

## CONVERGENCE IN GLOBAL TAX COMPLIANCE

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For many countries, comprehensive tax reform is a panacea for fiscal imbalances. However, structural factors do not fully account for the causation and scale of tax gaps in many countries. For some of these countries, substantial revenue leakages can be fairly easily contained by adopting simple measures to minimise information asymmetry. By leveraging on existing infrastructure, disclosures can be facilitated and incentivised without imposing an onerous burden on compliance. Some of the key developments put in place by leading advanced countries to reduce the payoffs in domestic as well as international tax avoidance and evasion are examined in detail. The article concludes that a discernible convergence in the use of similar tools and strategies to remedy information deficiency is indicative of their efficacy and trends in the tackling of tax evasion and aggressive avoidance on the current global tax reform agenda.

### I. INTRODUCTION

The current economic climate is characterised by unprecedented economic, financial and fiscal imbalances in many countries across the world. Some countries face muted growth with high unemployment rates while others that pursue economic expansion as a priority risk crippling price inflation. The trade and fiscal surpluses championed by some are viewed with disdain by others. Deeper interdependencies between nations have made markets far less indulgent of countries that thrive on external debts to finance persistent budget deficits driven by unsustainable social programs. Unyielding demand for better returns on capital has led to a quest by some nations to offer more competitive and stable environments to attract capital and investments. Some call this a ‘new normal’.

In this challenging environment, reducing funding gaps that are expected to rise might require considerable reform in some countries. There is no dearth of prescriptions for nations that seek to restructure their public finances to succeed or survive. Fiscal consolidation has been a dominant theme in the recent agendas of many governments. Over the last 10 years, many emerging economies have moved from pro-cyclical to counter-cyclical fiscal policies.<sup>1</sup> In many developed countries, the capacity to increase taxes or reduce public expenditures to balance budgets is

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<sup>1</sup> Jeffrey A Frankel, Carlos A Vegg & Guillermo Vuletin, “On graduation from fiscal procyclicality” (2013) 100 *Journal of Development Economics* 32.

severely constrained by other competing policy concerns, international competitiveness and weak economic fundamentals. Some advanced economies are poorly adjusted to cope with the pain of austerity measures implemented to reduce expenditures on social programs.<sup>2</sup> Others are advised to maintain public expenditures but hike taxes to balance the budgets. Even if countries secure the necessary political consensus to adopt any of these policies, there is probably no simple solution for ills as divergent as the world is confronted with.

In some cases, the remedy could be worse than the malady. For instance, short-term austerity measures may induce a more severe economic contraction that could jeopardise both social cohesion and economic rejuvenation. On the other hand, raising taxes is no longer purely a domestic concern as the demand and supply of global capital is increasingly more elastic in a deeply entrenched globalised market. As global competition is stiff, significant deviations in effective tax burdens between competing nations could increase the risk of mobile capital flight to jurisdictions that offer more competitive business environments. The dominance of intra-firm transactions in modern supply chains has also heightened the sensitivities of Multi-National Corporations (“MNCs”) to the impact of relative changes in geographical tax incidence.<sup>3</sup>

In the current circumstances, the tools and policy options available for broad-based comprehensive tax reforms are limited. Therefore, it is submitted that nations could consider allocating more resources to review the tax gaps in their systems. Some countries have benefited from detailed tax gap studies to bolster their administrative and legal capabilities to enhance the yield from current taxes. This paper seeks to highlight some recent developments being put in place by some leading advanced countries to target evasion and aggressive tax planning. This paper urges other countries, especially those in Asia, to embark on a systematic analysis of their tax gaps. Where tax gaps are found to result from significant compliance deficiencies, some of the measures outlined in this paper could be adopted to arrest revenue leakages and strengthen the integrity of the tax system.

## II. TAX GAP TRENDS

‘Tax gap’ is the difference between the full potential tax revenues that are legally due to the state and the actual tax revenues collected.<sup>4</sup> This is to be distinguished from potential tax revenues that are *economically* collectible. In reality, it is impossible for the state to collect every tax dollar that is legally due as some economic activities may not occur if the income derived from them is subject to tax.<sup>5</sup> Some key variables

<sup>2</sup> The political backlash in Greece is a good example. As a result of the bailout package, Greece increased VAT rate in 2010 from 10% to 23%.

<sup>3</sup> Organisation for Economic Co-operation and Development, *Intra-Firm Trade: A Work in Progress*, STD/TBS/WPTGS (2010) 24 (Paris: OECD, 2010).

<sup>4</sup> Parthasarathi Shome, “The control of tax evasion and the role of tax administration” in Luigi Bernardi, Angela Frascini & Parthasarathi Shome, eds, *Tax Systems and Tax Reforms in South and East Asia* (New York: Routledge, 2006) 35 at 40.

<sup>5</sup> See Norman Gemmill & John Hasseldine, *The Tax Gap: A Methodological Review*, Victoria University of Wellington School of Business Working Paper No 09/2012 (2012) at 13, online: Social Science Research Network <<http://ssrn.com/abstract=2199200>>.

that determine the size of tax gap in a country include the structure of the economy, the rule of law and tax morality. Although tax gap is often associated with tax evasion and avoidance, a broader measure of tax gap is simply non-compliance.<sup>6</sup>

Over the last decade, there has been an increasing interest in tax gap studies. Notwithstanding considerable differences in opinions over the credibility and utility of tax gap estimates, many countries are beginning to appreciate that periodic tax gap studies can enhance the compliance management powers of tax authorities.<sup>7</sup> The Organisation for Economic Co-operation and Development (“OECD”) endorses such initiatives as they promote enhanced risk management, transparency and public accountability.<sup>8</sup> In a recent survey by the OECD of 52 advanced and emerging economies, it was observed that 40% of the revenue bodies of these countries produced estimates of the tax gap for some or all of the major taxes administered, although this information may not always be made public.<sup>9</sup> The European Union (“EU”) has also been conducting value-added tax (“VAT”) gap studies for all its member states.<sup>10</sup>

For countries that have published the results of their national tax gap measures, a clear distinction emerges between the developed and the developing nations. However, an accurate and meaningful comparison of national tax gaps is difficult. Besides difference in methodologies, some countries prefer to confine tax gap studies to certain tax types.<sup>11</sup> There is also considerable debate over the reliability of the size of tax gaps since the gross numbers are at best estimates of the aggregate gaps in each tax type.<sup>12</sup> The accuracy of such studies is highly dependent on the quality

<sup>6</sup> Dave Rifkin, “A Primer on the ‘Tax Gap’ and Methodologies for Reducing It” (2008) 27 *Quinnipiac Law Review* 375 at 377; Robina Ather Ahmed & Mark Rider, *Pakistan’s Tax Gap: Estimates by Tax Calculation and Methodology*, Georgia State University, Andrew Young School of Policy Studies, International Studies Program Working Paper No 08-11 (2008) at 3.

<sup>7</sup> See Jacqui McManus & Neil Warren, “The Case for Measuring Tax Gap”, online: (2006) 4(1) *eJournal of Tax Research* 61 <<http://www.austlii.edu.au/au/journals/eJITaxR/2006/3.html>>. This includes Argentina, Australia, Denmark, Chile, France, Mexico, Sweden, the United States of America (“USA”) and the United Kingdom (“UK”).

<sup>8</sup> OECD, Centre for Tax Policy and Administration, Forum on Tax Administration: Compliance Sub-Group, *Monitoring Taxpayers’ Compliance: A Practical Guide based on Revenue Body Experience*, (Paris: OECD, 2008). See also Jeffrey Owens, “Tax Gap Measurement/Estimation—Does it have a role to play in modern tax administration practice?” (Presentation to CIAT 44<sup>th</sup> General Assembly, Montevideo, Uruguay, 12-15 April 2010), [unpublished]. See also OECD, Centre for Tax Policy and Administration, Forum on Tax Administration: Compliance Sub-Group, *Developments in VAT Compliance Management in Selected Countries*, (Paris: OECD, 2009).

<sup>9</sup> OECD, *Tax Administration 2013: Comparative Information on OECD and Other Advanced and Emerging Economies* (Paris: OECD, 2013) at 141.

<sup>10</sup> CPB Netherlands Bureau for Economic Policy Analysis, *Study to quantify and analyse the VAT Gap in the EU-27 Member States: Final Report*, (Warsaw: CPB, July 2013), online: European Commission <[http://ec.europa.eu/taxation\\_customs/resources/documents/common/publications/studies/vat-gap.pdf](http://ec.europa.eu/taxation_customs/resources/documents/common/publications/studies/vat-gap.pdf)> [CPB Final Report].

<sup>11</sup> See the Australian position in Australian National Audit Office, *Compliance Effectiveness Methodology, Audit Report No 39 2013-14*, (Canberra: Australian National Audit Office, 2014) at 30, 31, online: <[http://www.anao.gov.au/~media/Files/Audit%20Reports/2013%202014/Audit%20Report%2039/AuditReport\\_2013-2014\\_39.pdf](http://www.anao.gov.au/~media/Files/Audit%20Reports/2013%202014/Audit%20Report%2039/AuditReport_2013-2014_39.pdf)>.

<sup>12</sup> A useful primer on possible inaccuracies is provided in the paper by Norman Gemmill & John Hasseldine, *supra* note 5.

of the information available. Apart from legitimate concerns over its reliability, the differences in approaches may also reflect resource constraints, the state of public finance and divergent priorities among nations.

As the primary purpose of this paper is to highlight the potential remedies that some nations have applied to address the principal causes of tax gaps, it assumes that the existence of tax gaps is not in dispute. The reservations expressed over the veracity of size of tax gaps do not apply with equal force to the broad trends that unambiguously emerge from an exercise that attempts to do no more than contrast the divergence in the scale of tax gap estimates between developed and developing nations.

The tax gap estimates of developed nations are comparatively lower than that of developing nations. The latest study conducted by Her Majesty's Revenue and Customs ("HMRC") in the UK put the tax gap for 2011-12 at 7% of tax liabilities.<sup>13</sup> The Swedish National Tax Agency reported its tax gap in 2007 to be about 10% of taxable income.<sup>14</sup> A study on New Zealand reported an average tax gap of about 9% during the period from 1968-1994.<sup>15</sup>

In contrast, selected developing nations show significantly higher tax gaps. In Bangladesh, South Africa and Thailand, the average tax gaps are about 36%, 23% and 53% respectively with significantly lower averages of about 14%, 13% and 9% respectively in Australia, UK and USA.<sup>16</sup> For instance, Pakistan revealed a gap of no less than 70% in 2007/2008.<sup>17</sup> Afghanistan's tax gap was indicated to be 60% in a 2005 World Bank report.<sup>18</sup> Romania's VAT gap in 2011 was about 48%, as compared to Germany's VAT gap of 12%.<sup>19</sup> In Latin America, a study put the corporate income tax gap in Guatemala at 62.8% for 2006.<sup>20</sup> There are a number of possible reasons for this disparity. Many developing countries have either vast agricultural sectors or informal economic activities that cannot be readily taxed. In addition, the absence

<sup>13</sup> UK, Her Majesty's Revenue and Customs, *Measuring Tax Gaps: 2013 Edition*, (London, HMRC: 2013), online: Her Majesty's Revenue and Customs <[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/249537/131010\\_Measuring\\_Tax\\_Gaps\\_ACCESS\\_2013.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/249537/131010_Measuring_Tax_Gaps_ACCESS_2013.pdf)>.

<sup>14</sup> Swedish National Tax Agency (STA), *Tax Gap Map for Sweden, Report 2008:1B*, (Stockholm: STA, 2008) at 48, Fig. 8.

<sup>15</sup> David Giles, "Modelling the Hidden Economy and The Tax-Gap in New Zealand" in Gerald W Scully & Patrick J Caragata, *Taxation and the Limits of Government* (Massachusetts: Kluwer Academic Publishers, 2000) 195 at 212.

<sup>16</sup> Friedrich Schneider, "Shadow Economies around the World: What do we really know?" (2005) 21 *European Journal of Political Economy* at 598-642.

<sup>17</sup> See World Bank, *Pakistan Tax Policy Report: Tapping Tax Bases for Development, Report No 50078-PK (2009)*, (Washington, DC: World Bank, 2009) at 26, 50, online: World Bank <[http://www-wds.worldbank.org/external/default/WDSContentServer/WDSP/IB/2009/08/28/000334955\\_20090828015257/Rendered/PDF/500780v20ESW0P11official0use0only10.pdf](http://www-wds.worldbank.org/external/default/WDSContentServer/WDSP/IB/2009/08/28/000334955_20090828015257/Rendered/PDF/500780v20ESW0P11official0use0only10.pdf)>.

<sup>18</sup> See World Bank, *Afghanistan Managing Public Finances for Development Main Report, Report No 34582-AF (2005)*, (Washington, DC: World Bank, 2005) at 32, online: World Bank <[http://siteresources.worldbank.org/AFGHANISTANEXTN/Resources/305984-1137783774207/afghanistan\\_pfm.pdf](http://siteresources.worldbank.org/AFGHANISTANEXTN/Resources/305984-1137783774207/afghanistan_pfm.pdf)>.

<sup>19</sup> *CPB Final Report*, *supra* note 10.

