Chapter 12

Large business and international

Gord Parr and Francine Turcotte
Canada Revenue Agency

Large business taxpayers are of critical importance to the economies in which they operate. They produce the majority of export income, provide a large share of the tax revenue and, in many economies provide the majority of jobs. They also have complex business structures with multiple operating entities that engage in international transactions presenting distinct and significant tax compliance issues that can have major consequences on tax revenues if not adequately addressed by tax administrations.

In the wake of the work on the OECD/G20 project on Base Erosion and Profit Shifting (BEPS), which will provide tax administrators with new information and tools to address compliance issues related to this important taxpayer segment, it is incumbent upon tax administrations to ensure that their own actions do not create unnecessary tax uncertainty which could have negative consequences on economic growth and result in unpredictable government revenues. In this context, the issues surrounding tax certainty for both businesses and tax administrations will be of increasing importance.

In this chapter, we will explore the current trends in managing large taxpayer compliance that focus on compliance risk management, international collaboration, co-operative compliance, and tax certainty.

Compliance risk management

The majority of tax administrations have adopted a risk-based approach to compliance. As such, they have formal processes in place for identifying, assessing and prioritising their compliance risk areas as part of responsible tax administration. Advanced analytical tools that leverage more comprehensive data offer new opportunities for the use of business intelligence in the identification of non-compliance. As noted in the OECD's *Advanced Analytics for Better Tax Administration* report, "advanced analytics is proving an extremely valuable tool in improving tax administration effectiveness" (OECD, 2016). Through the use of these tools, tax administrations can more effectively assess and prioritise risks, and determine the appropriate level of intervention to achieve compliance.

As an example, in the context of its Approach to Large Business Compliance, the Canada Revenue Agency (CRA) has developed an automated Integrated Risk Assessment System that risk ranks its entire large taxpayer population based on a significant number of risk algorithms developed by subject matter experts in the domestic, international and tax avoidance areas. Experienced case managers, auditors, and industry specialists, taking into consideration inherent and behavioural risk factors, determine an overall risk profile for each taxpayer. The highest risk cases of non-compliance form the basis of regional and national work plans. This approach allows the CRA to focus its audit resources on the highest-risk cases of non-compliance and to reduce the compliance burden for businesses that are low risk. The business intelligence gathered at each stage of the risk assessment process and during the audit is used to improve risk algorithms and the overall risk assessment process.

In addition to having better tools to analyse data, tax administrations continue to access a range of different data sources. In the past, the majority of available data came from the various forms and tax returns filed by taxpayers. Administrations are increasingly looking to large businesses to provide them with more detailed information on their organisational structure, cross-border transactions and uncertain tax positions. Once implemented, the outcomes of BEPS Action Item 13, Transfer Pricing Documentation and country-by-country (CbC) Reporting (OECD, 2015a) will provide administrations with new information for transfer pricing risk assessment. This additional information, along with enhanced business intelligence tools, will allow tax administrations to be more effective in the compliance risk management of the large business population segment.

International collaboration

The large business environment has changed significantly in recent years. Along with the rise in globalisation and electronic commerce, there are more multinational business structures. The survival of these businesses depends heavily on their ability to succeed in a fiercely competitive global economy. This has led many businesses to actively consider various and complex tax treatment options, such as: hard-to-value intangibles; cross-border lease arrangements; thin capitalisation; related party and hybrid financing; restructuring and liquidations; and, determinations of permanent establishment. As such, effectively managing tax compliance risks in this environment is critical.

This competitive environment is also amplified by corporate tax rate variances between tax jurisdictions in order to attract international investment and the consequential economic benefits. Such initiatives typically lead to non-harmonised tax regulations between tax jurisdictions and the shifting of reported profits to countries with the lowest tax rates, thereby threatening the tax bases in various countries.

The BEPS package, approved in late 2015, is intended to address aggressive international tax avoidance strategies used by some multinational enterprises (MNE) to inappropriately minimise their tax obligations.[1]

Over the past several years, we have seen a significant increase in collaboration among tax administrations to address international tax evasion and aggressive tax avoidance issues, for example, through joint audits and risk assessments. The implementation of BEPS recommendations will provide additional tools to address these cross-border compliance issues.

Action 13 on Transfer Pricing Documentation, in particular, will provide new opportunities for tax administrations to work together on risk assessment using common data sets resulting from CbC implementation. Further enhancements to each tax administration's risk assessment processes can be achieved through combined efforts to identify risk indicators and industry-specific issues, and ensure that data is being interpreted in a consistent manner. Forums such as the OECD's Joint International Taskforce on Shared Intelligence and Collaboration (JITSIC) Network,[2] will continue to facilitate the sharing of business intelligence and strengthen the capacity of tax administration to tackle common risks.

In order for tax administrations to fully realise the value of this collaboration, they will need to continue to improve their capacity to risk assess and profile their large business population. For example:

- ***Improve automation*** – Aging systems need to be updated. New systems such as learning software that can improve our understanding of key relationships between corporations and other taxpayer groups are needed. The information gathered can be greatly beneficial in developing or enhancing risk algorithms and profiles across a broad spectrum of taxpayer segments.
- ***New skill sets*** – For the most part, staff in large taxpayer units have audit-related skills. However, expertise in the areas of risk assessment, profiling, and communications are new and important competencies that should be developed or acquired.
- ***Access to and use of external sources of data*** – The use of domestic and international data sources offer significant opportunities to not only improve monitoring, but to move toward real or near real-time compliance activities. Tax administrations will have the opportunity to use various data sources to consider the level of engagement or intervention needed to influence compliance behaviour.

