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“TAX REGISTRY ENHANCEMENT: DEBUGGING, UPDATING AND USE”

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Costa Rica**

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Taxpayers' Registry General Income Tax Office

SUMMARY: Summary. - 1. Introduction. - 2. Actions targeted at a continued updating and improvement of the Single Taxpayers' Registry in the current Comprehensive Information System of the Tax Administration (SIAT, in Spanish) - 3. Actions intended for the design, development, updating and continued enhancement of the RUT in Digital Taxation- 4. Effective legal provisions affecting tax registries- 5. Conclusions.

Summary

This paper sets out specifically the updating and debugging actions taken by the Costa Rican Tax Administration in order to have a taxpayers' registry apt to generate more reliable and updated information.

The strategies used since 2003 are explained, which are intended to locate hidden taxpayers, as well as the IT applications developed, the information loaded on-line from other institutions and the changes in the procedures that have resulted in a better registry.

Also, the paper explains the transitional process undergone by the Costa Rican administration towards a new way of managing taxes; the actions taken to migrate from one IT system to another without affecting the continuity of a business and to achieve improved information quality and operating efficiency and effectiveness.

Finally, the legal provisions which rule matters relative to the registration of taxpayers and the impacts of such rules and their interpretation in practice are presented, stating the analysis thereof as a relevant opportunity for improvement.

Introduction

The registry of taxpayers, denominated in Costa Rica “Single Taxpayer’s Registry” (RUC, in Spanish) until 2009, or “Single Tax Registry” (RUT, in Spanish) as from 2010, constitutes one of the primary management instruments and the first control level in the Tax Administration. With good reason many definitions describe it as the backbone of any country’s tax management system. Regardless of the term used to refer to it, this registry or census of taxable persons, the RUC or RUT – ultimately synonyms- must be the primary focus of the tax authorities in order to assure its quality and continued improvement.

The General Income Tax Office has established the updating of its taxpayers’ registry and the quality of the data its strategic objective, aware of the fact that having reliable and accurate information has become an indispensable instrument for the proper performance of the diverse extensive and intensive control actions, as well as for a better performance of the collection function. This objective may be summarized in the following actions:

Standardize and improve the content and design of RUT forms in order to enhance the quality and quantity of the information required by the Tax Administration.

Improve the quality of tax registries through correction protocols, drawing on the technical diagnoses performed and the experience accumulated from the different debugging programs carried out within the frame of management model modernization projects of the Costa Rican Tax Administration.

Implement effective procedures for updating actions, to be incorporated into all control actions, and provide timely assistance to taxpayers.

Review and enhance data capture and processing proceedings, maximizing the use of electronic means to achieve entry of quality information, and detecting, where possible, original errors or inconsistencies in order to correct them on a timely basis.

Make the best use of the information in the hands of other public and private institutions and organizations to incorporate potential taxpayers and update records.

As far as the income tax is concerned, in Costa Rica, the registry of taxable persons is composed only by the businesspersons and professionals subject to the corporate tax, as well as by withholders. As of December 31 of 2009, a total of 460,000 taxpayers were registered.

This census integration may be explained in the nature of income taxation in Costa Rica, where “permits” are required for the yields of corporate or professional

activities, labor and movable assets. The taxes on the last two types of yields are liquidated through a releasable withholding. The tax related to corporate yields (the corporate tax under the law) must be liquidated by means of an annual self-liquidation return, and the taxable persons must fulfill a series of obligations, such as registering themselves and making quarterly advances.

At the level of the primary identification data, there is the advantage that each citizen has a single identification number for all legal purposes in Costa Rica, which allows a great consistency of consultations and information. The consultation by identification number guarantees that the information displayed is the real information of the consulted person or identification number. For example, every time the identification number of a taxpayer or natural person is entered, the system searches through the Civil Registry's database – the primary, truthful and accurate source on a national level - and extracts from it the name of the person corresponding to the identification card, thus guaranteeing the integrity of the information.