<sup>20</sup> Juan Pablo Jiménez, Juan Carlos Gómez Sabaini & Andrea Podestá, *Public Finance and Administrative Reform Studies: Tax Gap and Equity in Latin America and the Caribbean, Fiscal Studies No 16*, (Eschsborn: GTZ, 2010), online: <[http://www.eclac.org/de/publicaciones/sinsigla/xml/0/39960/Fiscal\\_Studies\\_No16\\_End.pdf](http://www.eclac.org/de/publicaciones/sinsigla/xml/0/39960/Fiscal_Studies_No16_End.pdf)>.

of political will, institutional weaknesses and an inadequate machinery to enforce the rule of law are contributory causes to the revenue leakages.

### III. TAX GAP REDUCTION: DATA GAP

The choice of remedy is a function of the cause. Based on the recent developments in several developed economies, the author observes that there is a notable trend in domestic tax reform aimed at reducing information deficiency. Where a government is able to pass on the costs of tax collection to payors or paying agents, withholding of tax has been the main tool used to address potential tax losses arising from the lack of information sources and accurate disclosures.<sup>21</sup> The experiences in the USA and the UK demonstrate that compliance rates are much higher in cases where income is subject to withholding taxes. In the USA, a very low misreporting rate of 1.2% occurred in cases where withholding tax and substantial information reporting were in place, compared with 4.5% in cases subject only to substantial information reporting.<sup>22</sup> In the UK, labour income subject to the ‘Pay As You Earn’ Scheme (“PAYE”) had a lower level of under-declaration compared with business income.<sup>23</sup>

#### A. Correcting Information Deficiency

The OECD has highlighted the need for information as a critical part of an effective risk management strategy.<sup>24</sup> The absence of data is a principal impediment to the successful tackling of tax evasion. It has been observed in some developing countries that a key reason for the pervasive lack of information is the under-utilisation of financial institutions as a valuable source of tax-relevant information.<sup>25</sup> A robust information disclosure and exchange framework among companies, financial institutions and the tax administration can provide a potent self-policing mechanism in which the cost of collection and verification can be effectively shared between the state and the private sector. The perceived increase in transparency and sharing of information between multiple unrelated parties would minimize the amount of tax revenue at risk.

<sup>21</sup> Melissa A Dizdarevic, “The FATCA Provisions of the Hire Act: Boldly Going Where No Withholding Has Gone Before” (2010) 79 *Fordham L Rev* 2967 at 2976.

<sup>22</sup> US Internal Revenue Service, *IRS Updates Tax Gap Estimates—IR-2006-28*, online: Internal Revenue Service <<http://www.irs.gov/uac/IRS-Updates-Tax-Gap-Estimates>>; US Internal Revenue Service, *Tax Year 2001 Federal Tax Gap (Extended Version)*, online: Internal Revenue Service <[http://www.irs.gov/pub/irs-utl/tax\\_gap\\_update\\_070212.pdf](http://www.irs.gov/pub/irs-utl/tax_gap_update_070212.pdf)>. See also US Internal Revenue Service, *IRS Releases New Tax Gap Estimates; Compliance Rates Remain Statistically Unchanged from Previous Study—IR-2012-4*, online: Internal Revenue Service <<http://www.irs.gov/uac/IRS-Releases-New-Tax-Gap-Estimates;-Compliance-Rates-Remain-Statistically-Unchanged-From-Previous-Study>>.

<sup>23</sup> UK, Her Majesty’s Revenue and Customs, *Measuring Tax Gaps: 2014 Edition* (London, UK: 2014) at 48, online: <[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/364009/4382\\_Measuring\\_Tax\\_Gaps\\_2014\\_IW\\_v4B\\_accessible\\_20141014.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/364009/4382_Measuring_Tax_Gaps_2014_IW_v4B_accessible_20141014.pdf)>.

<sup>24</sup> OECD, Forum on Tax Administration: Cape Town Communique, *Study into the Role of Tax Intermediaries*, (Paris: OECD, 2008) at 27.

<sup>25</sup> See International Monetary Fund, *Investing in Public Investment: An Index of Public Investment Efficiency*, IMF Working Paper WP 11/37 (2010), online: IMF <<http://www.imf.org/external/pubs/ft/wp/2011/wp1137.pdf>>.

### 1. *Enhancing accounting disclosure standards*

In 2006, the US Financial Accounting Standards Board (“FASB”) released FIN 48 (FASB Interpretation 48) which clarified how Uncertain Tax Positions (“UTPs”)<sup>26</sup> are to be treated in the financial statements of businesses. These new guidelines are applicable to financial statements that adhere to the US Generally Accepted Accounting Principles (“US GAAP”).<sup>27</sup> Prior to that, some corporate taxpayers took full advantage of the flexibility to omit or even manipulate reported earnings through the positions taken on some uncertain tax issues.<sup>28</sup> The resulting inconsistencies in accounting treatment had severely limited the ability of the US Internal Revenue Service (“IRS”) to make meaningful comparisons of UTPs with information from other sources.<sup>29</sup>

The objective of FIN 48 is to improve the “relevance and comparability” of financial reporting by ensuring that “every tax position is accounted for” under a common standard.<sup>30</sup> Under FIN 48, an uncertain tax benefit must be evaluated under the ‘more-likely-than-not’ rule before it is measured and recorded in the financial statements.<sup>31</sup> A tax benefit can only be recognised if the probability that it would be sustained upon examination, based on technical merits, is greater than 50%.<sup>32</sup> For tax positions that satisfy the criteria, a taxpayer may record only the largest amount that is regarded as having a greater than the 50% cumulative probability of being obtainable in a final settlement with the tax authority.<sup>33</sup> If an uncertain position fails the test, the taxpayer is not permitted to record a tax benefit; alternatively, he may set aside a 100% reserve.<sup>34</sup> Business entities are also required to provide extensive and detailed disclosures of unrecognised tax benefits.<sup>35</sup>

The International Accounting Standards Board (“IASB”) has also considered the inclusion of a common accounting standard for UTPs.<sup>36</sup> Although the International Accounting Standards (“IAS”) requires detailed disclosure of changes

<sup>26</sup> US FASB, *FASB Interpretation No 48* (Connecticut: Financial Accounting Foundation, 2006) at 1, 2 [*FIN 48*]. UTPs are basically contingent tax liabilities that would have been incurred if the tax position taken could not be sustained when challenged by the tax authorities.

<sup>27</sup> Andrew W Jones, “FASB—The IRS’s New Best Friend: How FIN 48 Affects the Taxpayer-IRS Relationship and Potential Taxpayer Challenges” (2009) 25 Ga St U L Rev 767 at 773; US Internal Revenue Service, “FASB Interpretation No 48”, online: Internal Revenue Service <<http://www.irs.gov/Businesses/Corporations/FASB-Interpretation-No.-48,-Accounting-for-Uncertainty-in-Income-Taxes>>. It is mandatory for most US enterprises to adhere to GAAP.

<sup>28</sup> Jones, *ibid* at 772.

<sup>29</sup> Jones, *ibid*; *FIN 48*, *supra* note 26.

<sup>30</sup> *FIN 48*, *supra* note 26; see US FASB, *Consolidation of Variable Interest Entities—An Interpretation of ARB No 51*, online: Financial Accounting Standards Board <<http://www.fasb.org/summary/finsum46.shtml>>.

<sup>31</sup> J Richard Harvey, *Schedule UTP: An Insider’s Summary of the Background, Key Concepts, and Major Issues*, Villanova School of Law Working Paper Series Paper 161 (2011) at 25; Jones, *supra* note 27 at 774.

<sup>32</sup> *FIN 48*, *supra* note 26 at 2, paras 6, 7(a). See Harvey, *supra* note 31 at 25.

<sup>33</sup> *FIN 48*, *supra* note 26 at 3, para 8; Harvey, *supra* note 31 at 25-26.

<sup>34</sup> Harvey, *supra* note 31 at 25.

<sup>35</sup> This includes tabular reconciliations showing changes in unrecognised tax benefits arising from tax positions taken. Details of possible changes are also required for those that are reasonably likely to change within 12 months of a reporting date.

<sup>36</sup> International Accounting Standards Board, *Basis for Conclusions on Exposure Draft: Income Tax, ED/2009/2*, (London: IASCF, 2009) at 18; International Financial Reporting Standards Foundation,

to provisions as well as contingent liabilities including its nature and estimated financial impact to be recorded unless they are remote,<sup>37</sup> these standards are not entirely problem-free. The Interpretations Committee of the International Financial Reporting Standards Foundation has been asked to provide guidance on the accounting for income tax assets and liabilities arising from UTPs.<sup>38</sup> Following extensive discussions on the tentative agenda for this project, the Interpretations Committee has tentatively decided to develop a draft Interpretation reflecting its decisions as of November 2014.<sup>39</sup> It is likely, however, that the results of this project will have to be viewed in its broader context in IASB's research project on UTPs.<sup>40</sup>

## 2. Expanding information reporting obligations

Where weak enforcement of tax laws is one of the causes of tax gap, revenue authorities ought to be given more resources to enhance prevention, improve early detection and provide speedy resolution of disputes.<sup>41</sup> However, tax administrations must be mindful of the cost-benefit trade-offs in the allocation of its internal resources.<sup>42</sup> Since some taxes are simply not cost-effective to collect, it may be prudent to adopt a more targeted approach that focuses on significant areas of risk.<sup>43</sup>

In the context of enhancing effective tax collection, it is not surprising that empirical evidence supports a greater reliance on information reporting obligation. Professor Lederman identified asymmetric information to be a key problem for the enforcement of tax laws.<sup>44</sup> She points out that the state is entirely dependent on a taxpayer's disclosure or third-party sources while the taxpayer is often in possession

"IAS 12 Income Taxes—Tax effect of distributions to equity holders, Annual Improvements—2010 Cycle" (Draft Staff Paper for the IFRIC Meeting, March 2010). No new draft has been released.

<sup>37</sup> IAS 37 is similar to FIN 48. Strictly speaking, IAS 37 does not apply to income taxes.

<sup>38</sup> See International Financial Reporting Standards Foundation, *IAS 12 Income Taxes: Impact of uncertainty when an entity recognises and measures a current tax liability or asset*, online: International Financial Reporting Standards Foundation <<http://www.ifrs.org/Current-Projects/IASB-Projects/IAS-12-Measurement-income-tax-uncertain-tax-position/Pages/Home.aspx>>.

<sup>39</sup> See International Financial Reporting Standards Foundation, "The Interpretations Committee tentatively decided to develop a draft Interpretation, reflecting tentative decisions it had made at this meeting" (11 December 2014), online: International Financial Reporting Standards Foundation <<http://www.ifrs.org/Current-Projects/IASB-Projects/IAS-12-Measurement-income-tax-uncertain-tax-position/Project-news/Pages/Project-update-November-2014.aspx>>.

<sup>40</sup> See International Financial Reporting Standards Foundation, Interpretations Committee, "IAS 12 Income Taxes—Threshold of recognition of an asset on uncertain tax position" (Staff Paper for the IFRS Interpretations Committee Meeting, May 2014), online: International Financial Reporting Standards Foundation <[http://www.ifrs.org/Meetings/MeetingDocs/Interpretations%20Committee/2014/May/AP05A%20-%20IAS12%20-%20Uncertain%20Tax%20Position\\_CLS%20attached.pdf](http://www.ifrs.org/Meetings/MeetingDocs/Interpretations%20Committee/2014/May/AP05A%20-%20IAS12%20-%20Uncertain%20Tax%20Position_CLS%20attached.pdf)>.

<sup>41</sup> See the initiatives in the USA: See US Department of the Treasury, "Update on Reducing the Federal Tax Gap and Improving Voluntary Compliance" (8 July 2009), online: Department of the Treasury <[http://www.irs.gov/pub/newsroom/tax\\_gap\\_report\\_final\\_version.pdf](http://www.irs.gov/pub/newsroom/tax_gap_report_final_version.pdf)> at 12.

<sup>42</sup> Rifkin, *supra* note 6 at 406, 407.

<sup>43</sup> World Bank, *Pakistan Tax Policy Report: Tapping Tax Bases for Development*, *supra* note 17 at 51. See also UK, Her Majesty's Revenue and Customs, *Protecting Tax Revenues 2009*, (London, HMRC: 2009) at 12, 17, online: SB Consulting Limited <<http://www.sbconsulting.co.uk/storage/protect-tax-revenue-5450.pdf>>.

