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How Tax Authorities Use Data – The Digital Controversy War on Tax

Speaker: Filipa Correia, Nupur Jalan

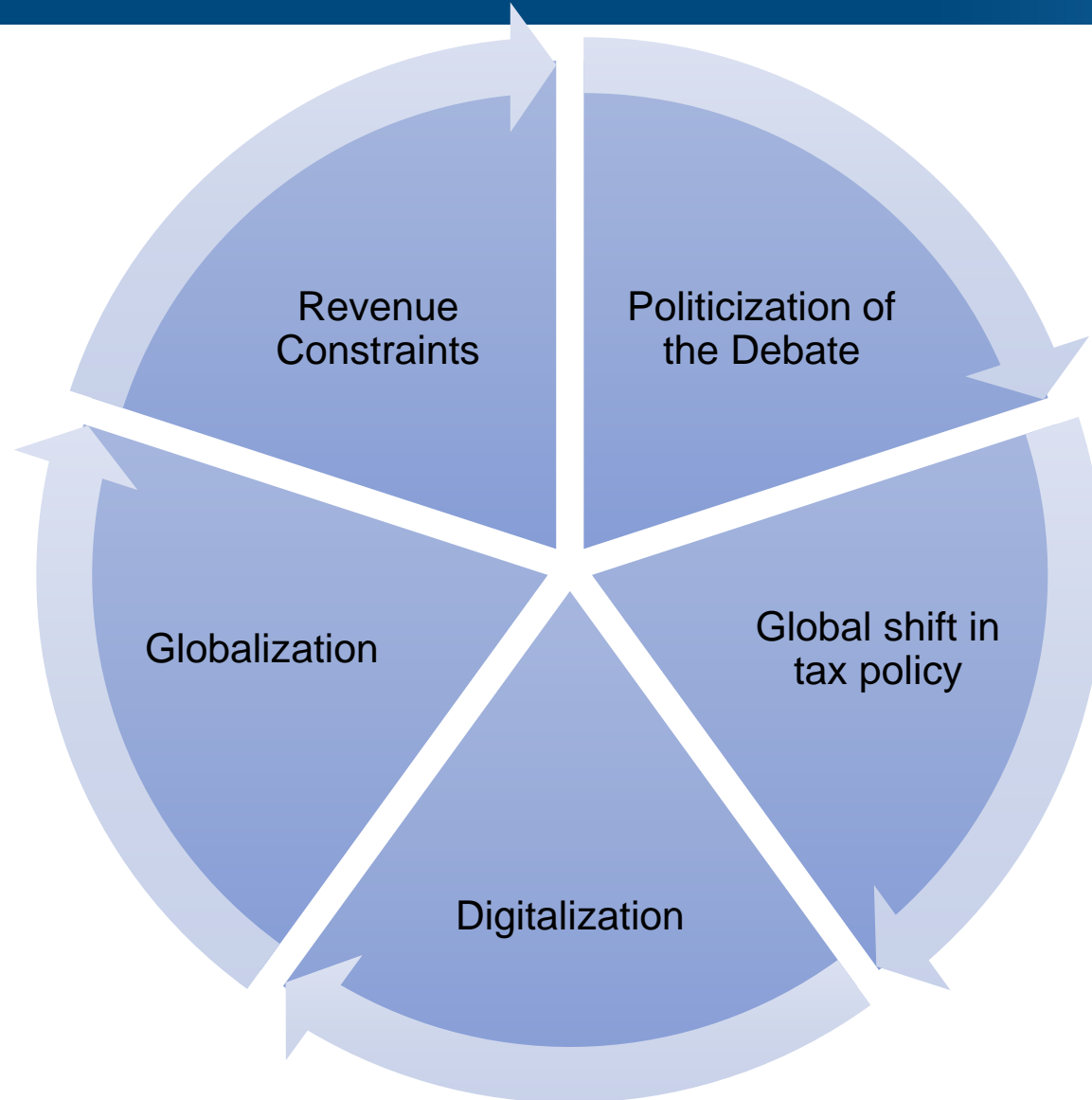
Panellist: Louan Verdoner

- The Agents of Change
- The Ultimate Power of Data
- The Tax Administration Route on Digitalization & Automation
- Some country specific examples
- Taxpayers' Rights and Digitalization of Tax Administrations
- Digital Transformation and Businesses
- Open questions

