

TOPIC 1

Facilitation EOI to prevent offshore tax evasion

1. Introduction

Globalisation results in the increasing number of cross-border transactions, and jurisdictions are more aware to the tax evasion practices through offshore schemes. One of the ways to cope with this situation is to set up and build tighter cooperation in the field of information exchange. The OECD has initiated and developed Exchange of Information (EOI) mechanism, which is expected to address offshore tax evasion.

EOI gains more recognition from jurisdictions, including SGATAR members, in particular after the initiation of assessment by the Global Forum on Transparency and Exchange of Information. The results of having gone through phase one and phase two assessments echo like a bell ring for jurisdiction to realise how important EOI is. SGATAR members also engage in this matter and have discussed it in several meetings, including the 43rd SGATAR Meeting. During this meeting, all member jurisdictions have shared their views and practical approaches on EOI.

2. Operation of EOI and its organisation

2.1 Legal basis and the internal process for responding to an EOI request

2.1.1 Legal basis of EOI in tax matters

SGATAR members exchange information based on their existing Avoidance of Double Tax Agreements/Conventions (DTAs). Some members have well developed their domestic tax law and regulations to facilitate EOI. Nevertheless, in case where there is no domestic provision to exchange information, DTAs have then been extensively used as legal basis for EOI. Most of SGATAR members adopt the EOI Article of the 2005 version of the OECD Model Tax Convention on Income and Capital. However in some member jurisdictions, there exist restrictions on persons covered and taxes covered.

Other international legal provisions that could be used to facilitate EOI and to deal with cross-border transactions in tax haven jurisdictions are such as Tax Information Exchange Agreements (TIEAs) and Multilateral Convention on Mutual Administrative Assistance in Tax Matters (Multilateral Convention). Nevertheless since the level of development is not the same, there are those who have not yet entered into negotiating TIEAs or signing the Multilateral Convention.

Most members have joined the Global Forum on Transparency and Exchange of Information for Tax Purposes and some have also joined the Joint International Tax Shelter Information Center (JITSIC) in order to have more efficient exchange of information especially on abusive tax schemes which is then aimed to deter such behaviour. The summary of international legislation supporting EOI for each member jurisdiction is as follows:

Member Jurisdiction	DTAs	Global Forum	JITSIC	Multilateral Convention	TIEAs
Australia	/	/	/	/ (Effective 2012)	/
People's Republic of China	/	/	/	/ (Signed 2013)	/
Hong Kong, China	/	/	x	x	/
Indonesia	/	/	x	/ (Signed 2011)	/
Japan	/	/	/	/ (Effective 2013)	/
Republic of Korea	/	/	/	/ (Effective 2012)	/
Macao, China	/	/	x	x	/
Malaysia	/	/	x	x	/
Mongolia	/	X	x	x	/
New Zealand	/	/	x	/ (Signed 2012)	/
Papua New Guinea	/	X	x	x	x
The Philippines	/	/	x	x	x
Singapore	/	/	x	/ (Signed 2013)	/
Chinese Taipei	/	/	x	x	x
Thailand	/	X	x	x	x
Vietnam	/	X	x	x	x

2.1.2 Main forms and process of EOI

There are various forms of EOI such as EOI on request, spontaneous EOI, and automatic EOI. Again not all member jurisdictions have implemented all three forms of EOI depending on their domestic legislation and information technology development. The following table summarises the EOI forms implemented in each member jurisdiction:

Member Jurisdiction	EOI on Request	Spontaneous EOI	Automatic EOI	Other Forms/Avenues
Australia	/	/	/	- Industry Wide EOI - Regular Communications between Competent Authorities (CAs) - Simultaneous Investigation - Tax Examination Abroad
People's Republic of China	/	/	/	Regular Communications between CAs
Hong Kong, China	/	x	x	Regular Communications between CAs
Indonesia	/	/	/	Regular Communications between CAs
Japan	/	/	/	- Regular Communications between CAs - Simultaneous Investigation - Tax Examination Abroad
Republic of Korea	/	/	/	- Regular Communications between CAs - Simultaneous Investigation - Tax Examination Abroad
Macao, China	/	x	x	Regular Communications between CAs
Malaysia	/	/	x	Regular Communications between CAs
Mongolia	/	/ (incoming only)	/ (incoming only)	Regular Communications between CAs
New Zealand	/	/	/	- Industry Wide EOI - Regular Communications between CAs - Simultaneous Investigation - Tax Examination Abroad
Papua New Guinea	/	x	x	Regular Communications between CAs
The Philippines	/	/ (incoming only)	/ (incoming only)	Regular Communications between CAs
Singapore	/	x	x	Regular Communications between CAs
Chinese Taipei	/	x	x	Regular Communications between CAs
Thailand	/	/ (incoming only)	/ (incoming only)	Regular Communications between CAs
Vietnam	/	/ (incoming only)	/ (incoming only)	Regular Communications between CAs

