

# *The role of tax examiners and tax auditors*

## **Raising awareness**

Tax examiners and auditors around the world are highly trained and skilled specialists, who in the course of their normal activities routinely examine the financial affairs, transactions and records of millions of individuals, companies and other taxpayers. However, they may be unaware of what the typical indicators of possible bribery or corruption are, as well as their own role in referring their suspicions to the appropriate law enforcement authority or public prosecutor where they have identified possible bribery or corruption. Furthermore, tax examiners and auditors should be reminded that bribes and other payments linked to corruption are not tax deductible and the proceeds of corruption are often taxable income or gains under domestic law. While the aim of this Handbook is to raise awareness among tax examiners and auditors of issues surrounding bribery and corruption, it is not meant to replace domestic laws, policies and procedures. Tax examiners and auditors must, at all times, carry out their duties in accordance with the laws, policies and procedures which apply in their country. Therefore, in ensuring that their country's domestic tax law is properly applied, tax examiners and auditors should be aware of their role in detecting bribery and corruption and thus alert to indicators of possible bribery or corruption.

In order to conceal evidence of bribery and corruption, taxpayers will often use the same techniques that they also use to conceal income when evading taxes or laundering the proceeds of crime. As in the case of recognising indicators of possible tax evasion or money laundering, tax examiners and auditors should therefore also be alert to indicators of possible bribery or corruption.

Throughout this Handbook, references are made to the fact that tax examiners and auditors should be aware of indicators of possible bribery or corruption. However, any actions that a tax examiner or auditor takes in the course of their enquiries must always be for the purpose of determining a taxpayer's civil tax liability. In the course of these enquiries a tax examiner or auditor should pay attention to indicators that may lead them to suspect bribery or corruption may have taken place, but it is not their role to determine whether an offence has been committed. Conducting investigations into possible criminal activity is the responsibility of the appropriate law enforcement authority or public prosecutor, and not the tax examiner or auditor.

## Detecting bribery and corruption

Corruption transactions, including the payment of bribes, may be “on the books” (in other words, they are found in an individual’s or business’s financial records and accounts) or “off the books”. Tax examiners and auditors are most likely to detect indicators of possible corruption that are “on the books”, as they review the taxpayer’s financial records. Generally, this should not create additional work for the tax examiner or auditor, as a review of financial books and records will be undertaken as part of their normal activities to verify the sources of taxpayer income and identify untaxed income or gains and non-deductible expenses. In order to identify indicators of possible bribery or corruption, tax examiners and auditors should use the same analytical and audit skills and training, together with their judgement, that lead them to detect possible tax evasion. However, it is vital that tax examiners and auditors are aware of what the possible indicators of bribery and corruption look like, in order that they will recognise them.

While indicators of possible bribery or corruption are discussed later in this Handbook, it is important to note that these fall into two broad groups, as follows.

- “Affirmative indications” indicate that acts *may* have been committed for the purposes of deception, concealment, or to disguise the facts. Affirmative indications are not in themselves sufficient to establish that bribery or corruption has taken place. Examples of affirmative indications include management or employees with a lifestyle which is not supported by known income; a business undertaking transactions with unusually high or low gross profit margins; and an unusually close relationship between a taxpayer and external consultants.
- “Affirmative acts” establish that a particular action, or series of actions, was deliberately committed for the purposes of deception, concealment, or to disguise the facts. Affirmative acts must be present in order to establish that bribery or corruption has taken place. Examples of affirmative acts include the omission of items from financial records where other similar items are included; the concealment of bank accounts; the failure to deposit money receipts into business accounts; and concealing the source or destination of payments.

In order to support tax examiners and auditors in identifying possible corruption, many tax administrations are adopting a risk based approach, based on three pillars: (i) intelligence, (ii) awareness and (iii) training. It is intended that this Handbook can be used to support each of these three pillars. By focusing on the areas of highest risk and discussing general and specific indicators of possible bribery or corruption, this Handbook can supplement other sources of intelligence in assisting tax examiners and auditors to plan their work to ensure resource is allocated where risk is greatest. As previously noted, the purpose of this Handbook is to raise awareness among tax examiners and auditors of the indicators of possible bribery or corruption. Furthermore, this Handbook stresses the importance of detecting and disallowing bribes for tax purposes and taxing the proceeds of corruption, as well as the importance of making referrals to the appropriate law enforcement authority or public prosecutor when evidence of possible bribery or corruption is identified. Therefore, this Handbook is structured so that it can be used both as a training tool and as a reference guide for tax examiners and auditors.

