Chapter 9

Co-operative approaches to tax

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Over the last decade an increasing number of tax administrations have adopted co-operative compliance programmes for large businesses. These are based on openness, disclosure and transparency between the tax payer and tax administrations and on the principle of trust. For business these programmes provide a higher degree of tax certainty at an early stage, enhance their internal understanding and management of risk and can lead to a reduction in compliance costs, particularly those associated with disputes, as well as reputational benefits. For tax administrations the main benefits are improved assurance of tax, reduction in disputes, increased awareness of business concerns and changes in business models as well as better allocation of resources.

This chapter examines developments in co-operative compliance approaches and the scope for multilateral initiatives which may help increase tax certainty more widely, helping to promote investment and growth.

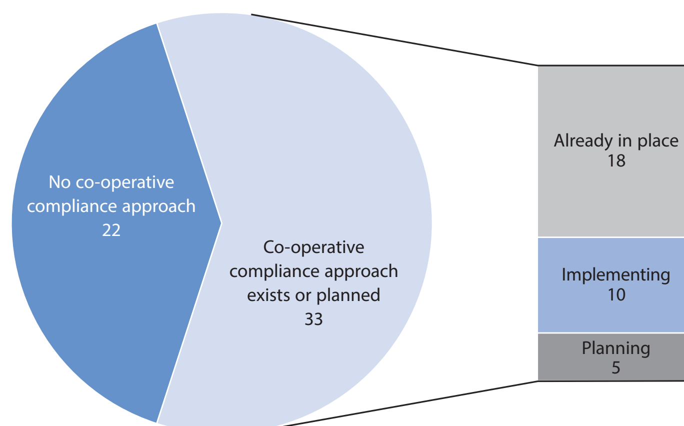
Mutual or conflicting interests

In the past the relationship between tax administrations and large businesses, particularly multinational enterprises (MNEs) could often be characterised as adversarial, with the former looking to maximise tax collected and the latter seeking to lower the total incidence of tax.

-While this may sometimes be the case, in particular in the face of the aggressive tax planning undertaken by some entities, as a general proposition this view is too simplistic. It ignores that businesses and tax administrations are part of the same social and economic framework and that tax is integral to that on an ongoing basis, covering both the revenues raised and the costs imposed by tax collection. While views may not always be aligned, for example on the interpretation of aspects of tax law, tax administrations and large businesses share a common interest in making the tax process as simple, transparent and cost-effective as possible, improving tax certainty and freeing up productive resource while paying the appropriate amount of tax and ensuring public trust.

This shared interest lies behind the development and implementation in 60% of the 55 countries that responded to the tax administration survey of programmes for co-operative compliance (see Figure 9.1). These programmes are aimed at providing greater certainty for large businesses which choose to participate in such programmes and at allowing tax administrations to apply their resources effectively and efficiently to this important group of taxpayers (which have the most complicated tax affairs).

Figure 9.1. **Co-operative compliance approaches – Existence and implementation status, 2015**



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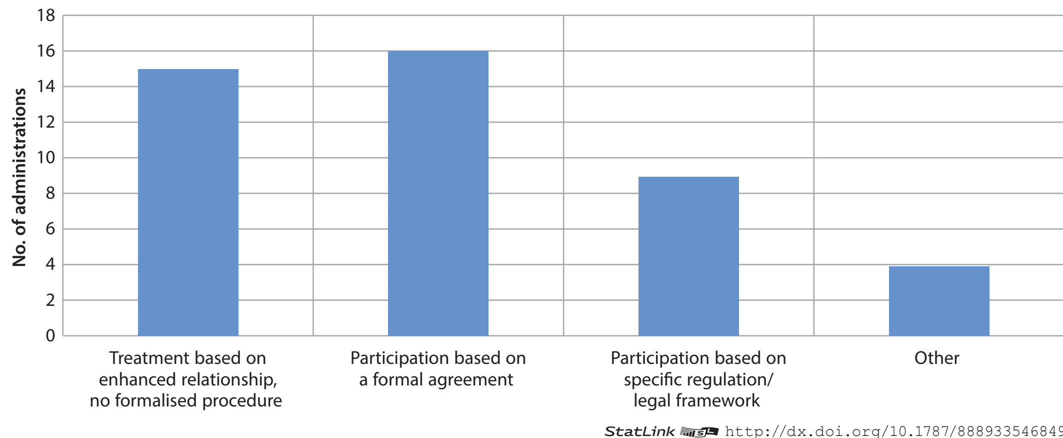
Source: Table A.141 Co-operative compliance – Existence and nature of the model.