Although it is realised that international interest has increasingly focused on automatic EOI, some member jurisdictions find it difficult to meet the OECD requirements and data format where IT investment could be needed. Having said that every member jurisdiction agrees that automatic EOI is useful, easy to distribute to responsible tax offices.

Upon receiving an EOI request, the working processes could generally be grouped into 3 phases:

Phase 1: Preliminary procedure phase. The EOI responsible unit or department will check for the validity of the request whether it has met requirements under DTA or other relevant

agreements/conventions, and match the name and address stored in database. In the case where request is unclear or the taxpayer in question cannot be located, there will be communications between treaty partners in order to get necessary and sufficient information. Once the responsible local tax authority of the involved taxpayer is known, the requested information will be transferred to such responsible local tax authority. However in some jurisdictions, there is only one level of tax authority who deals with EOI requests. In case where English is not an official language, translation work should also be done by the EOI unit or department.

Phase 2: Information gathering process. Once the information is transferred to the responsible local tax authority, the local tax officers preliminarily analyse the information and tax matters of relevant taxpayer with the materials of tax collection and administration in hand. Certain information may be within the database of the tax authority or other government bodies. Therefore there may not be a need to approach the taxpayer. However in some cases on-site visit or inspection may be required. Prior to the visit or inspection, the tax authority should prepare on-site visit or inspection plan, confirm the purpose, content, staff, measures, procedures and other relevant items, and then send the notice to taxpayer, withholding agent, agent or other third party.

Phase 3: Data analysis and report writing. According to the results of on-site visit or inspection, the report should include content and request of EOI, basic situation of inspected taxpayers, inspection process, inspection results and its handling information, other relevant data and documents, etc. The response will then be prepared by the EOI unit or investigation in English and sent accordingly to treaty partner.

2.2 Dedicated organization for EOI, its composition and work scope

Member jurisdictions have similar organisation structure in dealing with EOI where there is an international taxation division or an office dealing with EOI who are responsible for

management, supervision and coordination of nationwide EOI; responsible for enacting rules, working process design, staff education and training, performance appraisal, as well as communication and coordination with other government bodies.

2.3 Collection of financial information

In practice, the tax-related financial information of taxpayers generally includes the basic information and tax return information of the taxpayers; the accounting records information of the taxpayers; and the information of taxpayers retained by a third party. Despite bank secrecy law, there is no bank confidentiality to prevent treaty partners from obtaining information in response to an EOI request. Tax authorities have power to access financial information at different degree of accessibility. In case where the tax authority has power to access the financial information, the tax authority will send a request directly to the financial institutions. However in some member jurisdictions, the procedure might be a little more complicated where the notification or summon must have been issued before the financial information can be provided.

3. Use of information obtained under EOI

At present, the information obtained from EOI is used for tax purposes. Each year significant amount of tax revenue and penalties has been resulted from extensive use of EOI in tax investigation. However where law of both treaty partners are allowed and the requested party agrees, the information obtained may be used for non-tax purposes which are normally limited to activities involving drug trafficking, organised and serious crimes, and terrorism. This is to align with the OECD commentary.

The information obtained can be used to prevent aggressive tax planning schemes. There have global calls for all jurisdictions to sign TIEAs and participate in international efforts to achieve transparency and international standards of effective EOI.

In the implementation of EOI, the treaty partners should keep the information confidential. The confidentiality of information is the treaty obligation of the treaty partners. Domestic legislation might be launched to ensure the confidentiality when making, receiving and dispatching, transferring, using, and storing EOI.

4. Obstacles to EOI

4.1 Legal and policy issues

Due to domestic legislation and policy issues, some member jurisdictions may not be able to fully adopt the 2005 version of EOI Article. Also, for some members, domestic law may only allow the exchange of information when there is domestic interest.