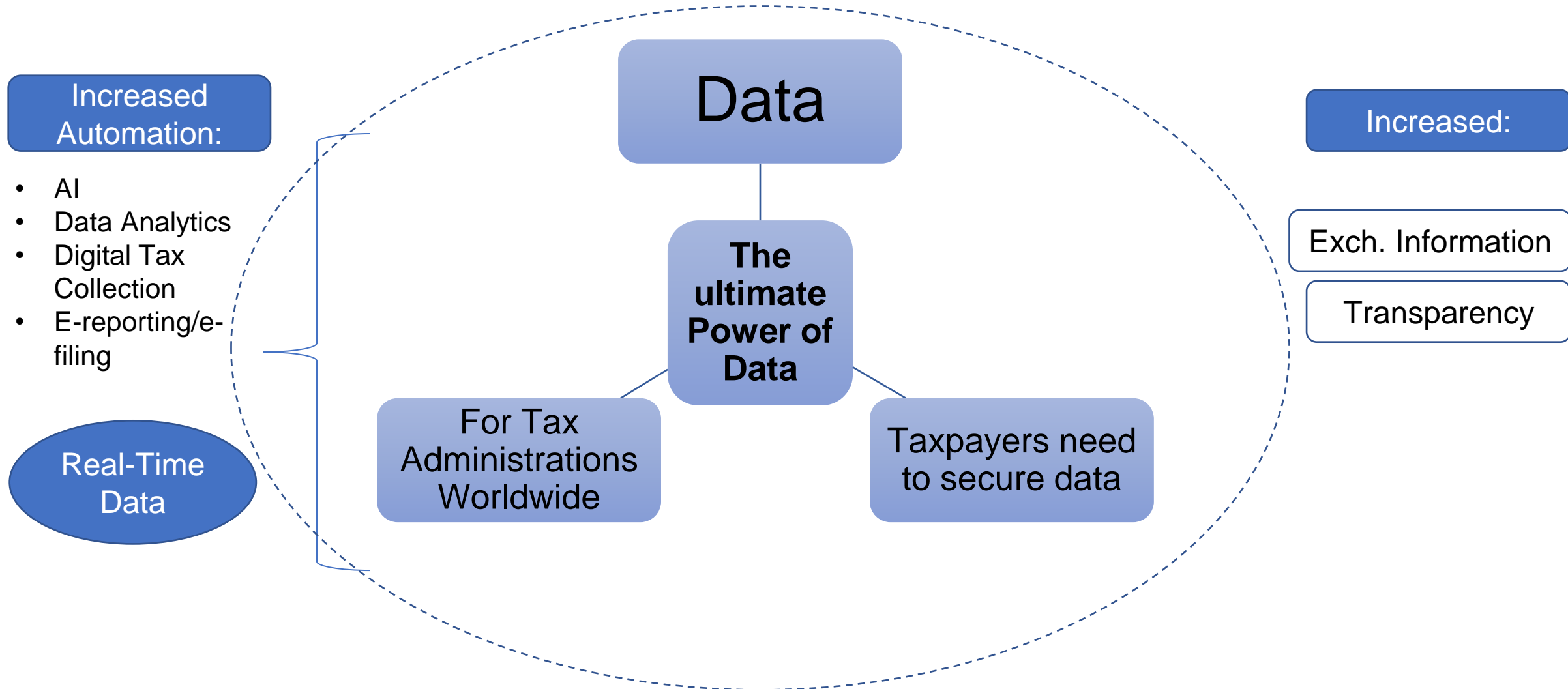
The Agents of Change



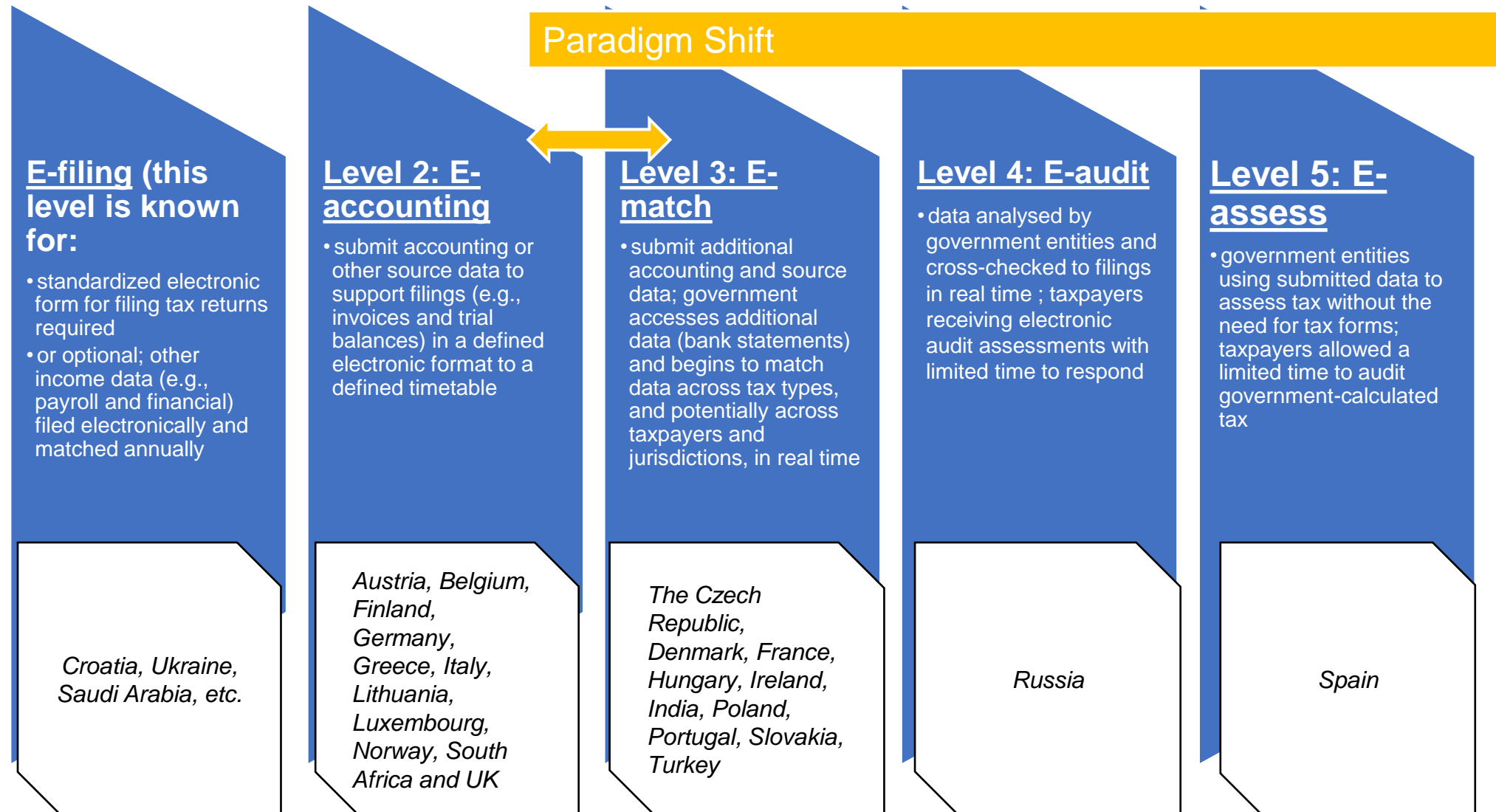
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The Ultimate Power of Data