Co-operative compliance programmes will not be suitable for all taxpayers. In some cases, taxpayers may not wish to invest the resource needed to fulfil the conditions of entering such a relationship, which needs to be across a group, preferring alternative controls. This might be the case, for example, if such programmes are not available in all the main jurisdictions in which a group operates. On the tax administration side, it may be considered inappropriate to establish such relationships in sectors which have been more characterised by aggressive behaviour or where they do not yet have a good understanding of the risks, for example those resulting from changes in business models. In addition, entry into such programmes may not be considered appropriate based on taxpayer's previous behaviour unless and until a tax administration is confident that the sources of such behaviour have been addressed and appropriately controlled.

Figure 9.2. **Nature of co-operative compliance programmes, 2015**



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Note: Administrations were able to make multiple selections.

Source: Table A.141 Co-operative compliance – Existence and nature of the model.

Risk management and taxpayer behaviour – the background to co-operative compliance

Taxpayers differ in many regards, including ownership structures, governance regimes, internal organisation, complexity, amounts of tax payable, industry or international orientation; and perhaps most importantly their attitude towards payment of tax which influences their decisions around strategy, transparency and/or the tax control they are willing and able to achieve.

The risk management approaches of tax administrations are increasingly looking to factor in these differences in attitude. This is not only as regards technical tax matters, such as complex transfer pricing arrangements, but also the behavioural risks of the taxpayer. This influences how administrations respond to the taxpayer, including any tailored interventions that are deployed, and how specific compliance risk interventions are used to support increased and sustainable compliance.

At the taxpayer specific level, tax administrations will take such decisions based, inter alia, on the actual compliance behaviour of the taxpayer, including the control measures it has taken. In this regard relevant information includes, among other things: information about tax strategy; the existence and quality of any tax control framework; self-monitoring activities; engagement of tax intermediaries; and assurance statements by senior management.

Box 9.1. **Use of legislation**

In order to influence taxpayer behaviour, in particular the understanding and management of tax risks, the United Kingdom has taken legislative measures that target the tax processes of large businesses. Under this legislation, businesses with a turnover of over GBP10 million or a minimum of 20 employees have to appoint a Senior Accounting Officer. The Senior Accounting Officer has the main duty to ensure and certify that the company establishes and maintains appropriate arrangements to allow tax liabilities to be calculated accurately in all material respects.

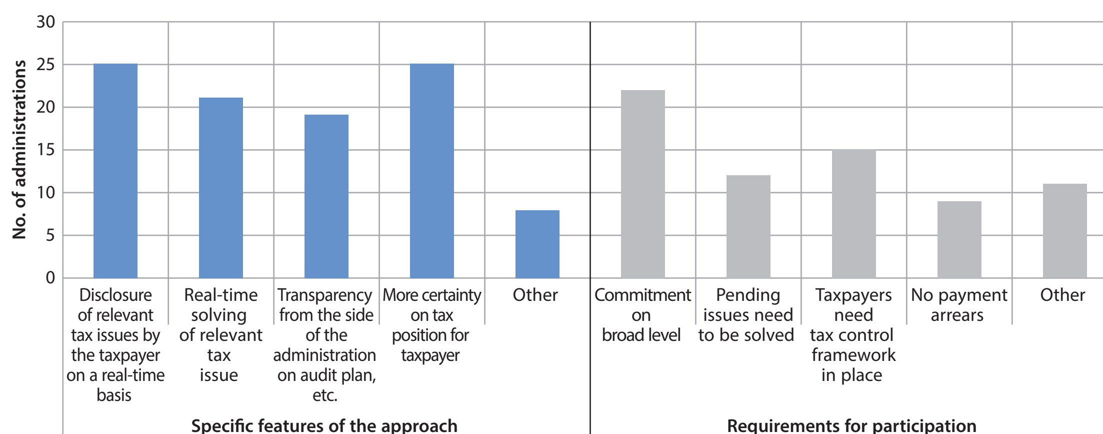
Box 9.1. **Use of legislation** *(continued)*

Very large businesses, whose turnover in the previous tax year was above GBP 200 million or whose balance sheet was over GBP 2 billion, are required to publish their tax strategy. The tax strategy should explain the business's tax arrangements, attitude to tax planning, including the role of external advice, the risk level and the approach to working with Her Majesty's Revenue and Customs (HMRC). Information from the Senior Accounting Officer and the tax strategy are used in the overall risk management process by HMRC.