4.2 System, organization and staff issues

Many member jurisdictions experience disproportionate burden in order to fulfill their treaty obligations leading to time delay in the process. Some member jurisdictions experience problem that there is a lack of awareness on the importance of EOI at the local level. This is because there exists an EOI unit who is responsible for policy issues and legislation issues, whereas the local tax offices may focus more on tax collection but yet are those responsible for getting the requested information. Therefore due to the pre-determined key performance indexes (KPIs), the local tax offices' priorities would be on tax collection rather than EOI.

4.3 Increase in taxpayer compliance cost

EOI potentially increases compliance costs for taxpayers. In particular, when special foreign information requests is inspected, taxpayers cooperate with tax authorities for investigation,

apart from normal operation activities, manpower, resources and time costs must occur, which not only burdens the taxpayers, but also virtually burdens the EOI process.

5. Conclusion - Ways to facilitate EOI

5.1 Legal and policy issues

For some member jurisdictions, there is a need to improve the domestic legislation in order to facilitate the information exchange and fulfill the international standard. To deal with tax avoidance scheme, there should be a continuous effort to promote the signing of EOI agreements with all relevant partners as promoted by the Global Forum.

5.2 System, organization and staff issues

As mentioned above, there is a gap between knowledge and awareness of tax officers at the local offices and at the EOI unit or department, to close the gap, strong cooperation is needed. Not only the information exchange is done through writing, there should be close communication between officers too. This could be done by face-to-face meeting or training on EOI.

5.3 Reduce compliance costs of EOI

Even when there is suitable legislation in place, an increase in collaboration between member jurisdictions and the use of information technology are crucial in developing and facilitating the EOI process. Face-to-face meeting and simultaneous joint audits have been implemented in some member jurisdictions in order to save time for both tax authorities and taxpayers. IT infrastructure has also been discussed. Tax authority's database system contains a huge

amount of useful information but sometime such information cannot be extracted due to inefficient data management. To improve database system will allow the tax authority to promptly respond to tax treaty partners if information requested has been stored in the database and less burden to taxpayers to provide the same information. A way forward is to generate electronic automatic information, so as to relieve manual workload.

5.4 Moving forward to improve EOI

The meeting opened to discussions on topics that could improve EOI procedures. Three topics were raised which are facilitating and expanding automatic EOI among SGATAR member jurisdictions; sharing common encryption software to exchange information electronically to reduce lead time; and sharing EOI manual among member jurisdictions.

Some member jurisdictions agree that automatic EOI may be useful and can lead to deeper analysis using the provided tax information. It may seem at the first instance that the information may not be of much use and could not lead to a significant amount of revenue raised. However another purpose of automatic EOI is that such information may lead to other activities which may have been overlooked or have not been recognised. For example, information on interest payments received by pensioners residing in one jurisdiction may seem not so attractive to tax authority, however such information could lead to an investigation in individual's bank deposit which has not yet been taxed. Some members also experience that by publicising offshore automatic EOI could significantly increase compliance rate and increase income returning to the source jurisdiction.

To be more efficient in sending EOI request, the information should be kept simple and precise. Flow charts and diagrams could be used to better explain the tax cases. The request sending jurisdiction must also make sure that the information on relevant taxpayers is sufficient for the receiving jurisdiction to conduct its due diligence and to identify and locate the taxpayers.

With respect to encryption software, some member jurisdictions suggested the use of PGP

(Pretty Good Privacy) software which is also publicly available on www.openpgp.org. This helps member jurisdictions to easily and safely communicate on EOI cases including acknowledge of receipt and feedback.

To improve EOI implementation, some member jurisdictions agree to share EOI manual if any. The Bureau of Internal Revenue of the Philippines has developed the EOI manual and is willing to share with SGATAR member jurisdictions upon request. The Australian Taxation Office and Inland Revenue Department of New Zealand are willing to extract their internal training materials and share with members so that the communications and sharing experiences between tax officers will not stop here but continue to improve EOI procedures.

TOPIC 2

Effective tax debt management

1. Introduction

Effective tax debt management is integral to every tax administration. The objective of Working Group 2 was to discuss the organisational capacity and recovery strategies of each SGATAR Member, with a view to enhancing our understanding of the most effective methods of managing tax debt. Each Member shared respective experiences and approaches adopted in administering their various taxation laws.

Working Group 2 considers the broad elements for successfully implementing an effective debt management regime require attention to be given to:

People

Tax collection officers must have the relevant skills and capabilities to effectively and efficiently deliver the activities assigned to them.

Processes

All business processes, both automated and manual, need to be well aligned to the nature of the tax defaulter's situation. Processes need to influence voluntary compliance as well as supporting enforcement for those who deliberately chose not to comply. These must also be subject to regular review to ensure their effective application and continued relevance.

