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CONTENTS

eJournal of Tax Research (2016) vol 14, no. 2, pp. 251-252

Editorial

There is a story from the 1990s involving a conversation with a Russian tax inspector. The Russian was incredulous at the high rate of voluntary tax compliance in Sweden. He was told that most Swedes paid their taxes for two reasons: because everyone else

intentional and/or fraudulent, just as taxpayers intentionally underreport or hide income in other contexts.[13] Notably, it is important to understand and appreciate this distinction, because the two ends of the spectrum present different enforcement

note, however, that the IRS figure is 'at best a sophisticated guess', in part because no one knows the extent of the underground economy.[18]

The Service divides the tax gap into three categories: (1) the filing gap; (2) the underreporting gap; and (3) the underpayment gap.[19] The underreporting gap is by far the largest of these three categories, accounting for $376 billion of the tax gap, while non-filing and underpayment account for $28 billion and $46 billion, respectively.[20] The individual income tax accounts for the largest segment of the gross tax gap (an estimated $296 billion) as compared to corporate income taxes, employment taxes, estate taxes, and excise taxes.[21] EITC noncompliance is categorised as underreporting of individual income tax, specifically, an overstated offset of tax due.[22]

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It is that the program is so complicated that people are inadvertently having difficulty figuring out where they fit and where they don't.'[38]

The most recent NRP study, published in August 2014, provides compliance estimates

next section considers intentional taxpayer noncompliance generally and how intentional EITC noncompliance may and may not be different.

3. IS INTENTIONAL EITC NONCOMPLIANCE SIMILAR TO OTHER TYPES OF INTENTIONAL TAXPAYER NONCOMPLIANCE?

This section compares two types of intentional noncompliance: EITC noncompliance and sole proprietor noncompliance. It provides a brief overview of selected theories of noncompliance.

At least with respect to the concern with *intentional* noncompliance, studies of sole proprietor noncompliance may provide useful insights and analogies as to intentional EITC noncompliance.

3.1 Sole proprietor noncompliance

> 'The problem [of the underground economy] is as old as the US tax system, and probably as old as taxation generally.'[50]

The tax gap data discussed in section 2 above indicates a correlation between taxpayer compliance and information reporting, finding high levels of noncompliance among sole proprietors.[51] Having identified this as the largest portion of the tax gap, the Taxpayer Advocate Service (TAS) conducted both a national survey and a community survey of sole proprietors, and it linked the results of these surveys to IRS estimates of the survey respondent's actual tax compliance.[52] This national survey sought to

EITC overclaims have become a political issue will itself lead to future taxpayer making intentional overclaims. As taxpayers read headlines highlighting EITC fraud, it undermines their faith in the system and creates a feeling that they are losing out being an honest taxpayer.

A quick Google search will provide one insight into the culture of intentional EITC noncompliance, as well as the public perception of this noncompliance. As but one example, a website called Twitchy compiled a list of 22 tweets in January 2013 of 'taxpayers looking to borrow children for tax credit', commenting with a hint of disdain: 'Gotta love American ingenuity. Yeesh.'[74] Upon closer examination, however, not all of the tweets linked were examples of noncompliance. The tweets did include several solicitations ('Can I claim ur kid on my taxes ill give $500'; 'Anybody have an extra kid I can claim on my taxes? I'll split the cash'; and 'Does someone have a kid I can use on my taxes this year? Thanks ahead of time.'), but also tweets more in the nature of wishful thinking ('I need to find a single mom soon…so I can claim her kid on my taxes asap') or laments ('I take her kid to school off and on. The least she can do is let me claim her kid on my taxes' and 'the only reason why i would want a kid right now is to get more money on my taxes lol'.)[75]

The concept of claiming someone else's child on one's taxes stems from the possibility that the parents who reside with and support the child, and thus would be statutorily entitled to claim the child, will not benefit from doing so. The inability to benefit from a credit that other people benefit from, a( )10.6 (c)-se o.6 (cu(f)6.9 (i44444e(y)1

file using head of household status based upon his children.[80] This is true despite the fact that the non-custodial parent may be required to pay child support for his children. As Book noted, Taxpayer Advocate Nina Olson made a legislative recommendation many years ago to allow the non-custodial parent a credit in this situation,[81] but Congress has not followed her recommendation, so the structural incentive remains.