Source: United Kingdom – HM Revenue and Customs (2017).

Tax administrations' general approach to compliance strategies for what they perceive to be lower risk large businesses has increasingly been formalised under voluntary co-operative compliance programmes. These rely upon an agreed set of commitments, demonstrated behaviours and actions by taxpayers which, taken together, give a high degree of reassurance as to the control of tax risks and ultimately the reliability of tax returns. Such programmes do not, though, give a more favourable tax outcome to participants. Tax administrations are of course required to administer laws and regulations for all taxpayers in an equal manner. Rather such programmes shift the emphasis of compliance away from, in broad terms, auditing after filing to reliance on the assurance systems of businesses coupled with a high degree of transparency towards the tax administration. This also allows, in some circumstances, for greater certainty to be provided to business in relation to specific approaches or transactions as part of upfront engagement and a system of "no surprises". Like all compliance strategies they are aimed at ensuring that the right amount of tax is paid at the right time. Figure 9.3 sets out both the specific features countries include in their programmes and the requirements for participation. It shows that board level commitment and the existence of a tax control framework are the most common requirements.

Figure 9.3. **Co-operative compliance programmes: Features and requirements, 2015**



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Sources: Tables A.142 Co-operative compliance – Participation and specific features of the approach and A.143 Co-operative compliance – Requirements for participation.

Co-operative compliance approaches also require tax administrations to adapt the way they interact with business. The commitment of business at senior management levels needs to be mirrored with a similar commitment within tax administrations. In addition an essential component of the co-operative compliance approach is that tax administrations must actively involve and engage the taxpayer, their representatives and other stakeholders in the evaluation and development of compliance approaches. This will include consideration and discussion of appropriate guidance and how to minimise burdens.

Box 9.2. **Use of tax risk management**

The Australian Tax Office (ATO) has published a tax risk management and governance review guide on its website. The guide was developed primarily for large and complex organisations, tax consolidated groups and foreign multi-national corporations conducting business in Australia, but the principles can be applied to a corporation of any size if tailored appropriately. The guide is focussed at two levels; board-level and managerial level responsibilities. ATO comments that within organisations that have good corporate governance processes in place many of the identified key controls will already exist. In addition if ATO needs to assess the tax governance processes, a strong tax control framework will give confidence that tax risks are well managed and an assessment is likely to take less time and resource than otherwise.

Sources: Australia – Australian Tax Office (2017).

Tax control framework – the central pillar

One of the findings of the OECD report *Co-operative Compliance: A Framework* (OECD, 2013) was the centrality of tax control frameworks to co-operative compliance programmes. This was reaffirmed in the light of the further experience of tax administrations in the report *Co-operative Tax Compliance: Building Better Tax Control Frameworks* (OECD, 2016). A Tax Control Framework (TCF) contains a set of actions and processes which allow large businesses to control, and be seen to control, the core elements of their tax position. The six essential building blocks of a TCF are:

- ***The tax strategy***, which should be clearly documented and owned at Board level.
- ***Comprehensive application of the TCF***, such that it governs the full range of the business's activity.
- **Clear responsibility**, with clarity that the Board is accountable for the design, implementation and effectiveness of the TCF and that the tax department's role and responsibility is clearly recognised.
- ***Governance*** documented, with a system of document rules and reporting which allows risks and anomalies to be identified and the effectiveness of the TCF reviewed periodically.
- ***Testing, monitoring and maintenance*** to ensure compliance with the TCF.
- ***Assurance*** – which can be seen as the overall result of the TCF – which should be capable of providing assurance to stakeholders, including tax administrations, that tax risks are subject to proper control and that tax returns can be relied upon.