Policy

There is a need for all Members to have the appropriate legal authority and legislative framework, which is supported by a sufficiently flexible yet robust policy to support the desired collection results while maintaining the integrity of the tax system. Operational policies should be regularly reviewed and evaluated to ensure they remain valid, relevant and appropriate to the wider economic conditions faced by people and businesses operating

within these conditions. They also need to be designed and applied for successful achievement of respective Government objectives.

Platform

IT systems must be consistently available, stable and capable of supporting collection initiatives and strategies. They must facilitate engagement with debtors in a way that primarily encourages voluntary compliance and self-service. They must support the “smart” targeting of non-compliant debtors, with a focus on ability (capacity) and likelihood (propensity) to pay being a priority in applying the relevant risk assessment model. Further, they must support effective work flow together with intelligent monitoring and reporting of results.

2. Current Issues

2.1 Size of tax debt

Many Members have recorded growth in annual tax debt when compared to annual revenue. Common causal factors include issues associated with the 2009 global financial crisis and in some Members significant “natural disasters”.

By comparison some Members have recorded reductions in the rate of tax delinquency or report a slowing down in the rate of growth. All Members however reflect that the management of tax debt is a significant challenge in an environment where governments want more from their revenue agencies to improve governmental accounts, but at the same time are also reducing revenue agency funding by reducing governmental expenditure.

2.2 Tax debt collection

The ability to make meaningful comparisons across all Members when considering the elements of cash/payments collected for outstanding tax and any remaining collectable debt, and those debts yet to be addressed but broadly viewed as probably uncollectable, is difficult. This is because of the individual conditions each revenue authority works within. For example, not all participating Members administer the same types of taxes and nor do Members mirror each other with their respective legislative powers to take specific actions for the recovery of unpaid amounts. It is apparent that many Members are focused on both prevention and collection strategies, and there is a complementary focus on enhancing the use of technology to improve the effectiveness of both strategies.

3. Organisational capacities

3.1 Authority of the tax administration

All Members use a variety of recovery and enforcement legislative powers. The majority of Members have some form of late payment charge in the form of interest and/or penalties which are designed to stimulate compliance, in addition to the power to order payment by third parties holding monies on behalf of the debtor.¹

Many Members also have travel restriction provisions preventing travel until outstanding taxes have been dealt with. Some have programmes that encourage the passing of information to the revenue authority by informants where a smaller number again pay a reward for such information.

3.2 Resources and organisation

¹ Third party notices ('garnishee notices') are commonly issued to collect a proportion of income streams such as wages, or monies held in bank accounts. They are also used to capture other assets that are being realised into cash eg: proceeds from the sale of property.

The Members reported significant comparative variation in the level of resources (as a percentage of total staff) applied to the business of debt recovery and management. Whilst some Members shared similarities in structure in terms of management of new and aged debt, differences in structure appear to be directly related to capabilities, internal processes and the respective government expectations.

4. Effective ways of tax debt collection

4.1 Improving direct methods

Broadly most Members demonstrated efficiency and effectiveness of ‘direct methods’ of debt collection which were comprised of two major themes:

4.1.1. Improved segmentation between groups of outstanding tax debtors taking into account compliance risk and the likelihood of gaining payment. This in turn shapes the selection of cases to work on, the priority given to different groups and the nature of the collection treatments applied to each.

4.1.2. The use of technology to automate suitable debt collection processes.

By improving the way authorities differentiate between debtors, and by targeting and tailoring interventions accordingly, not only can improved debt collection outcomes be delivered, but community confidence can be enhanced by ensuring there is integrity and fairness for those who do pay their tax on time.

At the core of effective segmentation is the use of analytical models that can distinguish between debt cases likely to be finalised without a high level of intervention (‘self-finalising cases’) and those cases requiring more intensive debt collection action to achieve resolution (‘non self-finalising cases’).

Many Members report that they are using a variety of tools to support both self-finalising cases (eg: the use of on-line services help individuals and businesses set up payment arrangements within certain parameters established by the revenue authority), and cases requiring more intensive treatment.

In the latter category, a number of Members report that they use tools that support tax collection officers and debtors alike when determining if a business has a viable future or if a proposed payment arrangement has a legitimate chance of being sustainable into the future. It is important in this instance for a debtor to be able to prove they have the capacity (based on quantifying the net income surplus income) to maintain the arrangement over time.²

It is clear from the experiences of Members that technological improvements which automate collections processes allow tax collection officers greater opportunity to work with those who don't voluntarily take steps to address their debt. This delivers measurable improvements in both the efficiency and effectiveness of debt collection activities.

