Chapter 11

Using digital delivery to enhance the integrity of tax systems

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Developments in digital technology and in the analytical tools available to tax administrations will facilitate fundamental changes in the way that tax is assessed, verified and collected. This has the potential to increase compliance while reducing burdens significantly, including direct costs, and freeing up resources for more productive activities. Tax administrations are at different stages of digital maturity and will profit from exchange of best practices and practical experience, in particular in the light of the pace of technological change, the associated change management issues and the proliferation of legacy systems.

This chapter looks at the building blocks of digital delivery, in particular robust identification of taxpayers and integration of natural systems, and suggests further work on measurement of outcomes.

Digital delivery and the evolution of compliance

Current tax administration is largely a mix of rules-based activities based around actions or processes that are normally are undertaken after the fact, and still in most countries rely heavily on the taxpayer to provide information normally in the form of filing. It is characterised in general by a high degree of complexity in areas which continue to require considerable interaction between taxpayers and tax administrations, often in-person or paper based. This can be prone to errors and misreporting (both accidental and deliberate). The size of the workload and the impact is large; with OECD Forum on Tax Administration (FTA) members reporting that around 14% of their staff is dealing with more than 450 million taxpayer inquiries annually (see Chapter 6 on operational performance).

Time and cost spent by taxpayers on tax administration will, in general, divert resources away from alternative productive activity, thereby representing an opportunity, or welfare cost. Of itself, reductions in the burden involved in complying with obligations to report and to pay tax also have implications for the degree of tax compliance. This can be both directly through increased accuracy and certainty and indirectly by helping to shape attitudes to compliance.

The shared goal of tax administrations, within legal and administrative constraints, is to maximise compliance with the least opportunity/welfare cost, and with cost effective administration. Over time, this means designing the tax system to make it more understandable and easier for taxpayers to comply, while minimising the opportunities for those seeking to stretch the rules or commit fraud.

Advances in technology and much greater access to data, as well as the ability to use that data more effectively, have the potential to fundamentally alter this equation, reducing the burdens arising from tax administration for compliant taxpayers while increasing compliance overall. Some of the underlying challenges and opportunities have been set out in a number of OECD reports, including *Right from the Start* (OECD, 2012); *Tax Compliance by Design* (OECD, 2014) and *Technologies for Better Tax Administration* (OECD, 2016).

As digital delivery is used more, traditional compliance approaches must also evolve. If a tax administration has designed and delivered its digital services effectively, then taxpayers should experience greater tax certainty and have improved trust and confidence in the system, which may improve overall levels of compliance. This may also present new opportunities for tax authorities to shift from post-event audits to "upstream compliance" and early intervention activities.

There are also significant change management aspects associated with a shift to greater digital delivery, to embed new technology and skills. In particular there will be a capability shift from post-event auditing expertise, to systems design and earlier, upfront assistance. Building, maturing and maintaining skills in digital literacy, support and client service will become increasingly important.

Stronger identity security

The starting point for the effective use of digital technologies is a comprehensive and robust system of registration and identification. At its core, the integrity of a tax system as well as the ability to reduce burdens (for example by supporting self-service, voluntary compliance, withholding and third party reporting) relies on knowing both who the taxpayer is and, where third parties are involved, what their relationship is to the taxpayer. This is also critical to reducing non-compliance whether through error, fraud or by activities taking place in the non-observed economy.

Digital technology is increasingly providing new and secure ways for taxpayers directly, or through third parties (including other parts of government) to establish and prove their identities at lower cost, more quickly and with greater certainty. Recent developments include:

- Australia's ***Document Verification Service*** (**DVS**). This is a national secure system that checks and matches government issued credentials (for example, drivers' licences) in real-time. It is available 24-hours a day, and provides confirmation of taxpayer credentials without requiring a face-to-face or paper-based interaction. The Australian Taxation Office (ATO) also utilises the DVS for requests to update date of birth details made on-line and over the phone and in procedures for compromised identities (Office of the Australian Information Commissioner, 2014). It provides a fast and secure way to verify the identity of the taxpayer, thereby protecting both the government and the wider community from identity crime (Document Verification Service, 2016).