While the existence of a TCF is central to giving a high-degree of comfort to tax administrations in how a business controls risk, it cannot be seen as a sole proxy of co-operative compliance but needs to sit in within a context of mutual transparency and engagement. In fact, almost half of countries that responded to the tax administration survey reported it as a requirement for participation in the programme (see Figure 9.2). It also needs to be subject to review of its effectiveness (including ensuring that over time tax administrations do not lose objectivity). Such reviews can be performed in different ways, for instance through the review of a self-monitoring report, reviews by third parties, or an audit of tax returns or particular tax risks.

Tax intermediaries can also play an important role in assurance of co-operative compliance. While they are not generally involved in the preparation of tax returns, they are frequently involved in providing advice about tax structures, including the adequacy of internal controls, and opinions on uncertain tax positions. Further, intermediaries are often involved in assisting a large business in setting up and implementing their tax strategy and TCF.

Several tax intermediary organisations have also set up multidisciplinary teams that combine corporate governance, accountancy and information technology. This is an interesting development and one that may offer benefits to both large businesses and tax administrations, particularly if this work expands and broadens the scope of their work to more holistic services on the overall tax policy and tax position of large businesses.

Exiting co-operative compliance

Despite a business's efforts to ensure compliance through investment in its TCF and self-monitoring, tax returns still can contain errors or issues can arise, such as differing legal interpretation, where parties might hold differing positions which might result in a legal case. By itself this is not necessarily a reason for terminating a co-operative compliance relationship provided that the overall framework remains robust and reasons for any errors are identified and rectified.

However, since co-operative compliance is a voluntary programme both parties have the option to end their participation. In the Netherlands a number of co-operative compliance arrangements have been terminated by mutual agreement and in a very small number of cases by unilateral action. If an arrangement is to cease, it is preferable that this occurs by mutual agreement, as this allows both parties to discuss how the tax affairs of the business will be managed going forward, given that the tax administration will need to adapt its compliance approach, for example undertaking a wider range of audit activity, requiring different information etc. Clarity on that can help in reducing burdens and minimising tax uncertainty.

In general revenue bodies have noted the following reasons for mutually ending an agreement:

- differing expectations about service levels
- insufficient investment in a TCF by a large business
- changes in the strategy of a large business, for example a change in attitude to risk or the taking of aggressive tax positions, or
- where significant issues are suspected or where serious enforcement action is being taken.

Next steps

As co-operative compliance approaches are built on the mutual interests and established processes of the parties they are able to readily respond to changes in legislation or regulation. This has seen them already being adapted to accommodate the requirements of initiatives like country-by-country reporting and other outcomes from the OECD/G20 Base Erosion and Profit Shifting (BEPS) project into the TCF of the taxpayer and into the risk assessment systems of tax administrations.

The 2013 *Co-operative Compliance* report recommended the development of multilateral co-operative compliance programmes. The changing international landscape, including as a result of the outcomes of the BEPS project, is leading to a stronger interest within tax administrations as to how they can co-operatively assess multinational enterprises and the opportunities for joint or simultaneous audit. This is partly with an eye to reducing the number of disputes coming into Mutual Agreement Procedures (MAP).

Against this background a number of members of the OECD's Forum on Tax Administration have agreed to pilot an international compliance assurance programme (ICAP) which builds on the principles of domestic co-operative compliance programmes. This project pilot will involve undertaking a co-ordinated multilateral risk assessment on a small set of low and medium risk MNEs.

The ICAP process is designed to be a swifter and internationally co-ordinated way of assuring the activities and transactions of MNEs, while isolating quickly key risk areas for further attention. The underlying drivers of this pilot are to test whether this may help minimise MAP disputes by increasing collaboration and co-operation between a MNE and multiple tax authorities at an early stage; to increase tax certainty for business; and to positively influence taxpayer behaviour. The pilot will also involve using the new country-by-country reporting on a multilateral basis for ICAP risk assessment which will also inform the wider use of this new information set in risk assessments for large businesses in general, in particular as regards transfer pricing.

Following the pilot, it is intended that there would be an assessment of the pros and cons of a broader roll-out, participation in which would be a decision for individual tax administrations.

References

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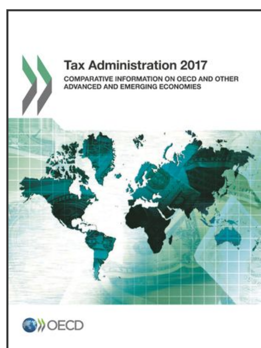

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