## Examination plan and compliance checks

During the planning phase, when conducting a review of tax returns, tax examiners and auditors, and their supervisors, should be alert to situations that lend themselves to the creation of illegal or improper payments, such as bribes. Valuable sources of information during this phase (and throughout an examination or audit) include internal audit reports, media reports, the internet, and (anonymous) tip-offs. Databases containing information on fair market prices can also be useful when comparing a taxpayer's position with business norms. When deemed appropriate and necessary, an examination plan should include consideration of the following compliance checks:

- an examination of internal audit reports and related working papers to determine if any reference is made to the creation of any secret or hidden corporate fund;
- a review of the taxpayer's copies of reports filed with other governmental regulatory agencies;
- consideration of the use of foreign entities and operations, the terms of contractual or pricing arrangements, details of fund transfers, and use of tax haven locations; and
- a review of the internet and other open sources.

## Information available from other government agencies

In planning and conducting their work, tax examiners and auditors should consider what information, if any, could be requested from other government agencies. Details of mechanisms for sharing information and other co-operation between domestic government agencies, together with descriptions of successful practices, are contained in the report *Effective Inter-Agency Co-operation in Fighting Tax Crimes and Other Financial Crimes* ("the Rome Report"), launched by the OECD in 2012.

## Information available from other countries

In planning and conducting their work, tax examiners and auditors should take steps to ensure they are aware of any information that may already have been received by their tax administration from abroad. Where a tax examiner or auditor requires further information for use in their enquiries, and they have exhausted options for obtaining this information in their own country, they should consider whether this information could be obtained from another country.

Various legal mechanisms provide for exchange of information between countries for tax purposes. These include bilateral instruments, such as Double Tax Conventions which contain an exchange of information article based on Article 26 of the OECD Model Tax Convention and Tax Information Exchange Agreements, and multilateral instruments, such as the Multilateral Convention on Mutual Administrative Assistance in Tax Matters. These instruments may also provide for other forms of international co-operation, such as the use of simultaneous tax examinations by tax administrations in more than one country. The terms and use of a wide range of instruments for international co-operation are described

in the publication *International Co-operation against Tax Crimes and Other Financial Crimes: A Catalogue of the Main Instruments*, published by the OECD in 2012.

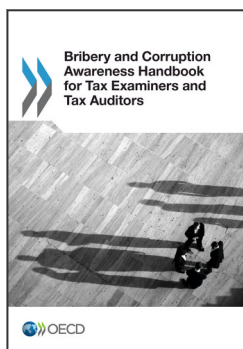
Exchange of information between tax administrations in different countries is handled by officials known as “competent authorities”, which are nominated by the countries’ respective governments. Direct contact between tax officials in different jurisdictions is not generally allowed. Where a tax examiner or auditor receives information from another country which indicates that a non-tax criminal offence may have taken place, they should seek advice from specialists within their tax administration as sharing the information with law enforcement authorities may be prohibited without the consent of the country which provided the information.

Where a tax examiner or auditor obtains information that is foreseeably relevant to the administration or enforcement of another country’s tax laws, they should consider whether they are able to exchange this information with that country’s tax administration through bilateral or multilateral conventions. This will include, for example, where the tax examiner or auditor suspects that bribes have been paid by a taxpayer in another country, which should be disallowed for tax purposes in that country. Again, any contact with the tax administration in another country should be conducted through each country’s competent authorities.

## Steps following the discovery of indicators of possible bribery or corruption

Where a tax examiner or auditor identifies one or more of the indicators referred to in this Handbook they should, subject to their domestic laws, where it is necessary and does not compromise a possible criminal case, conduct further enquiries to determine whether these are sufficient to suspect that bribery or corruption may be present. Where this is the case, they must take steps to ensure compliance with domestic rules to deny deductions for bribes and other payments connected with corrupt practices, and to tax the proceeds of bribery and corruption. The tax auditor is reminded that although he or she may form suspicions of possible bribery or corruption, the purpose of their actions must always be the determination of a civil tax liability, and not the determination of criminality. However, where during the course of an audit, and based on the findings of that audit, the tax auditor suspects that bribery or corruption may be present, he or she is encouraged to make a referral to the appropriate law enforcement authority or public prosecutor.

Where required by domestic law, the tax administration should also refer these suspicions to the appropriate law enforcement authority or public prosecutor. This referral must be in accordance with their country’s rules and procedures, which may include a standard format. An outline of the types of information that should be included in a referral is included in Annex B. Following a referral of suspected criminal activity, a tax examination or tax audit may generally continue, but all questions and enquiries concerning the suspected bribery or corruption must cease. This is both to protect the rights of possible suspects and to avoid jeopardising any criminal investigation. Nevertheless, a decision on the deductibility of payments may be made at the same time as making a referral to the appropriate law enforcement authority or public prosecutor.



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