While not an exhaustive list, the following briefly outlines a number of approaches used to collect unpaid tax or to support the integrity of the tax system if full payment cannot be achieved by the relevant due date:

- Outbound calling campaigns that generate high coverage and response rates for new and smaller debts. A number of Members report great success from making direct contact with debtors (and potential debtors) just prior to payment dates as well as following up very soon after a payment date has passed. In this context it is recognised that early intervention is a key contributor to slowing or even stopping the growth in debt.
- Off-setting refunds from different revenue types against other tax debt.
- Cross agency collaboration through information sharing as well as joint actions to help with a collection outcome.
- Late payment charges in the form of penalties and/or interest.

² A number of tools can be used to achieve both a direct and an indirect influence, i.e. supporting payments made on time as well as post a due date.

- Garnishee orders on income streams or money held in bank accounts, or by other third parties.
- Seizure and subsequent sale of assets.
- Registering a legal interest on property so that the owner cannot sell the property until the tax issue has been resolved.
- Travel restrictions.
- The use of respective bankruptcy and liquidation processes.
- Expanding the tax obligation to an associated person or entity is a mechanism a number of Members use successfully to recover tax when the primary “owner” of the obligation no longer exists or is unable to pay the full liability.
- The ability to pay off outstanding amounts by way of instalments when full payment cannot be made.

4.2 Improving indirect method

Enabling and positively influencing voluntary payment compliance are the primary objectives of ‘indirect methods’.

Members reported that there are a variety of “indirect methods” that achieve successful outcomes. Whilst not exhaustive, the following list is representative of the initiatives that have been adopted:

- The use of external comparisons between tax agencies and the private sector. Forums such as SGATAR provide a wealth of information for participants to learn about and to share ideas on “best practice” activities. All Members are strongly focused on learning from each other.
- A number of Members report that they influence compliance by preventing people and businesses from accessing other governmental services or funding. For example, obtaining registrations or licenses for other purposes are withheld until the tax debt issue is resolved.
- Notwithstanding various privacy laws a number of Members report that they have the ability to publish personal information about tax delinquents. For example, the public

disclosure of information can include a tax delinquent's name or a company name (in this instance the name of the CEO is also disclosed), age, job, address and a summary of the tax owed. Members that have such disclosure powers indicated that they achieve both a direct and indirect beneficial influence on compliance.

- Various online tools and services that assist taxpayers in managing their tax payment obligations are critical to supporting voluntary compliance. Calculators of various types that help taxpayers to self-assess their particular issues are increasingly becoming part of the respective voluntary compliance systems. These tools need to be designed with the key objective of making it “easy” for taxpayers to self-manage all of their tax payment obligations and interact with the tax authorities.
- A number of Members also reported developing a greater understanding and use of behavioural economic principles to improve voluntary payment compliance. The messaging in letters and via other channels is more explicit about the importance of paying tax for the benefit and well-being of communities that taxpayers live in. Additionally, this messaging often describes that on time payment of tax is necessary if the individual wants to be part of the majority group of taxpayers who consistently do pay the right amount and on time.
- Finally, a couple of Members commented on the linkages between an increased focus on improving the interaction between lodgement of outstanding returns and recovery of outstanding debt. Timely lodgement/filing of tax returns is the initial point of recognition that a payment is required, and without an up to date return filing position, the level of outstanding debt can be hidden from obvious view because without a confirmed assessment, the formal acknowledgement of a debt has not occurred and the recovery of it cannot start.

4.3 Improving administrative authority

Many Members referenced an “Integrated Tax Design” which better enables legislative provisions and policy to align sensibly with operational challenges in a supportive and complementary fashion.

Many Members also provided good examples of where there has been a particular collection problem and through collaboration with policy makers have developed workable solutions to reduce the harm being caused.

A number of Members highlighted the work they were doing internally to develop a better focus on preventative initiatives such as SMS reminders, outbound calls, and other communication channels to reach out to people and businesses prior to payment dates.