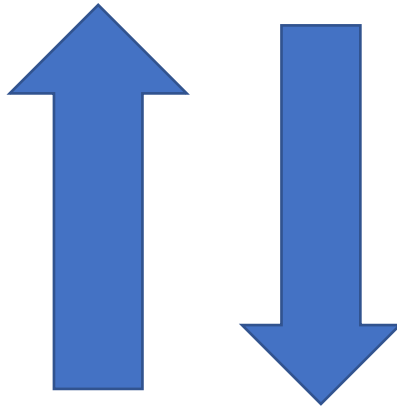
Tax Administration – Different Levels of Automation



- There can be significant tax risk as taxing authorities receive more source data and leverage sophisticated data analytic platforms to gain insight into that information, leading to e-audits and assessments, with increased exposure to tax and penalties.
- Hence, proper management of data becomes essential. Tax administrations are becoming data agencies (they use of analytics for predictions and patterns for risk assessments). However, the move to digital tax administration is not necessarily linear in all jurisdictions.

Benefits

- Transparency
- Efficiency
- Real-time reporting
- Embedded compliance
- Reduction in transaction costs



Drawbacks

- Privacy and data protection
- Cyber-security
- Lack of skill and knowledge gap
- Legacy systems Investment and maintenance

Tax Administration – Different Levels of Automation

Steps needed to be taken to bring more efficiencies



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- **Laying down proper strategies and capabilities**
- **Mechanism to address potential ramifications**
- **Workforce to handle disruptions**

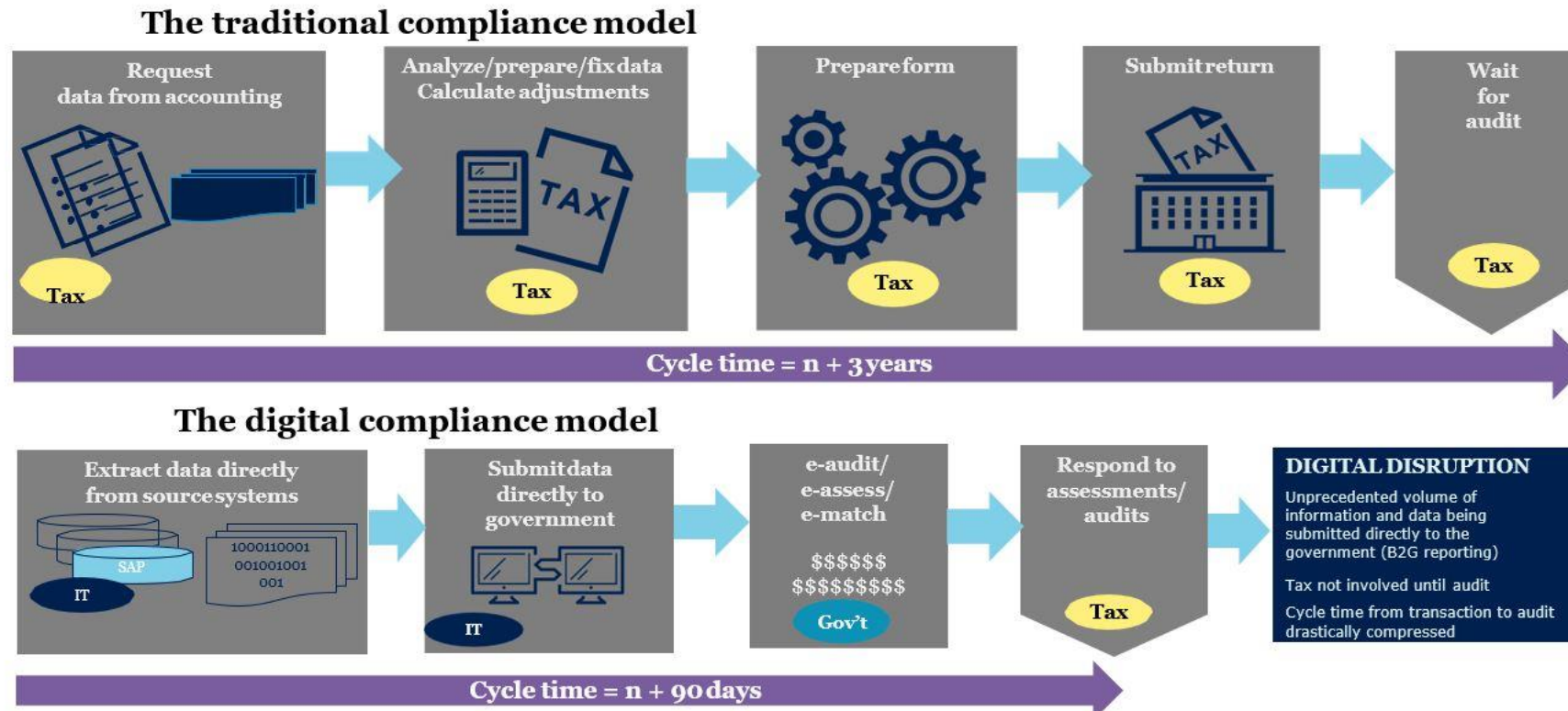
Automation at scale: Most relevant for a tax authority

