenagers will have the opportunity to start their careers at local tax offices. The duration of this professional education takes three years. Beside their work the teenagers also attend every year a special vocational school for ten weeks. Nowadays, we educate 240 young employees in tax & customs matters.

- On the academic level a bachelor and master's course of studies was developed - called "Tax Manager". The idea behind both qualifications is that graduates can work either within the tax administration, in

the tax department of a company or at the office of a tax adviser. Further information is available at the website: www.fh-campus.ac.at.

- For a visual possibility of explaining the tasks of the Austrian Tax & Customs Administration we have produced several video-spots. For example, the film "What happens with the Tax-Euro" explains how and for what revenues are spent. All the videos can be downloaded from the homepage of the Austrian Fiscal Administration (www.bmf.gv.at – Videoportal).

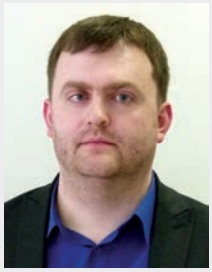
- Charter of the Austrian fiscal administration: Through the Charter, the Austrian fiscal administration has committed itself to a co-operative partnership with taxpayers. The Charter includes – besides the design of duties and responsibilities of the fiscal administration, services for citizens, as well as citizens' rights and responsibilities – and standards in quality and performance. Even so, it maintains its definitive commitment to the mission and core tasks. The Charter is available on the website (www.bmf.gv.at).



Over the last few years, Austria has become a space of reference in tax & customs education matters. Its formal and non-formal educational experience is a valuable asset for other countries that wish to create programmes or strengthen their strategies in this area. However, there is still a long way to go until the idea of tax citizenship is able to permeate the regional population and tax education is consolidated as a public policy.

Tax & Customs education strategies, like any educational process, are always medium or long-term and involve constant effort. The short-term challenge is to ensure that tax education becomes, in the eyes of citizens and public authorities, a relevant part of social transformation, enabling a critical reflection and better understanding of taxation and its relevance in the complex jigsaw of social cohesion.

The Easy E in the Estonian Tax and Customs Board



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Valeria Kadyrova is working in the Service Department and she is responsible for developing taxpayers' services. Her tasks for the next years are to implement a new homepage of ETCB and to work out a new concept of electronic self-service channel.

By

Rivo REITMAN, Head of Service Department
&
Valeria KADYROVA, Chief Expert of Service Department

ESTONIA

Nowadays it is almost impossible to imagine life without computers and Internet. IT devices and software have become an integral part of everyday work and consequently part of the work of tax administrations. The service strategy of the Estonian Tax and Customs Board (ETCB) is based on developing electronic solutions for taxpayers as well as for tax officials. Using e-solutions helps to make fulfilling tax liabilities and interacting with the ETCB easy, fast and streamlined for taxpayers – both for those who use electronic services and for those who prefer to organise their tax matters in service offices.

SERVICE STRATEGY OF ETCB FOR 2013-2016

Our brand new service strategy. Why and how we do it.

Simplification of the fulfilment of tax liabilities through the improvement of the quality of services provided and through implementation of innovative communication channels

An important issue in the field of service management is the reduction of the administrative burden of customers and the flexible approach regarding the needs and expectations of the target groups. Further development of already existing services, service channels, and implementation of new innovative solutions are equally important. All the solutions should enable the customers to fulfil their tax liabilities in an easy, fast and convenient way, regardless of the place where the services are needed or of the channel of service provision. Feedback from customers enabling to ascertain their needs and expectations carries the decisive role in the development of service management.

Enhancement of the law compliance of taxpayers through the development of communication and influencing methods

The most important factor in increasing the voluntary compliance of taxpayers with the law is the timely provision of correct information. The tax authority should take proactive role in communicating with its customers, making efforts to learn the wishes and problems they might have already in advance. ETCB tries to provide information to customers in plain language and customers feel the supportive attitude of the tax authority at fulfilling their obligations. Availability of high quality information for customers enables them to fulfil their obligations through self-service channels needing no further assistance from the tax authority. Provision of explicit information by the tax authority of the one part and confidence of the customers in the tax authority of the other part will ensure the increase of voluntary payment of taxes.

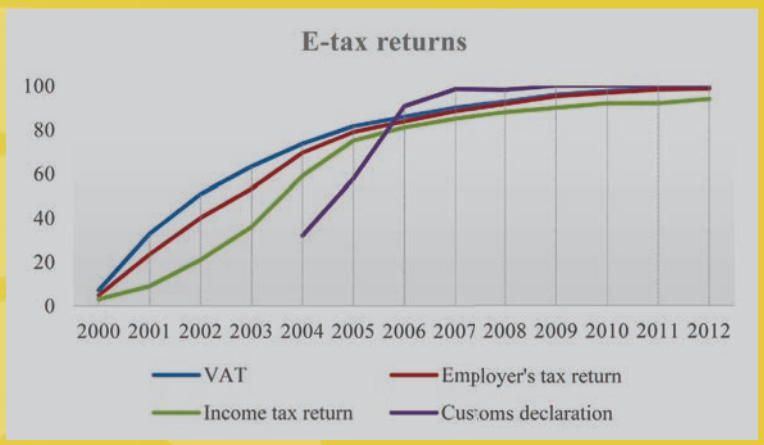
Making the service and work processes faster and more effective

The selection and application of the right work formats and service management measures, by means of which it is possible to achieve the best results at the same time using less resources, is of great importance for the development of the service line. Consistent analysis of the activities helps to find new possibilities for making the processes faster and more efficient. Automated systems replace manual work. Data collection for making sound decisions must be fast and effective.
The success in reaching these service objectives are measured by increased customer satisfaction, an increase in the number of customers who are using self-service channels and who have become more observant regarding reporting and following the law, as well as decreased cost of work processes.

THE RECENT SOLUTIONS IN ETCB

There is a wide variety of service channels that customers can use to communicate with the ETCB and fulfil their tax obligations. The most important is the electronic service channel e-Tax/e-Customs that was opened for use in 2000 already. It is significant to mention that the ETCB was the first government agency in Estonia that started to offer e-services to its customers.

(The growth of e-tax returns)



E-services provided by the ETCB are constantly being improved; taking into account the user's proposals, as the customers' needs change quickly. At present, taxpayers conduct an average of over 96% of their tax operations by electronic means, thus, it can be said that they have adjusted well to the changes and expect the development of comfortable services.

In addition, many other channels have been opened to offer every taxpayers' group the most comfortable way to communicate with the tax administration, e.g. service offices, homepage, contact centre

(incl. phone calls, e-mails and Skype), social media channels (forum on homepage, Twitter, Facebook), campaigns, fairs and information days. Trainings on taxation issues are organised and are very popular among taxpayers. In addition, the ETCB is linked to governmental channel X-Road that enables secure Internet-based data exchange between the state's information systems.

There are two new key services developed for taxpayers in 2013:

1. Providing online information for taxpayers about their monetary and non-monetary obligations

Since January 2013, the new notification system IRIS is in use. The system manages the taxpayers who do not pay their taxes or file tax returns on time. The system also provides pre-notification if the due date of tax payment or tax return filing is close. IRIS is a complex system that automatically sends e-mails (pre-notifying and notifying) and SMS-s (pre-notifying and notifying), sends orders semi-automatically (to pay your taxes or file tax returns, also orders to arrest your bank accounts).

This system is innovative in many ways. Firstly, management of tax arrears and tax return submission is in one system. The notification sent to a taxpayer contains all information about taxpayers coming and already arrived liabilities. Secondly, IRIS is a system which allows first steps to be made towards electronic delivery of administrative acts. IRIS delivers not only administrative acts electronically to taxpayers but also generates them electronically. The signed act is sent to the customers' mailbox in e-Tax/e-Customs and at the same time e-mail/SMS notification is sent to the taxpayer (she/he should log into e-Tax/e-Customs to view the document). If a customer visits e-Tax/e-Customs then he/she can see only this act (all other functionalities in e-Tax/e-Customs are disabled until opening administrative act). If a customer does not visit e-Tax/e-Customs within 7 days the tax official sends the administrative act by post. If the taxpayer is not an e-Tax/e-Customs user the tax official prints the administrative act out after creation (it is still created and signed electronically) and sends it directly by post (administrative act is not sent to e-Tax/e-Customs).

2. Generating and forwarding certificates electronically

Since May 2013, every user of the e-Tax/e-Customs can generate their own certificate of absence of tax arrears or statement of balance electronically. It is also possible to send the certificate as an official document to the e-mail address of the institution or organisation that needs the document, using the digital stamp. A digital stamp is used for certifying digital documents and it certifies that electronically sent documents or other information really originates from the institution that sent them.

PRECONDITIONS FOR DEVELOPMENT OF E-SERVICES

To develop high-quality services for taxpayers the ETCB highly appreciates their opinion and gathers information about their behaviour. There are several channels open for customers to give feedback: e-mail, phone, service offices, and a special feedback form on the homepage. Since 2011 the Promoter Index method has been in use to collect the information about services and service quality. Promoter Index is a special web-based customers' feedback system that enables receipt of feedback about a specific service case and reasons of satisfaction or dissatisfaction. Promoter Index shows how good the service is and what the trend is as well as enables to start dealing with shortcomings instantly.

To analyse the customers' behaviour and to know the reasons of customers' contacts as well as to collect their preferences, the Customer Relationship Management (CRM) system was implemented in 2011. The main purpose of implementing CRM system is to map the reasons of face-to-face contacts in service offices. This kind of information (analysis) indicates in what area the ETCB has to develop/advertise ICT facilities so that customers do not have to visit our service offices. In addition, it is possible to register calls and e-letters, to manage customers' preferences (i.e. the language a customer prefers to communicate with the ETCB, whether a customer prefers to communicate electronically etc.).

CONCLUSION

As tax collecting and payment of taxes have been rather unpopular activities from the beginning of time, the task of a tax authority is to change this attitude, as much as possible by providing high-level services, and fair, straightforward communication. Developing e-solutions and automated work process helps to reduce administrative burden of taxpayers and the costs of tax collecting for tax authority.

(Contacts in service offices are continuously reducing)

The straightforward focus on e-strategy has resulted in reduced number of contacts in service offices. This as a consequence has helped to stop customer running, reduce paperwork and save time spent on simple procedures, and to focus resources more on complex procedures (for example on tax audits).

To conclude, the success of developing and managing taxpayers' services are based on the following things:

- Keep thing as simple and convenient as possible
- IT is only a tool, but an effective one
- Automation of processes is cost-effective
- Good service = Satisfied customer

Young People and Voluntary Compliance

Increasing the tax morale by giving the "know how"

Tiina KARBIN

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By
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Finnish Tax Administration

FINLAND

The voluntary compliance rate in Finland is high. The challenge is however how to make our complex tax system look simple and complying easy. Education and communication are in our opinion the tools needed. Young people have a vast role in the future. It is important to get their attention early when personal norms still can be influenced. The right education at the right time is essential.

Young people as taxpayers are a difficult target group because they neither have much knowledge about nor interest in taxes. In Finland we have put a lot of effort on the education of the young. We have focused on the age group 15–25, consisting of students on high school or university level. At the age of fifteen they receive their first tax cards and many look for a summer job for the first time. Older students are studying for profession and some will perhaps start their own business and need entrepreneurs' tax guidance. The age range also determines the channels we use. Students are a coherent target group and an easy audience to gather.

Campaigning in schools – Right means, measures and channels

In Finland we grow up embracing the social norm that complying is one of the citizen's duties. Even if the taxpayer role is evident, the tax education given in schools is often theoretical and less time is spent on practical guidance. The tax system is complex and taxation can be difficult to grasp. To get our message through we must have the right strategy and the right channels put in place.

Because taxation most likely is not high on the list of interests for most young people, it is useful to have an active and responsive role in tax education. School visits enable to give taxation a friendly face. Students often have a lot of questions so it is also good to have somebody ready to give the answers and explanations right away.

In spring 2013 we organized in cooperation with a number of educational institutions all over Finland a Tax Event for Students. The main target groups were secondary or high school students (15-16 year-olds) and students that were starting their college or university studies (19-23 year-olds). Our staff members visited schools on a specific day with an information package specially targeted for students. The material was freely available online so that teachers could use it both before and after the event. The feedback from the students and also from the teachers was positive.

In the future we want to improve our concept. Working together with the Finnish National Board of Education would enable more systematic and continuous planning and more equal distribution of events all over Finland.

Working together with other governmental authorities

We have positive experience of working together with the Police and the Customs who have been campaigning with us against the underground economy. The campaign Grey Economy– Black Future started in 2012. The campaign's main focus is to promote individual responsibility and underline the effects that grey economy has on everyday life. The spark for the campaign comes from the national action plan to combat grey economy and economic criminality in Finland.