In my work directing a low-income taxpayer clinic, I have seen or heard of instances of both of these types of symbolic noncompliance. But I am even more familiar with a third scenario, in which the taxpayer who would be entitled to claim the children has little or no earned income, but no one else is legally entitled to claim the children. In some cases this is because the taxpayer receives social security disability payments, which are not earned income as defined in section 32(c)(2).[82] It may also be because the taxpayer is a mother who is out of the workforce for a period of years because she cares for her young children. In these cases, there may be a boyfriend in the household who does have earned income and plays a significant role in supporting his girlfriend's children. If he is not the father of the children and the couple is not married, he is not statutorily entitled to the claim the children for EITC. As with Book's other examples, a couple in this situation may be frustrated by the perceived inequity of the system and thereby motivated to engage in intentional symbolic noncompliance. After all, if other people are using Twitter to find strangers' children to claim, why should a hard-working taxpayer not benefit from his girlfriend's children whom he actually lives with and supports?

3.3 Combating social and symbolic noncompliance

If we accept that EITC claimants and sole proprietors share similar motivations in their intentional noncompliance, it follows, then, that proposals to reduce intentional EITC noncompliance should be crafted in a similar fashion as the TAS recommendations to address sole proprietor noncompliance. Recall that these recommendations include 'promoting trust in government and the IRS, including tax simplification and taxpayer education that is normative rather than technical'.[83] I am sceptical of TAS's recommendations, scep2.9ctEv (o)2 ((r)8.9 (i(s,)17.n)1 (s,)17.ea)113 (a)-

4. RETURN PREPARERS AND EITC NONCOMPLIANCE

This section will discuss EITC noncompliance in the return preparer context, including ways in which return preparers enable or instigate noncompliance. It will evaluate some of the IRS initiatives in place to detect and deter noncompliance. This

Circular 230 regulatdns governing practice before the IRS and are not affiliated with a nationally known tax preparation firm.[91]

The IRS's ill-fated attempt to regulate all return preparers was the culmination of years of concern about this phenomenon based on studies and reports of problems with the industry's accuracy, lack of due diligence, lack of professionalism, and unscrupulous behaviour.[92]

The Taxpayer Advocate and others mention EITC returns as a particular concern due to the size and refundable nature of the credit.[93]

As part of his work that builds on the Kidder and McEwen typology, Book categorizes this type of intentional noncompliance as ‘brokered noncompliance’, meaning the overclaim occurred on the advice of a tax professional.[98] Book notes: ‘[t]here is a wide range in the honesty of preparers, and there were reports of illicit preparers generating business through their guaranteeing the windfall of government EITC dollars.’[99]

Brokered noncompliance is of course not unique to EITC overclaims. It occurs in many contexts, including the sole proprietor context discussed above in section 3. Morse, Karlinsky and Bankman address this in their study and note that it includes a continuum of behaviour on the part of the preparer: ‘Many preparers in [the cash sector] adopt a “don’t ask, don’t tell” attitude toward their clients reported receipts. A small minority of preparers, however, actively aid in their clients’ evasion’.[100]

Brokered EITC noncompliance should be viewed in that larger context, as it poses part of a larger challenge the IRS faces. As revealed in the IRS’s most recent EITC compliance study, there is significant overlap between EITC noncompliance and sole proprietor noncompliance: recall that the study identifies the most common (and 51% of time, the only) EITC overclaim error as income misreporting, in particular self employment income misreporting.[101] Income misreporting can result either at the suggestion of the return preparer or at the taxpayer’s initiative coupled with a ‘don’t ask, don’t tell’ attitude.