- ▶ Cross-fertilize AI / automation skills between departments
- ▶ Mix between tactical taxpayer service and long-term strategic process / approach change
- ▶ Workforce dissatisfaction around potential impacts of automation
- ▶ Proactive talent management – upstream/ downstream
- ▶ Flexibility to manage unexpected results
- ▶ Managing (leveraging) public perception around AI use

Source - EY

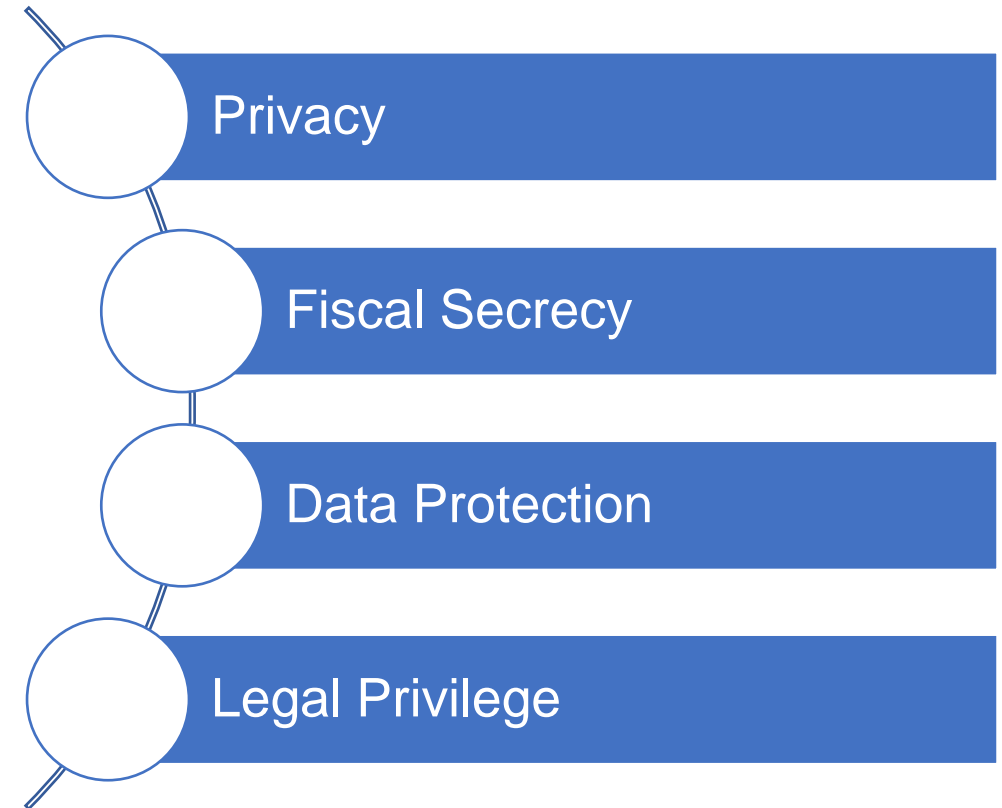
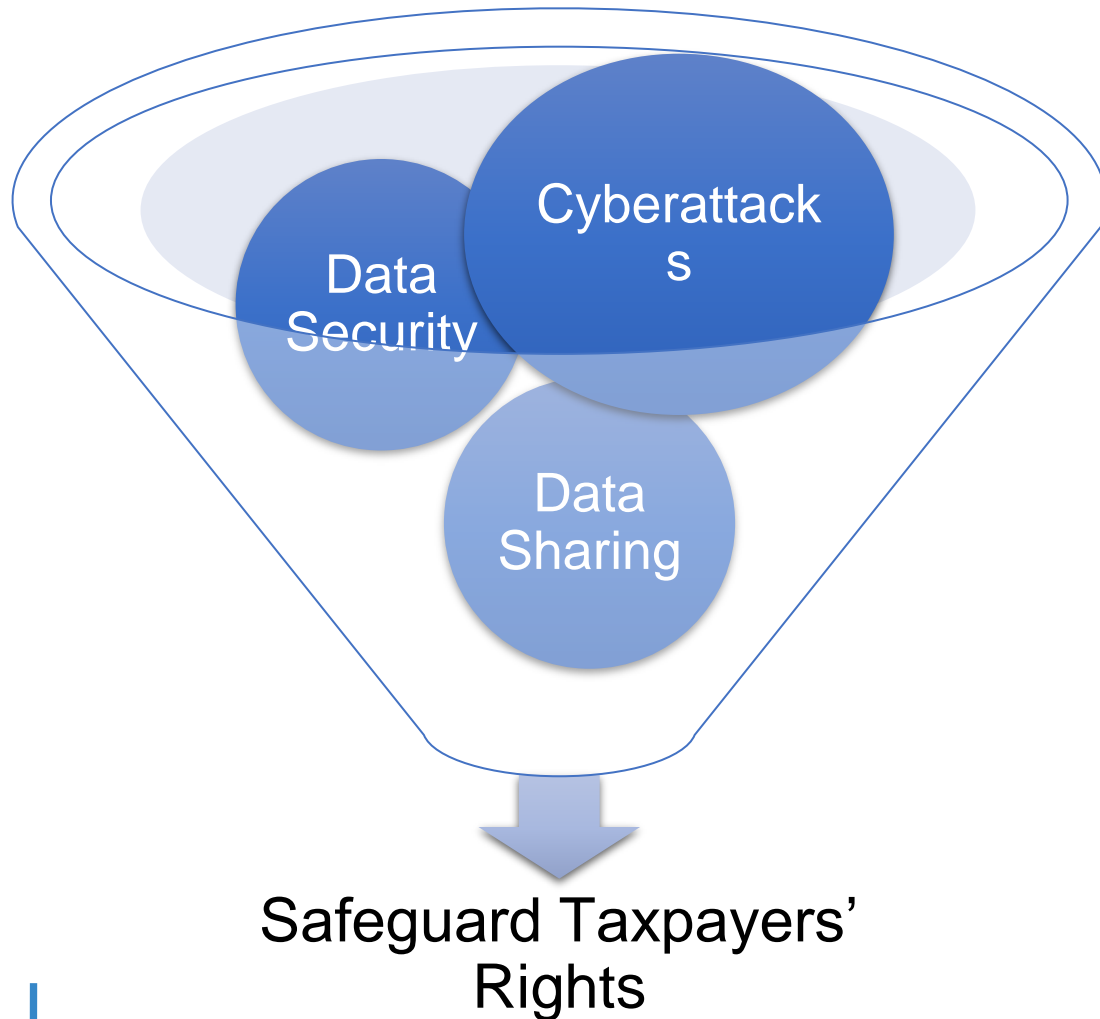
Tax Administration – Different Levels of Automation