<sup>44</sup> Leandra Lederman, "Reducing Information Gaps to Reduce the Tax Gap: When is Information Reporting Warranted?" (2010) 78 *Fordham L Rev* 1733 at 1735.

of the complete set of relevant facts. In the USA, IRS found misreporting for sectors supported by some third party information reporting was only 8.6% while the rate for those without was 53.9%.<sup>45</sup> Enhanced information reporting obligations by third parties can be an effective tool to verify tax returns filed by taxpayers.<sup>46</sup> This significantly reduces the payoffs to under-report income.<sup>47</sup>

(a) *Enhanced Disclosures by Taxpayer*: In September 2010, the US IRS decided to leverage on the disclosures by corporations in their audited financial statements prepared in compliance with FIN 48.<sup>48</sup> The IRS issued final statements mandating certain corporations to disclose some of the information relating to UTPs directly to the tax authority.<sup>49</sup> As at 2014, corporations with assets in excess of \$10m are required to comply with the UTP disclosures.<sup>50</sup> The IRS UTP Schedule applies to positions on US federal income tax regardless of whether FIN 48 applies.<sup>51</sup> Generally, disclosure is required if the corporation has recorded a reserve with respect to a UTP in its audited financial statements.<sup>52</sup> As an exception, disclosure is also required if no reserve was recorded but the corporation (or a related party) determines that the probability that the tax position would be litigated is more than 50%.<sup>53</sup> This includes a description of facts affecting the tax position and “information that reasonably can be expected to apprise the IRS of the identity of the tax position and the nature of the issue.”<sup>54</sup> As evidence of its policy of restraint, the IRS dropped its earlier position that would have required draconian disclosures of the amount of reserves, the rationale and the nature of tax uncertainties.<sup>55</sup>

The adoption of a UTP disclosure regime has been hailed as “the biggest change in tax administration in the last 50 years”.<sup>56</sup> In this author’s view, it is by far the most coercive approach taken by a tax authority. The description of tax positions and their relative rankings will greatly improve IRS’s efficiency and effectiveness

<sup>45</sup> US Internal Revenue Service, *Tax Year 2001 Federal Tax Gap (Extended Version)*, *supra* note 22 at 3.

<sup>46</sup> Lederman, *supra* note 44 at 1738, 1739.

<sup>47</sup> John S Carroll, “How Taxpayers Think about Their Taxes: Frames and Values” in Joel Slemrod, ed, *Why People Pay Taxes: Tax Compliance and Enforcement* (Ann Arbor: The University of Michigan Press, 1992) at 43-46.

<sup>48</sup> In addition to this, the US also imposes very robust disclosure requirements by taxpayers for ‘reportable transactions’, eg ‘listed transactions’, ‘transactions of interest’ etc.

<sup>49</sup> Kathryn J Kennedy, “IRS’s Recent Uncertain Tax Positions Initiative: A Tangle of Accounting, Tax and Privilege Issues” (2011) 9 DePaul Business & Commercial Law Journal 401 at 434, 435; See also Harvey, *supra* note 31 at 11.

<sup>50</sup> US Internal Revenue Service, *2014 Instructions for Schedule UTP (Form 1120)*, online: IRS <<http://www.irs.gov/pub/irs-pdf/i1120utp.pdf>>; US Internal Revenue Service, *IRS Announcement 2010-75: Reporting for Uncertain Tax Positions* at 4, online: IRS <<http://www.irs.gov/pub/irs-drop/a-10-75.pdf>>; see also Harvey, *supra* note 31 at 23. This was incrementally implemented over a 5-year period from 2010.

<sup>51</sup> Harvey, *supra* note 31 at 37; US Internal Revenue Service, *supra* note 50.

<sup>52</sup> Harvey, *ibid* at 24.

<sup>53</sup> UTP must be disclosed if the tax position is one which the corporation or a related party determines the probability of settlement to be less than 50% and no reserve was recorded because the corporation has determined that it is more likely than not to prevail on its merits when litigated.

<sup>54</sup> US Internal Revenue Service, *2014 Instructions for Schedule UTP (Form 1120)*, *supra* note 50 at 6, Part III.

<sup>55</sup> US Internal Revenue Service, *IRS Announcement 2010-75: Reporting for Uncertain Tax Positions*, *supra* note 50 at 7, 8.

<sup>56</sup> Harvey, *supra* note 31 at 4, quoting a former Commissioner, Lawrence Gibbs.



in identifying the issues to audit and in the resolution of tax disputes faced by large corporations. Larger corporations have better access to an industry of professionals who have the expertise to navigate the complicated tax code to structure complex transactions around existing reporting obligations.<sup>57</sup>

The UTP disclosure regime is highly desirable from the standpoint of tax administration. It promotes and fosters disclosures that are arguably vital in a system of self-assessment. Nevertheless, the regime has also been very controversial. It has been suggested that this reform misses the true cause of the tax gap.<sup>58</sup> Doubts have also been cast on the legality of the IRS's attempt to rely on returns powers to support the demand for disclosures. In addition, some of the disclosures may potentially conflict with the protection conferred on certain classes of information subject to privilege despite the IRS's success in the case of *United States v Textron Inc.*<sup>59</sup> The efficacy of the UTP regime is likely to be monitored closely by other tax administrations as it has ramifications that extend beyond income tax and the USA.

As an experimental reform, adhering to the policy of restraint is sound. In that respect, it would appear to be sensible at this stage to refrain from introducing penal sanctions for non-compliance as the priority is to foster acceptance of a measure that clearly increases compliance costs on taxpayers.<sup>60</sup> The impact of the absence of specific penalties for non-compliance remains to be seen even though taxpayers are likely to be mindful of the implication that manifestly inadequate compliance is likely to give rise to adverse inferences.<sup>61</sup> Last but not least, the full benefits of this enhancement in tax information disclosure can only be harnessed if the IRS complements it with clear and timely publications of technical guidance and its interpretations on uncertainties in tax issues.

A similar scheme was also adopted in Australia recently. The Australian Tax Office ("ATO") has created a Reportable Tax Position Schedule ("RTPS").<sup>62</sup> Under the Large Business—Risk Differentiation Framework, any large business may be required by the ATO to lodge an RTPS from income years commencing with 2012.<sup>63</sup> A reportable tax position under RTPS refers to one or more of the following: (a) a position that has an equal or less than 50% chance of being correct; (b) where an uncertain tax position has been recognized in the taxpayer's (or a related party's) financial statements; and (c) where the income recognised under financial statements exceeds A\$200 million but the assessable gains are less than half of that income.<sup>64</sup> The objective of this disclosure scheme is to enable the ATO to target their compliance resources on large business sectors that play a significant role in the tax system as

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<sup>57</sup> *Ibid* at 9.

<sup>58</sup> See Kennedy, *supra* note 49 at 406.

<sup>59</sup> 577 F (3d) 21 (1<sup>st</sup> Cir 2009). *Cf US v Deloitte LLP*, 610 F (3d) 129 (DC Cir 2010) and *Lluberes v Uncommon Productions LLC*, 663 F (3d) 6 (1<sup>st</sup> Cir 2011) at 22. See Kennedy, *supra* note 49 at 422.

<sup>60</sup> US Internal Revenue Service, *2014 Instructions for Schedule UTP (Form 1120)*, *supra* note 50 at 5.

<sup>61</sup> Harvey, *supra* note 31 at 63.

<sup>62</sup> The power is apparently derived from ss 161 and 161A of the Australian *Income Tax Assessment Act 1936* (Cth).

<sup>63</sup> Australian Tax Office, *Large Business and Tax Compliance*, NAT 8675-11.2013, (Canberra: Australian Taxation Office, 2013) at 4. A large business is defined as one with an annual turnover of over A\$250 million.

<sup>64</sup> See Australian Tax Office, *Annual Compliance Arrangements*, online: ATO <<http://www.ato.gov.au/Business/Large-business/In-detail/Key-products-and-resources/Large-business-and-tax-compliance-publication/?page=36>>.

well as to identify areas of uncertainty in the tax law that may benefit from more detailed guidance or legislative reform.

(b) *Supplementary disclosures by third parties*: However, any enhancement in information reporting processes must be undertaken with caution. One consideration is the additional cost imposed on the reporting party due to opposition from affected third parties.<sup>65</sup> Excessive information reporting requirements, particularly if it does not result in a meaningful reduction in tax gap or produce efficiency gains, may be detrimental to the economy.<sup>66</sup>

After the release of the results of the last tax gap study, the IRS successfully implemented several new measures to improve third party reporting.<sup>67</sup> From January 2011, organisations that process credit and debit card payments must submit annual reports of these payments to the IRS.<sup>68</sup> In addition, brokerage firms are required to file returns containing information that includes the adjusted basis in the customers' securities and the nature of any gains or profit.<sup>69</sup> Some businesses must file information returns for payments of at least \$600 to any corporation or individual for certain categories of services rendered.<sup>70</sup> If such information is already required for regulatory or other purposes, these measures merely impose a marginal cost on the relevant entities.

Besides the US, numerous other countries have also implemented similar third-party reporting obligations. In particular, in 2013, the OECD conducted a survey of the third party reporting obligations of Denmark, Estonia, Finland, Norway, Sweden, Iceland, Chile and Spain.<sup>71</sup> Across these countries, common types of reportable income include salary and pensions. On the other hand, the reporting obligations for deduction-based information, such as child care expenses and interest, tend to vary more widely from country to country.

For example in Ireland, businesses, professionals and certain entities are required to report details of any payment exceeding € 6,000 in connection with the provision of selected services.<sup>72</sup> In Canada, reporting requirements are specifically targeted

<sup>65</sup> Rifkin, *supra* note 6 at 412.

<sup>66</sup> Lederman, *supra* note 44 at 1741.

<sup>67</sup> See US Internal Revenue Service, *Reducing the Federal Tax Gap—A Report on Improving Voluntary Compliance* (2 August 2007), online: Internal Revenue Service <[http://www.irs.gov/pub/irs-news/tax\\_gap\\_report\\_final\\_080207\\_linked.pdf](http://www.irs.gov/pub/irs-news/tax_gap_report_final_080207_linked.pdf)>. These measures have been incorporated into the tax code.

<sup>68</sup> *Inland Revenue Code*, USCA tit 26 §6050W (1986) [*US Inland Revenue Code*]; *Housing and Economic Recovery Act of 2008*, 42 USC tit 4501 §3091(a) (2008).

<sup>69</sup> *US Inland Revenue Code*, *ibid* at §6045.

<sup>70</sup> See US Internal Revenue Service, *Form W-2*, online: Internal Revenue Service <<http://www.irs.gov/pub/irs-pdf/fw2.pdf>>. See also US Internal Revenue Service, *Form 1098*, online: Internal Revenue Service <<http://www.irs.gov/pub/irs-pdf/f1098.pdf?id=40>>; US Internal Revenue Service, *Form 1099*, online: Internal Revenue Service <<http://www.irs.gov/uac/Form-1099-MISC-Miscellaneous-Income->>. Generally, payments of \$600 or more for rent, services, prizes and awards, health care payments, crop insurance proceeds, cash payments for fish etc are reportable.

<sup>71</sup> OECD, *Tax Administration 2013: Comparative Information on OECD and Other Advanced and Emerging Economies*, *supra* note 9 at 298.

<sup>72</sup> See *Taxes Consolidation Act 1997* (Ireland), No 39 of 1997, ss 889, 894. Widely known as the 'Third Party Returns', the scheme covers services such as entertainment, merchandising and photography. See also Ireland Office of Revenue Commissioners, *Third Party Returns—Automatic Return of Certain Information—IT16*, online: Revenue <<http://www.revenue.ie/en/tax/it/leaflets/it16.html>>.

at sectors with higher non-compliance risks.<sup>73</sup> Construction businesses are required to record and report payments in excess of \$500 when made to subcontractors for construction services.<sup>74</sup>

The value of these third-party information disclosure regimes is immense. By ameliorating information asymmetry, which is the “core problem for enforcement of tax laws”,<sup>75</sup> compliance is enhanced through more accurate risk detection. Empirical data confirms the correlation between compliance levels and income subject to reporting obligations.<sup>76</sup> In particular, third party disclosure regimes deter tax evasion by small or casual businesses that trade in cash, keep poor or no records, have no external financing reporting requirements, or are closely held—factors that undermine detection of under-reporting. In respect of personal income tax, third party reporting enables the adoption of ‘pre-populated returns’, where the tax authority originates the tax return for the individual taxpayer’s affirmation or amendment in the assessment process.<sup>77</sup>

A calibrated approach allows revenue authorities to scrutinise the purpose of payments and the identity of recipients in sectors that pose the greatest risks of non-compliance.<sup>78</sup> The implementation of third-party reporting requirements are, however, not straightforward. A few challenges exist.<sup>79</sup> The interaction of reporting requirements with privacy and secrecy legislation merits close attention. Data privacy laws in different countries vary considerably. There are legitimate concerns about access and usage that may be incompatible with other legislative frameworks.<sup>80</sup> Information exchange between tax authorities is also subject to legal and operational constraints.<sup>81</sup> Last but not least, information is only useful if it is accurate and collected in a structured manner. There is a real risk of ‘information overload’ from multiple sources that may become counter-productive for tax administrations that do not have adequate resources to cope.

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<sup>73</sup> Sean Davidson, “Tax agency targeting middle-income tax cheats” *CBC News* (28 January 2014), online: Canadian Broadcasting Corporation <<http://www.cbc.ca/news/business/taxes/tax-agency-targeting-middle-income-tax-cheats-1.2499725>>.

<sup>74</sup> See Canada Revenue Agency, *Contract Payment Reporting System*, online: Canada Revenue Agency <<http://www.cra-arc.gc.ca/nwsm/fctshs/1999/m12/cnft-eng.html>>. For the Norwegian regime, see OECD, Centre for Tax Policy and Administration, Forum on Tax Administration: Compliance Sub-Group, *Information Note: Withholding & Information Reporting Regimes for Small/Medium-sized Businesses & Self-Employed Taxpayers* (Paris: OECD, 2009) at 52, 53, Annex 1. For the UK, see UK, Her Majesty’s Revenue and Customs, *Construction Industry Scheme*, online: Her Majesty’s Revenue and Customs <<http://www.hmrc.gov.uk/cis/>>.