A school tour has been an important part of the campaign. For the tour, we have chosen learning material that is relevant for students. Its layout has been made attractive to young people and the goal has been to represent matters in a way that interests the young, e.g. recorded tapes and comic illustrations have been used instead of normal slide shows.

The campaign will be running at least until 2015 and hopefully even longer. All the partners have found the campaign useful and the overall opinion is that it has been a great example of successful co-operation between authorities.

Reaching young men

In Finland we have a rather unique situation because all men above eighteen years are required to enter the military service. Altogether 27 000 men enlist annually so conscription time is an excellent chance to educate young men about tax matters.

The Tax Administration has been working with the Finnish Defense Forces on a regional level for several years. Our staff members have visited garrisons and held tax education lectures for groups as large as one thousand men. The material has consisted of information that the conscripts will need when they finish their service and start working or studying.

The advantage of the cooperation is that we can reach large audiences; one presentation can have a thousand listeners. Co-operating with the Defense Forces we are able to reach 25 000 men each year.

Other campaigns

Our aim is to run at least one big campaign every year that is specifically targeted at young people. This year it focused on getting the tax card over the web. We let the young participate in the making of the campaign so that they could give ideas and tell what would be the best way to share the in-

formation. In the campaign we used multichannel marketing that included radio advertising, online newsletters for schools, briefings, and academic calendars. Next year we plan to have a comprehensive marketing campaign for the entire year. The campaign will include several different themes and involve new channels such as social media marketing.

Sharing our experiences

International cooperation in taxation is essential. Voluntary compliance and the measures to increase it have been discussed in several IOTA workshops this year. In Finland we are paying more and more attention to compliance and trying to figure out ways to improve our communication strategies on compliance, both external and internal. Cooperation enables the exchange of best practices. We all share the same goal.

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Eurofisc Liaison Official since 2011 for the Observatory of Frauds

The use of open data to fight against tax evasion

By David GILLES

FRANCE

In its mission to fight against tax evasion each administration is facing the same problem; to validate the data reported by taxpayers. To meet this objective an extensive source of reliable information is required.

Due to the prevailing economic climate, the effective use of resources has become a recurring theme for tax administrations., Fortunately, despite taxpayers expecting less intervention from public authorities, easy access to a wide range of third-party information has grown exponentially.

Whilst almost all modern tax administrations have chosen the internet as a fundamental tool in dealing with taxpayers, the legal framework in which they operate is very often the result of old legislation that doesn't cater for the existence of new information technologies.

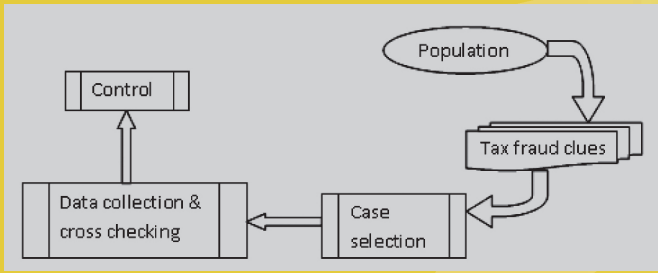
The fight against tax evasion requires a compromise between legal and IT tools that can be used against non-compliant taxpayers.

Personal data and information conveyed by social networks are now a vital element in the effective fight against tax fraud, but their use involves a change of working methods.

Structured approaches

Whilst a tax administrations' budget remains limited, they must look to optimize their resources. This search for efficiency implies streamlining information processing and reorganizing their investigation services.

Except the Guardia di Finanza (Italy), the vast majority of tax administrations are composed of civil servants the majority of who don't have a culture of using intelligence information, particularly as far as internal security and the fight against terrorist activities are concerned. This is due to continuing working methods that do not incorporate a systematic risk analysis approach to specific taxpayer populations. Surveys and cross-checks were originally made on the basis of clues that indicated a potential fraud, but rarely on its detection, following a process which could be summarized as follows:



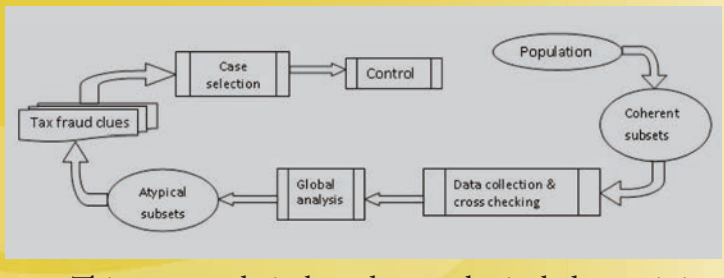
The development of risk analysis and of IT tools outside the headquarters environment made the development of this workflow possible by identifying unusual subsets within a population and comparing them with external information, and finally by selecting the riskiest cases.

This approach requires staff to be aware of the current fraud patterns and behaviours before they are able to identify those who meet the pre-defined criteria.

The limits of risk analysis come from the need to be able to easily recognise fraud patterns or behaviours. In this situation, risk analysis can't identify new trends and behaviours that are described as "normal."

However, segmentation of the population made with only internal data from the administration and not from external sources, cannot help to extend the analysis.

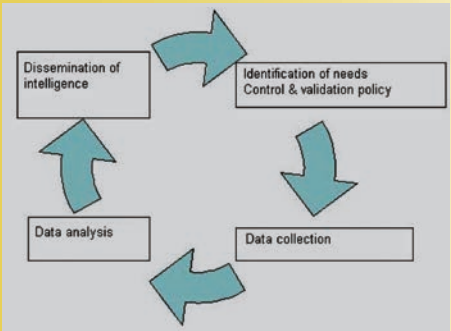
One solution is to determine consistent population subsets and enhance them with external data to extract groups of non-conforming behaviour.



This approach is based on a logical data-mining technique of comparing the definitions of consistent and atypical subsets to try and identify from the mass of potentially more important data the fraud cases, which in the first instance may involve only one identified case.

The use of large amounts of external information coming from different sources, and the successive segmentation of the large taxpayer population, imposes tight controls on the internal organization in order to avoid wasting available resources, particularly during the initial phase of information gathering and analysis.

Both civil and military intelligence professionals believe that the intelligence cycle is based mainly on the perfect understanding and knowledge of the information sources they use (SINT). For them, the main phases of this cycle (expression of needs, collection, processing, analysis and dissemination) cannot be carried out without raw materials, data or information.



These are usually classified according to their origin or type and can come from human sources (HUMINT), signals (SIGINT), open (OSINT) (IMINT) or official (OFSINT). The open classification is one element that adds value to information.

For intelligence professionals, crosschecking information sources allows data to be classified as more or less reliable and therefore to provide a strategically appropriate response to the expressed need.

Applied to the fight against tax evasion and to the detection of hidden activities or undeclared assets, this crosschecking approach is particularly relevant as the methods used by fraudsters are becoming more and more sophisticated.

Official sources

They can be called internal sources (within the administration) (INSINT) or official sources (OFSINT). Data automatically collected by a tax administration are its greatest asset, even more so when it encompasses the various calculated data (tax, various taxes, statistics...) and the annexes submitted by taxpayers (marital status, bank reference, accountant's identity, ...).

Until the late 1990s, the audits of French tax returns filed by individuals were carried out by comparing the amounts reported by taxpayers with those indicated by third parties reporting data. The information coming from third parties - employers, pension funds or social benefits, banks, professional fees, commissions and other compensation - is still the most important source of external information received by the General Directorate of Public Finance. Other than data relating to fees, commissions and other remunerations for businesses and self-employed professionals, all data has, for several years, been subject to an automatic reconciliation with the information reported by individuals. This is pre-printed on tax returns before validation by the taxpayers.

Simplification and automation of this crosschecking has helped to significantly reduce the sources of errors and omissions that could be made in good faith by taxpayers who have multiple sources of wage income. However, this is not enough when the source of income is hidden or earned outside the country of residence.

The first way in effectively fighting against the concealment of assets and income from abroad was undoubtedly the signature of bilateral tax treaties, allowing countries to share in a legal framework their tax information, which in principle is protected by tax secrecy.

However, this preliminary solution contains many limitations, among which is a rigorous formalism and the lack of freedom for countries to spontaneously send certain information.
Willing to improve its legislation, the European Union established, under Directive 2003/48/EC (June 2003), a mechanism to exchange information on savings income and to allow the proper taxation of these incomes in the beneficiaries' country of residence. This Directive also provided a better understanding of financial assets held outside the borders. Recent developments in international taxation have focused on the need for improving this legislation. Even if this directive is not yet implemented by some European States, it is used by non-European countries such as the Cayman Islands and Anguilla.

Organisations outside the EU are also affected by the need for a better understanding of the movement of goods and cross-border operations. At a European level the main risk identified is an increase in VAT fraud through sophisticated carousels, combining legitimate companies with operators whose organisation may last only a day, with the sole purpose of obtaining VAT refunds on unpaid tax.

In order to limit the risk of fraud and to provide member states with a tool for exchange of information, in 1977 the European Union implemented an information exchange system for VAT under the Standing Committee on Administrative Cooperation (SCAC). This mechanism has changed over the past 30 years, in line with the identification of new risks, and at the end of 2010 led to the creation of the Eurofisc network.

In relation to savings income, the purpose of this exchange of information is to allow tax administrations to benefit from a third source of information, designed to be cross-checked with their taxpayers VAT's statements.

The tools aimed at the sharing and exchange of information provide a very important contribution towards the fight against fraud, even if on occasion they prove to be incomplete , particularly in relation to the identification of an individuals' assets are concerned.

The implementation of procedures for the exchange of information between foreign jurisdictions belongs to the field of information coming from external sources (EXSINT). As they are of OFSINT nature from the perspective of the country of origin, they are not automatically of the same quality for the country of destination. This is due to the fact that the transmission must have taken place within a legal framework, and there may be constraints on the use of them. Some countries do not allow the transmission of criminal information for a tax or a civil case, or to a third party. Nevertheless the information arising from mutual assistance will be more relevant to evaluate data than another EXSINT coming from any private website or source.

Open external sources

The vast majority of research services within tax administrations have focused part of their data collection procedures towards external sources. The aim of this is to bypass the formalities involved in the transmission of information between countries, to provide a broader spectrum of data from different sources and to take full advantage of the potential of e-information.

To avoid confusion with free software also known as "open source", OSINT (open source) information is referred to as "open data" here, even if this word is often used to refer to information held by national government agencies and made freely available to the public.

Without listing all official OSINT sites on the internet, different categories of OSINT can be identified, including legal information about companies. Legilux (Luxembourg), Zefix or Moneyhouse (Switzerland), companies house (UK), Sunbiz (Florida, USA), INPI (France) are all accessible databases on the Internet and some of them can be downloaded free of charge.
In 2013, the French National Directorate of Tax Investigations (DNEF) carried out an experiment to identify assets, and especially real estate owned abroad by high net worth tax payers. Before starting the data collection phase, DNEF's teams identified that some U.S. counties allowed free access or free download of their database of local property taxes. Even if there was little likelihood that many French (or European) citizens had a property in Georgia or Wisconsin, the experiment on half of the counties in Florida identified several hundred French people and a number of companies with a real estate property abroad.
Many private organizations, associations, NGOs and other structures also provide public information that may be very interesting for the tax services. NGO or private individuals sometimes release on the internet classified information, such as the Offshoreleaks database posted by ICIJ in June 2013. Although this data is about only a few taxpayers, for many administrations this list is a priority because of the potential frauds that this information can reveal. From the point of view of DNEF, when this data becomes public, they can be used it for any investigation or audit, as well as for intelligence purpose.

In March 2013, the American Government Accountability Office released a report stating that at the end of 2010 the U.S. Internal Revenue Service (IRS) handled more than 39,000 records representing 5.5 billion dollars through their "offshore" voluntary disclosure program. This report highlighted the positive impact of processing mass data using data mining. Since 2010, the French tax authorities have experimented with different methods and processes to improve the quality of their data mining techniques. Under the authority of the Tax Audit Directorate, a new program was set up in 2013 to develop data-mining analysis within the DNEF. This program uses a specific data-warehouse which contains all the data related to business activities and companies' tax returns. The goal of this ex-

periment is to build a kind of VAT fraud predictive model, and if successful to expand its use to other important tax frauds.

Recently the American press revealed that the IRS had set up automated systems to collect from websites like eBay, Facebook or online payment services, data on taxpayers. The goal of this program, which is not linked with PRISM which was revealed by Edward Snowden in June 2013, is to create a large data centre with data coming from a variety of different sources, to offer the most precise view on what taxpayers do with their money, or if they buy more than they earn.

In June 2013, a French group of students posted on the web an interactive map that amalgamates the statistical data of the Paris population (income, employment, assets, etc.) with the map of the subway. This type of geolocation allows, for instance, someone to know the scale of traffic through a subway station or the typical profile of a Parisian resident. All these results, which involve nearly 2 million people, come from public data and did not require expensive investment.