Digital compliance cycle



Source – WU presentation (Likely Implications of the New Technologies on future Tax Policy and Administration: An Update)

Taxpayers' Rights and Digitalization of Tax Administrations



- For enhancing transparency, OECD introduced BEPS Action Plan 13 for 3-tier documentation. Local file (information of the local entity), Master file (qualitative information about the group), Country by country reporting (quantitative information about the group). Further, OECD notified electronic format for the exchange of CbCR between countries - XML Schema.
- Further, OECD is using CbCr for impact assessment for Pillar 1 (Unified Approach) and Pillar 2 proposals. Also, tax authorities are increasingly focusing on substance and transaction level information and is looking to use CyBC as a tool for assessing risk. With multiple qualitative and quantitative reporting, the tax authorities have the ability to comprehend such MNE consolidated level information and use the same for determining the rationale at transaction level. With more open exchange of information between Countries, CbCR will also be an active tool for seeking information during assessment proceedings.
- Launched of International Compliance Assurance Program (ICAP) scheme (the approach where taxpayers and tax administrations work co-operatively and multilaterally in close to real time to undertake risk assessment)
- Common Reporting Standard (CRS) requires financial institutions to report information on accounts held by non-resident individuals and entities (including trusts and foundations) to their tax administration
- Automatic Exchange of Information (AEOI) standard/ portal for online support for the implementation of automatic exchange of information in tax matters.

The Impact of Technology on the Nature of Disputes

Tax authorities are improving their **risk assessment** activities as well as investing in **audit resources** to issues that taxpayers and industries identified as high-risk (examples: UK, Australia)

Use of risk assessment among other tax authorities is more **widespread**

Tax authorities are also investing deeply in technology for risk assessment purposes and develop audit priorities.

Increased collaboration among tax administrations (ICAP Pilot, Joint audits, etc.)

If risks are identified, tax administrations are adopting **forensic approaches to test the evidence** which might lead to future assessments, penalties increased disputes

Increased **sharing of information** among tax administrations and use of technology to collect data for risk-assessing to identify issues to then enquire further;

Increased use of **Electronic tax audits**

In transfer pricing disputes it is expected that disputes involve into a scenario where we will have MNEs managing **multi-tax authority disputes**

CbCr

- CbCr is a good example of how Tax administration will use data analytics to assess risks within Country-by-Country Reporting (CbCr) data.
- First exchanges of CbCr reports in June 2018
- OECD publication “*Country-by-Country Reporting: Handbook on Effective Tax Risk Assessment*,” released in September 2017 sets out recommendations for national tax authorities
- The CbCr data will provide tax authorities with a full breakdown of MNEs revenue, profits, tax and other attributes by tax jurisdiction
- The OECD handbook on CbCr s is an excellent tool for companies willing to carry out a sort of pre-submission check-ups to ensure their compliance risk assurance approaches are consistent with the one which is expected to be out in action by the tax authorities
- Along with CbCr and TP documentation data, many countries will have also access to info on arrangements and transactions through so-called ‘Action 12’ disclosure requirements.