<sup>75</sup> Lederman, *supra* note 44 at 1735.

<sup>76</sup> UK, Her Majesty’s Revenue and Customs, *Measuring Tax Gaps: 2014 Edition*, *supra* note 23.

<sup>77</sup> OECD, Centre for Tax Policy and Administration, Forum on Tax Administration: Compliance Sub-Group, *Information Note: Using Third Party Information Reports to Assist Taxpayers Meet their Return Filing Obligations—Country Experiences with the Use of Pre-populated Personal Tax Returns* (Paris: OECD 2006), online: OECD <<http://www.oecd.org/tax/administration/36280368.pdf>>. The key benefits from the use of pre-populated returns are pointed out.

<sup>78</sup> *Ibid* at 15.

<sup>79</sup> Mila Gascó, ed, *Proceedings of the 12<sup>th</sup> European Conference on e-Government* (Reading, UK: Academic Publishing International Limited, 2012) at 123.

<sup>80</sup> For instance, the EU Data Privacy Directive (Directive 95/46/EC) provides very stringent rules on data processing and sharing to provide safeguards against abuse.

<sup>81</sup> See the discussion on Exchange of Information at Part III(B)(1) of this paper.

(c) *Incentivising Disclosures—Whistleblowing*: In this respect, the perception of the value of instituting a whistleblowing program to incentivise disclosures is rather divergent. As an additional tool to bridge the informational asymmetry, it has merits. Potential whistleblowers are typically insiders who possess some form of information on any tax evasion scheme. If the experiences of some countries are of any value, the amount of recovered tax revenues that are attributable to whistleblowing is not significant. Two reasons may be offered. First, potential whistleblowers who are insiders may refrain from divulging information if there is a real risk of self-incrimination by reason of their interests or involvement in the schemes. Second, the perceived value of confidentiality undertakings by the tax administration may be deemed to be inadequate. There will always be tensions between the tax administration's commitment to protect the identity of the whistleblower and potential obligations to submit to discoveries in any civil proceedings.

In 2006, the IRS enhanced the whistleblowers' program by establishing a Whistleblower Office.<sup>82</sup> A reward of 15-30% of the amount of taxes recovered is payable if the information supplied substantially contributes to the recovery of taxes or related payments in excess of \$2m.<sup>83</sup> The table below shows the details of the program from FY 2006 to 2012.<sup>84</sup>

	2006	2007	2008	2009	2010	2011 <sup>85</sup>	2012	2013
Cases Received	4,295	2,751	3,704	5,678	7,577	7,471	8,634	—
No. of paid Awards	220	227	198	110	97	97	128	122
Collections > \$2 m	NA	12	8	5	9	4	12	6
Awards Paid (m)	\$24	\$14	\$22	\$6	\$19	\$8	\$125	\$53
Taxes Collected (m)	\$259	\$182	\$156	\$206	\$465	\$48	\$592 <sup>86</sup>	\$367

The US Government Accountability Office has issued a report with recommendations to improve the processes and outcomes of the Whistleblower Office.<sup>87</sup> The proposed changes include the tracking of processing time to reduce delays in awards, enhancing communication with whistleblowers, improving the robustness of criteria for the determinations of awards and detailed reporting to Congress on the progress. While the aggregate revenue yield may appear to be negligible relative to the size

<sup>82</sup> §7623(b) of the *US Inland Revenue Code* was created by the s 406 of the *Tax Relief and Health Care Act of 2006*, 26 USC tit 1 (PL 109-432).

<sup>83</sup> *US Inland Revenue Code*, *ibid*, §7623(b). See also §7623(a): Awards are given at the discretion of the IRS where the sums fall below this threshold.

<sup>84</sup> See US Internal Revenue Service, *Fiscal Year 2010 Report to the Congress on the Use of Section 7623*, online: Internal Revenue Service <[http://www.irs.gov/pub/whistleblower/annual\\_report\\_to\\_congress\\_fy\\_2010.pdf](http://www.irs.gov/pub/whistleblower/annual_report_to_congress_fy_2010.pdf)>; US Internal Revenue Service, *Fiscal Year 2012 Report to the Congress on the Use of Section 7623*, online: Internal Revenue Service <[http://www.irs.gov/pub/whistleblower/2012%20IRS%20Annual%20Whistleblower%20Report%20to%20Congress\\_mv.pdf](http://www.irs.gov/pub/whistleblower/2012%20IRS%20Annual%20Whistleblower%20Report%20to%20Congress_mv.pdf)>.

<sup>85</sup> See US Internal Revenue Service, *Fiscal Year 2011 Report to the Congress on the Use of Section 7623*, online: Internal Revenue Service <[http://www.irs.gov/pub/irs-utl/fy2011\\_annual\\_report.pdf](http://www.irs.gov/pub/irs-utl/fy2011_annual_report.pdf)>.

<sup>86</sup> The large jump in 2012 was due to the US\$104 million payout to Mr Bradley Birkenfeld for his information on UBS AG.

<sup>87</sup> US Government Accountability Office, *Tax Whistleblowers: Incomplete Data Hinders IRS's Ability to Manage Claim Processing Time and Enhance External Communication (GAO-11-683)*, online: US Government Accountability Office <<http://www.gao.gov/new.items/d11683.pdf>>.

of the tax gap, it is submitted that the existence of such a facility has beneficial indirect benefits. An additional source of informational supply to the tax authority may restore a healthier level of fear in the purveyors and purchasers of tax planning schemes.

Singapore has a similar scheme for whistleblowers to come forward with information that leads to the recovery of tax. The reward is 15% on the tax recovered, capped at \$100,000.<sup>88</sup> The UK has yet to establish a comprehensive whistleblowing program. Currently, HMRC has a whistleblowing hotline although the reward given is at HMRC's discretion.<sup>89</sup>

## B. *International Tax Gap Reduction*

Tax evasion assumes greater dimensions with globalisation. The opportunities for tax evasion have increased with the mobility of capital. The complexity of cross-border transactions make it increasingly difficult for tax authorities to identify and monitor.<sup>90</sup> In some countries, international tax evasion contributes a significant portion of the tax gap.<sup>91</sup> Under an established rule in private international law, it is considered to be contrary to public policy and sovereignty for a country to assist another in the direct or indirect enforcement of the latter's revenue claims.<sup>92</sup> There has been limited success in judicial attempts to restrict the operation of this rule.<sup>93</sup>

The continued fragility that permeates the global economy makes it imperative for tax administrations to enhance their cooperation to tackle the causes of tax gaps. In recent years, there has also been a marked increase in the sharing of best practices among national tax administrations to improve the quality of tax administration and customer services that is essential to foster high levels of voluntary compliance.<sup>94</sup>

### 1. *Exchange of Information ("EOI")*

In 2008, international tax cooperation changed dramatically when the G20 nations and the OECD Global Forum on Transparency and Exchange of Information for Tax Purposes ("Global Forum") set out to secure the widespread global adoption of the

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<sup>88</sup> See Inland Revenue Authority of Singapore, *Report Tax Evasion or Fraud*, online: Inland Revenue Authority of Singapore <<http://www.iras.gov.sg/irashome/page.aspx?id=6510>>.

<sup>89</sup> UK, Her Majesty's Revenue and Customs, *Protecting Tax Revenues 2009*, *supra* note 43 at 14, 15. See also UK, Her Majesty's Revenue and Customs, *Tax Compliance*, online: Her Majesty's Revenue and Customs <<http://www.hmrc.gov.uk/tax-evasion/faqs.htm>>.

<sup>90</sup> Shome, *supra* note 4 at 40.

<sup>91</sup> See Rifkin, *supra* note 6 at 391.

<sup>92</sup> *Government of India, Ministry of Finance (Revenue Division) v Taylor* [1955] 1 AC 491 (HL).

<sup>93</sup> See exceptions to this rule in Philip Baker, "Transnational Enforcement of Tax Liabilities" in Robert Langston, *Tolley's International Tax Planning 2008-09* (London: LexisNexis, 2008) at c 21. See also *In re State of Norway's Application* [1990] 1 AC 723 (HL).

<sup>94</sup> See OECD, Press Release, "Tax: 7th meeting of the Forum on Tax Administration 'Strengthening Tax Compliance through Cooperation'" (19 January 2012) online: OECD <<http://www.oecd.org/newsroom/tax7thmeetingoftheforumontaxadministrationstrengtheningtaxcompliancesthroughcooperation.htm>>. The forum brought together the heads of tax administrations from 43 countries.

OECD's EOI standards.<sup>95</sup> At present, the Global Forum has 123 members.<sup>96</sup> The primary aim of EOI is to facilitate the exchange between tax authorities of information relating to the tax base of their respective residents to prevent the frustration of domestic tax laws of contracting states. The scope and mechanism for EOI is subject to the agreed safeguards for privacy and the domestic interests of the requested state.<sup>97</sup>

Ongoing peer reviews by the Global Forum will ascertain the adequacy of national regulatory frameworks and their implementation processes.<sup>98</sup> To preserve a level playing field, the Global Forum has also extended invitations to selected non-member countries.<sup>99</sup> Shortcomings identified in peer reports on several jurisdictions are being addressed.<sup>100</sup> The peer reviews are divided into two stages. In Phase 1, the review is concerned with the substantive legal and regulatory framework governing EOI in a given jurisdiction. In Phase 2, the procedural issues relating to the implementation of an EOI framework will be evaluated. At present, there are 150 peer reviews, of which 79 are Phase 1 reviews, 45 are Phase 2 reviews, and 26 are combined Phase 1 and 2 reviews.<sup>101</sup>

The massive success of the Global Forum's efforts can be seen in the adoption rate of the new EOI standards in the short time between the Washington G20 Summit in November 2008 and August 2011. The number of Double Taxation Agreements ("DTAs")/Tax Information Exchange Agreements ("TIEAs") updated or inked rocketed by more than 15 times from 44 to 712.<sup>102</sup> Unlike in 2009, most jurisdictions surveyed by the Global Forum in 2012 have substantially implemented the EOI standard.<sup>103</sup>

However, the effectiveness of EOI is subject to numerous operational and practical limitations. First, as the Global Forum itself acknowledges, there remains a need to provide technical assistance to some developing countries and smaller jurisdictions to overcome capacity constraints in meeting the international standard for EOI on

<sup>95</sup> See OECD, *The Global Forum on Transparency and Exchange of Information for Tax Purposes, Statement of Outcomes*, online: OECD <<http://www.oecd.org/tax/transparency/ENG%20Jakarta%20Statement%20of%20Outcomes.pdf>> [*OECD November 2013 Statement of Outcomes*].

<sup>96</sup> See OECD, *The Global Forum on Transparency and Exchange of Information for Tax Purposes, Tax Transparency 2014 Report on Progress*, at Annex 6, online: <<http://www.oecd.org/tax/transparency/GFannualreport2014.pdf>> [*OECD Tax Transparency 2014 Report*].

<sup>97</sup> OECD, *Model Tax Convention with respect to Taxes on Income and on Capital*, art 26(1); *OECD November 2013 Statement of Outcomes*, *supra* note 95 at 17.

<sup>98</sup> *Ibid* at 14, Annex IV. Nearly 200 reviews were concluded by 2014. See Exchange of Information Portal, *Schedule of Reviews*, online: Exchange of Information Portal <<http://www.eoi-tax.org/keydocs/schedule-of-reviews#y2012>>, for a schedule of national reviews over 2 phases.

<sup>99</sup> See *OECD November 2013 Statement of Outcomes*, *supra* note 95 at 2.

<sup>100</sup> OECD, *The Global Forum on Transparency and Exchange of Information for Tax Purposes, Statement of Outcomes*, online: OECD <<http://www.oecd.org/tax/transparency/ENG%20Jakarta%20Statement%20of%20Outcomes.pdf>> at paras 10, 11 [*OECD October 2014 Statement of Outcomes*].

<sup>101</sup> *OECD Tax Transparency 2014 Report*, *supra* note 96 at para 12.

<sup>102</sup> *OECD November 2013 Statement of Outcomes*, *supra* note 95 at 24, Annex IX.

<sup>103</sup> In 2009, 36 tax havens and 8 financial centres had not implemented the international standards. 4 jurisdictions were not committed to the international standards: see OECD, *A Progress Report on the Jurisdictions Surveyed by the OECD Global Forum in Implementing the Internationally Agreed Tax Standard*, online: OECD <<http://www.oecd.org/ctp/42497950.pdf>>. By 2014, the situation had changed dramatically: see *OECD Tax Transparency 2014 Report*, *supra* note 96 at 32.

request.<sup>104</sup> Programmes designed for this purpose include drafting of guidelines, training, pilot projects and platforms for national tax authorities to share their best practices.<sup>105</sup>

Second, the terms of exchange of information by request presupposes that requesting states are in possession of basic information relating to the existence or identity of the taxpayers whose income they seek to impose tax.