Budget issues vs. individual freedoms

As the use of private data has been recently debated, tax authorities need to think about the use of external data in terms of a taxpayer's individual freedom, including respect for their privacy.

In the field of the fight against tax fraud, there is a major risk of developing technological and legal tools that could be seen as intrusive and be subject to future constraints that may be imposed by such agencies as the Commission Nationale Informatique et Libertés (France), the Office of the Information Commissioner in the UK or the Privacy Commissioner in Canada.

In order to respect the fundamental rights of taxpayers and the rules of such procedures, the French General Directorate of Public Finance recently had to submit details of the project to develop the data warehouse assigned to the detection and fight against tax evasion to the CNIL. This new tool will integrate the main INSINT data and cross-check it with OFSINT data provided by third parties as well as EXSINT from private databases.

Conclusion

Globalization of trade and the free movement of goods, capital and people at the European level, increases exponentially the opportunities to hide assets or incomes.

The development of automatic exchange of information between tax administrations is the main tool to fight against tax evasion, but remains insufficient.

The development of electronic exchanges, the increasing digitalisation of the economy, the identification of hidden assets and incomes involve the need to design tools to search for scattered data and analyse it in order to be able to highlight inconsistencies and fraudulent situations in the future.

Investment in technology to improve the access to information as well as changes in organization and in legislation will be needed to ensure the continued fight against fraudsters and ethical treatment of taxpayers will be necessary to see tax administrations remain effective in the 21st century.

Lending operation between associated enterprises from arm's length principle point of view

Transfer Pricing Case Study

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I have been working for the Hungarian tax administration in control and legal field since February 2006. I gained experiences in the first and second instances. I worked at the national level tax administration as well which is responsible for the direction and supervision of the control activity. Since the beginning of 2013 I have been working for the major department responsible for advance pricing arrangements and supporting transfer pricing controls at the Large Taxpayers Directorate of the National Tax and Customs Administration.

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Introduction

In respect of taxation transfer pricing must be treated as a high-risk area. Lending operations are the most frequent type of transactions between the associated enterprises. Tax assessments regarding pricing of these transactions are one of the most disputed ones. Thus it is very important how the judge take a position in these cases.
The controlled transaction in the court case presented in this article concerning transfer pricing tax assessment related to group financing was an international one. The involved parties are a legal entity registered in Hungary (further referred to as HUC), and a foreign company (with the abbreviation of FC). It should be premised that non of them was a credit institution.

Transfer pricing documentation of the taxpayer

Controlled transactions (loan, „deposit")
In the transfer pricing documentation of HUC there is a reference to a

loan contract, and an overview of its conditions, out of which the most important ones are the followings: FC is the creditor, while the debtor is HUC. Currency applied is Hungarian forint. The aim of the contract is short term financing. As an interest rate the followings are indicated in the transfer pricing documentation: The reference rate is 1 year HUF BUBOR and on the top of it there is an interest surcharge of 1,45%, which consists of 0,45% + 1%. Latter one is considered as a country specific risk rate. In the transfer pricing documentation there is a reference to a „deposit" contract as well, but the terms and conditions are not described.

Determination of arm's legth price
In case of the loan contract the taxpayer chose the comparable uncontrolled price method (CUP) for the determination of the arm's length price. The taxpayer examined the average interest rate which has been charged by the commercial banks in HUF corporate loans. The database used by HUC was the statistical data available on the website of the Central Bank of Hungary (further referred to as CBH). HUC applied an „annual" interest range based on monthly data considering their minimum and maximum values. Transfer pricing documentation of the transaction referred by HUC as a deposit has not been prepared. The taxpayer did not examine whether the interest was an arm's length price or not.

Result of the control procedure

Loan
During the control procedure the tax authority accepted the comparable uncontrolled price method, the CBH statistics database used by HUC, and the argumentation related to the application of the method and database. The tax authority rejected the method of the database application, namely the creation of an „annual" interest range instead of applying monthly data. The argumention of the tax authority was that in case of short term loans with monthly interest settlement the average interest rate of the actual month was more consistent with the requirements of comparability. Furthermore the tax authority rejected the adjustment of the „annual" interest range by 1%, since the country risk has been included in the interest statistical data of CBH. The tax authority made a calculation of interest based on the loan interest rates available on the CBH's website, and as a result stated that HUC accounted a higher amount of interest expenditure, so the tax authority increased the corporate tax base of HUC.

„Deposit"
In connection with the so called „deposit" transaction the tax authority disclosed that HUC defined the controlled transaction wrongly as a deposit. According to the standpoint of the tax authority the provisions of the Hungarian legal regulations should have been taken into consideration. The tax authority declared that the transaction referred to as „deposit" in HUC's transfer pricing documentation was in fact a loan granted for FC. Tax authority characterised the controlled transaction as a loan transaction, refused the standpoint of the taxpayer according to which the loan transaction was compared to deposits. The tax authority considered the loan interest rates available on CBH's website as a basis of comparison, made a calculation of interest accordingly, and as a result stated that HUC accounted a lower amount of interest revenue, so the tax authority increased the corporate tax base of HUC.

Administrative action, argumentation in the court procedure, court decision

Since HUC found the final decision of the tax authority unlawful, he filed for legal action and moved for expert testimony. The main elements of the argumentation in the court procedure and the key parts of the court decision were the followings:

Loan
I. Burden of proof, the tax authority's obligation of ascertaining the relevant facts of the case
According to the standpoint of the plaintiff (HUC) the tax authority should have proved the irregularity of the price (and not the pricing). The defendant (the tax authority) took stand as follows: HUC applied CBH statistics wrongly, due to violation of the principle of comparability the final result could't be right either. The tax authority determined the arm's length price, thus it proved that the transfer price was not arm's length. The taxpayer raised ob-

jection against that there was no motion for probation from the tax authority's side in the legal proceedings. The tax authority stated that the burden of proof lied with HUC in the legal proceding; the taxpayer should have proved that the degree of the adjustment applied and the price determined by the tax authority was not arm's length. The tax authority declared that the expert opinion was not suitable for proving that transfer price was arm's length, the expert didn't certify that the procedure of the tax authority was false.
Related to the burden of proof the most important elements of the court decision can be summerized as follows: The legal requirement related to the preparation of transfer pricing documentation lies burden of proof with the taxpayer from the standpoint of the tax base correction application. Above all, the taxpayer must document the arm's length price, the method applied to determine it, furthermore the supporting facts and circumstances. During the control procedure the tax authority had to examine whether the method pointed out in the transfer pricing documentation of plaintiff, the selected database which contains data considered by the taxpayer to be comparable, the method of the application of the database, furthermore the adjusment applied by the plaintiff were justified and whether the degree of adjustment applied was appropriate, and the range determined in this way was indeed arm's length. If the tax authority found any deviation related to the data registered in the transfer pricing documentation, the objections had to be presented and explained. Burden of proof lies with the plaintiff in the legal proceedings, plaintiff should have proved that against the arm's length price he determined, the adjustment applied by the tax authority does not reflect the arm's length countervalue.

II.
Determination of the lending operation's arm's length price
II.1. Method of the CBH database application

It was an issue to decide in the legal proceeding what the (more) comparable in case of short term loans with monthly interest was: applying the average interest rates of the actual month or creating an „annual" interest range? HUC applied an „annual" interest range, while according to the standpoint of the tax authority and the expert, the average interest rates of the actual month are more consistent with the requirements of comparability in case of short term loans with monthly interest settlement. In the judge's opinion the standpoint of the expert certifies the correctness of the tax assessment.

II.2. Arm's length interest rate of loan transaction: price or range?

HUC disapproved that the tax authority didn't examine the dispersion range of the interest rates published by CBH. HUC's opinion was that the arm's length price was a range. The expert stated that from the final result perpective HUC's calculation was correct. He agreed with HUC that arm's length price was a range, according to his opinion +/- 10% difference is acceptable in general. The tax authority emphasized that in this case using CBH statistics the arm's length interest rate could be exactly determined; if it is possible to determine the arm's length price as a single figure (price) further calculation of a range is not justified. The tax authority pointed out that there were no any sources and data which could have served as a proof of expert opinion.
The judge highlighted in the court decision that the determination of the arm's length price should be based on comparable data or based on data suitable for comparison. Value or value range, which is based on data deriving from a non-objective, non-controllable source, can not be considered as an arm's length price. In connection with the issue of price or range the judge's standpoint was the following: A range as an arm's length price can be applied only on an auxiliary basis, in case there is no possibility to determine the arm's length price as a single figure. Compilation of published CBH statistics is based on the data disclosure related to significant number of transactions of numerous banks. Statistics published by CBH indicate the mean calculated on the collected sample, they are expressly able to determine the exact arm's length price of the loan interest rate. If it is possible to determine the arm's length price as a single figure (price) further calculation of a range is not justified.

III. Adjustment of the interest range by the taxpayer referring to the country risk

HUC applied adjusment referring to the country risk. According to the the tax authority's standpoint and the expert opinion country risk is included in the CBH interest rate statistics.
On the basis of the expert opinion the judge took a position in such a way that the adjustment of the CBH statistic data with reference to the country risk would result in duplicate evaluation of this factor, violating the comparability seriously.

„Deposit"

HUC stated that the governing law was not the Hungarian law. According to the resolution of the tax authority, which was in line with the expert opinion, the Hungarian legislation was applicable. In HUC's opinion tax authority characterised the „deposit" contract concluded between the parties as a loan transaction in an unfounded way. According to the standpoint of the tax authority due to lack of comparability it was a mistake to apply the (lower) deposit interest rates instead of the loan interest rates in the determination of arm's length price. The tax authority higlighted that lending and depositing were different kind of transactions. While loan can be granted by anybody, only credit institutions are entitled to receive deposits. Receiving repayable funds from the public, which is one of the most substantial element of deposit's definition, doesn't get realized in the controlled transaction. It is worth to mention that in an other lawsuit the tax authority explained in details that granting loan for associated enterprises is more risky than a deposit, by this means induces higher expected yield (low risk due to the strong capital base, prudential requirements and special guarantees is ensured only in case of deposit.)
According to the decision of the court the tax authority didn't have to apply foreign law. Due to the fact that the Hungarian legislation is applicable for the purpose of legal classification of the transaction, the tax authority lawfully did not characterised the transaction as being a deposit as for the judge's opinion. In connection with the question regarding the characterization of the controlled transaction the judge, referring to the expert opinion, took a position in such a way that the tax authority assessed properly that the amount of money deposited by plaintiff at the associated party in fact could be considered as a loan granted for the associated enterprise. In the judge's opinion, since receiving deposits may be pursued by credit institutions only, the interest of deposit received was rightfully compared by the tax authority with the higher interest rate being the characteristic of lending transactions. As it was stated in the court decision, receiving repayable funds from the public (deposit) and financial operations conducted between a parent company and its subsidiary (group financing, treasury activity) were different categories, they mean dissimilar transactions, by this means they were not comparable.

Summary

The case presented above has been won by the tax authority, the court dismissed the plaintiffs's action. In the last resort the resolutions representing the professional arguments of the tax authorities are reviewed by the courts. Winning court case is always important in itself. Besides, in the area of transfer pricing, where framework regulation exsists and comparing to other high-risk areas of the taxation, less court decisions are available, value of a court decision related to issues of fundamental importance has increased from the perspective of the feedback of correctness of the tax authority's standpoint.

Attitudes towards compliance and the Norwegian Tax Administration's use of policy instruments

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NORWAY

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The article examines the relationship between the attitude of Norwegian businesses towards acting in accordance with the tax regulations (compliance) and the Norwegian Tax Administration's use of policy instruments. We have conducted a major survey to identify the attitudes towards compliance among Norwegian businesses. The identification of these attitudes was based on the OECD's risk management model which divides the taxpayers into four segments in accordance with their willingness and ability to follow the tax regulations. Insight into these attitudes enables us to direct policy instruments at various groups. We find that three out of four businesses in a representative sample do not tolerate tax evasion and believe they are familiar with the regulations. We find similar attitudes at businesses the Tax Administration has audited. The results show that many of the businesses which the Tax Administration has audited have attitudes that indicate that they could have been reached using less expensive and more appropriate policy instruments other than audits.

1. Introduction

The tax administrations in several countries have obtained inspiration from the OECD in their work with strategies for improving compliance. The OECD (2004, 2010) presents a model that groups the taxpayers into four segments based on their attitudes towards compliance and emphasizes that different policy instruments are effective for different segments. There are not many countries that have attempted to estimate the size of these segments.

On assignment from the Norwegian Tax Administration and the Collaboration against Underground Economy, SMSØ), Opinion Perduco has conducted a survey directed at 3,000 Norwegian businesses. Based on the results of this survey we have estimated the size of the various segments among Norwegian businesses. Another important objective of the survey was to compare attitudes of the businesses that the Tax Administration had conducted audits of with the attitudes of a representative sample.