Co-operative compliance

The concept of co-operative compliance is based on the premise that taxpayers provide timely and detailed information about their tax transactions and issues and, in turn, the tax administration will review that information in real-time and provide early tax certainty to the taxpayer regarding their tax position prior to them filing their tax return. With major potential tax issues largely settled before filing, taxpayers are generally subject to a timelier and more narrowly focused post-filing examination. It also allows the tax administration to raise issues with the taxpayer before taking a tax position.

In recent years, a number of OECD tax administrations have adopted a co-operative compliance approach. The form of the approach can vary: some are based on enhanced relationships with no formalised procedures some use formal agreements, and others rely on specific regulations or a legal framework. Whichever approach is utilised, the goal is to have an open and transparent relationship between the taxpayer and the tax administration; one that is built on trust.

As concluded in the OECD report *Co-operative Compliance: A Framework: From Enhanced Relationship to Co-operative Compliance* (OECD, 2013), a tax control framework (TCF) is considered to be centrally important to effective co-operative compliance programmes. A TCF ensures that the large business or MNE has the proper internal controls and governance in place with respect to its tax processes and tax function. A TCF can prevent tax errors, allow companies to manage compliance-related risks more effectively, and promote transparency and co-operation with tax administrations.

An evaluation of the effectiveness of the TCF allows the tax administration to complement its existing risk assessment and adjust its audit plan accordingly. A TCF requires transparency by both parties; the business must allow the tax administration to review its TCF, and the tax administration should be prepared to discuss the impact of the framework on its assessment of risk and planned audit activities. It is only with such transparency that trust can be established, which in turn leads to the desired outcome of tax certainty and compliance.

Tax certainty

Although most tax administrations provide taxpayers with guidance and education about their tax obligations, improving tax certainty through effective public information, clear forms and instructions, face-to-face meetings between taxpayers and tax authorities, collaborative compliance approaches, efficient programmes for advance tax position rulings, and Advance Pricing Arrangements can assist in maximising voluntary compliance. Clear, consistent and timely responses to enquiries, reasonable interpretation of the law, and transparency of processes can help taxpayers make sound and timely business decisions and reduce their compliance costs.

By actively involving and engaging taxpayers, their representatives and other stakeholders such as industry associations to achieve a better understanding of the taxpayer’s tax compliance obligations, improved outcomes and reduced costs for both the taxpayer and the tax administration can be achieved. The knowledge gained by engaging stakeholders can in turn be applied to tailor products and interventions, to design processes and solutions that are more meaningful, and to improve the overall effectiveness of the tax system.

Following the major changes flowing from the BEPS package, concerns that resulting tax uncertainty could negatively impact business decisions, have a negative effect on growth and result in unpredictability of government revenues, will prompt tax administrations to further examine and engage on the issue of tax certainty.

The challenge for revenue bodies will be to implement policies and practices in ways that support tax certainty, and minimise compliance intervention and burden for low-risk taxpayers.

Many of the BEPS Action items and existing compliance approaches can in fact assist in providing tax certainty for both tax administrations and businesses. As an example, CbC reports will provide new information for transfer pricing risk assessment and enable tax administrations to work collaboratively from the same data set to assess transfer pricing risks and tailor responses that can be utilised across multiple jurisdictions. Furthermore, BEPS Action Item 14 will require tax administrations to implement more effective and efficient Mutual Agreement Procedures processes (OECD, 2015b). Also, existing international Forums such as JITSIC can be leveraged to address significant risk issues at an earlier stage, thereby enhancing tax certainty for compliant taxpayers.

While collaboration amongst tax administration is an important condition to achieve tax certainty in this global context, effective communication and transparency between tax administrations and taxpayers can lead to improved outcomes and reduced costs for both the taxpayer and the tax administration. The knowledge gained can in turn be applied to tailor products and interventions and to design processes and solutions that improve the overall effectiveness of the tax system.

Future direction

The global context in which tax administrations operate continues to change at an unprecedented pace. New technologies, increasing global collaboration and the tightening of tax rules provide tax administrations with new opportunities and tools to improve compliance outcomes for the large business taxpayer segment. These developments together with advances in the sophistication of risk-assessment will continue to build the individual and collective capacity of tax administrations to effectively deal with existing and emerging tax risks in a timely manner.

As countries move to implement BEPS, those businesses that continue to engage in aggressive tax avoidance arrangements will experience a more concerted effort both on a domestic and international level to combat these arrangements, and to make non-compliance more difficult.

At the same time, effective implementation of BEPS measures by tax administrations demands reconsideration of relationships with largely compliant taxpayers and in particular those enterprises operating in multiple jurisdictions. While tax administrations acquire increased confidence about risk assessment, taxpayers are looking for assurance that their compliance efforts are being recognised with reduced burden and greater certainty. Transparent engagement can go a long way toward encouraging compliant behaviour, identifying opportunities to reduce taxpayer risk and limit the potential for tax controversy. The higher this level of engagement can be, both on the part of the taxpayer and on the part of the tax administration, the greater its potential impact will be on compliance behaviour and the promotion of trust.

The implementation of collaborative approaches, which can take many forms, will therefore be an important priority in an environment where taxpayers and tax administrations alike seek to have cost-effective confidence and certainty. It will be beneficial if all stakeholders can move to a place where avoiding tax disputes and thereby creating certainty, will be recognised and valued over resolving problems after they occur.

Notes

1. For further information on the BEPS package please see www.oecd.org/tax/beps/.
2. For further information on JITSIC please see www.oecd.org/tax/forum-on-tax-administration/jitsic/.

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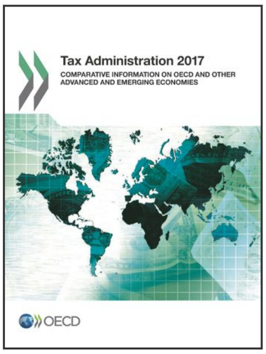

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