In addition to the identification data, the fiscal domicile of each taxpayer is included, as well as their business domicile; i.e., the place where taxpayer carries out their business activity which may obviously coincide with the fiscal domicile. The fiscal domicile defines the enrollment of taxpayer in a certain territorial administration, in conformity with the regulation. Both for changes associated with registrations – changes in the relevant census information (changes in domicile, legal representative, etc.) – and changes associated with deregistration, an official census statement must be used. The failure to perform this formal duty is categorized as an infraction and is subject to administrative penalties.

The registry contains information on the diverse tax obligations, including taxpayer's obligation to submit information statements and the frequency of such statements. The economic activity carried out by the taxpayer is also registered.

Today, the Costa Rican Tax Administration is undergoing a transitional process towards a new integral tax management model that stems from the need to achieve improved management, control and services, supported by the strategies of Digital governance. This new model, reflected in an ambitious large-scale project, entails profound modifications in the organization, regulations and procedures; and the new information system, called Digital Taxation, which has been operating since late 2007, stands as a big opportunity to consolidate a process of correction and updating of the taxpayers' registry, which has characterized the Administration's actions over the last years, while at the same time has fulfilled the strategic objective of migrating towards a single registry of taxpayers of higher quality and in line with the world's highest standards, to conclude no later than by 2011.

This paper comments on the past and ongoing actions intended to achieve such strategic objective, in addition to specifying the characteristics, the interpretation

and the practice of the legislation that has been evaluated and which is believed to need greater improvement in order to adapt to the objective.

Actions targeted at a continued updating and improvement of the RUC in the current Integral Information System of the Tax Administration (SIAT)

For several years different actions have been continuously and permanently been implemented, which have affected positively the information quality included in the RUC. Based on a series of diagnoses made between 2001 and 2003, all them consistent with the need to improve the registry, which was at that time outdated and had a great amount of incorrect information, intensive work has been developed, among which actions stand out the following:

- Ongoing debugging plans in sectors of greatest fiscal interest: large taxpayers, excise taxes, consumptions, special systems and taxes (duty-free zone, duty-free customs system (*perfeccionamiento activo*), casinos and gambling, simplified taxation) and certain selected groups of taxpayers.
- Engagement of all the staff at the General Income Tax Office in the update of the RUC. An Order provided the responsibility of all tax officers to obtain all relevant data and update the system when interacting with taxpayers.
- Officers in the Territorial Administrations devoted exclusively to updating the RUC as part of the operating plans in the areas of Tax Collection and Records.
- A series of strategies were implemented for taxpayer location, such as: exchange of information with other State institutions that provide first need services, which have updated and highly reliable information, such as power and telecommunications companies, water supply companies, social security organizations and insurance companies. The exchange of information was also used with the institutions in charge of the national registries of natural persons and bodies corporate.
- Drawing on the joint work with such institutions, an integrated consultation system was developed, called "Telephone consultation", which allows accessing all the information in such institutions on line. In supplement of the consultation system, the services of a private company engaged exclusively in providing data of natural persons and bodies corporate were hired.
- In the services field, a summarized catalogue of material and formal obligations was prepared, to deliver to the new taxpayers at the time of registration. Such catalogue sets out the obligation of taxpayers to modify their registry data upon any changes made, or upon deregistration or cessation of activities.
- The registration diligence requirements were simplified by way of the instructions "*Summary of requirements for addressing diligences at the Taxpayers' Registry*" and "*Voluntary registration, deregistration and modification procedures at the Taxpayers' Registry of the General Income Tax Office*", which contemplate overall case requirements and integrate any other registration diligence that was hitherto regulated individually.