Some Examples

Australia

“Australia has had a very detailed schedule around transfer pricing called the International Dealing Schedule for some time and has in parallel developed quite a few risk filters and factors off the back of analysing that data. So the move to country by country reporting is a big step, but it’s not a step from nothing. We’ve already developed some strong functionality around being able to analyze free text and non-standard data sets. In Australia, for CbCR we have set up a structured schema that makes the data more searchable. In terms of the risk factors, there are the 19 put out by the OECD ,but we actually have more than 100 that we apply to international dealings. Our plan is to progressively make those transparent to the taxpaying community, so that people know where we stand and can consciously decide whether they want to have a high or a low risk position. We sometimes call this the “setting out the flags at the beach” strategy, which means that if you put out the flags, you hope that people will swim in between the flags and be safe. For those who swim outside the flags, they should not complain too much if they get caught by a rip and get taken out to sea, because they’ve chosen the position of being at risk.”
[Jeremy Hirschhorn, Deputy Commissioner at the ATO - Australian Taxation Office]

China – China will cross-check TP and CbCr info with the exploitation of Intellectual property

UK - HMRC tax enquiries are focusing on a forensic nature of reviews in many areas requiring production of evidence to assess explanations that taxpayers have provided, often involving the forensic review of emails, interviews with staff and third-party evidence obtained from business customers.

Further source of possible controversy

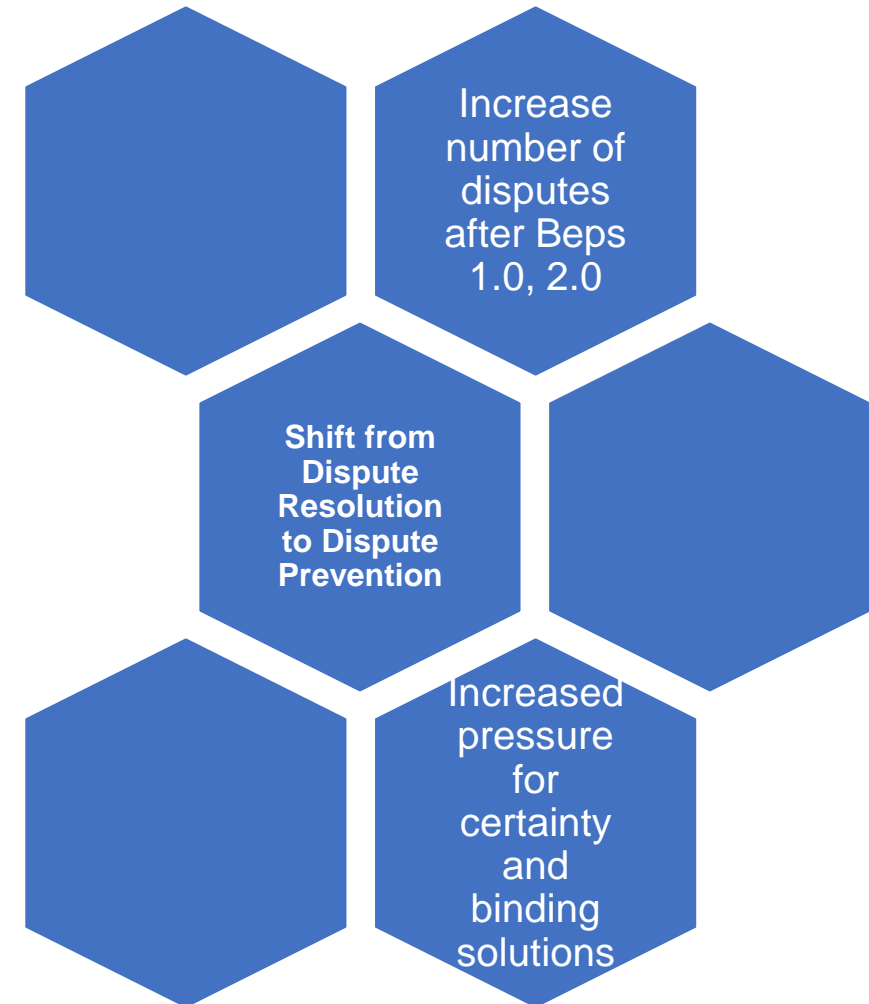
- If the OECD digital proposals will be accepted, MNEs with a certain scale will be taxed either under the current international tax system and the new framework as proposed in OECD's report. (No consensus is reached on the mechanism to bring tax certainty i.e. to handle disputes arising out of the proposals)
- Other times, MNEs will be taxed partly under the old rules (ALP) and partly under the new ones (unified approach).
- Companies can experience being taxed in their headquarter country by the ALP and in the country in which it generates business via the new rules.

Double/ Multiple taxation/Lack of Certainty/Increased Disputes

Is Single solution possible?