2. Theory

Most of the research on compliance deals with individual taxpayers. There has been less focus on the attitudes towards paying tax among businesses. However, there is reason to believe that many of the findings from the research on individual taxpayers is relevant to businesses since it is individuals that own and make decisions in the businesses (Alm and McCellan 2012).

Allingham and Sandmo (1972) were largely responsible for establishing the theoretical basis for research on compliance. They presented a theoretical model for what influences taxpayers to evade tax. The model indicates that people will choose to evade tax if the expected benefit is greater than the product of the probability of detection and the degree of punishment. Based on this model, the most practical compliance strategy is to create an increased risk of detection through audits and strict sanctions such that taxpayers will consider the risk of committing tax evasion to be too great. The model has since been tested and criticized through economic and psychological research.

Feld and Frey (2002) and Frey (2003) argue that Allingham and Sandmo's model overestimates tax evasion and that observed compliance is higher than what the model indicates. More studies (see, among others, Clotfelter 1983, Beron, Tauchen & Witte 1988, Slemrod, Blumethal & Christian 2001) have also shown that the probability of detection and the extent of the punishment are not statistically significant variables for explaining why certain taxpayers choose to evade tax and that the effect of an increased risk of detection even can go in the opposite direction.

Frey (2003) proposes an alternative theory based on behavioural economics and psychological research. This theory places emphasis on tax morale for explaining compliance. The argument is that taxpayers are not exclusively motivated by external factors such as punishment and rewards but are also motivated by an inner motivation to pay tax. The trust between taxpayers and the tax authorities and the trust between taxpayers are of decisive importance to tax morale. Based on this perspective, the most appropriate compliance strategy is to build up trust among those who are willing to comply.

A Danish study (Kleven et al. 2010) finds support for a modified version of Allingham and Sandmo's model, which focusses to a large extent on the possibilities of evading tax. They found that the percentage of tax evaders was low for reporting based on third-party information, while the figure was 37 per cent for self-reported income. The study also indicates that compliance can be influenced through audits and increased risk of detection for groups that have better opportunities to evade tax.

The OECD (2004 and 2010) has developed a risk management model for tax administrations. This model provides a good summary of many important findings in compliance research, both for individual taxpayers and businesses. The model

[1] Collaboration against underground economy (No: Samarbeid mot svart økonomi, SMSØ) is an alliance of key parties in business and industry – the Norwegian Association of Local and Regional Authorities, the main confederations of trade unions, the Confederation of Norwegian Enterprise and the Norwegian Tax Administration – focused on joint preventive efforts to combat the black market.

emphasises that the tax authorities should adapt their compliance strategies based on the attitudes taxpayers have towards compliance. The model is illustrated as a pyramid consisting of two segments for those who do not wish to comply at the top, and two segments for those who wish to comply at the bottom. Deterrents such as audits are considered to be effective against taxpayers who do not wish to comply, while simplification and instruction are better suited for those who wish to comply. We have used this model as the starting point for defining taxpayers into segments based on their attitudes towards compliance.

3. Sample

The sample in the survey was drawn from the Tax Administration's data warehouse of businesses that were active in the Value Added Tax Register. To ensure that all business sizes were represented, we stratified the selection based on the number of employees. The target group was 3,000 businesses divided into three groups:

- 1,000 businesses in a representative sample
- 1,000 audited businesses where errors were detected
- 1,000 audited businesses where no errors were detected.[2]

The subgroups that had been audited were then divided into two different audit forms. Half of the audited businesses had been subject to field audits and the other half had their submitted VAT returns audited (desk audit). In a field audit, the Tax Administration visits the business and reviews all or parts of the accounts, while for desk audits the business is usually contacted in writing. The Tax Administration will most likely appear most visible to businesses when conducting a field audit. The amounts that are uncovered are also normally greater in a field audit since errors that were made several years previously can be back-dated.[3]

The survey was conducted in the form of a telephone survey (CATI). The respondents were primarily the managing directors of the businesses. In instances in which the managing director could not be available for an interview, the finance manager, chief accountant or similar were interviewed.

The non-response analysis showed that businesses without employees were somewhat underrepresented in the final sample. We have taken this into consideration by weighting the results based on the business size. However, we did not find that businesses that had been subject to more than one audit or had large amounts detected during the audits, were less willing to respond than others.

4. Methodology

In order to group Norwegian businesses in accordance with the OECD's segments, we have prepared four pairs of mutually exclusive statements which the respondents were asked to address. These four claims were:

<u>Attitude towards tax regulations</u>

- I know that my business has a good overview of the tax regulations and that the possibility of us making an error is low
- My business could unconsciously make an error because we do not have an adequate insight into the tax regulations.

<u>Attitude towards guidance</u>

- If my business received an offer of more general guidance from the Tax Administration about tax issues, we would gladly accept this.
- I cannot see that my business requires more general guidance from the Tax Administration regarding tax issues.

<u>Attitude towards evasions</u>

- It is never acceptable for a business to deliber-

[2] For the audited businesses where no errors were detected, the Tax Administration made no amount-related changes with regard to what was reported nor did it give instructions that the business must improve its routines.

[3] For businesses that have had a field audit where errors were detected, the errors were related to changes of amounts in either reported taxable sales ,the business' income, gross employment income or employers' national insurance contributions.

ate evade taxes.

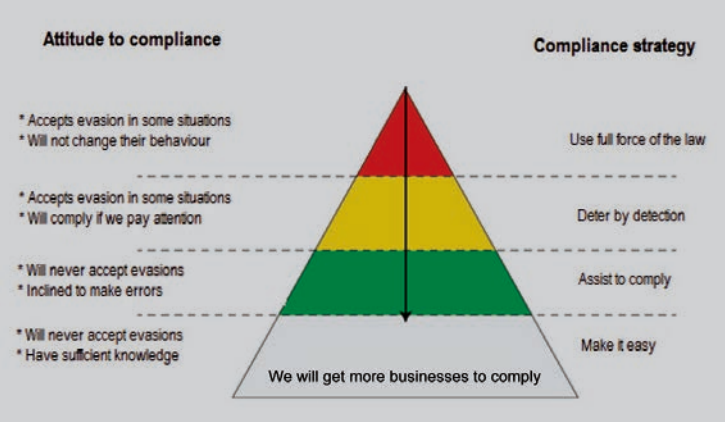
- In some cases it can be accepted that businesses deliberately evade taxes.

Attitude towards deterrence

- More audits or stricter punishments would make us even more diligent about ensuring that no errors were made in our reporting.
- More audits or stricter punishments would not influence how we carry out our reporting.

The left hand side of Figure 1 shows how we have grouped the businesses into a red, yellow, green and white segment based on how they responded to the statements. On the right are the strategies that the OECD promotes as being the most effective for each segment.

Figure 1 Operationalization of the segments



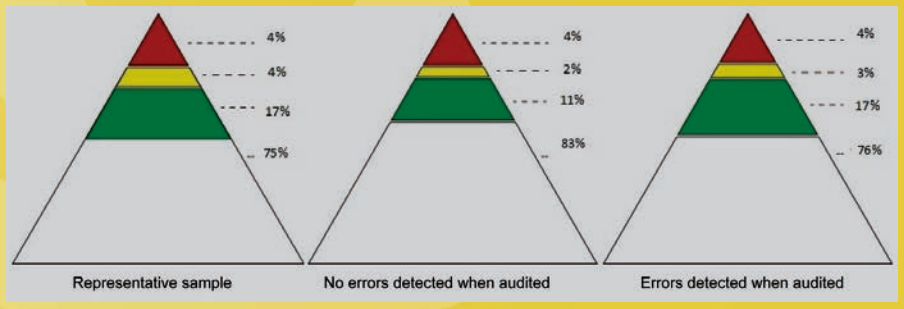
The main difference is between those who can accept tax evasion and those who cannot. Those who can accept tax evasion are again divided into two segments for those who are receptive to influence (categorized as yellow) and those who are not (categorized as red). Among those who cannot accept tax evasion there are two segments; one which could make errors because they have an inadequate overview of the regulations (categorized as green), and one segment which believes they are confident with the regulations (categorized as white).

5. Results

Attitudes among audited businesses compared with the representative sample

In figure 2 the representative sample is compared with audited businesses where no errors was detected, and audited businesses where errors were detected.

Figure 2 The percentages in the four segments in the representative sample and for businesses that have been audited. The result is weighted.



Three out of four businesses in the representative sample are in the white segment and one out of four businesses lack either the will or the ability to comply. There are minor differences between the attitudes in the representative sample and in businesses which have been audited by the Tax Administration. This applies for both businesses where the Tax Administration has detected errors and for businesses where no errors were detected. There are many who are apparently willing to comply in the group where errors were detected during audit. This can indicate that the majority of businesses where the Tax Administration detects errors generally have attitudes that indicate that they want to do the right thing.

Eight per cent of the businesses in the representative sample are categorized in the red or yellow segment. However, there are a number of challenges involved in measuring the percentage of businesses in the segments that do not wish to comply through a survey, something that can result in these percentages being underestimated. Firstly, it is likely that some of the businesses in the yellow and red segments are operating in secret. Unregistered or

apparently inactive businesses fall outside the sample in the survey. Secondly, there are businesses that have ceased operations after having been audited. Among active businesses in 2007, 40-43 per cent of those where errors were detected during audits have ceased operations in 2012 - compared with 35 per cent in a representative sample. A third challenge is that respondents in surveys can provide responses that they consider socially desirable [4]. SKAT (Danish Tax Authority) in Denmark has measured compliance among businesses based on results from random audits (SKAT 2006, 2008)[5] . Despite using a different approach, they estimated that the combined percentages for the yellow and red segments were 7 per cent in 2006 and 10 per cent in 2008. There is therefore reason to believe that the result from this survey provides a reasonable estimate of the size of the segments in Norway.

What does the survey tell us about the Norwegian Tax Administration's use of policy instruments?

Based on the strategies presented as being the most suitable for each segment in Figure 1, the red and yellow segments are, in principle, the most important target groups for the Tax Administration's auditing activities. However, we do not find that the percentages in the red and yellow segments are greater for those that have been audited. Despite the fact that the survey can underestimate the percentages in the red and yellow segments, a conspicuously high number of businesses which the Tax Administration has audited generally want to do the right thing and therefore could have been reached through means other than audits.

In the representative sample, approximately 60 per cent of those businesses that had stated that they lack an overview of the regulations responded that they would gladly accept more guidance if they were offered this. This emphasizes that many can be reached with policy instruments that are less resource-demanding than audits.

In the survey, all the businesses were asked whether they had been audited by the tax authorities during the past five years. Almost 40 per cent of all the businesses which the Tax Administration actually audited did not state this in the survey. Businesses where errors were detected during audits stated more often than others that they had been audited. In addition, those that had recently been audited stated that they had been audited more often than those who had been audited further back in time. This indicates that some may not remember or notice audits conducted by the Tax Administration. There is also a difference between those that had been subject to a field audit or a desk audit. More were aware of the audit among those who had been subject to a field audit than businesses that had had a desk audit. This was in line with what we expected since the Tax Administration is more visible during a field audit.

Those who stated that they had been audited were also asked whether errors had been detected during the audit. 35 per cent of the businesses where the Tax Administration found errors during field audits remembered both the audit and that errors were detected. For desk audits, only 19 per cent remembered both the audit and that errors were detected. The amounts caused by errors was also of some importance.

The survey also shows that audits contribute to an increased risk of detection. In response to the probability of the tax authorities detecting tax evasion in the industry, four out of five businesses in the representative sample stated that the probability was high or very high. The percentage was higher among businesses that have been audited and highest for those that had errors detected during a field audit. There was also a larger percentage among those that had been audited that believe that it is probable that they will be audited in the next two years compared with the representative sample.

5. Conclusion

The survey demonstrates that three out of four businesses in Norway cannot tolerate tax evasion and believe that they have an adequate overview of the

[4] Elffers, Weigel and Hessing (1987) provide an example of this.

[5] The number of audits was approximately 11, 000 in 2006 and nearly 3,000 in 2008

regulations. For these businesses, simplification of the regulations and guidance could make it easier for them to comply. The target group for the Tax Administration's auditing activities is businesses that are found high up on the pyramid, preferably in the red and yellow segments. Part of this target group will also consist of businesses which are difficult to reach for this type of survey, either because they are not registered or because they ceased operations after an audit. However, the survey shows that many of the audited businesses have similar attitudes to the representative sample and that many therefore could have been reached with increased use of guidance. However, a challenge in targeting guidance is that there is not enough knowledge about the effect of different types of various guidance initiatives (such as online help or information, letters, educational visits or courses for people starting up new businesses etc.) on different groups of taxpayers. Some auditing activity in the white and green businesses can be justified based on a desire to make the Tax Administration more visible and the audits can also be necessary to establish practices within complicated tax matters.