Effective resource planning and management was another key improvement theme. Methodologies that support the effective balancing of cost, quality and service dimensions are essential to confidently managing a limited resource to best effect. All agree that in order to create a more efficient and effective workflow, elements to consider include, greater automation for more straightforward debts, improved targeting of cases, understanding more deeply debtor behaviours and the causes to better respond, increasing the skills of debt collection officers especially when addressing habitual non-compliers, setting clear priorities and performance goals at the organisational level as well as the individual level and having complementary monitoring and reporting mechanisms. Many of these elements are enhanced through improved technology such as analytic tools.

Many Members record the need to access 3rd party data to improve each authority's understanding about income streams and wealth positions in advance of making contact with a delinquent taxpayer. It was thought that a greater level of access to information held by banks would be very beneficial to support collections results.

Additionally, another fundamental challenge is to keep up to date with contact information. Many Members reflected on the difficulties of locating new address information for "missing" people.

5. Conclusion

5.1 Evaluation and way forward

In order to be successful all Members need a multifaceted approach – there is no one single aspect of change that can resolve all the issues faced by each revenue authority’s collection function. It is clear that the impacts of the global economic environment will continue to affect taxpayers’ willingness and capacity to pay.

In addition to the comments made throughout this paper and the underlying working papers (which are recommended reading for all senior tax collection leaders within Members), a range of focus areas can be observed for each Member’s individual circumstances. But largely these are:

- minimising the inflow of debt and the number of debts requiring intervention to be resolved – through a combination of debt prevention strategies and strategies to positively influence payment compliance behaviour enabling taxpayers to self-manage their tax payment obligations, including any debts that may arise
- optimising the allocation of our resources using risk models, analytics and effective workflow mechanisms
- ensuring the use of the most appropriate and effective collection treatments
- strong alignment between legislation, policy and operational challenges and the systems in which taxpayers’ operate (their ‘natural systems’).
- ensure our debt collection strategies are adaptive and keep pace with changes in taxpayer behaviour and the external environment
- Leverage the benefits of technology across all fronts.

In summary – Work to fully integrate People – Process – Policy & Platform.

Finally, the Working Group spent some time discussing the benefits of increased international co-operation. Some Members felt that by enhancing international engagement we would significantly improve the ability to address the problem of greater mobility of individuals and capital. Some Members commented on how hard it is to trace off-shore assets and potential income streams without the help of the overseas authority where an asset or income stream is based.

It was felt that a greater use of international collection assistance tools such as Tax Treaties and Multilateral Convention On Mutual Administrative Assistance In Tax Matters would increase the opportunities to deliver better collections outcomes. In addition to these legal

tools, developing closer relationships between tax authorities and key individuals within them are essential to gaining the maximum benefit possible.

TOPIC 3

Exposing the underground economy

1. Introduction

The purpose of this topic “Exposing the Underground Economy” was to broaden members’ understanding of the underground economy in order to effectively and efficiently address this sector, and to exchange thoughts and experiences of members in this endeavour

We have to note, however, that many of the discussion points, compliance programmes, initiatives and policies, etc., were not specifically targeted to combat the risks associated with the underground economy. The points discussed were part of a member’s plans to tackle non-compliance and/or tax evasion matters on a whole. Some members had also adopted their generic non-compliance strategy into tackling issues from the underground economy.

Definition and size of the underground economy

There was no standard definition to the term “underground economy”. While the Organisation for Economic Co-operation and Development (“OECD”) defined it as “legal activities that are deliberately concealed from the public authorities to avoid payment of taxes or complying with regulations”, many members had broader definitions that included illegal and criminal activities.

In addition, there were no agreed or commonly recognised methods to measure the underground economy. Some members pointed to the study conducted by Professor F. Schneider of the University of Linz in Austria – his report (Schneider, FS, 2012. *The Shadow Economy and Work in the Shadow: What Do We (Not) Know?*), estimated the range of the sizes of the 21 OECD countries to be between 7.2% and 25.1% of the country’s official gross domestic product (“GDP”) in 2007. Some members, using their own estimation methods, recognised the sizes of their underground economy to be as low as 3% to as high as 43.8% of their jurisdiction’s official GDP; while other members did not put a measurement to the size of their underground economy.

Characteristics of the underground economy

In general, members were of the view that the activities defined under the underground economy, whether or not they were illegal activities, had the following common characteristics:

- Heavy reliance on cash transactions, barter trades, etc.; where it would be difficult for tax administrations to reconstruct the transactions unless taxpayers keep proper records
- Numerous sales transactions with small dollar amount per transaction
- Inappropriate keeping of books and records
- Varied and diverse – underground economy activities could exist in many sectors including food and beverage, personal services, e-commerce, transport services, retail, construction, manufacturing, etc.