Third, information sought may be refused by the requested state on grounds that the disclosure is contrary to public policy or prohibited by law. In particular, information may be protected from disclosure if it is subject to legal privilege (“LP”). While communications between clients and legal advisers are generally considered privileged, the precise scope of LP differs between jurisdictions. For instance, in the UK, information given in the course of obtaining tax advice from accountants,<sup>106</sup> as well as communications between third parties and lawyers in cases where there is no independent input, are not protected. Communications made to an in-house counsel for legal advice is likewise not privileged within the European Community.<sup>107</sup> The scope of LP is slightly different in Singapore and Australia. In Australia, privilege is extended to communications made by third parties, provided that it was made for the dominant purpose of giving legal advice.<sup>108</sup> In Singapore, there is authority that as long as accountants were employed to produce information to be channelled to an external lawyer for the purposes of litigation, the information would be privileged.<sup>109</sup>

In the near future, international tax transparency is set to be further bolstered by the automatic exchange of information (“AEOI”) between sovereign authorities. This remarkable step was triggered by intergovernmental implementation of the US Foreign Account Tax Compliance Act,<sup>110</sup> which inspired the OECD to develop and release a new single standard for AEOI (the “AEOI Standard”) on 15 July 2014.<sup>111</sup>

Strongly endorsed by the G20 nations in September 2014, a total of 89 Global Forum member jurisdictions have thus far committed to implementing the AEOI Standard.<sup>112</sup> First exchanges are scheduled to commence in 2017-2018.<sup>113</sup> It is the stated aim of the AEOI Standard to simplify the process for information exchange, raise effectiveness, and lower compliance costs for all stakeholders concerned.<sup>114</sup> Further, in recognition of the constraints faced by developing countries, the Global

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<sup>104</sup> OECD October 2014 Statement of Outcomes, *supra* note 100 at 24; OECD November 2013 Statement of Outcomes, *supra* note 95 at paras 10, 11.

<sup>105</sup> *Ibid.*

<sup>106</sup> *R (Prudential plc) v Special Commissioner of Income Tax* [2010] EWCA Civ 1094 at paras 72, 83 (CA).

<sup>107</sup> *Akzo Nobel Chemicals Ltd v Commission of the European Communities* [2011] 2 AC 338 (Court of Justice of the European Union).

<sup>108</sup> *Pratt Holdings Pty Ltd v Commissioner of Taxation* [2004] 207 ALR 217 (FC).

<sup>109</sup> *Skandinaviska Enskilda Banken AB (Publ), Singapore Branch v Asia Pacific Breweries (Singapore) Pte Ltd* [2007] 2 SLR 367 at paras 36, 52 (CA).

<sup>110</sup> See the discussion on the Foreign Account Tax Compliance Act at Part III(B)(3) of this paper.

<sup>111</sup> OECD, Centre for Tax Policy and Administration, *Automatic Exchange of Financial Account Information—Background Information Brief*, (Paris: OECD, 2014).

<sup>112</sup> OECD November 2013 Statement of Outcomes, *supra* note 95 at para 5.

<sup>113</sup> *Ibid.*

<sup>114</sup> OECD, *Standard for Automatic Exchange of Financial Account Information in Tax Matters*, (Paris: OECD, 2014) at para 9.

Forum will, together with the World Bank Group and other financial organisations, aid these nations in implementing the AEOI Standard.<sup>115</sup> Ultimately, the AEOI scheme, described as a “step change” in tax transparency, facilitates the timely exchange of information even if tax administrations have had no previous indications of non-compliance.

In addition, eighty-four countries, including Singapore, have signed the Convention on Mutual Administrative Assistance in Tax Matters (“CMAATM”).<sup>116</sup> The CMAATM is a multilateral instrument to implement the AEOI Standard.<sup>117</sup> In addition to AEOI, signatories to the CMAATM are obliged to provide spontaneous exchanges of information, conduct simultaneous examinations, perform tax examinations abroad, assist in the recovery of tax claims and measures of conservancy.<sup>118</sup>

Besides the OECD EOI framework, the EU Savings Directive is worth a mention. It mandates automatic EOI between member states on interest payments from a paying agent in one state to the beneficial owner in the other.<sup>119</sup> EU members who opt out of EOI are required to impose a withholding tax on the interest earned and transfer 75% of the tax revenue collected to the resident state of the beneficial owner.<sup>120</sup> These rules have been strengthened by a revised Savings Directive passed on 24 March 2014 based on a review of the directive conducted since 2008, which is expected to be transposed by member states into national rules by January 2016.<sup>121</sup>

On 15 December 2014, the European Council adopted a directive to implement the global AEOI Standard developed by the OECD within the EU, namely

<sup>115</sup> *OECD November 2013 Statement of Outcomes*, *supra* note 95 at para 6.

<sup>116</sup> The CMAATM is the product of collaboration between the OECD and the Council of Europe in 1988 and as amended by Protocol in 2010. See OECD, *Convention on Mutual Administrative Assistance in Tax Matters* online: OECD <<http://www.oecd.org/ctp/exchange-of-tax-information/conventiononmutualadministrativeassistanceintaxmatters.htm>>. See also OECD, *Jurisdictions Participating in the Convention on Mutual Administrative Assistance in Tax Matters: Status—1 June 2015*, online: OECD <[http://www.oecd.org/ctp/exchange-of-tax-information/Status\\_of\\_convention.pdf](http://www.oecd.org/ctp/exchange-of-tax-information/Status_of_convention.pdf)>.

<sup>117</sup> See Elvinger, Hoss & Prussen, *Luxembourg Ratifies the Multilateral Convention on Mutual Administrative Assistance in Tax Matters*, online: Elvinger, Hoss & Prussen: <<http://www.ehp.lu/legal-topics/newsletters-and-alerts/newsletter-detail/article/luxembourg-ratifies-the-multilateral-convention-on-mutual-administrative-assistance-in-tax-matters/>>.

<sup>118</sup> *Convention on Mutual Administrative Assistance in Tax Matters*, 1 June 2011, Articles 4-10, online: OECD <<http://www.oecd.org/ctp/exchange-of-tax-information/ENG-Amended-Convention.pdf>>.

<sup>119</sup> See EC, *Council Directive 2003/48/EC of 3 June 2003 on taxation of savings income in the form of interest payments*, [2003] OJ, L 157/83. See European Commission Taxation and Customs Union, *Rules Applicable*, online: European Commission <[http://ec.europa.eu/taxation\\_customs/taxation/personal\\_tax/savings\\_tax/rules\\_applicable/index\\_en.htm](http://ec.europa.eu/taxation_customs/taxation/personal_tax/savings_tax/rules_applicable/index_en.htm)>.

<sup>120</sup> Initially, Belgium, Austria and Luxembourg opted to levy a withholding tax. The current applicable rate is 35%. On 1 January 2010, Belgium adopted the automatic exchange of information regime. Luxembourg did the same from 1 January 2015: see William H Byrnes IV, “2014 Expanded EU Savings Directive Adoption Announced” *LexisNexis Legal Newsroom: Tax Law* (25 March 2014), online: LexisNexis <<http://www.lexisnexis.com/legalnewsroom/tax-law/b/fatcentral/archive/2014/03/25/2014-expanded-eu-savings-directive-adoption-announced.aspx>>. Without a sunset clause, an EU-wide automatic exchange is not possible until Austria and Switzerland accept automatic exchange of information.

<sup>121</sup> EC Taxation and Customs Union, *Revised Savings Taxation Directive*, online: European Commission <[http://ec.europa.eu/taxation\\_customs/taxation/personal\\_tax/savings\\_tax/revised\\_directive/index\\_en.htm](http://ec.europa.eu/taxation_customs/taxation/personal_tax/savings_tax/revised_directive/index_en.htm)>. The main changes were implemented to address tax avoidance.



the Competent Authority Agreement (“CAA”) and the Common Reporting Standard (“CRS”).<sup>122</sup> This move will significantly extend the scope of the current AEOI in the EU to cover new categories of income and capital. Also, given the wide scope of income and capital covered by the directive, there is a possibility that the Savings Directive may be repealed in the future due to the resulting legislative overlaps.<sup>123</sup>

## 2. *Bilateral withholding tax agreements*

In this respect, the developments in Switzerland merit a special mention. Since March 2009, Switzerland has amended many of their DTAs to comply with the new EOI standards.<sup>124</sup> As at August 2014, forty-one DTAs with an extended administrative assistance clause and three TIEAs were in force.<sup>125</sup> What is most interesting, however, is the emergence of an alternative to these EOIs—the Rubik Model Agreement.

The Rubik Model Agreement, named after the famous puzzle, was proposed by the Swiss Bankers Association in 2010. It seeks, *inter alia*, to recover unpaid taxes by one-off payments as well impose withholding taxes on future investment income and capital gains. These agreements were entered into by Switzerland with Germany and the UK in August 2011,<sup>126</sup> followed by a similar agreement with Austria in April 2012. On 7 November 2012, a negotiations mandate was adopted by the Greek and Swiss governments to discuss the possibility of a fiscal agreement between the two nations.<sup>127</sup> Further, the Hungarian government announced in 2013 that it intends to negotiate a Rubik Model Agreement with Switzerland.<sup>128</sup> There have been no further developments since.

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<sup>122</sup> EC, *Commission Implementing Regulation (EU) No 1353/2014 of 15 December 2014 amending Implementing Regulation (EU) No 1156/2012 laying down detailed rules for implementing certain provisions of Council Directive 2011/16/EU on administrative cooperation in the field of taxation*, [2014] OJ, L 365/70.

<sup>123</sup> EC, *Automatic Exchange of Information: Frequently Asked Questions*, online: European Commission <[http://europa.eu/rapid/press-release\\_MEMO-14-591\\_en.htm](http://europa.eu/rapid/press-release_MEMO-14-591_en.htm)>.

<sup>124</sup> See Switzerland Federal Department of Finance, *The requirements for administrative assistance in tax matters should be revised*, at 4, online: News Portal of the Federal Administration <<http://www.news.admin.ch/NSBSubscriber/message/attachments/22119.pdf>>.

<sup>125</sup> See Switzerland State Secretariat for International Financial Matters, *Double Taxation and Administrative Assistance*, online: SIF <<https://www.sif.admin.ch/sif/en/home/themen/internationale-steuerpolitik/doppelbesteuerung-und-amtshilfe.html>>.

<sup>126</sup> Switzerland Federal Department of Finance, *Switzerland and Germany initial tax agreement*, online: Federal Department of Finance <<http://www.efd.admin.ch/aktuell/medieninformation/00462/index.html?lang=en&msg-id=40533>>; Switzerland Federal Department of Finance, *Switzerland and the UK initial tax agreement*, online: Federal Department of Finance <<http://www.efd.admin.ch/aktuell/medieninformation/00462/index.html?lang=en&msg-id=40731>>. See also UK Her Majesty’s Revenue and Customs, *UK-Swiss Confederation: Taxation Cooperation Agreement*, online: UK Government <<https://www.gov.uk/government/publications/uk-swiss-confederation-taxation-co-operation-agreement/uk-swiss-confederation-taxation-co-operation-agreement>>.

<sup>127</sup> Klonis Bonadio Bonadio, *Withholding tax agreements: the ‘Rubik Agreements’*, online: KBB <<http://www.kbblegal.ch/files/The%20Rubik%20agreements.pdf>>.

<sup>128</sup> See Balázs Békés, “Hungary May Negotiate a Rubik Agreement with Switzerland” *International Tax Review* (1 March 2013), online: International Tax Review <<http://www.internationaltaxreview.com/Article/3160962/Hungary-Hungary-may-negotiate-a-Rubik-agreement-with-Switzerland.html>>.

The payment of the withholding tax (26.375% for Germany, 25% for Austria, and between 27% and 48% for the UK, depending on the nature of the capital income) is deemed to discharge the tax obligations owed to the country of residence. This final withholding tax is levied directly by the Swiss paying agent and preserves the anonymity of the account holder. In addition, these agreements provide for retrospective taxation. A German, Austrian or UK resident may make an anonymous lump-sum tax payment (21% to 41% of the assets in question for German residents, 15% to 38% for Austrian residents, and 19% to 34% for UK residents) or elect to disclose his past fiscal circumstances to the tax authorities.<sup>129</sup> In effect, the agreement permits taxpayers resident in the contracting states (eg Germany, UK, and Austria) to continue depositing their assets anonymously and legally in Swiss banks, subject to the payment of a final withholding tax collected by the Swiss paying agent and paid to the home state of the account holder.

The agreements with Austria and the UK entered into force on 1 January 2013. An upfront payment of CHF 500 million was made to the UK as security for minimum tax revenues to be recovered from anonymous retrospective taxation.<sup>130</sup> The UK was also paid CHF 372 million in July 2013 and a further £469.5 million by August 2014 from retrospective taxation of assets. The agreement with Austria made no provision for an upfront payment. Austria was paid CHF 515 million in the first tranche of payments from the retrospective taxation of assets in July 2013,<sup>131</sup> and another €738.3 million between July 2013 and August 2014.<sup>132</sup> By February 2014, around CHF 21.5 billion of assets had also been disclosed to the UK and Austria.<sup>133</sup> The agreement with Germany was aborted due to the refusal of the German Parliament to ratify the agreement.<sup>134</sup>

<sup>129</sup> Sebastiano Garufi, "FATCA vs. RUBIK: Two models for tax information exchange" *Pragma* (Issue 17—August 2013), online: Pragma <<http://pragma-eu.com/wp/wp-content/uploads/2013/08/FATCA-vs-RUBIK-Two-models-for-tax-information-exchange.pdf>>.