Audits contribute to an increased risk of detection and the businesses say that they generally change their routines when they have made errors. The focus for the Tax Administration in the future should therefore be to direct the audits more towards the, in relative terms, smaller percentage of businesses in Norway that do not wish to comply. To have a better success rate for audits, we should also obtain more knowledge about actual compliance and the types of errors that are made by businesses. The systematic registration and analysis of error types will be an important initiative.

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Tax Evasion and Tax Avoidance

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I have been working at the First Tax Office in Opole for more than 24 years. From 1994 to 2005 I held the position of a Head of the Assessment Unit and since 2005 as the Head of the Tax Audit Department. I hold fifth Civil Service Servant degree, one of the highest in Poland. I am also involved in risk and quality management in the office, mainly as a leader of a few teams and numerous projects such as the project 'Athena'. My main aspiration is to create a truly positive image of the Polish Tax Administration in the eyes of the society.

By
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POLAND

INTRODUCTION

Globalization, free movement of capital and ease of transactions at the global level have created the possibility of using solutions whose main objective is to minimize the tax burden.
The use of "tax haven vehicles" to optimize the tax liabilities and creating the so-called "conduit company" in order to exploit favourable provisions in double taxation Treaties, are examples of the challenges, which tax administrations confront every day.
Is tax non-compliance only a tax evasion or tax avoidance as well? How to combat this type of phenomena? The answers to these questions were tackled during a meeting held in Budapest on 16-18.10.2013.

TAX NON-COMPLIANCE

The activity consisting of balancing the edge of the law often is associated directly or indirectly with tax evasion or tax avoidance. What is

the difference between these two concepts?

Tax evasion is the illegal evasion of taxes by individuals, corporations as well as trusts. It means that tax evasion is a serious fraud and it takes place when individuals or entities deliberately do not pay their appropriate taxes.

On the other hand, *tax avoidance* is not illegal. It is considered as a legitimate minimizing of taxes or legal usage of tax law regulations to reduce tax burdens of individuals or entities. It means that tax avoidance is not a fraud and it happens when tax rules and regulations are modified in a way that a tax system did not intend to allow.
Obviously, tax evasion as well as tax avoidance can be considered as tax non-compliance. Both tax evasion and tax avoidance, concern various taxpayers' activities that are not favourable for tax administrations and cause a considerable decrease in national incomes.

EXAMPLES OF NON-COMPLIANCE

TAX HAVEN VEHICLES

One example of taxpayers' non-compliance action is the use of tax havens to optimize tax liabilities. Many different methods of using tax heaven are known. Their basis can rely on:

- changing the place of residence of an individual person,
- establishing a company in tax havens – then dividends are paid to individual persons as investors who are anonymous for other tax administrations,
- using offshore companies as conduit company in order to distribute the income.

Tax haven vehicles are used in large transactions, management of stocks and shares, offer full confidentiality and anonymity. This phenomenon is all the more worrying because it applies not only to International Companies whose activities are monitored by the tax administrations of individual countries, but also, to an increased number of small and medium sized entrepreneurs, that realized the opportunities arising from this kind of technology. Although the amount of tax avoided by small and medium sized entrepreneurs is lower in comparison to International Companies, the number of cases is considerably higher.

This issue is extremely important. Each tax administration will take action to mitigate the negative effects of this phenomenon, such as:

- legislative – by introducing an obligation to keep proper documentation or recording of financial transactions, allowing tax authorities to estimate the income when its less than the market value, etc.
- prevention - consisting of conducting information campaigns in the media
- repressive - by conducting tax audits and application of penalties.

It should be noted that the evaluation of evidence in the course of inspection is very difficult because of the anonymity of the participants, as well as, there is limited access to documents. It is often difficult to identify the ultimate owner of tax haven vehicles.
Not without significance is the lack of cooperation agreements on exchange of information in tax havens countries. Obtaining any information in these cases is almost impossible. So it is important to get as many documents as possible in the course of audits and use all possible methods for obtaining them. At the same time a number of important information can be obtained by making searches and read data from computers and mobiles from the management levels of the particular company. Disclosure of all management communication should bring the best results.
The need for close cooperation between tax administrations was observed. This does not involve only the exchange of information but also sharing good practices and steps taken in cases of similar kind.

CONDUIT COMPANY

Another example of tax optimization, widely used by International Companies, is the method of involving a conduit company.

In order to reduce tax burdens, conduit companies are formed, which are used to channel incomes between other entities. It is crucial to mention that a

conduit company does not use this income itself and only acts as a 'pipeline' for transferring income from one company to another. The increasing amount of such companies suggest a potential tax risk.

Such companies might create problems connected with the usage of double taxation treaties' regulations. Some of them are established only to obtain treaty benefits that would not be available without their existence.

Presented at the workshop the example involves company C registered in Bulgaria which obtained credit from company B registered in the United Kingdom owned by the parent company A registered in Greece. It was crucial in the above case, that company B was registered in the UK for the purpose of funding companies in the group and did not give credits to any non related parties. Moreover, credit agreement between C and B was guaranteed by parent company A.
Taking advantage of favourable regulations of the Double Taxation Treaty between Bulgaria and the UK, company B applied for 0% withholding tax rate in respect of income from interest paid by Bulgarian company C.
The conducted investigation showed that company B did not carry out economic activity or even have staff, nor independent office. So company B was formed as a *conduit finance vehicle* for the purpose of the parent company. It means that company A by avoiding direct lending and financing company C avoided withholding tax in Bulgaria according to the Double Taxation Treaty between Bulgaria and Greece.
In conclusion, auditors stated that company A, not company B, was an actual holder of the interest income. According to the *beneficial owner regulation*, company B being only a recipient but not an actual owner of this income was not entitled to benefits under the provisions of the Double Taxation Treaty between Bulgaria and the UK.
As it was demonstrated, according to the Double Taxation Treaty, 0% rate of withholding tax could be applied in Bulgaria only when company B is not only a recipient but also the owner of the income in the economic sense.
Moreover as far as company B does not carry out any economic activity and provide any real service, the income should be treated as a hidden distribution of profit between related parties.

Beneficial owner regulation aimed at preventing treaty shopping was applied in this case. When an entity is formed only for the purpose of obtaining benefits by reducing the level of withholding tax, the arrangements must be checked in order to examine if the conduit company is a beneficial owner of the income. The conduit company cannot be regarded as the beneficial owner when as a formal owner of income has only narrow powers in relation to the income concerned. This concept brings together the actual owners of income to the owners in the economic sense.
The conduit company cannot be regarded as the beneficial owner if the formal owner has very narrow powers which renders it, in relation to the income concerned, a mere trustee or administrator acting on behalf of the interested parties.
It should be noted that one of the key actions that should be taken into account by the tax administration in order to prevent tax avoidance is a comprehensive revision of the benefits included in the various Double Taxation Treaties. Very often, the unauthorized parties, by appointing a conduit company use the agreements in order to optimize or even eliminate the tax burden.

POLISH EXAMPLES

Combating tax evasion and avoidance is one of the most important challenges the Polish Tax Administration meets nowadays. New solutions, as well as more and more sophisticated ideas of tax evasion and tax avoidance bring many problems. Many risk areas exist. The common thinking about these areas is that they tend to be very complicated and complex. And of course we meet legal as well as organizational obstacles in the fight against tax evasion and tax avoidance.

One lately identified risk area is connected to partnership companies such as registered partnership, limited partnership or limited joint stock partnership. Their activities are often seen as tax optimization. Many problems are caused by those companies. The bottom line of most of them lays in the

fact that those partnerships have no legal personality. One of it concerns transactions between related parties when the party of transaction is a partnership company.

In accordance with the Polish tax law, and in particular article 11 of the Corporate Income Tax Law and article 25 of the Personal Income Tax Law the Polish transfer pricing regulations apply to domestic and cross-border relationships. However, the definitions of these relationships differ.

A Polish and a foreign company are considered "related" if one of the following three conditions is met:

- A Polish taxpayer participates directly or indirectly in the management or control of a company located abroad or holds a share in its capital;
- A foreign resident participates directly or indirectly in the management or control of a Polish taxpayer or holds a share in its capital; and
- The same legal or natural person, at the same time, participates directly or indirectly in the management or control of a Polish and a foreign entity or holds shares in their capital.

Polish companies are considered "related" when one of the following conditions is met:

- A domestic entity participates directly or indirectly in the management or control of another domestic entity or holds a share in its capital;
- The same legal or natural person participates, at the same time, directly or indirectly, in the management or control of two domestic entities or holds a share in their capital;
- Relationships of a family nature, resulting from employment contracts or common property, exist between ;
  - two domestic entities or
  - persons involved in their management, control or supervision; and
- The same person combines managerial, supervisory or controlling duties in both entities.

It is important that if, as a result of such relations, there are agreed or imposed conditions substantially different from those which would be agreed between independent entities and, as a result thereof, such entity does not disclose any income or discloses the income smaller than might be expected, if such relations did not exist – the income of a given entity and the tax due shall be assessed without taking into account the conditions resulting from such relations.

Unfortunately, those regulations cannot be applied, when one of the parties of the transaction is a partnership company. A partnership company has no legal personality. That is why taxpayers of income tax are its partners. Therefore a partnership company cannot be considered as a *domestic entity* under the provisions of the income tax law because it is not taxable by corporate or individual income tax.

Facing this problem, the changes in tax laws are being prepared. The changes are essentially intended to secure the income tax system by eliminating the tax optimization mechanism used by partnership companies.

Another example of tax optimization, which has been already successfully reduced, is connected to establishing a conduit company in Cyprus. Until last year, in order to reduce tax burdens Polish companies often established conduit companies in Cyprus, which were used to obtain treaty benefits that would not be available without their existence. The strategy was very simple:

The income tax in respect of dividends paid by a Polish company to an individual Polish investor is 19%. When this Polish company, established a conduit company in Cyprus and paid dividends through it to the Polish individual investors, the income tax was deducted of a hypothetical Cyprian withholding tax of 10%. So, in reality only 9% of income tax was paid in Poland.

Such optimization of taxes was made possible through the use of the *tax sparing method* with respect to dividends received by individual Polish investors from the company established in Cyprus. There were variations in the translation Polish and English versions of the Double Taxation Treaty between Poland and Cyprus. According to the Polish version only tax which was paid in Cyprus could be

deducted from Polish tax. According to the English version tax payable in Cyprus could be deducted from Polish tax. Differences in translation meant the acceptance of the English version which gives the possibility of using fictional credit. This significantly reduced the real tax burden.
Currently, tax on dividends paid in Poland can only be reduced by the tax actually paid in Cyprus. It is due to the Agreement signed last year between the Polish Government and the Cyprus Government to amend the Double Taxation Treaty, the purpose of which was to remove the so-called tax sparing clause, which allows a deduction from the tax payable on the dividend tax in Poland that would be obtained in Cyprus (even if it has not been obtained).

By securing the tax system, Poland also has increasingly more agreements on the exchange of tax information (TIEA). In the last two years, it has signed eleven TIEA: with the Isle of Man, Jersey, Guernsey, San Marino, Andorra, the Commonwealth of Dominica, Grenada, Gibraltar and Belize, the Bahamas and the Republic of Liberia.

It should also be noted that there are plans to change the tax laws that provide for the taxation of income of controlled foreign companies (CFC). CFC regulations are widely used to combat tax evasion and tax avoidance caused by related parties.

The bottom line of this comes down to the obligation to include in the tax base of Polish resident (individual or a taxpayer of corporate income tax law) incomes of controlled foreign companies with lower levels of taxation than applicable in Poland.

The changes are essentially intended to secure the income tax system by eliminating tax optimization mechanisms that use mainly subsidiaries located in countries with low levels of taxation. The proposed changes assume that the Polish company would pay tax in Poland also on the income generated by the controlled company established or administered in a country with lower tax - revenue would be taxed at the rate of 19 %.

CONCLUSIONS

The disparity between tax avoidance and tax evasion is not visible. These phenomena are often interrelated and occur interim. It should be noted that attempts of tax evasion or tax avoidance will occur for as long as the differences between the tax systems of each country are not balanced out.
The regulations of the national laws with respect to direct taxes, with few exceptions, are not harmonized within the European Union so it's up to each of the Member States to decide on the method of levying direct taxes. However, it would be worthwhile to engage in discussions on the possibility of harmonization of some of the issues associated with these problems.

Another important aspect of this problem is the need to take preventive measures, involving, among others, the introduction of legislative changes in the tax law to adapt to a rapidly changing environment. However, we must remember that the changes occur constantly, which allows the taxpayers that partake in tax avoidance, to act very quickly.