The underground economy would affect the jurisdiction's economy and people's wellbeing. It undermines fair taxation and lowers tax revenue, thereby decreasing the jurisdiction's operating revenue. As such, a jurisdiction would have less than the fair amount of revenue for fiscal budgeting, thus limiting the potential resources it could have used in boosting the economy, as well as restricting, to a certain extent, the benefits that could have been accorded to the residents.

2. Efforts, to date, to address the underground economy

2.1 Organisation and staff

The manners with which members organised themselves to address the underground economy were varied. Some members had some form of a dedicated team or task force; while the other members relied on introducing specific initiatives or programmes to deal with the issues and risks posed by the underground economy.

A specialised unit usually consisted of a number of dedicated staff who had experienced in various aspects of tax administrations. The most specialised units took on the work of developing strategic frameworks and compliance programmes, analysing trends and data-mining compliance targets, executing the investigations, etc., in a contained department. Other members had units who focused on devising compliance strategies and identifying audit targets, while the responsibilities of the execution of the compliance programmes fell onto other departments.

Other members, who had identified specific risks arising from the underground economy, had organised themselves to deal with those risks directly. Some of the specific risks included non-compliance of tax registrations (especially for newly incorporated businesses), poor record keeping practices by taxpayers, etc. Specific initiatives were introduced to tackle these issues head-on.

2.2 Basic administrative infrastructure and legal basis

Members relied on legislative provisions to aid them in combating the underground economy. Some of the common provisions were:

- Mandatory registration of businesses – whereby registration for tax would be mandatory as well
- Record keeping regulations
- Compulsory filing of employees' remuneration records
- Powers to obtain information, enter and search premises, require interview under oath, etc.
- Withholding tax regimes where the tax withheld would not be the final tax (businesses would have to declare the income earned to reclaim some of the taxes being withheld)
- General tax evasion and fraud provisions – whereby errant taxpayers would face heavy fines and/or penalties, and might face prosecution

Having strong legal powers, regulations, and requirements to combat the underground economy would work to a certain extent. However, there was a general consensus that resources and efforts would have to be put in to combat the risks of non-compliance to those laws and regulations. With a strong legislation, members could have the added measure of prosecuting errant taxpayers and might be able to deter other taxpayers from committing similar offences.

For members whose scope included illegal and criminal activities, they would have the legislative powers to bring such activities to tax, if uncovered. Often, such illegal activities were outside the scope of the members' tax administration focus. These criminal activities would often be investigated by the police and dealt with accordingly under criminal laws and their equivalents. Proceeds from such activities might be confiscated in entirety, as they were illegal in the first place.

2.3 Priority areas

The areas of focus with regard to the underground economy were largely determined by a member's economic activities and her stage of maturity in dealing with the associated risks.

Some members believed that the larger the contribution to the GDP a particular industry had in a member's jurisdiction, the more likely it was for there to be higher levels of underground economy in that industry. This might be so because errant individuals and businesses find it easier to cheat the tax system in an industry that had very high demand and supply.

The amount of past efforts put in to tackle the risks associated with the underground economy also affected members' priorities in addressing those risks. Members who had tackled the associated risks for a longer term would prioritise their current efforts in researching recent technologies for payments (for example, bitcoin) and their risks. Other members had prioritised their resources on tackling non-compliance issues such as non-registration of businesses, non-filing of tax returns, inappropriate record-keeping practices, etc.

Some members focused their resources on larger taxpayers who have had the potential to be fraudulent in their transactions. These members believed that most of the participants from the underground economy would not be subject to tax. This was so because many of the participants were very small in scale and, therefore, would not reach the minimum income thresholds to be liable for tax. Trying to dedicate resources into these areas would, very likely, be very expensive. Hence, these members would prefer to prioritise on investigating larger taxpayers.

Members also discussed the manner with which one could detect and identify the participants of the underground economy. A notable topic of discussion was related to the gathering of transactional data of a potential participant of the underground economy from banks. While it might be useful for the tax administrators to gather such information for review, analysis, and for determining the revenue size of the potential evader, tax administrators often found difficulties in getting the data in the first place due to the secrecy provisions in members' banking act or the equivalent, which prevented the disclosure of such information to a third party.

These were some of the other ways that members employed to identify potential participants of the underground economy:

- Relying on tip-offs from informant, such as anonymous reporting from the public
- Gathering of information from internal sources, such as other government agencies (for example, the law enforcer or the police)
- Gathering of information from third parties, such as banks, credit card companies, e-commerce websites where they facilitate sales between numerous buyers and sellers
- Analysing intelligence reports such as seasonal trends, industry averages in gross profit, sales turnover, assets turnover, etc.