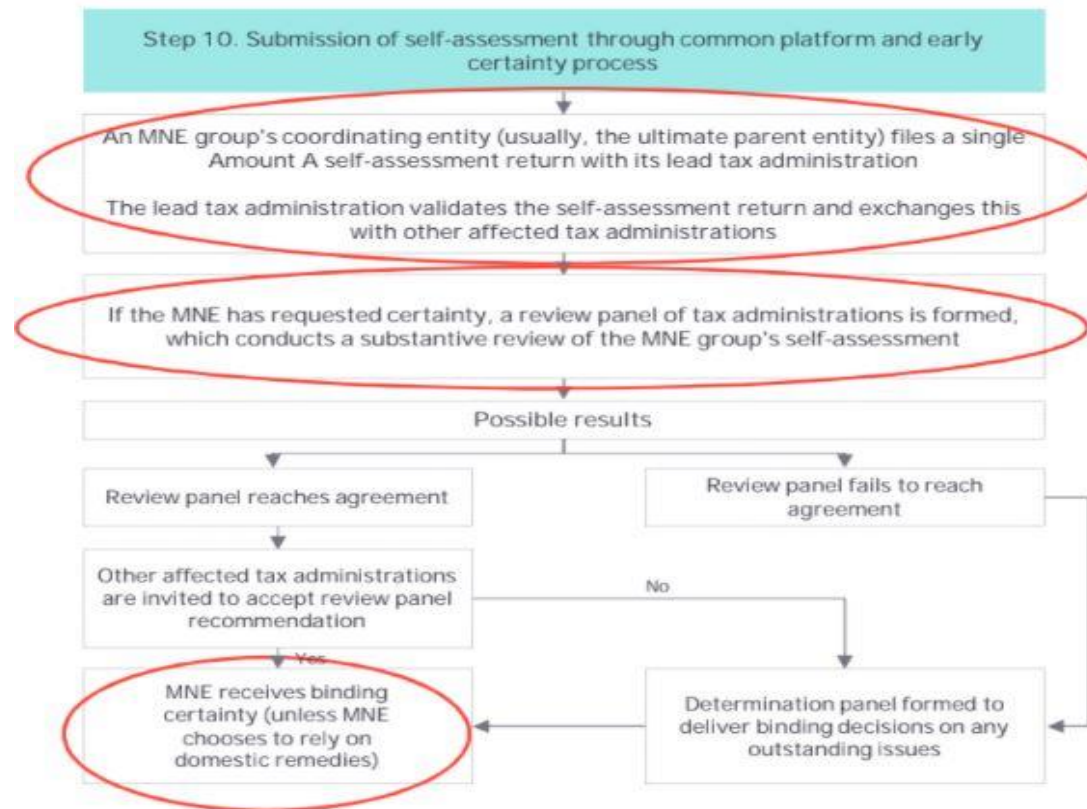
- APA, Multilateral APAs?
- ICAP?
- Arbitration?
- Other?

If no, does the complex and time taking approach suggested under Pillar 1 is a solution. In next slides we discussed the solution proposed under the latest Pillar 1 document.



Unified Approach – Amount A

Submission of self-assessment through common platform and early certainty process



Aims at providing certainty upon request, before tax adjustments, for all aspects of Amount A

If there is no agreement between the review panel, relevant questions framed by review panel to be submitted to second review panel and this second review panel (determination panel is obliged to reach the decision)

If MNE's are not agreeing to the decision of panel, it may withdraw its request. If MNE doesn't want to file application for certainly, then it may resolve the issue through MAP

Source : EY, WU Transfer Pricing Workshop: Managing transfer pricing controversy effectively



Electronic filing/ processing of tax returns and e-assessment scheme



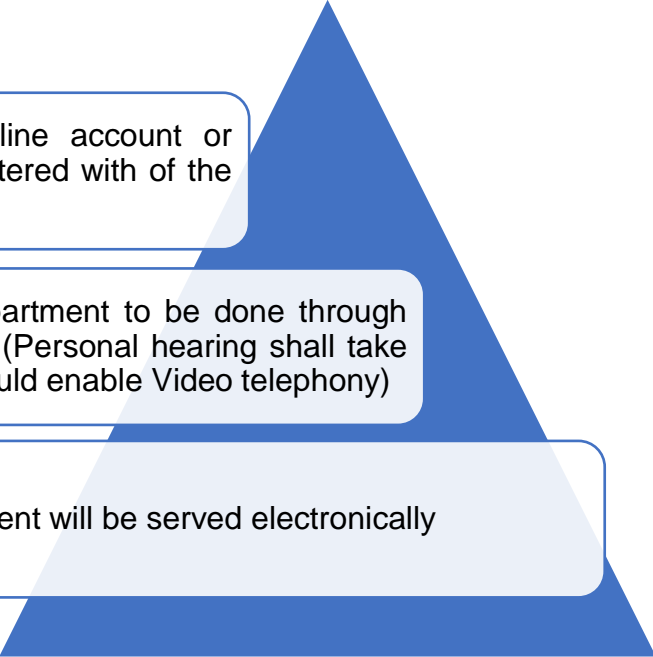
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E-filing:

Overtime more and more countries are moving for electronic filing of tax returns. Usually, a database is maintained, and cross linked to facilitate automatic updating of fields. For e.g. in India, processing of returns are electronic with options to upload response to the notices and queries raised by the Tax authorities and there are facilities for provision of electronic submission of rectifications and grievances.