If approximately one-half of EITC overclaims are due to income misreporting, then this is part of a broader noncompliance phenomenon, and one that has proven very diffi

The IRS makes efforts to educate return preparers about the due diligence requirements and Form 8867.Paid preparers who filed ten or more EITC returns without Form 8867 in filing season 2013 received a warning letter, and the IRS issued penalty letters to 225 of these preparers when they again filed ten or more EITC

4.2 Targeted return preparer education

Though resource intensive, the IRS believes that targeted preparer education is an effective tool to combat EITC noncompliance. These include data-driven compliance and warning notices, preparer audits by field examiners, and 'knock and talk' visits from IRS Criminal Investigator agents.[120] The degree to which these efforts are effective in reducing noncompliance must surely be hard to measure, but the Commissioner reported that an expanded pilot program in 2013 'protected an additional $590 million in revenue from being paid out improperly.'[121] Of course, $590 million is but a fraction of the estimated 17.7 billion in improper EITC payments made in fiscal year 2014.[122]

4.3 Pursuing injunctions and permanent bars against the most egregious preparers

As the US District Court for the District of Columbia emphasised in its *Loving* opinion, 'Congress has already enacted a relatively rigid penalty scheme to punish misdeeds by tax return preparers.'[123] In addition to various monetary penalties, the Code permits the government to bring civil action to enjoin tax return preparers from engaging in certain conduct. The IRS and the Department of Justice Tax (DOJ) Division work together under this statutory authority to pursue injunctions and permanent bars against the most egregious offeim

Congress should be applauded for the inclusiveness of these provisions, even if the downside is complexity (and a corresponding higher error rate).

The complexity used to be even worse than it is now. Congress moved to a uniform definition of qualifying child in 2004.[135] These changes were an improvement, but still today the Code's benefits for families do not perfectly align. For example, for a taxpayer to claim a qualifying child as a dependent, the qualifying child must not have provided more than half of their own support for the tax year.[136] A taxpayer claiming a 'qualifying child' for EITC has no support requirement at all, while a taxpayer claiming the head of household filing status must pay more than half the cost of 'maintaining the household' in a tax year.[137] If the child doesn't meet the 'qualifying child' test, the taxpayer might still be able to claim the individual as a dependent if they meet the 'qualifying relative' test, but only if (among other requirements) the taxpayer provided more than half of the person's total support for the year.[138] While a 'qualifying relative' can be claimed as a dependent, this individual cannot be claimed for EITC or child tax credit.[139] These subtle differences make it difficult for taxpayers to keep track of how to file properly. It is possible for the same taxpayer to be entitled to EITC but not head of household filing status; to be eligible for the EITC but not the child tax credit; or to be eligible to claim an individual as a dependent but for no other purpose.

Section 32, authorising the EITC, contains over 2,400 words. It contains cross-references to more than 20 other sections or subsections of the Code, including international tax provisions, passive loss rules, and capital gain definitions.[140] It references half a dozen federal statutes outside of the Code.[141] It is no wonder that taxpayers — and even preparers — make unintentional errors in determining eligibility.

The Service attempts to translate these statutory requirements to plain English, using simplified forms, flowcharts and illustrations in its publications.[142] Some of these resources are terrific, presuming the taxpayer can find them and/or has the patience and sophistication to study them. But the most logical place to provide the requirements is on Form 1040 itself. If Form 1040 does capture the most essential information. Taxpayers claiming a qualifying child are required to fill out Schedule EIC to provide the child's name, social security number, year of birth, relationship to taxpayer, and number of months the child lived with the taxpayer during the tax year.

[135] Working Families Tax Relief Act of 2004, Pub L No 108-311, 118 Stat 1166, Sections 201-208; see John Buckley, 'Uniform Definition of a Chw (-)TjhTw 1(C)7.3 7pt32xa

Schedule EIC is written clearly and captures the most relevant information concerning the EITC requirements for a qualifying child on one page, but it doesn't fully capture the complexity, alert the taxpayer to certain pitfalls, or highlight the differences between the EITC, head of household filing status and the child tax credit. The next section of this article discusses why taxpayer intent matters, and how ascertaining intent is key to developing appropriate and effective sanctions. Section 6 will suggest an even more comprehensive approach to involve the taxpayer in information gathering.