- ***Voiceprint authentication*** is used by a number of tax administrations (OECD, 2016). A voiceprint is inherently more secure than other credentials, as it is unique to each individual. Digital technology matches features of each voiceprint differently to the human ear, and can detect with high accuracy if the voiceprint matches the taxpayer (Australian Department of Human Services, 2016). Technology is also used to convert each voiceprint to a "hashed" series of numbers and characters (a numerical algorithm which cannot be reversed) meaning a stolen voiceprint is useless.

- Many countries provide taxpayers with ***unique digital identities*** for accessing government, and in some cases private sector services. In Belgium since 2009, citizens over the age of 12 have been issued an eID, which as well as providing online security for day-to-day activities like online shopping, library loans or as a train ticket allows the secure lodging of tax returns. In Denmark 4.5 million citizens have a NemID, a common login to securely lodge tax returns and access other government services, as well as services provided by some private companies, including Danish banks. In Singapore all citizens over the age of 15 can apply for a SingPass ID to use government online services, including tax services.

As well as enhancing the delivery of various interactions between the tax administration and taxpayer, certainty of identity is also necessary to establish a taxpayer's overall tax position, which is critical to improve overall compliance and reduce the associated burden.

A taxpayer's overall tax position often includes multiple income sources, a range of offsets or benefits, multiple expenses, and potentially multiple relationships with other entities (for example, in the case of a business there will be relationships with suppliers and purchasers). The ability to map tax-related data to the right taxpayer, and to match and understand a complex set of information is impossible without certainty of identity and relies on having a mature digital capability.

By way of example, in Canada, the Canada Revenue Agency (CRA) can trace and match data to link corporate entities to major shareholders, their value added tax, payroll and importer accounts as well as to foreign affiliates and associated transactions. Company proprietors are also linked to their spouses and family, and income levels benchmarked against appropriate comparators. Using digital technology, a sophisticated data matching system like this can map large, disparate data sets to the right identity and allow wider analysis to be conducted of the data as a whole.

Integration with natural systems

Digital delivery also provides a mechanism by which tax authorities can integrate tax services with the "natural systems" that taxpayers use in other aspects of their day-to-day activities. Natural systems in this context encompasses the range of tools and recording systems used by taxpayers, such as business and accounting software, banking services and payment systems, point-of-sale systems, use of intermediaries, third party applications etc. Integration of such information, including by supporting the development of third party apps and software, has the potential to significantly reduce reporting burdens and improve the way in which data is collected. Examples of such integration include:

- The introduction of a **Single Touch Payroll** service by the ATO through business payroll software. This will require large employers to report to the ATO each employee's salary, wages and tax withholding and superannuation at each payroll event (currently only reported annually). Employees will also have access to the reported information that relates to them, providing them with visibility throughout the year of their income, tax and superannuation amounts. By using digital technology to embed this tax service into the natural system of the employer (in this case, the payroll components of their business management software) the data can be automatically provided with little or no effort. Single Touch Payroll will be available for all employers from July 2017 and will be mandatory for large employers from July 2018.

- New Zealand Inland Revenue also delivers **integrated digital services** via accounting and financial systems to encourage seamless service delivery and improved compliance. Some online accounting products are integrated with online banking, reducing double-handling of bills and reconciliation of invoices, with the option to file Goods and Services Tax (GST) returns directly to the Inland Revenue Department.

- The Federal Tax Service of Russia has also introduced an **e-Registration requirement** for cash registers which will help to verify tax accounting procedures at the point of sale. This will enable the tax administrations to automatically validate data, track and match certain information related to sales, and provide better data for audits in close to real time.

Brazil is among a number of countries that have **mandated e-invoicing**: electronically sending, receiving and storing invoices between suppliers and buyers (either business to business or business to government). This has helped establish a national digital bookkeeping system, "SPED", which enables direct reporting of annual income taxes and other tax information. The Brazilian tax administration can now review, assess and act on some information almost instantly, including issuing penalties in near real-time. As a result, the number of audits, their assessed value and total tax collected has significantly increased. There is also greater overall reported participation in the tax system.