<sup>130</sup> Switzerland Federal Department of Finance, *Withholding tax agreement: Switzerland transfers upfront payment to United Kingdom*, online: Federal Department of Finance <<http://www.efd.admin.ch/dokumentation/medieninformationen/00467/index.html?lang=en&msg-id=47599>>.

<sup>131</sup> Switzerland Federal Department of Finance, *Withholding tax agreements off to a good start: Switzerland transfers first tranche to Austria and the United Kingdom*, online: Federal Department of Finance <<http://www.efd.admin.ch/dokumentation/medieninformationen/00467/index.html?lang=en&msg-id=49751>>.

<sup>132</sup> Ernst & Young Tax Insights, *Switzerland, Austria and United Kingdom: Swiss Federal Tax Administration publishes data on regularization of untaxed assets under agreements with Austria and United Kingdom*, online: Ernst & Young <<http://taxinsights.ey.com/archive/archive-news/switzerland-austria-and-united-kingdom-swiss-federal-tax-administration-publishes-data.aspx>>. Cf UK Commons Select Committee, *HMRC tax collection: Annual Report & Accounts 2012-13: report published*, online: UK Parliament <<http://www.parliament.uk/business/committees/committees-a-z/commons-select/public-accounts-committee/news/hmrc-tax-collection/>>.

<sup>133</sup> Switzerland Federal Department of Finance, *Report on International Financial and Tax Matters 2014*, (Berne: Federal Department of Finance, 2014) at 35, online: Federal Department of Finance <<http://www.efd.admin.ch/dokumentation/00737/00782/02690/index.html?lang=en>>

<sup>134</sup> Klonis Bonadio Bonadio, *supra* note 127. See Birgit Jennen, "Swiss Tax Deal Seen Buried amid Prominent German Cases" *Bloomberg* (18 February 2014), online: Bloomberg <<http://www.bloomberg.com/news/articles/2014-02-17/swiss-tax-deal-seen-buried-after-prominent-german-cases-revealed>>.

On 29 January 2013, Austria and Liechtenstein entered into a similar Rubik Agreement.<sup>135</sup> However, the scope of the Agreement is broader than the Austrian-Swiss Agreement.<sup>136</sup> It extends beyond capital assets of Austrian citizens held in Swiss banks to include those held in Liechtenstein foundations and managed globally by trustees on behalf of Austrian citizens.<sup>137</sup>

While the withholding tax approach has a long-term impact equivalent to the automatic exchange of information, these Rubik Model Agreements have had limited influence on the debate on tax transparency within the EU.<sup>138</sup> This may be due in part to the concurrent international push for the adoption of the AEOI.<sup>139</sup> The nature of the Rubik Model Agreements indubitably exerts a negative influence on the progress of global tax transparency. The commentators who have been critical of Rubik Model Agreements argue that they are “undesirable from a policy perspective in the era of global fiscal transparency.”<sup>140</sup> The uncertain future of Rubik Model Agreement can be seen in the recent amendment to the double taxation agreement between Switzerland and Italy, which allows Italian citizens to regularise their affairs before the AEOI comes into force.<sup>141</sup> This interim measure also contains a Voluntary Disclosure Programme for Italian residents to disclose untaxed assets in exchange for reduced penalties.<sup>142</sup>

### 3. Contractual obligations to share information and withhold tax

Aside from encouraging foreign authorities to disclose information, international tax information exchange could be enhanced by a carrot and stick approach. One such approach is the Qualified Intermediary (“QI”) programme, enacted by the US in 2000. Under the QI programme, foreign financial institutions (“FFIs”) may voluntarily contract with the IRS to assume certain documentation and withholding responsibilities. In exchange, QIs secure for themselves the ability to refrain from disclosing proprietary account holder information to a withholding agent that may be a competitor, without affecting their eligibility for treaty benefits, as well as simplified information reporting for their foreign account holders.<sup>143</sup>

<sup>135</sup> Austrian Federal Ministry of Finance, Press Release, “Tax convention signed with Liechtenstein” (29 January 2013) online: BMF <<https://english.bmf.gv.at/ministry/press/pressreleases2013/january/tax-convention-signed.html>>.

<sup>136</sup> Eleonor Kristoffersson *et al.*, eds, *Tax Secrecy and Tax Transparency* (Frankfurt: PL Academic Research, 2013) at 124.

<sup>137</sup> Austrian Federal Ministry of Finance, *supra* note 135.

<sup>138</sup> See Tracy A Kaye, “Innovations in the War on Tax Evasion” (2014) 2 BYUL Rev 363 at 404.

<sup>139</sup> Samuel Jaberg, Bern, “Decades of Swiss Banking Secrecy Have Left Their Mark” *Swissinfo* (3 February 2015), online: Swissinfo <<http://www.swissinfo.ch/eng/multimedia/-decades-of-swiss-banking-secrecy-have-left-their-mark-/41249784>>.

<sup>140</sup> See Pasquale Pistone, “Exchange of information and Rubik Agreements: the Perspective of an EU Academic” (2013) 67 *Bulletin for International Taxation* 216.

<sup>141</sup> Samuel Jaberg, Bern, *supra* note 139.

<sup>142</sup> The Society of Trust and Estate Practitioners, “Italy and Switzerland Sign Treaty to Prevent Tax Evasion” *STEP* (26 February 2015), online: STEP <<http://www.step.org/italy-and-switzerland-sign-treaty-prevent-tax-evasion>>.

<sup>143</sup> US Government Accountability Office, *Tax Compliance: Qualified Intermediary Program Provides Some Assurance That Taxes on Foreign Investors Are Withheld and Reported, but Can Be Improved (GAO-08-99)* (Washington, DC: GAO, 2007) at 10, 11. See also US Inland Revenue Service, *Qualified*

In a bid to further combat offshore tax evasion, the US also enacted the Foreign Account Tax Compliance Act (“FATCA”) in March 2010, which generally requires US taxpayers holding foreign financial assets exceeding US\$50,000 to report information about those assets to the IRS.<sup>144</sup> Under FATCA, FFIs may register with the IRS and agree to report information about financial accounts held by these US taxpayers thereto, upon which they may be required to withhold 30% on certain payments to foreign payees that do not comply with FATCA.<sup>145</sup> An FFI that fails to register and agree to report such information to IRS will face a 30% withholding tax on certain US-sourced payments made to them, unless otherwise exempted. To this end, the conclusion of a QI agreement by an FFI does not qualify as an exemption from the FATCA.<sup>146</sup> The FFIs subject to these requirements include, *inter alia*, banks, mutual funds, hedge funds, private equity funds and certain insurance companies that have cash value products or annuities.<sup>147</sup>

In order to reduce the burden imposed by the FATCA on each FFI operating within a jurisdiction, as well as to remove the domestic legal impediments to compliance, a country may sign an Inter-Governmental Agreement (“IGA”) with the US. These IGAs contemplate that the partner government will require all the FFIs located in that jurisdiction to identify US accounts and to report information relating to these accounts to the IRS. There are 2 models of IGAs. Model 1 envisions that the FFI would report its information to a partner government, who would be responsible for transmission of the information to the IRS, usually on an automatic basis. Model 2 requires a partner government to facilitate the direct reporting of the account information by all FFIs located in its jurisdiction to the IRS.<sup>148</sup>

Currently, 55 countries have concluded and signed bilateral IGAs with the US. Of these, 48 have implemented Model 1, while 7 have implemented Model 2.<sup>149</sup> Further, there are another 57 countries that have reached an agreement in substance with the US as of end 2014. Of these, 50 have opted for Model 1, while 7 have opted for Model 2.<sup>150</sup>

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*Intermediary FAQ*, online: Internal Revenue Service <<http://www.irs.gov/Businesses/International-Businesses/Qualified-Intermediary-Frequently-Asked-Questions>>.

<sup>144</sup> US Internal Revenue Service, *FATCA Information for Individuals*, online: Internal Revenue Service <<http://www.irs.gov/Businesses/Corporations/FATCA-Information-for-Individuals>>.

<sup>145</sup> US, The Joint Committee on Taxation, *Technical Explanation of the Revenue Provisions Contained in Senate Amendment 3310, The ‘Hiring Incentives to Restore Employment Act,’ under Consideration by the Senate (JCX-4-10)* (Washington, DC: JCT, 2010) at 42. See also US Internal Revenue Service, *FATCA Information for Foreign Financial Institutions and Entities*, online: Internal Revenue Service <<http://www.irs.gov/Businesses/Corporations/Information-for-Foreign-Financial-Institutions>>.

<sup>146</sup> US, The Joint Committee on Taxation, *ibid* at 42.

<sup>147</sup> Singapore, Inland Revenue Authority of Singapore, *Foreign Account Tax Compliance Act FAQ*, online: Inland Revenue Authority of Singapore <[http://www.iras.gov.sg/irashome/uploadedFiles/Quick\\_Links/Tax\\_treaties/FATCA%20FAQs%20-%20F.pdf](http://www.iras.gov.sg/irashome/uploadedFiles/Quick_Links/Tax_treaties/FATCA%20FAQs%20-%20F.pdf)>.

<sup>148</sup> US Internal Revenue Service, *FATCA Information for Governments*, online: Internal Revenue Service <<http://www.irs.gov/Businesses/Corporations/FATCA-Governments>>.

<sup>149</sup> US Department of the Treasury, *Resource Center: FATCA—Archive*, online: <<http://www.treasury.gov/resource-center/tax-policy/treaties/Pages/FATCA-Archive.aspx>>.

<sup>150</sup> *Ibid*.

In Singapore, the government signed a Model 1 IGA on 9 December 2014.<sup>151</sup> The Income Tax Act<sup>152</sup> was amended to empower the Minister to declare this IGA as an international tax compliance agreement and to implement Singapore's obligations thereunder.<sup>153</sup> Specifically, "reporting Singaporean financial institutions"<sup>154</sup> in Singapore must provide the information requested by the Comptroller for the purposes of complying with FATCA.<sup>155</sup> A failure to comply attracts criminal liability.<sup>156</sup>

### C. Effective use of Penalties

Penalties advance the equity of the tax system. It promotes voluntary compliance as it reinforces the cost of non-compliance. They impose tangible economic consequences on taxpayers who use or intermediaries who promote abusive transactions. Where the risks of detection are real and the costs of the consequences are sufficiently high, penalties can generate a valuable deterrence effect on future abuses.

New Zealand, for example, imposes a penalty computed based on a percentage of the shortfall (also known as a shortfall penalty). These penalties apply to most taxes and duties except child support payments. There are five categories of breach, from the lack of reasonable care which results in a penalty of 20% of the shortfall, to adopting abusive tax positions or evasion which result in a penalty of 100% and 150% respectively.<sup>157</sup>

#### 1. Role of tax intermediaries as suppliers of tax avoidance schemes

It has been pointed out that as long as "the tax-avoidance game represents the triumph of technical proficiency", those who devise them to outwit the taxman would argue that "shareholder value...demands no less."<sup>158</sup> If tax is regarded as no more than a price to pay for participation in a civilised society, the provision of tax planning services by tax intermediaries may arguably be justified as a natural market response to the forces of demand and supply.<sup>159</sup> Yet, the negative externalities created by aggressive tax planning schemes cannot be ignored.

<sup>151</sup> Singapore and United States, *Agreement between the Government of the Republic of Singapore and the Government of the United States of America to Improve International Tax Compliance and to Implement FATCA*, online: <[https://www.iras.gov.sg/irashome/uploadedFiles/IRASHome/Quick\\_Links/International\\_Tax/FATCA-Singapore\\_IGA.pdf](https://www.iras.gov.sg/irashome/uploadedFiles/IRASHome/Quick_Links/International_Tax/FATCA-Singapore_IGA.pdf)>.

<sup>152</sup> *Income Tax Act* (Cap 134, 2014 Rev Ed Sing) [*Singapore Income Tax Act*].

<sup>153</sup> *The Income Tax (Amendment) Act 2013* (No 19 of 2013) came into effect on 5 November 2013. See *Singapore Income Tax Act*, ss 105I-105Q.

<sup>154</sup> *Singapore Income Tax Act*, s 105P; *Income Tax (International Tax Compliance Agreements) (United States of America) Regulations 2015* (S 134/2015 Sing), reg 4.

<sup>155</sup> *Singapore Income Tax Act*, ss 105N, 105L and 105MA.

<sup>156</sup> *Singapore Income Tax Act*, s 105M.

<sup>157</sup> See New Zealand Inland Revenue, *Shortfall Penalties*, online: Inland Revenue <<http://www.ird.govt.nz/how-to/debt/penalties/shortfall-penalties/>>; <<http://www.ird.govt.nz/how-to/debt/penalties/shortfall-penalties/sf-penalty-what.html>>.

<sup>158</sup> "The Price of Tax Avoidance" *The Guardian* (2 February 2009), online: The Guardian <<http://www.theguardian.com/commentisfree/2009/feb/02/tax-gap-series-avoidance>>.

<sup>159</sup> *Compañía General De Tabacos De Filipinas v Collector of Internal Revenue*, 275 US 87 at 100 (1927) (Oliver Wendell Holmes J (dissenting)).