5.2 Intentional noncompliance on self-prepared returns: How increasing due diligence can help the IRS ascertain taxpayer intent, and why that matters

Certainly some percentage of self-prepared return noncompliance is intentional. One problem the IRS currently faces is that its examination and enforcement mechanisms are reactive and not equipped to ascertain whether a taxpayer's overclaim was intentional or not. Increasing required due diligence, coupled with imposing more meaningful sanctions for intentional noncompliance, could serve to better deter social a

5.2.1 Accuracy related penalties apply to all overpayment claims

Taxpayers who erroneously claim the EITC are subject to the section 6662 20% accuracy penalty,[143] regardless of whether the error was unintentional and intentional. In November 2013, in a decision that was viewed as quite favourable to low-income taxpayers, the US Tax Court held that this accuracy related penalty could not apply to the *refundable* portion of a credit (commonly referred to as the negative income tax): that is, the amount refunded to the taxpayer in excess the amount of tax shown on the return.[144] However, the Tax Court was legislatively overruled two years later when Congress amended the definition of underpayment to explicitly include refundable credits in the calculation of the accuracy related penalty.[145]

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Even within the tax code, there are examples of increased reporting or due diligence requirements in other taxpayer realms, including ones that typically involve moderate or high-income taxpayers. Consider the burdensome reporting regime imposed upon US citizens holding foreign accounts. At certain income thresholds, these taxpayers are subject to two separate and potentially overlapping reporting regimes: foreign bank and financial account reporting (FBAR) and the Foreign Account Tax Compliance Act (FATCA). Taxpayers who run afoul of these reporting requirements, even non-wilfully, can face significant civil penalties, and criminal penalties may also apply. The penalty structure is far more serious than anything faced by EITC claimants. While there are many legiti

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Taxpayer rights in Australia twenty years after the introduction of the Taxpayers' Charter

Duncan Bentley[1]

Abstract

Twenty years after the introduction of the Australian Taxpayers' Charter this article reviews its purpose, its development and its sufficiency to meet future challenges. It outlines, in the context of developments in compliance theory, the Charter's important role in developing trust between taxpayers and the Australian Taxation Office. However, the article outlines future challenges and identifies the growing importance of research into a balanced legal and compliance framework.

1. INTRODUCTION

Twenty years ago, I set out a framework for formulating a Taxpayers' Charter of Rights.[2] My proposition was that the nature of any charter is complex and the final product will always depend both on what the drafters are trying to achieve and how they go about achieving it. The Australian Taxpayers' Charter (the Charter) has probably achieved far more than its drafters anticipated. Its nature and content has also gone beyond initial expectation.[3]

However, its effect remains constrained by its formulation as an administrative statement. As a standard bearer for the infusion of a service culture into the tax administration; as a support for the effective implementation of increasingly sophisticated compliance frameworks; as a basis for engaging more effectively with taxpayers in how the tax administration should operate: it has undoubtedly fulfilled its purpose. And that may have been quite adequate for the Australian tax system.

The Charter has done little to extend or clarify legal rights. That is not to underplay its role in developing 'soft law'.[4] But its function was, at most, to articulate the administrative operation of legal rights. Any extension of legal rights was specifically excluded at its introduction.

Twenty years on, is its current role still sufficient? Or should there be consideration of a different approach?

First, I outline the context for the introduction of the Charter and explore the problem it was trying to solve as one of a range of policy measures. Second, I describe its nature and how it has developed as an important element of a stable system to fulfil its objectives: first as part of the tax compliance framework; and second as part of the legal framework. Third, I outline some of the pressing challenges to tax policy and administration, and use two current challenges to illustrate how these might develop in light of the experience in other jurisdictions and undermine current stability. Fourth, I set out a framework, in which the Charter plays an integral part, to address these challenges.

2. THE INTRODUCTION OF T HE CHARTER

There was much debate as to whether it should be l

by the ATO at every stage powerfully reinforce voluntary compliance through legitimating the tax system.

For example, the penalty framework has been carefully integrated with the self-assessment system, particularly the rulings regime, to encourage taxpayers to enter into early dialogue with the ATO. This positive reinforcement to move taxpayers back down the pyramid can be seen in the combination of the law and ATO rulings, which both give significant discretion to the Commissioner and his staff in applying penalties and interest.[32] Wilful non-compliance is dealt with severely, but every effort is made to encourage back down the pyramid those who don't want to or don't care about complying.

