



Policy Statement

Improving tax efficiency: the responsibilities of tax administrations and taxpayers

Prepared by the Commission on Taxation

Governments must assess and collect sufficient revenue to meet their goals and obligations. However, it is important that the costs of compliance and administration for taxpayers and tax administrations be reduced wherever possible.

This ICC Policy Statement makes recommendations intended to improve the efficiency in administering and complying with a particular tax system. ICC's comments are based on the following economic proposition:

“Given a particular targeted level of tax revenue, a tax system that requires fewer resources to administer (monitor, legislate, audit and collect) **and** to comply with (understand, comply, report and transfer tax payments) is better than a tax system that costs more.”

This economic proposition is referred to as “efficiency.” ICC offers the following suggestions or best practices which can reduce the overall cost of tax compliance and administration for tax administrations and taxpayers, thereby promoting an efficient tax system. Tax administrations should view themselves similar to business that provide services to customers and should constantly strive to improve the manner in which they provide such services.

Simplification

Tax administrations should administer the substantive tax regime in a manner that is no more complicated than necessary to assess and collect tax.

All else being equal, simplification should result in lower costs for tax administrations and taxpayers because:

1. fewer resources are required to apply simple rules than to apply complex ones;
2. the time to conduct an audit may be shortened and thus reduce the costs typically associated with protracted audits;
3. fewer tax controversies may be expected to arise; and
4. simpler rules provide more certainty over tax reporting which thus improves financial reporting.

Tax administrations should accept that they cannot capture absolutely all of the taxable economic activity. The increased costs associated with a complex administrative tax regime may outweigh the additional tax revenue collected, thereby suggesting the need for balance.

Shorter audits

A reduction in the time for tax administrations to begin and conduct a compliance audit would lead to considerable cost savings.

Tax administrations should strive to begin and conclude a tax audit as soon as possible after a tax return is filed. A taxpayer can more quickly respond to a tax audit when the needed information is readily available to the taxpayer and its tax department. A taxpayer is more likely to recall and locate relevant information shortly after the filing of a tax return than many years after the filing. In addition to turnover within the taxpayer's tax department, which inherently reduces responsiveness, the passage of time makes it more difficult to locate documentation responsive to a particular question even if such documentation is available.

Delay in the tax audit also compounds the potential impact of an audit adjustment as a taxpayer may have adopted a similar position to that challenged by the tax administration on subsequent returns. A proposed adjustment by a tax administration is less likely to be resisted if future tax filings are not as heavily impacted, which will be the case if tax returns are reviewed promptly and tax audits concluded relatively swiftly.

Transparency

The increased transparency of tax rules should be a continuing goal of every tax administration. Taxpayers should know the rules of the game under which their economic activities will be taxed.

A useful definition of transparency is provided by the International Monetary Fund:

"Tax laws, regulations, and other documents relating to administrative interpretation of tax law should be accessible to the general public. Explanatory materials (e.g., instructions and pamphlets), usually prepared by the tax agency, should also be kept up-to-date. New budget revenue measures should be given sufficient publicity so that taxpayers understand how they might be affected. To this end, the material the tax agency uses in applying the tax laws (e.g., manuals and legal opinions) should be publicly available and there should be mechanisms in place whereby taxpayers can have their queries answered (e.g., by setting up a dedicated office in the tax agency to do so)."¹

Training of tax administrators

Both tax administration examiners and corporate tax professionals need to be properly trained to perform their duties. The training should permit both parties to operate on approximately the same level of tax knowledge. A tax system can only minimize costs if both "sides" are equally versed in the underlying rules.

¹ IMF, Manual on Fiscal Transparency, I. Clarity of Roles and Responsibilities, The Framework for Fiscal Management, Par. 46 available at <http://www.imf.org/external/np/fad/trans/manual/sec01b.htm>.

Tax authorities should be adequately resourced to attract and retain appropriate personnel with the skills required to conduct their business.

Prospectivity of rule changes

A tax administration that quickly audits compliance will be able to respond to positions it believes are inappropriate. Such response may include a modification in administrative positions and practices. However, these changes should be prospective only. ICC believes that this recommendation may also reduce the long-term cost of tax administration because each party will have less time and costs invested in any particular tax position, given the possibility of prospective changes.

Use of business records

The assessment of tax liability depends upon the review of the taxpayer's books and records. Three aspects of record-keeping are particularly relevant to the reduction in the costs of compliance and administration.

First, taxpayers should ensure that books and records appropriate to their economic activities are created and maintained. The cost of administration increases when taxpayer records are inadequate or unavailable.

Second, the books and records reasonably maintained by a taxpayer for the purposes of its enterprise should normally be sufficient for the tax administration. It should not normally be necessary for a taxpayer to create or reformat its books and records to comply with the requirements of tax compliance.

Third, once reasonable business records have been provided, the burden of persuasion should be on the tax administration to demonstrate that a taxpayer has not properly complied with the transparent tax regime.

Confidentiality

Tax administrations must continue to strive to maintain the confidentiality of tax return information they receive. Strict adherence to this standard is in the best interests of tax administrations as it facilitates the willingness of taxpayers to provide the information tax administrations need to audit tax filings.

Maintenance of an impartial appeal process

Inevitably, reasonable disagreements may arise even under the most transparent tax systems. In such situations, an impartial adjudication process should exist that has as part of its function the publication of its decisions, taking into account privacy concerns of the affected taxpayer. Such a procedure will promote confidence in the system, ultimately increasing voluntary tax compliance. An adjudication system that rarely sustains the position of a taxpayer is unlikely to be viewed by taxpayers as being fair.

ICC Recommendations

ICC encourages tax administrations to adopt the suggestions in this paper to improve their tax systems including:

- Implementing rules that are no more complicated than necessary to assess and collect tax
- Reducing the time to begin and conduct a compliance audit
- Increasing the transparency of tax rules
- Increasing the resources of tax administrations in order to perform tax audits in a timely manner and improving the training of tax administration personnel
- Making only prospective changes to tax practices and policies
- Using business records created by enterprises
- Maintaining the confidentiality of taxpayer records
- Maintaining an impartial tax appeals process

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