3. Major efforts and experience

3.1 Major efforts and experience

Members have been addressing the risks posed by the underground economy on different levels. While some members launched large-scale compliance programmes on identified sectors / industries to combat the risks directly, some members opt to deal with the challenge on a more strategic level with the aim to shape taxpayers' behaviour and encourage voluntary compliance. The other members employed a mix of the two.

There were various methods with which members identify risky areas for their major audit and investigation programmes. Many members employed data analyses / data mining, qualitative analyses and observations, public feedback, etc. Usually, the risky areas would have characteristics as discussed in paragraph 1.2.1. These were some of the typical sectors that members had had major efforts on in recent times:

- Food and beverage industry, where majority of the businesses were small stallholders
- Personal services, such as house cleaning, hair dressing, computer maintenance, etc.
- Transport services plying their routes without being registered
- Businesses dealing with e-commerce

Another approach to tackle the risks would be to shape taxpayers behaviours with the aim for them to comply with tax regulations voluntarily. Such policies could be drawn up by the tax administrator alone or be coordinated at a higher, more strategic level with other government agencies. The following were some examples of the policies drawn up to encourage voluntary compliance:

- Encouraging the use of non-cash payment methods, coupled with proper and/or standardised electronic forms of record-keeping
- Educating the public on tax laws and regulations to raise people's awareness of tax payments and to foster people's habits and values of declaring their fair share of taxes
- Simplifying tax rules so that taxpayers would find it easier to comply with their tax filing and payment obligations

Members have had successes in their efforts to combat the underground economy. For members who drew up compliance programs, they experienced recovery of unpaid taxes and penalties by executing the programmes and investigations. For members who set up initiatives such as the use of uniform invoices, encouraging the issuance of receipts for cash transactions, etc, they, too, experienced an increased take-up rate of the desired outcome of these initiatives.

4. Conclusion – Way forward

Although the issues brought about by the underground economy was not new, members generally agreed that there was room to make additional and continual efforts to address the associated risks and bring these taxpayers into the tax net. This was so because the underground economy might undermine a member's economy in terms of generating a lower tax revenue and, therefore, lowering the fiscal budgets available for various government's programmes. It might also undermine the integrity of the member's tax system that could lead to a loss of taxpayers' faith in the equity and fairness of the tax system.

The way forward, driven mainly by each member's progress in dealing with the risks from the underground economy, for each member would be different. While the way forward might seem to be similar to the major efforts as discussed in paragraph 3, we have to understand that all members were at different stages in dealing with the risks arising from the underground economy. Many members who had set up specific frameworks to deal with the associated risks were already evaluating or had plans to evaluate, and take stock of the progress of their work. Other members had a multitude of plans to address these risks, with some of the potential plans as indicated below:

- Undertaking research to understand if there would be a practical limit to how much the cash economy could be further reduced
- Reviewing the popularity of cash usage and introducing or encouraging cashless initiatives
- Training assessing officers and field auditors to keep them abreast of knowledge in this area

- Introducing foreign asset reporting system whereby taxpayers would have to declare their assets (both movable and immovable) to the tax authority
- Educating taxpayers of proper record-keeping requirements and their subsequent tax obligations
- Sending strong deterrence message to the public
- Investing in information system and databases for enhanced data mining of risky cases, matching of input and output taxes for value-added tax or goods and services tax
- Encouraging voluntary compliance by cultivating social norms and values, simplifying the tax filing and payment process, simplifying tax rules for the participants in cash economy, etc.
- Further collaboration among members on international matters relating the underground economy.

The responsibilities and efforts on combating the non-compliance of tax regulations cannot fall onto the tax administrator's shoulders alone. There has to be extensive cooperation among all internal government agencies, and, more importantly, cross-borders cooperation among various government bodies.

Finally, members agreed that the SGATAR meeting was an excellent forum for one to learn from the others. As discussed throughout the working group sessions, members would be taking back many learning points from each member's journey in tackling the issues from the underground economy, and issues on non-compliance of tax obligations in general. As a result from this meeting, members could perhaps look into the potential roadblocks each initiative or policy would bring and could then refine or tweak the potential solution that would suit their jurisdiction. Members could also study the future initiatives by other members and consider whether to adopt similar policies in their jurisdictions.