- The registration form was originally a single-version multipurpose form that contained the three diligences, i.e.: registration, modification and deregistration. Upon conducting a survey that concluded that users had trouble filling them, the contents of the form were simplified and broken down by diligence, in addition to assigning a different color to each form and issuing the relevant brochures for each diligence.
- A summary of information relating to all diligences concerning the registration, requirements, special registrations, legal bases, etc., was prepared and posted on the web page.
- As regards systems, a full redesign of the Taxpayers' Registry's modules in the current information system of the Tax Administration was performed. The statistics module was adjusted for a new redesign, allowing for the tabulation and lists of taxpayers and statistics in accordance with the registration, modification and deregistration diligences.
- Additional modules were created, such as the supplementary RUC, the error correction module and the module that identifies all taxpayers appearing as not localized. This module is one of the primary inputs for Tax Administrations when performing data updates and debugging.
- The economic activity databases were updated to be entered into the United Nation's International Standard Industrial Classification of All Economic Activities, Version III. This change allows obtaining accurate statistics by economic and industrial sector. Additionally, tax obligations were tied to the performance of a specific economic activity. This has made it possible to allocate the tax obligations actually corresponding to a taxpayer upon registration, assuring correct statistical data for each tax.
- The taxpayer's registration, modification and deregistration system was developed and made available on the Internet through the TRIBUNET "*Pay your taxes over the Internet*" system, as well as the registration of electronic billers.
- The Taxpayer Identification System, "SIC" (in Spanish), was implemented. This is a practical application for inquiring and verifying the name or corporate name and the personal identity card number of natural persons and bodies corporate. It is available on the web page of the Income Tax Office, as well as in compact disk format. It is mainly intended to facilitate the presentation of the identity card and the name of third parties that are to be specified in information statements.
- Each module and tool that is implemented in the RUC has been accompanied by lectures or training workshops provided to the officers at the offices responsible for these proceedings.
- Quality control processes were implemented to oversee the quality of registration forms. This action had a positive effect, for a considerable percentage of errors were detected, which allowed taking the relevant corrective measures.
- The registration modules of the SIIAT are maintained on a permanent basis, on the assumption that they must operate effectively and coexist with the new system for a period of at least two years.

Actions intended for the design, development, updating and continued enhancement of the RUT in Digital Taxation.

From the stage of definition of the requirements and the scope of the new digital taxation management model in 2005, to the planning, budgeting and hiring processes, and concluding with the start-up of the project by late 2007, a balance strategy has been discussed extensively to maintain the effective operation of the current system (SIAT), as explained in the previous section, and assure that the new system (Digital Taxation) contemplates in its design and implementation all that is necessary to fulfill the objectives of high quality and effectiveness.

The implementation of the developments in the Digital Taxation Project is attributable to a “controlled pilot” strategy under which the new products will be tested in practice with large taxpayers and a few other taxpayers who contribute most to tax revenues and whose information has the greatest transcendence for tax control purposes, or are easier to control.

As far as the tax registry is concerned, since 2008 all large national and local taxpayers have operated in the new system, those who would file their returns on the Internet before the implementation of the new system, taxpayers of specific and excise taxes and taxpayers engaged in certain economic activities under special conditions who are, on account of that, easier to identify and control. These taxpayers can make use of the voluntary services of data modification and deregistration from the RUT, and the Administration has mechanisms to assist all updating process in the system.

The registration module is currently being developed for the rest of taxpayers. This has required the creation of a data migration strategy from the current to the new information system; even so, when this strategy was exhausted, taxpayers should undergo mass re-registration processes and start the process all over again.

From 2008 and during 2009, segmented loads of taxpayer information were made from the Integral Information System of the Tax Administration (SIAT) to the new Digital Taxation solution, migrating in the first place the data of large taxpayers, specific taxes and other taxes, as explained above. Following this first stage, conceived under the controlled pilot for preparation and refinement of the tools until its final implementation, is the migration strategy that must be developed in 2010 and 2011, which should conclude with the implementation of the Digital Taxation of most taxpayers who have not yet been migrated from the SIAT to the new system.

The process begins in 2010 with the announcement to the organization of the strategy intended to achieve a successful migration of the category “Other taxpayers” (mass migration) to the new digital solution.