An important issue is the need to raise the awareness and thereby taxpayers' tax compliance. The greater the awareness of the need for proper regulation of tax obligations, the fewer taxpayers will benefit from solutions that violate the law. On the other hand, it is important to severely punish the deliberate efforts of tax evasion. Higher penalties for deliberate non-compliance would make incorrect behaviour less common. It is also clear that effective prevention of such risks requires prompt and intense international cooperation and one of the most crucial elements is the process of gathering and exchanging information between administrations of the European states. It should be noted that participation in the meetings organized by IOTA allows the representatives of the tax administrations of different countries to share best practices and solutions adopted by each tax administration. It is essential to remember that we are not alone and similar problems exist across Europe.

Engaging and involving SMEs and their Intermediaries in Tax Administration Processes

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INTRODUCTION

Small and medium-sized enterprises (SME) represent a large majority of the entrepreneurs running their own businesses. SMEs differ from large companies significantly. The size of this group of taxpayers makes it impossible to treat each SME individually. Subsequently it is necessary to cooperate with "intermediaries" that help tax administrations to notify SMEs about relevant content, information and messages.

Fundamental to the improvement of the fiscal correctness of SMEs is knowing and understanding the causes of their incorrect behaviour. Factors shaping the tax awareness are many but the most important seems to be *trust*, without which cooperation of tax administration with SME would not be possible. Therefore, modern tax administrations make effort to be transparent and relationships with businesses and their representatives were based on mutual cooperation to ensure confidence and tax justice.

It should be noted, that an increase in the tax correctness of entrepreneurs is possible not only by stimulating compliance but also by preventing noncompliance. Shaping the image of the proper tax administration in the eyes of society and the high quality of services are challenges with which modern tax administrations tend to be faced with.

Participation in meeting held in Budapest on 05-07.02.2014 by IOTA with partnership with the OECD, enabled participants to learn about best practices developed by the tax administrations of other countries, including preventive measures such as simplification of procedures, elimination of administrative barriers etc.

SME CHARACTERISTIC

SMEs represent a large majority of entrepreneurs operating in both domestic and international markets. The group of SMEs is very diverse and different from the group of large taxpayers. SME *need a special approach because they*:

- are different from large taxpayers (size, assets, capital (equity) ,management, number of employees, background, knowledge, experience, accountancy, awareness, intermediaries, bookkeepers,)
- have different *needs, problems, expectations, priorities*
- make more *errors* - mostly *unintentional*. Most mistakes are not made deliberately but caused by insufficient knowledge, carelessness etc.
- have d*ifferent reasons for noncompliance*, and different, *more diverse range.*

The risk of noncompliance in this group is very high. Although the amount of each individual tax loss is not huge, cumulatively they produce a high amount. Therefore, tax administrations must undertake measures which would increase the level of voluntary tax compliance by SME.

COMPLIANCE STRATEGY FOR SMEs

It is important to understand that tax administrations have a public mission to fulfil as they serve both society and its citizens alike. The interests of both parties are not necessarily contradictory. The services they offer are often compulsory and they are not very popular. Therefore, it is very important to take client satisfaction into account and to create a proper image of the tax administration in the public mind. In order to achieve the *highest possible level of voluntary tax compliance*, both preventative and repressive measures should be used through:

- *Stimulating compliance*: most tax administrations believe that majority of SMEs want to comply with their fiscal obligations. Therefore it`s important to make it easy for them to do so; provide high quality of services, make sure that obligations are clear for them, carry out helping hand projects, communicate with specific groups, or being visible provide information about tax administration strategy and fiscal legislation. Through enhancing confidence to tax administration the *level of voluntary tax compliance of SME is increasing.*

It should be pointed out that *communication* is a fundamental element in a building of a relationship of trust between tax administration and SMEs. It is common knowledge that the key to creation of trust is to act in ways which taxpayers will see to be fair. The aim is to enhance confidence. Communication can take different forms and can happen through different channels, including printed, digital and electronic media, telephone, letters, emails and physical interaction. It is the first step in involving taxpayers in the tax processes. *Consultation*, *as* the next step can take place through formal mechanisms or on a more informal and ad hoc basis, including surveys, focus groups and social media. It can also be integrated into regular client interaction. Consultation offers influence SMEs and stakeholders by bringing their views and perspectives into design and decision-making involvement.

Important is also *transparency and openness* - the aim is to increase satisfaction of SMEs in their relationship with the tax administration. It should be based on environment of trust, credibility and respect.

- *Preventing non-compliance*: most tax administrations realize that besides SMEs who are willing fulfil their duty there are also those who decide not to comply. In that case, taxpayers should be informed about their rights and obligations. They must be made aware that tax administration will detect their non-compliance and take enforcement actions. It means that appropriate actions can be enforced, which graduate in severity, such as repressive audits, penalties, enforcement communication, or even prosecution.

The compliance program should include a *mix of both proactive and reactive strategies* that cover all aspects of compliance management from education to prosecution. Compliance strategy should *provide a progressive response to compliance behaviour* - making it easy for those who want to comply and applying credible enforcement to those who don`t want to comply.

But the most important task in building a relationship of trust between tax administration and SMEs is to create a *proper image of tax administration in the public mind.* It should reflect *two different faces of the tax administration* - one which is friendly to good taxpayers and the other which is restrictive for those who are not-compliant. The *service and audit function should be well balanced.* Tax Administration should use tools that on the basis of risk analysis allow to predict entrepreneurs that attempt to bypass the law. With such solutions, tax offices can concentrate on applying control measures at the subjects avoiding taxation while limiting the burden for entrepreneurs that fulfil their obligations.

Also, it is relevant to coordinate the work in the most optimal way using public resources reasonably. They are limited so the use of them should be maximized.

It should be pointed out that to achieve the highest level of voluntary tax compliance as well as the high quality of services, *high competences of the staff are necessary.* In view of many changes of the tax system as well as fast changes of surrounding society (technological progress, the development of information technology, globalization etc.), and difficult situation that members of the staff are facing quite often it is necessary to keep the knowledge of employees up to date and improve their skills. Also, it is important *that employees know how to proceed and where to turn for guidance, training, support or encouragement. That is why it is necessary to change the way of thinking, change in mentality from own staff which is not the easiest step.*

It should be noted that from 2013 operates a unified system of training in the Tax Administration which coverage includes Tax Offices, Tax Audit Offices and the Ministry of Finance. Furthermore, available is program ATENA2. It is a modern system which supplements the traditional stationary training, which allows, among others: to increase accessibility of training, standardization of knowledge and reduction of costs associated with the organization of training.

It must be emphasized that the tax administration officials regularly train entrepreneurs, among others, about subjects related to the tax law regarding business and the use of cash registers or new technologies (in this example, the possibility of submitting a declaration through the Internet). Much of the training is organized jointly with business organizations.

An example of a project aimed at increasing *competences of the staff* implemented at a local level could be the project "*ATHENA*" successfully implemented in the First Tax Office in Opole in Poland. The project is based on the idea of the Olympic Games – *mutual cooperation as well as competition between participants in order to achieve the best results.* Exploration of new areas of mutual improvement to achieve better results and ultimately gain a degree of knowledge and skill that allows sharing knowledge with others as well as training others is something everyone should strive for. *Activities are conducted within five main areas* symbolizing the Olympic wheels: learning together; training representatives of Polish Tax Administration; sharing experience with representatives of tax administrations of other countries; learning best practise from others; training entrepreneurs. It is also important that employees not only educate and get to know each other but also work together with entrepreneurs. Educating entrepreneurs do not only affect the correct development of the office's image in the eyes of the society, but also *raise awareness of taxpayers indicating by its actions that the interests of both parties do not have to be contradictory.* By nature, taxpayers do not like to pay taxes but it is an important part of tax revenue of the state and allows society to function properly. The project also assumes to *improve the image of the tax office* in the eyes of taxpayers, and as a result increase the level *of voluntary fulfilment of tax obligations* by taxpayers and thus increase government revenue. Increasing the level of voluntary tax compliance will designate it as available resources for conducting prevention actions by tax offices. It is assumed that the control actions will be mainly designated to taxpayers who deliberately fail to comply with tax obligations. This also will increase the feeling of fair taxation.

Another important aspect of SMEs compliance strategy is that it should *be tailored to SMEs needs*

and expectations. It means that the need is a result-oriented as well as client-focused management system that allows to:

- identify and address risk at an early stage by taking steps such as: following new trends; observing the external environment; analysing all external information(anonymous) and internet; exchanging best practises; proper selection for the audits; and performing random controls;
- built relationship with taxpayers based on trust and acceptance of each other rights and responsibilities;
- reduce the administrative burdens;
- increase legal security and feeling of fair taxation;
- cooperate with SMEs;
- use new technologies, IT systems;
- act in real time and up-front creating certainty on the tax position, solving problems in advance;
- *engage* and involve SME and other stakeholders in tax processes;
- *cooperate* with tax intermediaries, branch and industry organisations, providers of software and online services etc.

CONCLUSIONS

In order to achieve a high level of voluntary fulfilment of tax obligations by SMEs it is necessary to create a strategy for tax correctness, dedicated to small and medium-sized enterprises.

This is all the more important since SMEs make up the largest group of taxpayers. Processes occurring in society, including globalization, rapid technological development, ease of mutual communication, make SMEs operate in ever broader spectrum and tax non-compliance and related problems are diverse, complex and often with a sophisticated structure. Such strategy should include measures of a preventive nature, all targeted at SMEs such as: provision of high quality services; facilities and development opportunities for electronic forms of collaboration (e-Tax); information campaigns; support programs; training. At the same time, taking into account the distinctiveness of SMEs, restrictive actions should also be included, mainly based on inspections or enforcement.

The most important, however, is to act in a timely manner to prevent problems before they appear. Cooperation of tax administration with entrepreneurs and their representatives based on mutual trust and confidence in tax system is the most important tools to achieve that objective. It should be noted that the process of building trust is long and clearly requires a change in the awareness of all participants in the process. Essential to the process are fundamental elements such as:

- transparency of procedures;
- uniformity and stability of the tax law;
- management focused on results and SMs;
- uniform standards for accounting programs and other programs used by SMEs – free of charge etc.
- the obligation to submit documents in electronic form;
- simplification of fiscal burden;
- provision of maximum facilitation of voluntary and proper fulfilment of tax obligations;
- balancing service and control functions;
- increasing the efficiency of control measures towards dishonest taxpayers;
- creation of efficient and effective system which uses information and communication technologies.

The most significant, however, seems to be the formalized cooperation with SMEs industrial associations and tax advisors, accountants associations, etc. Use of "intermediaries" in shaping of the correct image of the tax administration, the exchange of information on key risk areas and transfer of information which reaches significant number of taxpayers represented by these organizations and companies is a valuable asset. It should also be noted that such initiatives are already being implemented by some countries (the Netherlands, Slovenia), and locally in some tax offices in Poland.

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I was born in 1982 in Smederevo, small town in Serbia. From 2008 I am employed within the Tax Administration of Serbia. Currently I am working as internal communication officer and I am responsible for the administration of STA's web site. I graduated from the University of Economy in Belgrade and got the master degree in macroeconomic policy and development.

Providing assistance to start up businesses within the Serbian Tax Administration

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SERBIA

Since the radical reform of the Serbian Tax Administration is currently going on, the experiences gained at the IOTA Workshop held in Budapest in November 2013 were very useful for the forthcoming changes.

Our Tax Administration, through an IPA project approved by the European Commission is working hard to improve its efficiency and to simplify the Serbian tax system, as well as to adjust tax rules and procedures to be adequate to the new environment. Together with experts from EU countries, we are trying to find the best solutions to professionalize our current procedures and minimize the burdens for both tax administration and taxpayer.

We therefore entered year 2014 with a new unified information system. Accurate records of tax debts and monitoring the dynamics of payments, improving tax discipline, increasing the quality of reports for public revenue fund users, improving the quality of services to taxpayers - are just some of the advantages of introducing this new and improved information system. Introduction of the unified pay-

ment system is our major goal in the nearest future –one e-tax return will replace the current eleven tax returns submitted in paper; one payment account will be used instead of 205 existing nowadays. This will greatly reduce paperwork for the employees in our tax administration, and also the taxpayers' burden from coming to the tax administration's offices, which will be reduced to minimum. We strive to improve voluntary compliance and reduce the expenses of tax audit by introducing a Voluntary Compliance Plan in accordance with the IMF recommendations and based upon the OECD model. This means that we plan to strengthen the Risk Management Unit within the administration, so we could improve voluntary compliance and have better collection rates.

The IOTA workshop pointed out the importance of providing practical assistance to taxpayers at one place through the presentations given by the tax administrations of Poland, Estonia, The Netherlands, Azerbaijan, Italy, Lithuania, Ireland and Finland. They shared their experiences, approaches and obstacles they were faced in providing assistance to startup companies. Having in mind those experiences, we plan in the nearest future to provide assistance to taxpayers in one place by enhancing performance of our current website. That means that we plan to have, besides electronic tax returns, guidlines for every public revenue in video format.
Therefore, within our tax administration electronic communication with the taxpayers is now introduced as a must. We plan to improve it and raise it on a higher level by providing the taxpayers, from the middle of the year, possibility to file tax returns only electronically. Also, last year we started to inform the taxpayers through the newly established website of the Tax Administration of Serbia on a daily basis, where they can read all about the news in the area of public revenues in general, as well as to inform them of the steps taken by our tax police department.

