Challenges to Tax Collection in the Early 21st Century – Emerging Patterns and Where To Look for Solutions

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Introduction

The world changes at an incredible speed. New business models and working methods emerge every year, people are connected twenty four/seven, and smartphones offer functionalities and processing capacity that make our old PCs look like dinosaurs.

Taxpayers and citizens are increasingly demanding. They expect the tax administration to demonstrate fairness, equity and transparency in all its activities. But they also want to be relieved of all unnecessary burden and to be serviced any time, using their favourite devices and communication channels. At the same time, concealing transactions and money remains easy, despite progress in the exchange of information with, and between, tax authorities.

In a context of severe budgetary constraints, and with a flow of information never reached so far, tax administrations are challenged to keep the pace, answer the taxpayers' new needs and expectations while keeping tax compliance under control, and tax fraud at bay.

We have heard yesterday about the inspiring initiatives taken by some tax administrations to reinvent themselves, in order to provide a better service to citizens and raise more money. This morning, I would like to address two main challenges that all tax administrations are facing worldwide, and discuss how they can be addressed to secure proper tax collection in the 21th century.

Challenge n° 1 : Re-thinking the compliance strategy.

All European tax administrations aim at achieving the right balance between service and control, in order to reach and maintain the highest possible level of voluntary compliance. This being said, although there are exceptions, we see a European trend towards more control, not only through tax audit but also by means of new obligations and devices for controlling the taxpayer's activity : electronic cash registers, on-line access to the taxpayers transactions, recapitulative statements, guarantees upon registration, and so on. In view of the EU VAT gap study published every year by the Commission, such measures may contribute to reducing the VAT gap, by limiting certain types of fraud such as missing trader Intra Community fraud, but it remains to be seen how they actually improve voluntary compliance, in the context of a more comprehensive compliance strategy.

In our experience and from what we heard yesterday, efficient compliance strategies have the following common features :

1) A **compliance measurement framework.** Tax compliance is often measured using global tax gap estimates, but many countries still lack a comprehensive dashboard measuring compliance with every tax obligation, for every segment or group of taxpayers.

2) Areas and segments of non-compliance are identified through a comprehensive and regular **risk analysis**. Once compliance risks are identified, the reasons for not complying are analysed, and non-compliance is treated through a wide range of actions, engaging all possible stakeholders and intermediaries (or service providers). Tax audit and systematic control are used only when more proactive actions proved ineffective.

3) **Taxpayers** and segments of taxpayers are treated according to their compliance history, and prospect. Compliant taxpayers are offered enhanced service and limited control activities. Enforcement is reserved to proven and persisting non-compliance, and prosecution only apply to the most serious cases of tax fraud or evasion.

4) Priority is given to fulfilling **future obligations**, as opposed to catching up with the past. Why can't tax administrations, within the boundaries of their rights and obligations, voluntarily give

up part of their power to control and enforce in exchange of future compliance? It is presumably the hardest step to take, but also the most critical part of modern compliance strategies.

5) A **sound penalty system** sanctions non-compliance, and is applied fairly. Tax laws provide for a full range of administrative penalties, including fines, interests and surcharges to deter non-compliance for all tax obligations. Literature on the impact of the penalty system on tax compliance is scarce, and tends to focus on the law rather than on the administration of penalties. Experience however suggests that, more than the law, it is the use which is made of the penalty system which promotes or prevents tax compliance. Flexibility, selectivity and progressivity seem to be the key words, and systematic and cumulative application of all the penalties planned by the law often translates into uncollectible debts and countless objections.

6) Procedures and processes are regularly **reviewed** to ensure that they serve compliance, and that they meet the needs of the taxpayers and tax administration. Taxpayers' representatives and intermediaries are invited to participate into the review or the reengineering of the processes, especially for new business models and IT solutions.

Governments, Parliaments and citizens still need to be convinced that such compliance strategies actually pay off, and

that tax administrations need to be given a sufficient level of initiative and flexibility to actually implement them. We have seen yesterday that it worked in Australia.

We are convinced that this type of events, bringing together tax administrations, internal organisations and business representatives, can help in conveying a common message.

Challenge n° 2 : Information technology : a blessing or a curse?

Of all changes faced by tax administrations, Information Technology is probably the most important. Information technology is at the same time a blessing, and a curse.

A blessing because it helps improving taxpayer services and reduce costs for taxpayers and the administration through automated case management, web-based solutions, and mass processing.

A blessing because it helps in detecting and evidencing mistakes, fraud and evasion.

A blessing because it allows tax administration to treat and analyse in real time large datasets coming from multiple sources, thus making risk analysis more and more effective.

But it can easily become a curse.

A curse if risk analysis and data mining techniques are only used for tax audit selection, or for issuing tax assessments or penalties without proper filtering.

A curse if risk analysis, data mining and massive cross-checking drown the tax administration under flows of information that cannot be processed, analysed and used adequately :

In our view, risk analysis should primarily be used for detecting areas of non- compliance and identifying the cause, rather than for sheer tax audit selection.

Data mining is still mining : it is a heavy industry, requiring massive IT capacity to access, process and analyse huge datasets, for uncertain results.

Massive cross-checking systems and real time control mechanisms are no silver bullet, and may prove counter-productive at the end of the day. They can trigger shifts in non-compliance, such as non-recording transactions instead of not reporting them, and in extreme cases they may reject entire segments of taxpayers into the shadow economy. They tend to place a glass ceiling over the head of tax administrations, when the only missing transactions finally taxed are the ones detected by IT, leaving untouched the underwater part of the iceberg. And finally they can create huge backlogs of objections and uncollectible debts, if those techniques are used to issue bulk assessments or penalties without prior investigations.

Commission's initiatives for addressing these two main challenges

The Commission is taking its part in supporting EU tax administrations in addressing these challenges.

First, we make proposals to modernise and simplify the EU VAT system, with for example the Mini One Stop Shop for telecommunication, broadcasting and electronic services. We provide tax administrations with the tools to cooperate and exchange information between them including via pan-European IT networks.

We offer a discussion platform for business and tax authorities in the context of the EU VAT Forum.

The Commission also makes recommendations to the EU Member States on their fiscal and structural reforms, including in the area of tax administration and compliance, in the context of what we call the European Semester.

We publish an EU VAT gap study every year, which can assist Member States in measuring non-compliance. And two projects are running to explore possible methods and tools for estimating the VAT fraud, and the direct taxes gap.

The Commission is co-funding and promoting the TADAT assessment tool for tax administrations. We finance and

organise capacity-building activities, via exchange of practices and technical assistance.

From all we have heard at this conference, time has come for the EU Member States to come together and develop a common agenda for their tax administrations, in order to accompany the evolution of the EU tax system. And address the challenges.

Now I leave the floor to you to discover your take on society's needs and expectations and how to address them.