What is pursued is that the Administration and the involved divisions at the General Income Tax Office should know the procedure to follow during the data migration

process. Once this is communicated, the process will be delimited as per each division and the task to be performed within the whole process.

Lastly, priority should be given to specific groups, in accordance with the completeness of their data and the performance of their obligations as a condition for migration.

The following main actions have been identified:

Determination of the balance of taxpayers: The final balance of taxpayers apt for migration must be determined by searching the databases. This will entail official automatic deregistration intended to clean the register of inactive taxpayers.

Execution of the official deregistration: The official deregistration will proceed in order to reduce effectively the register of taxpayers at the SIIAT. This official deregistration will proceed with taxpayers who as of 2008 have recorded no income tax payments for 3 years.

Determination of the new balance: A balance will be in place prior to the income tax return for 2009. Such balance includes some inactive taxpayers in two maximum periods; this will be considered a provisory balance until the tax return for that period is filed, whose deadline is due on March 15 of the year following such period. In this case, it was due last March 15 so it is from that date that the whole information may be processed, which could take some additional months.

Provisory deregistration: The IT Area will mark out in the SIIAT the taxpayers who are deregistered and will maintain them provisionally under such condition until the tax return filing of 2009 occurs or not, in order to render it final. If taxpayer fails to file 2009's tax return, an official automatic deregistration of such taxpayer is made in the SIIAT. Alternatively, taxpayers who file 2009's tax return will be removed from the provisional deregistration and will be incorporated into the migration population.

Migration population: The RUT Subdirectorate will determine (after the filing of 2009's income tax return) the active population to be migrated to Digital Taxation. Such population would be composed of as follows:

	SIIAT's active taxpayers
Minus	Taxpayers deregistered automatically
Minus	Inactive taxpayers (failed to file 2009's tax return)
Plus	Temporary inactive (filed 2009's tax return)

Inclusion of "Dummies": The Digital Taxation requires that at least some taxpayer's identification data should exist in order for the migration to take place, on account of such data being mandatory. The IT Division, pursuant to the guidelines set forth by the RUT Subdirectorate, will proceed to update or

complete the identification data of taxpayers that are incomplete. To this purpose, some filling or “dummy” data have been created which allow the migration. This does not mean that these data will remain as such, for the taxpayer will have the obligation to update them when first signing up in the Digital Taxation. The *Rule FURNRUT17- Validation of migrated master data* was created for this purpose.

Data loading in the Digital Taxation system: Once the data extracted from the SIIAT are refined, they are forwarded to the Digital Taxation Project section, where they will be loaded into the new digital solution. Given the uncertainty of its continuity or activity, this database will be treated as per the rules on compliance with the income tax return, as follows:

If taxpayer files tax returns with data, they are maintained in the Digital Taxation database and are included in the category of active taxpayers.

If taxpayer files tax returns with zero data, they are placed under the category of temporary inactive taxpayers.

If taxpayer fails to file the tax return, they are placed under the category of temporary inactive taxpayers.

Temporary inactive taxpayers: Under the business rules for the operation of the Digital Taxation system a database was created for inclusion – for identification purposes- of taxpayers filing tax returns with zero data (inactivity indicator) or who fail to submit tax returns for a certain time. They will remain in this database for three years until their inactivity is (or not) rendered final; upon the lapse of this period, the official automatic deregistration will proceed.

It should be stated that this process does not include taxpayers who have been reported in information statements; neither does it include taxpayers who have shown signs of non-performance as per the information available in the tax intelligence and risk management processes, or who have unfinished diligences or requirements.

If during this period the taxpayer files a tax return, they will be removed from this database and the cycle will begin again, and they will be reincorporated into the Digital Taxation database.

Active taxpayers: Taxpayers whose filings are constant and who show signs of activity will be maintained in the active taxpayer database.

Notwithstanding the possible case that the migration strategy is exhausted, as briefly described before, the Costa Rican Tax Administration does not rule out the possibility of resorting to a re-registration process in order to assure that the RUT is consistent, supported by correct information and updated on a permanent basis.