The OECD recognises the need for tax administrations to address the role of tax intermediaries on the supply side of tax planning and avoidance.<sup>160</sup> In this regard, several countries have enacted statutory provisions to deal with the role of promoters of tax avoidance schemes. In relation to tax avoidance, the new approach targets prevention, early detection and counteraction. In the last decade, countries such as Australia, Canada, New Zealand, South Africa, the UK and the USA have introduced laws that oblige tax promoters or agents to report transactions that bear prescribed ‘hallmarks’. Some of the more common ‘hallmarks’ include:

- transactions for which the fee payable to the promoter is partly or wholly contingent on the tax benefits to be obtained,<sup>161</sup>
- transactions that contain arrangements that have indicators that are significantly similar to those that fall foul of general anti-avoidance legislation for the lack of substance,<sup>162</sup>
- transactions that are blacklisted by tax authorities as being unacceptable tax avoidance schemes,<sup>163</sup> and
- transactions in which confidentiality undertakings against other promoters or the tax authority exist.<sup>164</sup>

An interesting feature of reportable obligations on promoters can be found in the UK report on “Tackling Tax Avoidance”.<sup>165</sup> One of the key components of this strategy involves an enhancement of its tax disclosure regime. The Disclosure of Tax Avoidance Schemes (“DOTAS”) legislation requires the promoter of a bespoke or generic tax avoidance scheme that bears certain hallmarks to disclose the arrangement to the HMRC within 5 days if it involves an arrangement, including any scheme, transaction or series of transactions, that is expected to procure a tax advantage for any person.<sup>166</sup>

One of the hallmarks of a tax avoidance scheme that must be disclosed is one subject to confidentiality undertakings between the promoter and the user of the scheme. In such cases, the regulation abrogates the contractual obligation as the promoter or scheme user is required to disclose the scheme to HMRC.<sup>167</sup> The only area where confidentiality prevails is where legal professional privilege applies.

<sup>160</sup> OECD, *Study into the Role of Tax Intermediaries*, *supra* note 24 at 18-21.

<sup>161</sup> *Income Tax Act*, 1962, (S Afr) No 58 of 1962, ss 80M-80T [*South Africa Income Tax Act*].

<sup>162</sup> For transactions entered into after 2010, see *Income Tax Act*, RS C 1985, c 1 (5th Supp), s 237.3.

<sup>163</sup> See US Internal Revenue Service, *Internal Bulletin No 2009-31: Notice 2009-59*, online: Internal Revenue Service <[http://www.irs.gov/irb/2009-31\\_IRB/ar07.html](http://www.irs.gov/irb/2009-31_IRB/ar07.html)>. There are currently 34 ‘listed transactions’ and 4 ‘transactions of interest’.

<sup>164</sup> UK, Her Majesty’s Revenue and Customs, *Guidance: Disclosure of Tax Avoidance Schemes*, (London: HMRC, 2013) at 32, online: Her Majesty’s Revenue and Customs <[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/341960/dotas-guidance.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/341960/dotas-guidance.pdf)>.

<sup>165</sup> See UK, Her Majesty’s Treasury, *Tackling Tax Avoidance*, (London: HM Treasury, 2011) at 2, online: Her Majesty’s Treasury <[http://cdn.hm-treasury.gov.uk/2011budget\\_taxavoidance.pdf](http://cdn.hm-treasury.gov.uk/2011budget_taxavoidance.pdf)>.

<sup>166</sup> *Finance Act 2004* (UK), c 12, ss 306-319. The duty to notify HMRC falls on the taxpayer if the promoter is a non-resident of the UK or if the promoter believes that the information is subject to legal privilege.

<sup>167</sup> *The Tax Avoidance Schemes (Prescribed Descriptions of Arrangements) Regulations 2006*, SI 2006/1543, regs 6, 7.

However, if the lawyer is ‘marketing’ the scheme, the lawyer may not be entitled to claim legal privilege.<sup>168</sup>

When introduced in 2004, the scope of DOTAS was confined to schemes concerning employment or financial products and some VAT products. Subsequently, it was widened to include income tax, corporation tax and capital gains tax. As it proved to be highly successful, DOTAS was further extended to national insurance contributions, stamp land duty tax and inheritance tax.<sup>169</sup> In 2013, DOTAS was also extended to a newly introduced Annual Tax on Enveloped Dwellings (“ATED”), a tax payable by entities that own properties.<sup>170</sup>

The failure to comply with the requirements of the DOTAS attracts penalties. Each disclosed scheme is tagged with a scheme reference number (“SRN”). From 2010, every promoter must furnish the HMRC periodically with full details concerning clients to whom SRNs have been issued.<sup>171</sup> HMRC reports that the total number of disclosures for direct and indirect taxes has increased by about 10 times from August 2004 to April 2010.<sup>172</sup> Since April 2006 to March 2013, 821 schemes have been disclosed under the main regime. This legislation has closed off £12 billion in avoidance opportunities between 2004 and 2009.<sup>173</sup>

Another pillar of the UK strategy involves a reinforcement of its legislative and operational powers to make immediate changes to revenue legislation to defeat tax avoidance schemes that have been identified. Briefly, the “Protocol on unscheduled announcement to changes in tax law” sets out the process and criteria for the exercise of Ministerial power to effect changes in tax legislation before the final amending legislation comes into force. Briefly, a Written Ministerial Statement outside a scheduled fiscal event may be made in situations where: (1) there would otherwise be significant risk to the Exchequer; (2) significant new information has emerged to identify the risk or indicate its scale; and (3) changing the law immediately would prevent significant losses to the Exchequer.<sup>174</sup> Given the wide ranging powers, HMRC has reiterated its commitment to strike a balance between the need for stability in the tax system and allowing decisive action when risks to the Exchequer have been identified. In particular, it reassured the public that changes would generally be confined to specific risks and any retroactive changes to a date earlier than an announcement date would be “wholly exceptional”.<sup>175</sup>

<sup>168</sup> UK, Her Majesty’s Revenue and Customs, *Disclosure of Tax Avoidance Schemes: Guidance November 2013*, online: Her Majesty’s Revenue and Customs <[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/341960/dotas-guidance.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/341960/dotas-guidance.pdf)>.

<sup>169</sup> See UK, Her Majesty’s Revenue and Customs, *Tax Avoidance and Disclosure Statistics*, online: Her Majesty’s Revenue and Customs <<http://www.hmrc.gov.uk/avoidance/avoidance-disclosure-statistics.htm>>.

<sup>170</sup> UK, Her Majesty’s Revenue and Customs, *Disclosure of Tax Avoidance Schemes (DOTAS) Regime and the Annual Tax on Enveloped Dwellings (ATED): Draft regulations and Taxes Information and Impact Note*, online: Chartered Institute of Taxation <<http://www.tax.org.uk/Resources/CIOT/Documents/2013/07/DOTAS%20dotas-ated-tech-note.pdf>>.

<sup>171</sup> *Finance Act 2010* (UK), c 13, sch 17, cl 6.

<sup>172</sup> See UK, Her Majesty’s Revenue and Customs, *Tax avoidance and disclosure statistics*, *supra* note 169.

<sup>173</sup> See UK, Her Majesty’s Treasury, *Budget 2010: Securing the Recovery* (London: The Stationery Office Limited, 2010) at 78, online: <[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/247878/0451.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/247878/0451.pdf)>. This accounts for about one-third of the tax gap.

<sup>174</sup> UK, Her Majesty’s Treasury, *Tackling Tax Avoidance*, *supra* note 165 at 17–20.

<sup>175</sup> *Ibid* at 17.

In addition to reporting obligations, most of these countries provide for the imposition of penalties on tax promoters in prescribed circumstances. For example, New Zealand provides for a promoter penalty equal to the tax shortfalls resulting from the taking of an abusive tax position on an arrangement for which the promoter would have been liable to a penalty if he were a party to that arrangement.<sup>176</sup> In Australia, promoter penalty laws came into effect in 2006.<sup>177</sup> These laws empower the Commissioner to apply to the Federal Court to impose a penalty on or grant an injunction against a person who promotes any scheme that avoids or evades tax, or abuses product rulings.

## 2. Tax Amnesty: A disclosure inducement

Tax Amnesty programs are often used by tax authorities to target taxpayers who under-declare their taxable income. It is especially useful in cases involving foreign income where the enforcement powers of the resident tax authority is severely limited. The common inducement offered in exchange for voluntary disclosure of past untaxed income is a significant but temporary reduction in tax liabilities including penalties. The rationale for instituting tax amnesty programs usually involves a pragmatic judgment to forgo the maximum potential tax revenue that has proven to be difficult to enforce with the objective to maximise the current and future revenue collection for a given category of income or taxpayers. The UK House of Lords in a case commonly known as the *Fleet Streets Casuals* case<sup>178</sup> noted that the tax authority's decision to forgo maximum potential taxes in the light of enforcement costs was made for "good management" reasons and ought to be upheld.<sup>179</sup>

The attractiveness of tax amnesty programs is especially high where there is financial pressure to secure an immediate increase in tax revenue that cannot be readily achieved through normal budgetary or enforcement measures.<sup>180</sup> Tax amnesties may also prove to be helpful in improving the overall compliance levels through an enlargement of the taxpayer base.<sup>181</sup> For example, Italy's tax amnesty program reportedly managed to repatriate 98% of illegally-held funds and provided €5bn in additional tax revenue.<sup>182</sup> In January 2012, the US IRS reported significant success with its Offshore Voluntary Disclosure Program ("OVDP").<sup>183</sup> US\$4.4 billion was collected from 33,000 disclosures under the two OVDPs in 2009 and 2011.

<sup>176</sup> *Tax Administration Act 1994* (NZ), 1999/166, s 141EB.

<sup>177</sup> *Taxation Administration Act 1953* (Australia) at Sch 1, Div 290.

<sup>178</sup> *R v Inland Revenue Commissioners, ex p. National Federation of Self Employed and Small Businesses Ltd* [1982] 1 AC 617 (HL).

<sup>179</sup> *Ibid* at 637.

<sup>180</sup> Katherine Baer & Eric Le Borgne, *Tax Amnesties: Theory, Trends, and Some Alternatives* (Washington, DC: International Monetary Fund, 2008) at 1, 2; James Alm, *Tax Policy Analysis: The Introduction of a Russian Tax Amnesty*, Georgia State University, Andrew Young School of Policy Studies, International Studies Program Working Paper 98-6 (1998), online: Georgia State University <<http://icepp.gsu.edu/files/2015/03/ispwp9806.pdf>>.

<sup>181</sup> Baer & Le Borgne, *ibid* at 6; Alm, *ibid* at 4; Elliot Uchitelle, "The Effectiveness of Tax Amnesty Programs in Selected Countries" (1989) FRBNY Quarterly Review 48 at 49.

<sup>182</sup> See "Italian tax amnesty raises 95bn euros" *BBC News* (29 December 2009), online: BBC <<http://news.bbc.co.uk/2/hi/8433762.stm>>.

<sup>183</sup> See US Internal Revenue Service, *IRS Offshore Programs Produce \$4.4 Billion To Date for Nation's Taxpayers; Offshore Voluntary Disclosure Program Reopens*, online: Internal



Responding to strong interest from taxpayers and buoyed by the considerable success, the IRS has reopened a third OVDP with similar features but some key differences in penalty structures. Unlike the first two, there is no formal deadline to submit applications. The success of a tax amnesty is contingent upon a real and credible threat of detection and punishment.<sup>184</sup> The attractiveness of the US OVDPs was clearly boosted by the threat of enhanced enforcement measures under FATCA.<sup>185</sup> If administered judiciously, such programs have the potential to increase the long term compliance rates.

Nevertheless, amnesties have their detractors. Besides doubts on the accuracy of statistics used to measure success, there are also disagreements among economists about the beneficial impact of such programs.<sup>186</sup> Indeed, ill-considered repetitions of tax amnesty programs could create insidious expectations of future programs. At its worst, it could jeopardise the integrity of the tax system and encourage the perception among some taxpayers that tax evasion during the intervening periods could prove to be profitable.<sup>187</sup> Any reduction in perceived fairness of the system may adversely affect the compliance rates of otherwise honest taxpayers.<sup>188</sup> Several studies have provided evidence that additional tax amnesties are likely to produce decreasing yields and discourage future compliance.<sup>189</sup>

For instance, India has implemented at least six Voluntary Disclosure of Income Schemes (“VDIS”).<sup>190</sup> While the absolute number of income disclosures had increased with each scheme, the ratio of VDIS collections to GDP figures in 1997 was only marginally higher than that in the earlier schemes.<sup>191</sup> It is also noteworthy that there was a decline in the percentage of declarants to assessment from 6.8% and 33% respectively in 1975 and 1985 to 3.6% in 1997. There has been no VDIS since 1997. A possible reason could be a realisation that frequent repetition of such schemes may incentivise further tax evasion among some delinquent taxpayers who expect a better deal in the next VDIS.<sup>192</sup>

Revenue Service <[http://www.irs.gov/uac/IRS-Offshore-Programs-Produce-\\$4.4-Billion-To-Date-for-Nation%E2%80%99s-Taxpayers;-Offshore-Voluntary-Disclosure-Program-Reopens](http://www.irs.gov/uac/IRS-Offshore-Programs-Produce-$4.4-Billion-To-Date-for-Nation%E2%80%99s-Taxpayers;-Offshore-Voluntary-Disclosure-Program-Reopens)>.