Likewise, we increased our activity on public networks. Such as Facebook and Twitter and the permanent increase of the number of users and followers on those networks are indicators for us to see our success in that kind of electronic communication with the taxpayers. Activities of our Contact Centre were widened by launching information campaigns to the taxpayers by informing them by phone about the status of their obligations, in order to increase voluntary compliance in the field of collection of public revenues as well as to protect taxpayers from paying penalties for non-compliance within the deadlines.

The IOTA Workshop allowed us to hear the best practical experiences, to extend our knowledge and share ideas. Also we now have a better insight of methods to assist taxpayers in starting businesses. Our awareness of the challenges we need to deal with, increased a lot and we realized that we have to widen the knowledge of our employees as well as their skills to find more appropriate practical solutions in that field, so they can be of great help to the new taxpayers starting their business and to guide them through our legal system.

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Exchange of tax information: A key tool for tax administration

By
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SPAIN

The need for mutual administrative cooperation in the field of taxation is growing very fast in the globalization era. The mobility of taxpayers, the increasing number of cross-border transactions, the internationalization of financial instruments, the e-commerce and the free movement of capitals make it very difficult for countries to assess the relevant taxes in their own countries without the assistance of other countries.

The lack of mutual administrative cooperation gives rise to aggressive tax planning, tax fraud and tax evasion. Individuals and companies can take advantage of this situation producing a devastating effect on public budgets, as we are experiencing nowadays.

In the current circumstances national tax administrations must cooperate and assist each other to fight against tax fraud in an effective way, being exchange of information the main form of administrative cooperation in the field of taxation.

Administrative cooperation is compulsory, improving all basic forms of exchange of information (specific, spontaneous and automatic) and developing interactive forms of administrative cooperation, such as simultaneous controls or tax examinations abroad. In this regard, the increasing importance of automatic exchange must be mentioned.

Tax havens are one of our main problems and Tax Information Exchange Agreements (TIEAs) are being regarded as an effective way to fight against them. The conclusion of a TIEA is not only the way to fight against tax fraudsters, but it is also a way to limit a possibility of tax fraud by reducing the jurisdictions in which no information exchange is allowed. The discussion of the practical use of TIEAs is on the agenda of many international meetings. It's becoming a trendy topic in this field.

Tax fraud, exchange of tax information and tax havens are becoming worldwide topics appearing periodically in the news. In this context, exchange of information can become a powerful tool to overcome the negative effects of globalization. The ultimate goal of tax administrations must be the eliminating of tax fraud and persuading taxpayers to pay their taxes.

Governments have finally become aware of the great importance of having an efficient procedure for getting information in a timely manner. Over the last years many things have happened in the field of information exchange, not only as far as the legal basis is concerned, but also in the field of practical issues.

Legal Basis for Administrative Cooperation[1]

Double Taxation Conventions (DTCs) based on the OECD Model.

Article 26 of the OECD Model Convention is one of the basic instruments to exchange information between tax administrations. Many changes have been made to the Article over the years in order to achieve that information might be exchanged to the widest possible extent.

Article 26 and its commentary provide the OECD standard for exchange of information. It covers all forms of information exchange (on request, spontaneous and automatic) and all taxes, since the exchange of information is not restricted by Articles 1 (Persons covered by the Convention) and 2 (Taxes covered by the Convention)

The latest developments in Article 26 are shown below:

- Foreseeably relevant information. The competent authorities shall exchange the information foreseeably relevant for carrying out the provisions of the Convention or to the administration or enforcement of the domestic laws concerning taxes. In that regard, more commentaries to Article 26 have been added, defining broadly the scope of the foreseeably relevant information, pointing out explicitly that requests concerning a group of taxpayers are allowed.
- Use of information for other purposes. Article 26 allows for the use of the information for non-tax purposes, provided that such information may be used for such other purposes according to the legislation of both States and the competent authority of the supplying State authorizes it.
- Speeding up the administrative process. The new commentaries on this issue provide that if the information is already in possession of the requested State it should be provided in 2 months. However, if the information is not yet possessed by the requested State it should be provided in 6 months. Although it is an optional blueprint for the States, it is a step forward to achieve an effective exchange of information. Getting the information in a timely manner is essential.

[1] In this Article no reference is made to the specific legal basis that enables the exchange of information concerning Customs duties or Excise duties.

[2] Automatic exchange of information requires a preliminary agreement between the competent authorities.

The Multilateral Convention on Mutual Administrative Assistance in Tax Matters

The Convention was opened for signature by the member states of the Council of Europe and the OECD on 25 January 1988. It was amended by Protocol in 2010 to respond to the call of the G20 to align it to the international standard on exchange of information and particularly to open it to all countries. The amended Convention was opened for signature on 1 June 2011 and since then many different countries have become signatories to the Convention. The signatories to the Convention represent a wide range of countries including major financial centers and developing countries.

The main aim of the Convention is to find an appropriate balance between the international cooperation required to fight against tax evasion and tax avoidance effectively and the respect for the fundamental rights of the taxpayers.

One of the advantages of the Convention, on top of the growing number of signatories allowing the information exchange with territories where no other legal basis is available, is the broad scope of the Convention, because it provides for all forms of administrative cooperation between countries in the assessment and collection of taxes. This cooperation includes:

- All forms of exchange of information (on request / spontaneous / automatic[3]).
- Simultaneous tax examinations and participation abroad.
- Service of documents.
- Assistance in recovery.

Moreover, it covers all taxes except customs duties. Nevertheless, it is also a flexible instrument. Countries can make reservations on certain issues, such as the taxes covered or the forms of assistance.

Tax Information Exchange Agreements (TIEAs) - OECD Model.

The OECD Model Agreement represents the standard of effective exchange of information for the purpose of OECD's initiative on harmful tax practices. TIEAs were promoted by the OECD as a way to tackle tax haven abuse. They are bilateral agreements under which territories agree to cooperate through exchange of information. The main provisions of the OECD Model Agreement are set out below:

- Taxes covered. The Agreement applies to direct taxes and may also apply to indirect taxes.
- Application. Information must be exchanged for both civil and criminal tax matters.
- Retroactivity. Entry into force of the Agreement may be different depending on whether it is a criminal tax matter or not.
- Financial information. Information held by banks, other financial institutions and any person acting in an agency or fiduciary capacity including nominees and trustees has to be provided upon request.
- Forms of exchange of information. The Agreement only covers exchange of information on request. However, Contracting Parties may agree to expand their cooperation on matters of exchange of information for tax purposes by covering automatic and spontaneous exchange.
- Tax examinations abroad. The Agreement allows the possibility of carrying out such examinations, but it is only an option. The decision of whether to allow the examinations and if so on what terms, lies exclusively in the requested Party.
- Limits: general and specific.

Within the European Union

Council Directive 2011/16/EU on administrative cooperation in the field of taxation and repealing Directive 77/799/EEC

[3] Automatic exchange of information requires a preliminary agreement between the competent authorities.

Directive 2011/16 builds on the achievements of Directive 77/799 but provides for clearer and more precise rules governing administrative cooperation between Member States where necessary, in order to establish, especially as regards the exchange of information, a wider scope of administrative cooperation between Member States.

This Directive covers all forms of exchange of information: on request, spontaneous and automatic. It is important to point out that automatic exchange of information is mandatory. Other forms of administrative cooperation are also regulated:

- Administrative notification.
- Simultaneous controls.
- Presence in administrative offices and participation in administrative enquiries.

This Directive applies to all taxes levied by a Member State, including local taxes. However, VAT, Customs Duties, Excise Duties, Social Security contributions, fees or dues are excluded.

In order to ensure that the information exchange is timely and thus effective, time limits for the provision of information are laid down in this Directive. If the information is already in possession of the requested Member State it shall be provided within two months. If not, it shall be provided within six months.

The regulation of feedback as mandatory is also important when it is requested by the competent authority that has provided the information. Likewise, it is mandatory to send feedback on the automatic exchange of information. Feedback on information sent will encourage administrative cooperation between Member States.

As far as possible requests for information will be sent by electronic means using a standard electronic form. It is essential for tax administrations to be able to adapt their systems to the new technological environment.

Other legal basis[4]:

- Council Directive 48/2003 on taxation of savings income in the form of interest payments.
- Council Regulation 904/2010 on administrative cooperation and combating fraud in the field of VAT.
- Council Directive 2010/24/EU concerning mutual assistance for recovery of claims relating to taxes and duties.

Key elements of exchange of information.

- Commitment to exchange of information is mandatory, provided that all requirements are met. Different regulations use the verb shall and not may.
- Foreseeably relevant information. It is required that at the time a request is made there is a reasonable possibility that the requested information will be relevant.
- No fishing expeditions. A requested Party/State is not required to provide information in response to requests regarded as fishing expeditions. These are speculative requests that have no apparent link to an open inquiry or investigation.
- It covers civil and criminal tax matters. Information must be exchanged for both civil and criminal tax matters.
- Other uses of the information exchanged. Information exchanged for tax purposes may be used for other purposes, provided that such information may be used for such other purposes under the laws of both Parties/States and the supplying Party authorizes such use.
- Confidentiality. Information exchanged shall be covered by the obligation of official secrecy and enjoy the protection extended to similar information under the national law of the Party/State which received it.

[4] These regulations are mentioned for information only. They go beyond the scope of this Article.

Limits and obligations in the field of exchange of information.

- **Limits**
  - Exhaustiveness. The requesting Party/State must have exhausted the internal sources of information, except those that could jeopardize the success of the investigation or those that would give rise to disproportionate difficulties.
  - Lack of reciprocity. The requested Party/State may decline to exchange information where the requesting Party/State is unable to provide similar information in similar cases.
  - Secrecy and public policy (ordre public). The provision of information may be refused where it would lead to the disclosure of a commercial, business, trade, industrial or professional secret or a trade process, or of information whose disclosure would be contrary to public policy.
  - Not contrary to its legislation or administrative practice. The requested Party/State will not be compelled to carry out enquiries or measures or to supply information, if it would be contrary to its legislation or administrative practice to conduct such enquiries or to collect the information requested for its own purposes.

- **Obligations**
  - No domestic tax interest required. The requested Party/State cannot decline to supply information solely because it has no domestic interest in such information.
  - Must exchange bank information. The requested Party/State cannot decline to supply information solely because this information is held by a bank, other financial institution, nominee or person acting in an agency or a fiduciary capacity or because it relates to ownership interests in a person.

Exchange of information between different countries and territories is growing very fast. That shows that we are moving in the right direction. Information exchange works and it plays an increasingly useful role in the field of taxation. Quality of information exchanged is improving and measures are being taken to speed up the administrative process. Getting bank and financial information from territories such as Luxembourg, Switzerland, Curaçao or Panama, amongst others, is not a pipe dream anymore.

A successful example is the evolution in the information exchange between Switzerland and Spain. It has been a step-by-step process. The Double Taxation Convention between Spain and Switzerland had no Article concerning exchange of information. Subsequently, it was included the relevant Article, but only for cases of tax fraud or the like. An Article concerning exchange of information is currently in force allowing the information exchange in all cases, provided that all requirements are met.

Likewise, FATCA[5] and the above mentioned legal basis are giving a boost to automatic exchange of information. In the near future tax administrations will have a lot of useful information available that, in some cases, will be used as an indication of fraud or irregularities in order to initiate tax audits which, in turn, may give rise to specific requests for information. In other cases, the information will be used to carry out directly the relevant tax assessments. And, in any event, it will act as a deterrent to non-compliance with tax rules.

[4] The US Foreign Account Tax Compliance Act.

International Tax Issues derived by a Capital Gain

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SPAIN

Article 13 of the Model Tax Convention on Income and Capital of the OECD establishes the right to tax capital gains on operations involving companies resident in different countries. Depending on how this Article is applied in each Tax Treaty, the source country could have unlimited rights to tax an operation, have limited rights to tax or no rights to tax at all.

This article discusses if it is possible to tax, under Spanish law, the relinquishment of the rights to subscribe to shares issued by a local company when the operation involves a French company.

First of all, a description of the facts is required. Let's assume that there are four enterprises that belong to the same group (N Group). The first company ("S") was incorporated under Spanish law (resident in Spain) and is wholly owned by a French company ("F") established in Paris. Besides those entities, there is a third company ("N") resident in the Netherlands. "F" and "N" are wholly owned by the parent company of group ("H"), which is also resident in the Netherlands.
At the end of its financial year "S" raises its capital by 20 million Euro

issuing 20 million shares without the right to vote (33% of its capital). These shares are entitled to receive dividends before the holders of common shares (preferential shares).
This capital increase is not subscribed by the company owner, "F". Instead of that, "F" relinquishes its rights to subscribe to the newly issued shares in favour of an associated Dutch company, "N".

