



WORKSHOP ON INTELLIGENCE GATHERING AND AUDIT – KEY IN COMBATING NON COMPLIANCE

INTRODUCTION

- The purpose of this workshop is to consider how intelligence gathering and audit can combat non compliance by taxpayers with the tax laws.
- As tax administrators, we are mandated to implement and administer complex tax laws and policies.
- These tax laws and policies are designed by our Governments to generate revenue to pay for programs and services delivered to the people of our countries.
- Our Tax Regimes are tasked to maximize revenue from taxes at minimum costs.
- Revenue Maximization can be achieved through various measures and initiatives including:
 - 1) Voluntary compliance taxpayers.
 - 2) Self assessment and payment of taxes accurately.
 - 3) Quality taxpayer services; education, assistance and support of taxpayers.
 - 4) Compliance and monitoring activities to control and limit the impacts of tax avoidance schemes which may not be consistent with the intent of fiscal policy measures and tax laws.
 - 5) Enforcement measures to combat tax evasion and to improve tax compliance:
 - Identification and Registration of individuals and entities that should be on the tax rolls
 - Intelligence Gathering
 - Risk Profiling and Management
 - Audit
 - Special Investigations
 - Collection/Debt Management
 - Sanctions for offences under Tax Acts; Administrative Settlements; Legal Actions; Prosecution Offenders
 - 6) Strengthening of tax laws through tax reform initiatives; plugging of loopholes.
 - 7) Modernization of tax processes and systems through state-of-the-art information and communication technology, integration of tax services and operational activities, and streamlining organization structures and functions.
 - 8) Building Human Resource capacity in Tax Regimes through training and development to enhance the knowledge, skills and experience of staff.

- In this workshop, we will focus on two key measures utilized by Tax Regimes to combat non compliance. These are:
 - 1) Intelligence Gathering
 - 2) Audit

OBJECTIVE OF THE WORKSHOP

- To highlight and to share ideas on how intelligence gathering and audit can combat non compliance.

NON-COMPLIANCE

In any Tax Regime, one of the major challenges is non-compliance. Non compliance is generally considered to be situations where taxpayers (both self employed and companies) fail to comply with the tax laws. Non compliance generally occurs in the following areas:

- **Self Employed Persons**
These taxpayers employ various methods, both legal and illegal to underreport revenue and inflate expenses. This results in tax evasion and tax avoidance.
- **Incorporated Entities**
 1. Companies fail to:
 - Report their business affairs accurately
 - Prepare their Financial Statements in accordance with GAAP and Tax Laws
 2. Companies also utilize various methods to avoid and minimize their tax payments e.g. tax havens, loopholes in the tax legislation, tax avoidance schemes etc.
- **Value Added Tax Administration**
 1. Overstatement of input VAT credits
 2. Underreporting and remittance of output VAT (e.g. tax collected not remitted)
 3. Issues relating to underreporting of sales/supplies
- **Importers/Customs Declaration**
 1. Incorrect classifications; under valuations; failure to accurately declare the imported goods.
 2. Smuggling of goods (e.g. fuel, alcoholic beverages and vehicles etc) to evade taxes such as Customs Duties, VAT and Excise Tax

Non-Compliance Issues

1. Intra-group services fees, charges and allocations

Occurs mostly by multinational companies e.g. expense dumping risk etc.

2. Income and or cash (assets) stripping

Income stripping can occur when a business is taxable in more than one jurisdiction; and it does occur when the jurisdiction where the taxable income is declared is different from where the income is generated e.g. transfer pricing; sham transactions; transfer of capital assets and intangibles.

3. Thin capitalization

This is relevant when corporations receive capital or loans from their shareholders; there is significant tax difference between a shareholder loan and a capital injection e.g. equity vs. debt financing.

4. Residency and the CARICOM Tax Treaty

This is to determine whether world wide income is taxed e.g. taxation of residents and non residents, withholding taxes and taxes on branch operations.

5. Income timing

The expenses incurred to derive income should be reported in the same period as the income e.g. the matching principle and revenue recognition; hire purchase transactions; allowances for bad debts.