Effective legal provisions affecting tax records

The Tax procedures act or general taxation act of Costa Rica, called Code of Tax Rules and Procedures, contains five sections that govern the fiscal domicile and one that sets forth the non-performance of the taxpayer's or taxable person's obligation to report identification information to the Tax Administration. As these sections are short, we will transcribe them below:

SECTION 26.- Natural persons

For all taxation purposes, the country domicile of natural persons is assumed to be:

- a) The place of their usual residence, which is presumed to be the place where the natural person remains for more than six months during the fiscal year;
- b) The place where the natural person carries out their civil or business activities or has taxable property, in the case the residence is not known or is difficult to locate.
- c) The place where the taxable event occurs, in the absence of the above; and
- d) That chosen by the Tax Administration in the event there is more than one domicile of those contemplated in this section.

SECTION 27.- Bodies corporate

For all taxation purposes, the country domicile of bodies corporate is assumed to be:

- a) The place where their management or central administration is located;
- b) The place of their headquarters in Costa Rica, in the case such management or central administration is not known;
- c) The place where the taxable event occurs, in the absence of the above; and
- d) That chosen by the Tax Administration in the event there is more than one domicile of those contemplated in this section.

The provisions of this section are also applicable to de facto corporations, trusts or estates and analogous entities other than natural persons.

SECTION 28.- Persons domiciled abroad

The following rules apply to persons domiciled abroad:

- a) If they have a permanent domicile in the country, the provisions of sections 26 and 27 shall apply;

- b) In the rest of the cases, the domicile is that of their legal representative; and
- c) In the absence of a legal representative, the domicile shall be the place where the taxable event occurs.

SECTION 29.- Special domicile.

Taxpayers and tax-liable persons may establish a special domicile for taxation purposes with the express authorization of the Tax Administration, which may deny its acceptance by a grounded resolution if this is detrimental to the proper performance of tax termination and collection tasks.

The acceptance by the Administration shall be presumed in the absence of any opposition issued within thirty days.

The special domicile thus constituted is the only valid domicile for all taxation purposes.

The Tax Administration may at any time demand the constitution of a special domicile or a change in the existing domicile when, by means of a grounded resolution, it proves the occurrence of the circumstances contemplated in the last part of the first paragraph of this section.

SECTION 30.- Obligation to report the domicile

The taxpayers and taxable persons are obliged to communicate their tax domicile to the Tax Administration, providing the necessary references for an easy and proper localization thereof.

Such domicile shall be rendered legal for as long as no new changes are reported.

In the event of default in the obligation to report the domicile, the domicile will be determined by applying the presumptions referred to in the preceding sections, notwithstanding the penalties applicable under the provisions of this Code.

SECTION 78.- Failure to file the statement of registration, modification or deregistration

The taxpayers, taxable persons and other individuals who fail to file to the Tax Administration the statement of registration, deregistration or the modification of any relevant information on their legal representative or their fiscal domicile within the terms provided in the relevant regulations or laws concerning the different taxes, shall liquidate and pay a penalty equal to fifty percent (50%) of their base salary for each month or fractional month, but

the total penalty may not exceed the amount equivalent to three base salaries.

The previous section relative to the fiscal domicile seems to be suitable and consistent with the organizational scheme of the Costa Rican Tax Administration, which is characterized, like most of them, by a territorial segmentation by taxpayer type and the centralization of guiding functional decisions at a national level.

As convenient as it may be, the enrollment of taxable persons in a certain territorial administration is not without problems.

Our practice has shown us that taxpayers, taking advantage of it, will attempt to “vanish” by fixing a fiscal domicile where they may be least noticed by the Tax Administration. For example: a merchant engaged in operations of a considerable magnitude in the Southern Zone of the country (characterized, at least as far as internal tax management is concerned, by a minor business development and a dominant rural territory), who is for that reason very visible, establishes his fiscal domicile in San José (the country’s capital). Hence, he becomes just one more among the numerous taxpayers enrolled in the Territorial Administration of San José, a section with a lower relevance within such Administration. As a result, the high probabilities of withstanding inspections on account of being enrolled in the Territorial Administration of the Southern Zone are enormously reduced in San José. Needless to say, all the operations, including the business management, are maintained in the Southern Zone.