E-assessment scheme:

India example

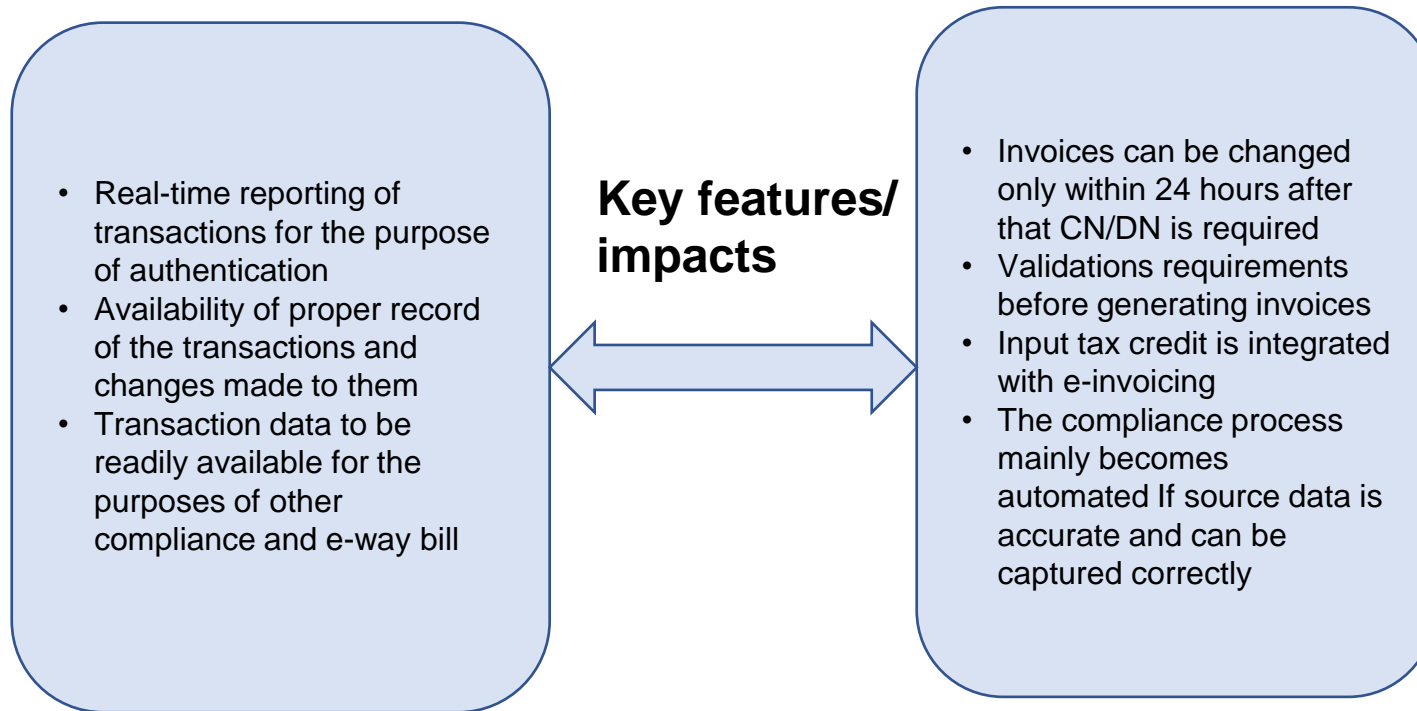
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Communication is done generally with the taxpayer's online account or through the registered email address or mobile number registered with of the tax department

Mostly all internal communication within the income tax department to be done through electronic mode. Taxpayer can request for personal hearing (Personal hearing shall take place through Video conference, through a software which would enable Video telephony)

Any notice in the due course/ order on completion of assessment will be served electronically

Tax authorities are going digital and more and more mechanism are devised to strength the cooperation between taxpayers and tax-authorities. Some countries have introduced e-invoicing mechanism for GST. India example is presented below:



Country examples – Technological advancements



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EUROPE

Italy

E-services/ E-invoicing/ Data enabled compliance initiatives

Netherlands

Move towards data driven tax administration/ replacements of staff with data scientists

Finland

Mandatory use of e-services for businesses/ development of APIs in tax administration

Belgium

Use of data to create profiling of non-paying taxpayers/ Data mining from sources beyond tax administration

Portugal

E-services for taxpayers/ simplify reporting obligations
Electronic mailbox for corporates and PEs for notifications

LATIN AMERICA

Columbia

Voluntary e-invoicing for large companies

Chile

E-invoicing in 2004, majority of corporate taxpayers are required to use e-services

Mexico

E-invoicing in 2014, invoices required, authorization of invoices, filing of tax returns and supporting docs in processable format

ASIA

China

Has most integrated digital environment – social network, shopping, private and public services

Singapore

Making a steady progression from:
Efficient tax authority (1992)/
Service organization (1998)/
Partners of the taxpayers (2005)/
Enablers of the community (2016)

AFRICA

South Africa

E-filing (registration/return submissions/ payment obligations)

Kenya

Mobile phone based financial service platform (M-Pesa) / enabled e-commerce, tax payments and revenue administration

Nigeria

Online mechanism for VAT and CIT filing functionality

- How does advanced technology change the way dispute resolution is being implemented?
- Can we secure that analysis of raw and/or rich data is a reliable basis for classical decision-making procedures?
- Can digitally based taxation models end up into purposeful or unintended reversal of the burden of proof to the detriment of the taxpayer?
- How do you reasonably estimate the disruptive consequences of future state taxation models resulting in a 'war on taxes' and an explosion of tax and transfer pricing disputes?
- Do you think financial data retrieval through Country-by-Country reporting and Pillar 1 based market data retrieval through tax administrations will weaken taxpayer's rights in court proceedings based on the rule of law principles?

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