<sup>184</sup> See Uchitelle, *supra* note 181 at 51.

<sup>185</sup> *Ibid* at 51, 52; See also US Internal Revenue Service, *2012 Offshore Voluntary Disclosure Initiative Frequently Asked Questions and Answers*, online: Inland Revenue Service <<http://www.irs.gov/Individuals/International-Taxpayers/Offshore-Voluntary-Disclosure-Program-Frequently-Asked-Questions-and-Answers>>.

<sup>186</sup> Steven E Crane & Farrokh Nourzad, “Analyzing Income Tax Evasion Using Amnesty Data with Self-Selection Correction: The Case of the Michigan Tax Amnesty Program” in Joel Slemrod, *Why People Pay Taxes: Tax Compliance and Enforcement*, *supra* note 47, 167 at 174.

<sup>187</sup> Baer & Le Borgne, *supra* note 180 at 2, 3; Uchitelle, *supra* note 181 at 49.

<sup>188</sup> Carroll, *supra* note 47 at 47. See also Kristina Murphy, *Procedural Justice, Shame and Tax Compliance*, Australian National University Working Paper 50 (2004) at 1, 2, online: Australian National University <<http://hdl.handle.net/1885/43172>>.

<sup>189</sup> Hari Sharan Luitel & Russell S Sobel, “The Revenue Impact of Repeated Tax Amnesties” (2007) 27 *Public Budgeting & Finance* 19 at 29, 30.

<sup>190</sup> Comptroller and Auditor General of India, *Report of the CAG on the Union Government for the year ended March 1999: Voluntary Disclosure of Income Scheme, 1997*, at Annexure 1.2, online: Comptroller and Auditor General of India <[http://cag.nic.in/reports/d\\_taxes/2000\\_book2/index.htm](http://cag.nic.in/reports/d_taxes/2000_book2/index.htm)>.

<sup>191</sup> See Ministry of Finance, India, *Economic Survey 1997-98*, at 17, online: Ministry of Finance <<http://indiabudget.nic.in/es97-98/chap22.pdf>>.

<sup>192</sup> See *All India Federation of Tax Practitioners v Union Of India* (1998) 231 ITR 24 (SC).

### 3. Shaming offenders

In some countries, an alternative to secure higher voluntary compliance without an attendant increase in administrative costs utilises a different tactic on tax evaders. Publishing the identities and details of tax evasion to direct public resentment at tax evaders can have a significant deterrent effect especially on large corporations and wealthy high-profile individuals. Shaming and public criticism increase the social and financial costs of evasion through the resultant loss of reputation or social standing.<sup>193</sup> However, its effectiveness is the function of the offender's ability to deal with criticism including opportunities to deflect personal responsibility to third parties or the state.<sup>194</sup>

Greece has recently started a program that publishes the names of high profile tax evaders.<sup>195</sup> In the UK, the HMRC publishes information about deliberate tax defaulters if the tax penalties imposed exceed £25,000.<sup>196</sup> The IRS has also been known to publish the names of tax offenders in a bid to shame them.<sup>197</sup> However, strict confidentiality laws in the US may limit the opportunities for the IRS to shame errant taxpayers as freely as it might have desired.<sup>198</sup>

The discretion of a tax authority to freely publish details may also be constrained by the scope of the laws that safeguard taxpayer privacy and confidentiality of tax information. Some jurisdictions have enacted legislation to address the issue. South Africa's income tax laws prohibit disclosure of tax related information except under limited circumstances which includes the publication of identities of some offenders.<sup>199</sup> The UK has also enacted legislation to allow the shaming of offenders under the UK Managing Deliberate Defaulters programme.<sup>200</sup> The Income Tax Department in India is also working on a plan to enable the tax authorities to publish names of tax defaulters on their website, with a view to shame them.<sup>201</sup>

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<sup>193</sup> See Rifkin, *supra* note 6 at 414, 415.

<sup>194</sup> Murphy, *supra* note 188 at 5, 17.

<sup>195</sup> See Helena Smith, "Greece to name and shame rich tax evaders" *The Guardian* (16 May 2010), online: <http://www.guardian.co.uk/business/2010/may/16/greece-debt-crisis-tax-evading>.

<sup>196</sup> See UK, Her Majesty's Customs and Revenue, *Managing Deliberate Defaulters Programme*, online: Her Majesty's Customs and Revenue <<http://www.hmrc.gov.uk/about/tax-defaulters.htm>>. See also UK, Her Majesty's Revenue and Customs, *Compliance checks: Publishing details of deliberate defaulters—CC/FS13*, at 2, online: Her Majesty's Customs and Revenue <<http://www.hmrc.gov.uk/compliance/cc-fs13.pdf>>.

<sup>197</sup> See US Internal Revenue Service, *Offshore Tax-Avoidance and IRS Compliance Efforts*, online: <<http://www.irs.gov/uac/Offshore-Tax-Avoidance-and-IRS-Compliance-Efforts>>; Matthew Allen, "US tax cheats pay for secret Swiss accounts" *Swiss Broadcasting Corporation* (3 August 2010), online: Swissinfo <[http://www.swissinfo.ch/eng/Specials/Rebuilding\\_the\\_financial\\_sector/Spotlight\\_on\\_banking\\_secretary/US\\_tax\\_cheats\\_pay\\_for\\_secret\\_Swiss\\_accounts.html?cid=19988822](http://www.swissinfo.ch/eng/Specials/Rebuilding_the_financial_sector/Spotlight_on_banking_secretary/US_tax_cheats_pay_for_secret_Swiss_accounts.html?cid=19988822)>.

<sup>198</sup> *US Inland Revenue Code*, §6103; Rifkin, *supra* note 6 at 415, 416.

<sup>199</sup> *South Africa Income Tax Act*, *supra* note 161, ss 4, 75A. See also Sheila Killian & Maeve Kolitz, "Revenue Approaches to Income Tax Evasion: A Comparative Study of Ireland and South Africa" (2004) 4 *Journal of Accounting, Ethics and Public Policy* 235 at 247.

<sup>200</sup> *Finance Act 2009* (UK), c 10, s 94.

<sup>201</sup> See Press Trust of India, "I-T dept to 'name and shame' habitual tax evaders" *The Economic Times* (14 April 2013), online: [http://articles.economictimes.indiatimes.com/2013-04-14/news/38529346\\_1\\_defaulters-income-tax-department-direct-taxes](http://articles.economictimes.indiatimes.com/2013-04-14/news/38529346_1_defaulters-income-tax-department-direct-taxes).

In the Philippines, the Bureau of Internal Revenue (“BIR”) has enlisted the help of the public to complement a new ‘name and shame’ initiative. It has been reported that employment income subject to source deduction bears over 85% of total individual income tax collected. It hopes to redress the imbalance by getting self-employed professionals like doctors, dentists, engineers, accountants, architects and lawyers to comply fully with their tax liabilities.<sup>202</sup> In August 2011, the BIR announced a plan to crackdown on the “highest-paid but perennially under-taxed” professional sector.<sup>203</sup> It will embark on a ‘name and shame’ drive by publishing lists that rank professionals for each industry based on taxes paid with particular attention paid to those at the top and bottom of their industry. Besides enhancing registration and book keeping requirements, the BIR has urged the public to assist in the campaign by demanding for official receipts to be issued for services rendered.<sup>204</sup>

#### IV. CONCLUSION

There is a discernible convergence in the development of strategies that different countries are formulating to tackle flagrant tax evasion and complex tax avoidance schemes. Tax administrations face a compelling need to evolve effective means to acquire more information about taxpayers and transactions. Tax shelters not only result in the loss of tax revenue, they can also compromise the integrity of the tax system if aggressive or abusive structures become pervasive. Measures to curb them are more likely to be productive if they comprehensively address both the supply and demand sides of the tax planning industry.

While some of the more advanced economies have implemented sophisticated measures to counteract information deficiency, it appears that less developed countries face far more significant challenges. Not only do they have larger tax gaps, but they also have sizeable proportions that are generally attributable to the pervasiveness of shadow economies. A study on 145 countries estimates that the average size of shadow economies in developing countries is approximately 40% of the official GDP.<sup>205</sup> An IMF paper estimates that the average size of the informal economy in developing/transition countries is about twice that of the high income OECD countries.<sup>206</sup> As the factors that account for the size of an informal economy can be highly disparate and structural in nature, there is no quick fix solution.<sup>207</sup>

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<sup>202</sup> See Gerry Baldo, “House Set to Investigate Tax Case filed by BIR vs Manny Pacquiao” *Metro* (5 December 2013), online: House of Representatives Legislative Library Online <<http://hreplib.congress.gov.ph/cis/?tag=tax-evasion>>.

<sup>203</sup> See Daxim M. Lucas, “BIR Lowers Boom on Professionals” *Philippine Daily Inquirer* (26 July 2011), online: Inquirer Business <<http://business.inquirer.net/9023/bir-lowers-boom-on-professionals>>.

<sup>204</sup> See Lemuel P Maglinte, “The Terminator destroys Hurricane” *The Freeman* (8 August 2011), online: The Freeman <<http://www.philstar.com/Article.aspx?articleId=714218&publicationSubCategoryId=107>>.

<sup>205</sup> See Friedrich Schneider, *The Size of the Shadow Economies of 145 Countries all over the World: First Results over the Period 1999 to 2003*, Discussion Paper Series, IZA DP No 1431 (Bonn: IZA, 2004) online: IZA <<ftp://repec.iza.org/RePEc/Discussionpaper/dp1431.pdf>>.

<sup>206</sup> Barrie Russell, *Revenue Administration: Managing the Shadow Economy*, at 3, online: International Monetary Fund <<https://www.imf.org/external/pubs/ft/tmm/2010/tmm1014.pdf>>.

<sup>207</sup> See Richard M Bird & Eric M Zolt, Introduction to Tax Policy Design and Development (2008) at 23 [unpublished, archived at World Bank], online: World Bank <<http://siteresources>.

There is, however, some consensus among scholars that initial reforms should focus on the centrality of tax administration.<sup>208</sup> Improving tax administration would certainly reduce tax gaps and enhance revenue yield. For instance, the UN notes that 40% of the tax gap in Africa is due to inefficient administration of the tax system.<sup>209</sup> The OECD recommends the adoption of sound and rational human resource management practices by tax authorities.<sup>210</sup> In many developing countries, the work of poorly equipped revenue authorities is often done manually without the use of computers.<sup>211</sup> Without harnessing the power of computer technology, any reform to enhance the disclosure of information by taxpayers is likely to increase costs without any corresponding benefit to the tax system.

Nevertheless, the enhanced disclosure rules implemented by some developed economies to remedy information deficiency are likely to be of interest to developing countries that have the administrative capacity to enforce them. An effective strategy to tackle aggressive tax avoidance is paramount to the risk management function of tax administrations. This is important irrespective of the fiscal health of the country as the integrity of a tax system is critical to the long term tax competitiveness of a country. Some of the leading countries in Asia have taken steps in the last decade to strengthen transfer pricing regimes as well some aspects of off-shore tax avoidance. In this and the other aspects highlighted above, it is imperative that their tax administrations continue to adopt international standards to strengthen institutional legitimacy and capacity to curb tax abuses.<sup>212</sup>

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worldbank.org/INTTPA/Resources/BirdZoltPaper.pdf>. See also Nabamita Dutta, Saibal Kar & Sanjukta Roy, *Informal Sector and Corruption: An Empirical Investigation for India*, Discussion Paper Series, IZA DP No 5579 (Bonn: IZA, 2011), online: IZA<<http://ftp.iza.org/dp5579.pdf>>.

<sup>208</sup> Richard M Bird, *Tax Policy and Economic Development* (Baltimore, MD: Johns Hopkins University Press, 1992) at 204.

<sup>209</sup> United Nations, Economic Commission for Africa, *Economic Report on Africa 2004: Unlocking Africa's Potential*, (Ethiopia: Economic Commission for Africa, 2004) at 44, online: Economic Commission for Africa <<http://www.uneca.org/sites/default/files/PublicationFiles/era2004full.pdf>>. See also Richard Goode, "Some Economic Aspects of Tax Administration" in Richard M Bird & Oliver Oldman, eds, *Taxation in Developing Countries*, 4th ed (London: Johns Hopkins University Press, 1990) 475 at 475.

<sup>210</sup> OECD, Centre for Tax Policy and Administration, *Principles of Good Tax Administration—Practice Note*, Tax Guidance Series, GAP001 (Paris: OECD, 2001), online: OECD <<http://www.oecd.org/tax/administration/1907918.pdf>>.

<sup>211</sup> Arindam Das-Gupta & Dilip Mookherjee, *Incentives and Institutional Reform in Tax Enforcement: An Analysis of Developing Country Experience* (New Delhi: Oxford University Press, 1998) at 257.

<sup>212</sup> See Glenn P Jenkins & Rup Khadka, *Reengineering Tax Systems in Low-Income Countries: An Application to Nepal* (The Hague, The Netherlands: Kluwer Law International, 2002).