Increasingly, tax administrations are also applying digital end-to-end solutions to design integrated services that extend beyond the tax system itself. For instance, in Australia the ATO is also responsible for administering the country's superannuation system and has used digital technology to deliver its "Super Stream" service. This service introduced standard electronic messaging for the exchange of data and payments from employers to superannuation funds, and leverages the employees' Tax File Numbers to ensure payments are made correctly. For the December 2016 quarter approximately 32 million transactions were made through the Super Stream service, to the value of AUD 70 billion. This service has strengthened the integrity of the system, providing greater assurance for 11 million

employees entitled to superannuation contribution payments. In November 2016, Super Stream won the "Gold Award" in the Institute of Public Administration Australia (IPAA) Prime Minister's Awards for Excellence in Public Sector Management.

Emerging technology

As highlighted by the OECD in its report *Technologies for Better Tax Administration: A Practical Guide for Revenue Bodies* (OECD, 2016), the challenge facing all organisations including tax authorities is keeping pace with ever evolving technology and, as necessary, rethinking how services and delivery can be changed to best utilise that technology. This needs to be done, though, with a clear focus on the end objectives of reducing burdens, including on the tax administration budget, while increasing compliance.

For example some tax administrations are currently exploring the opportunities presented by the use of blockchain technology. This new technology is, in essence, a distributed ledger that records when a transaction occurred, the details of that transaction, including transfers of assets and ownership, and provides assurance that the required business rules have been met without the need for third party verification. Updates to the blockchain are subject to consensus from all participants in the network, making it virtually impossible for any one individual, or group of individuals, to falsely change or create records. Each transaction is protected by a cryptographic key, which includes the key of the prior transaction, creating an immutable historic "chain" of transactions.

As such, blockchain may offer new ways for tax authorities to combat fraud, trace and match data and automate reporting. The Estonian government has already started using this in tax and business registration systems. The Danish tax administration has started a proof of concept to better track and secures vehicle registrations using a blockchain solution, to confirm that all related tax payments are paid as ownership or other changes occur. In the United Kingdom, the government is considering its applications to better track tax revenue, while the Australian government is conducting a comprehensive review to examine its potential for a range of government services.

As with other aspects of emerging digital developments, this may be an area where sharing of information and experience between tax administrations will be of high value.

Measuring the impact of digital delivery

Overall, developments in digital delivery look set to allow tax authorities to reshape not just the taxpayer experience, but the broader compliance landscape. Previously dim features on that landscape can be brought to light and those already visible come into sharper focus. As compliance improves and participation in the system grows, revenue will not only be protected, but potentially be increased.

That raises the question, though, of how tax authorities can best measure digital delivery success to inform both strategy and resource decisions. The most common metric is currently digital uptake. However, considering the direct relationship between digital delivery and compliance, further work on compliance-related metrics would be helpful. For example, a decrease in outstanding lodgements, a decline in post-event audits as more information arrives digitally, or an increase in accuracy of case-selections may be attributed to effective digital service delivery. Metrics could also be explored for the timely transfer of third party data, the effectiveness of automated matching and the quality of data collection.

And finally

As tax administrations around the world embrace digital technology to deliver better services to taxpayers, overall tax compliance may also be enhanced. The theory is simple: by meeting taxpayer expectations and simplifying the service experience, then taxpayers should find it easier to comply. Therefore, digital service delivery may drive an increase in voluntary compliance, which would then increase revenue and participation, and improve overall trust and confidence in the system.

References

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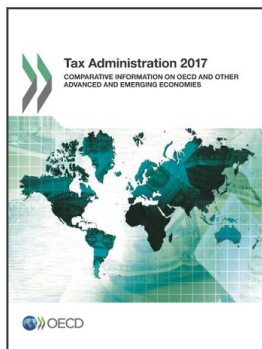
From:
Tax Administration 2017
Comparative Information on OECD and Other Advanced and Emerging Economies

Access the complete publication at:
https://doi.org/10.1787/tax_admin-2017-en