The same happens with some taxpayers who, when informed that an administrative action has been initiated, change their fiscal domicile despite not having moved the place of their business management or business operations, with the only purpose of misleading the tax authorities and, ultimately, attempt to frustrate the administrative action.

This state of affairs has been leveraged by a well intentioned, though mistaken, administrative criterion. So far, the Administration has believed that the options contained in subsections a) through d) of section 26 (domicile of natural persons) and the same subsections of section 27 (domicile of bodies corporate) of the Code of Tax Rules and Procedures, are freely chosen by the taxable person.

After reviewing the issue, it has been recently concluded that, on the contrary, this entails a preferential relation of options, under which the first option should be registered and if, and only if the first is not possible, the second, and so forth. Obviously, the registration of a domicile different from the first domicile would assume the taxpayer’s motivation and the express acceptance of the Administration.

Why is that so? Because the fiscal domicile is not only the place to deliver any notices to the taxpayer, but also the place where any administrative actions should take place intended to verify and assure the performance of tax obligations. It

should be underlined that in the case of natural persons, option a) of section 26 cited above, it is the place of usual residence, and in the case of bodies corporate, option a) of section 27, it is the place where the management or the central administration is located.

Both options are consistent with international stipulations, albeit with some difficulty in the case of natural persons, where it should be understood that it clearly concerns the “vital center” for bodies corporate, because the text is consistent with the idea of “effective management”. In the latter case, this is the most adequate place: it is, ultimately, the place of the effective management, where the persons knowledgeable of the businesses are located, those who make decisions, who can answer to administrative requirements. It is at such place where the records and the information required for the performance of any administrative action are carried.

At present the Government of Costa Rica is driving a National Program for the Prevention and Fight against Tax Fraud, within which frame, and as a result of several months of studies conducted by the technical officers of the highest ranks of the institutions of the three Branches of the Republic, having competence on tax matters, a special plan has been created to implement the recommendations made by such technical team. Many of them are targeted at the modification of regulations and laws concerning tax procedures, in order to provide more effectiveness to the Tax Administration and to rule out loopholes that may lead to tax elusion or evasion which favor a lower compliance today. In this sense, the review of the legislation and the above cited criteria represents an important chance for improvement with high probabilities of success.

CONCLUSIONS

Arguing about the transcendence of the taxpayer census would be redundant. It is around such census that the success of the tax management revolves.

While it could well be said that the taxpayer census or registry in Costa Rica presents a design consistent with modern conceptions and that great efforts have been made in recent years to improve it, with very clear and concrete achievements, there is still a long way to go.

The transition towards a different way of managing taxes, "*Digital Taxation*", has forced the Costa Rican Administration to redesign process and procedures in order to achieve substantial improvements, increase performance, quality, services and speed, as well as control capabilities. The registry of taxpayers has not been alien to this transition and, on the contrary, it sees in it the possibility of consolidating as a tool for providing accurate, updated and highly effective information, as it should be the case.

The implementation of the recommendations within the frame of the National Program for the Prevention and the Fight against Tax Fraud could improve the regulations that govern matters related to the registry of taxpayers, and thus become another valuable and close opportunity to enhance it.

To conclude, the Costa Rican experience shows a process that has evolved since 2003 from a registry more dependent on taxpayer's willingness to enroll, modify or update their data on their own initiative, to a more active registry that, apart from the voluntary services, takes advantage of any updating possibilities that arise, whether as a result of the interaction with taxpayer or the intensive use of external information sources. This vision of a more active and dynamic registry is constantly strengthened and is incorporated as a priority into the modernization projects of the Tax Administration as a whole, as well as into the opportunities for regulatory reforms that could turn it more effective.