6. Underreporting, best judgement assessments and fraud

Some of the risk factors are: closely held family businesses; cash businesses; related party transactions; family on the payroll; substandard accounting records

7. Tax concessions

Watch for related party transactions with non-concession companies e.g. expense dumping from tax Concession Company to taxable related company; income manipulation from taxable related company to tax Concession Company.

8. Employee Remuneration

Employment status such as distinction between employees and self-employed contractors

9. Insurance Industry

The need to define insurance as 'Life' and 'Non-Life'

10. Manipulation of arms length transactions by companies

Creating dishonest arrangements to evade tax liabilities, and/or creating false transactions

11. Failure to submit returns.

12. Failure to maintain records.

13. Failure to pay taxes assessed.

Consequences of Non-Compliance

- Non-payment of taxes that are legally payable in accordance with the Tax Acts
- Overstatement of expenses
- Tax evasion
- Underreporting of income
- Negative impact on revenue collection

Intelligence Gathering

Since Intelligence is one of the best means of gathering information, methods of networking should be employed to deal with non-compliance issues facing Tax Regimes.

An Intelligence & Risk Management Unit should be set up with trained staff to:

- Conduct extensive research from domestic and international sources
- Establish linkages of a network of informants
- Analyze and disseminate information

In view of the fact that intelligence will aid in determining whether returns submitted by self employed persons and companies are consistent with their business activities, both internal and external sources are used in gathering information:

- Internal Sources -
- 1) Returns filed by taxpayers
 - 2) Currencies declaration
 - 3) Import information
 - 4) Export information
 - 5) Registration of vehicles
 - 6) Data from Returns submitted
 - 7) Utilize Information Technology systems
 - 8) Data warehouse
 - 9) Comparative analysis of industries
 - 10) CCTV Surveillance Cameras

- External Sources -
- 1) Linking with other Government Departments/Ministries
 - 2) Banks
 - 3) Insurance Companies
 - 4) Airlines
 - 5) Utilities Companies
 - 6) Newspapers/Magazines/Publications
 - 7) Internet
 - 8) Post Offices
 - 9) Building Networks with third parties sources
 - 10) General Public
 - 11) Informants to gather information

Auditing

Audit is critical in combating non compliance issues in any Tax Regime. There is need to streamline the audit program and audit process as follows:

- Sound methodologies and criteria should be employed in audit selection
- Audit preparation (Initial Interviews etc.)
- Audit planning
- Audit execution (Examination of accounting records, tour of premises, determining whether the declarations submitted in returns are consistent with the business activities)
- Audit finalization (Discussions with taxpayers with regards the findings of the audit, assessment of additional tax liabilities, interest and penalties).
- Instructions for future compliance
- Audit follow up
- Compliance monitoring

Intelligence gathered will enable auditors in the selection, preparation, and planning the audit. In addition, auditors should be available to verify taxpayers' records utilizing the following methods:

- Computer Assisted Audit Techniques
- Information and communication technology
- Keeping abreast with developments in accounting, auditing, business community, knowledge of business systems and processes.
- Sector specialists for audits e.g. in the areas of insurance, mining, financial institutions, forestry, oil, transportation etc.

OPPORTUNITIES TO ACHIEVE BETTER RESULTS FROM INTELLIGENCE AND AUDITING IN COMBATING NON-COMPLIANCE

- Sharing of information
- Joint audits of multinational companies
- Communication among member states of CARICOM
- Exchange of information agreements
- Coordination of audit plans
- Cooperation in intelligence gathering, auditing, non-compliance resolution
- Audit training coordination
- Consistency in Tax Legislations
- Taxation Agreements
- Audit results sharing

INITIATIVES TO MODERNISE OUR TAX REGIMES

- Organizational design and structuring e.g. along functional lines
- Investment in Information Technology
- Integration of core operational activities
- Surveillance/Monitoring Systems
- Consolidation and delivery of quality services
- Network of informants (financial incentives for information leading to results)
- Financial incentives for Tax Auditors or salaries to minimize risk of corruption