Considering these circumstances, the analysis of the transaction must be considered as follows:

- If the operation is a capital gain under the definition of Article 13
- If the capital gain can be taxed in Spain
- If the shares without the right to vote could be considered a "hybrid instrument"

With regard to the first question, article 13.2 of the Tax Treaty between Spain and France establishes that gains from the alienation of shares or other rights which means a substantial participation in a Spanish company can be taxed in Spain.
As the Article specifically mentions "shares or other rights" it is reasonable to assume that the resignation of subscription rights is within the scope of the Article. In line with this interpretation, paragraph I.5 of the Commentaries on Article 13 explains that, even though the Article does not give a definition for capital gains, the words "alienation of property" cover, among others situations, "the sale of a right, the gift and even the passing of property on death". Therefore, the forfeit of subscription rights must be considered a capital gain.

With regard to the second question, once the definition of the transaction is clear, in order to decide if the forfeit of rights can be taxed in Spain, two issues must be discussed.
On the one hand, according to the Tax Treaty, participation is considered to be substantial when it entitles the holder to at least 25% of the capital or at least 25% of the rights over the profits of the enterprise. In the present case, this requirement is fully satisfied since the purchaser of the subscription rights will acquire 33% of the capital in "S".

On the other hand, the Tax Treaty between Spain and France establishes that capital gains derived by a resident of a Contracting State from the alienation of a substantial participation in a company resident in the other Contracting State shall be taxable only in the Contracting State of which the alienator is a resident when a tax deferral regime is applicable to the transaction. Therefore, if a tax deferral regime could be applied to the relinquishment of rights by the French company, the operation would only be taxed in France.
Therefore, it is necessary to analyse if such a tax deferral regime can actually be applied. The Merger Directive (2009/133/EC) establishes the main deferral regime for cross-border transactions within the EU. This rule is applied only for very specific operations: mergers, divisions, partial divisions, transfer of assets and exchanges of shares in which companies from two or more Member States are involved.
The transaction between the French and the Dutch company cannot be defined as either of the above mentioned alternatives. In particular, the relinquishment of subscription rights is not a transfer of assets as this operation means that a company transfers one or more branches of its activity to another company in exchange for the transfer[1] of securities representing the capital of the company receiving the transfer . Therefore, as "F" is not receiving shares of the Dutch company "N", Spain will have the right to tax the operation as there is no tax deferral regime applicable.

Finally, the third issue must be analysed under the recent OECD work "Addressing base erosion and profit shifting[2] ". Since shares without the right to vote can be treated as a debt under Spanish legislation (at least a substantial part of their total amount), they could be considered as a "Hybrid financial instrument" if they were treated as equity under the holding company's national legislation (the Dutch internal legislation in this case). If this were the case, the Spanish company "S" could reduce its tax base through the interest payment of

[1] Article 2, Council Directive 2009/133/EC of 19 October 2009 on the common system of taxation applicable to mergers, divisions, partial divisions, transfers of assets and exchanges of shares concerning companies of different Member States and to the transfer of the registered office of an SE or SCE between Member States

[2] http://www.oecd.org/tax/beps.htm

the debt; whereas the Dutch company would not pay taxes for this income as it would qualify as dividend. This issue then had to be reviewed under the Tax Treaty between Spain and Netherlands. Unlike more recent Tax Treaties signed by Spain, the Spanish-Dutch Convention does not include a clause against the use of hybrid elements or the possibility of starting a conflict of qualification. Hence, it will be very difficult for the Tax Authorities to challenge this unintended double non taxation. As it has been stressed by the OECD in its recent publications, greater efforts must be made to avoid these kinds of undesirable situations.

Regardless of the complexity of the operation demonstrated by this case, it can be concluded that the resignation of the subscription rights of a Spanish company by a French company can only be taxed under Spanish law if the transfer of the rights involves substantial participation and if a deferral tax regime is not applied to the transaction.

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"Combating Tax Evasion and Avoidance" – Understanding the Legislative Context in UK Avoidance Cases

By
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UK

I attended the IOTA "Combating Tax Evasion and Avoidance" Workshop in Budapest in October 2013The discussions around my case study brought home to me the different legal criteria in the represented IOTA member countries and that different solutions would be appropriate for different core regimes. There were also varied views on what constituted evasion and avoidance.

In order to understand the full impact of any UK avoidance case and any potential read across to other countries' regimes, it is first necessary to understand the legislative context (and underlying principles) of the UK's taxing regime, particularly in an avoidance context.

The UK's rules of tax law interpretation have largely developed over time via judicial interpretation. The initial landmark case providing guidance was that of IRC v Duke of Westminster [1935]. The case involved the Duke covenanting to make payments to persons who were

(mainly) in his employment. At the time, payments under deeds of covenant were allowable in calculating liability to tax but payments for wages/salaries were not. The covenants were valid documents and the payments were allowable for tax. The Court provided guidance that where no sham is involved "every man is entitled if he can to order his affairs so that the tax attaching under the appropriate Acts is less than it otherwise would be. If he succeeds ... he cannot be compelled to pay an increased tax". This interpretation was based on a literal reading of the law.

The above principle existed for many years until the case of W. T. Ramsay Ltd v CIR (1981) was decided by the UK House of Lords in 1981. In the Ramsay case the company made two separate, interest bearing loans to a newly acquired subsidiary company. The interest on the first loan was reduced to nil while the interest on the second loan was doubled. The second loan was then sold to another company at a capital profit. The first loan was repaid at par. The company then incurred a capital loss in respect of the sale of shares in the subsidiary to another company. The company sought relief for the capital loss but contended that the capital profit was exempt from tax as a debt on a security. It was held that where there was an integrated and interdependent series of transactions which had (effectively) produced neither a gain nor a loss, in those circumstances it would be wrong and a faulty analysis to pick out and segregate for tax purposes the one transaction that produced the loss. The scheme would be treated as a nullity for tax purposes and so produced no loss and no gain within the meaning of the relevant legislation.

In the Ramsay case the court decided that where a scheme relied on a series of pre-planned interdependent transactions (whether legally enforceable or not) it was necessary to consider those arrangements as a composite in conjunction with the purpose of the relevant statute. This purposive view of the law meant taking into consideration what Parliament intended in enacting the particular law (for example the nature of the transactions to be taxed or relieved) and whether the arrangements as actually undertaken met those requirements. There were therefore two things to be considered – the facts of the case and the purpose of the law in point.

In this case the UK House of Lords held that this wholly artificial loss was not the kind of loss contemplated by the legislation.

This "Ramsay" approach (actually correctly stated a purposive approach) to statutory interpretation has been most recently formulated by the Courts as follows - "The ultimate question is whether the relevant statutory provisions, construed purposively, were intended to apply to the transaction, viewed realistically". This again highlights the need for consideration of two things: a realistic view of the facts i.e. what has really happened; and a purposive interpretation of the relevant statute. Whilst both areas need consideration and no order of preference is actually set, it could be argued that without a full appreciation of the factual position it is not possible to decide which piece of statute might in point. As a result the factual position is perhaps best established first.

Returning now to the case study considered at the workshop, this involved individuals claiming losses in respect of their shares of a partnership loss. The partnership loss arose as a result of an asset being purchased (using funds from partners' contributions) and minimal income being generated by the asset. The individuals' contributions to the partnership consisted of 25% from their own personal funds and 75% via a non-recourse loan dependent on the income/profitability of the activity involving the partnership asset. The tax advantage in this case was the effect of the set off of losses against the individual's other income which would otherwise be taxed at 40% (a tax saving) when the "cost" of the loss to the individual was in effect only 25% - the amount they actually contributed. In generic terms, individuals were seeking to obtain more tax relief than the economic cost suffered.

Ultimately the avoidance scheme in the case study failed because the whole amount expended was not allowable expenditure under the relevant legislation (the legislation's purpose was to only give relief for expenditure on the asset) and realistically this was only the real cost of 25% to the individuals, the remaining 75% simply circulated as

part of a tax avoidance scheme. The UK has since introduced new legislation to put the tax position of such schemes beyond doubt. These measures include general annual limits on the amount of losses which can be set against other income plus in the main no losses are allowable at all if tax avoidance arrangements are involved.

More recently a General Anti Abuse Rule (GAAR) has been introduced in the UK. The GAAR came into effect on 17 July 2013 and applies to abusive tax arrangements (as defined in the legislation). Arrangements are "abusive" if they are arrangements the entering into or carrying out of which cannot reasonably be regarded as a reasonable course of action, in relation to the relevant provisions having regard to all the circumstances including –

- Whether the substantive results are consistent with policy objectives and underlying principles
- Whether the means of achieving those results involves contrived or abnormal steps
- Whether the intention is to exploit any shortcomings in the legislation

The GAAR does not replace any existing anti avoidance legislation (such as specifically targeted rules) or rules of interpretation.

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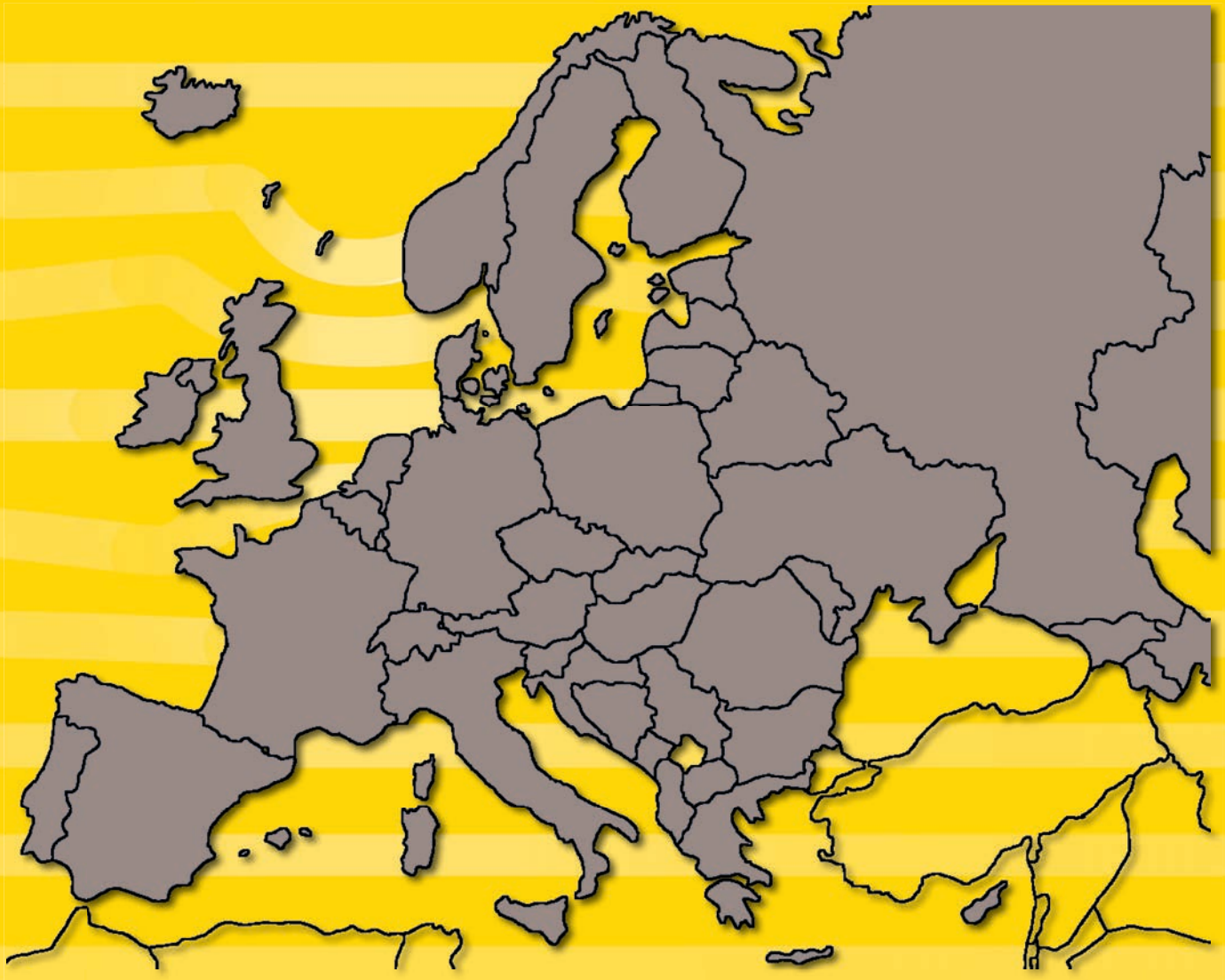

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