Figure 2 sets out the business model designed to take a risk-based approach to managinen ttag . eTT1 .7 f21232

authority: service builds trust as it supports taxpayers and builds their capacity to comply with the law. The theories also encourage the exercise of power both to enforce compliance in the interests of justice and fairness and to deter non-compliance.

James, Murphy and Reinhart in 2004 argued that the Charter 'has moved on from a simple list of principles and become more embodied in the culture of the ATO'.[44] Over a decade later, the Charter is still clearly seen by the ATO as a fundamental component of its culture and norms. The outcomes from the Inspector-General of Taxation 2015/16 review of the Charter will shed further light on whether and to what extent the ATO's perspective is shared by taxpayers.[45]

3.2 The legal framework

Australia opted for an administrative taxpayers' charter. There is no legislative charter and neither is there a combination of legislated rights supplemented by an administrative charter formulated and implemented as a complete and integrated set of rules. Nonetheless, there is legislation that protects taxpayers' basic legal rights. The question is whether the compliance and legal frameworks are mutually reinforcing.

9 Australia has a number of primary legal rights at the ina ha 9t15pattart foustu wha5P <</MCCID

Cases.[49] As a result, income tax is levied by the Commonwealth and any taxpayer rights in respect of income, consumption and other Commonwealth taxes derive from Commonwealth legislation.[50]

None of the five explicit Constitutional rights relate directly to individual taxation.[51] There have been cases brought under Section 99 of the Constitution, which forbids the Commonwealth to prefer one State over another in matters of trade, commerce or revenue, to challenge disparities in effective tax rates,[52] but recognises causes of action for individual taxpayers are extremely unlikely.[53] Recently implied rights relate to freedom of speech and have limited application in income tax cases.[54] This

enforcement, there are significant areas for the Commissioner to exercise discretion. The advantage of this is that the more stringent requirements of, for example, the Criminal Code are not applied to an administrative process. However, a wider discretion means that there is also more limited right of review for the taxpayer.

The tax law cannot set out every step of every process. Administrative rules that can change as the context changes ensure that the law and the system can operate effectively. This goes to the heart of the issue as to whether there is a gap in legal protection. In administering the tax law, the actions and decisions of the Commissioner are subject to both legal and merits review under the Taxation Administration Act 1953 (Cth) (TAA 53), and in specific sections of the relevant taxing acts. However, there is very limited legal review under the Administrative Decisions (Judicial Review) Act 1977 (Cth) (AD(JR) Act), except for serious breaches of procedural fairness or natural justice in the making of a decision. The latter might apply where there has been a breach of the requirement to provide reasons for certain decisions, for example, a decision not to remit the general interest charge or a decision to exercise access powers.[70]

The rights of review ffCID(on10.9d (e)-1.7(r)6.9(n)10.5 (t)-4.6 (he)9.2 (A)4.6D(A)4.6 (()6.9 (J)31

Australia has taken the approach that the fundamental basis of the legal system and basic human rights are protected by the Constitution and international treaties implemented through domestic legislation. Rights are further assured by the requirement for

and will impact on how revenue authorities and other agencies will need to act.[87]

6. The unanticipated disruption of the digital era, ranging from political uprisings, cyber-crime and cyber warfare, to undreamed of capacity to transfer and use big data is almost impossible to model at scale and is therefore largely ignored beyond incremental change based on the known.

7. The extent of future economic constraint and difficulties in assuring the national tax base in the face of the growth of corporate and individual mobility is the subject of public review and much hyperbole. However, political and public commentary remains largely uninformed, increasingly hysterical and largely ignores the inability of individual nation states to enforce their tax systems in the face of unconnected and highly competitive systems.[88]

The potential for global disruption is self-evident. Its impact on the tax system could significantly upset the stability of the current compliance framework. To illustrate some potential effects, I consider just two recent developments arising from the last point: increasing debate over confidentiality of information; and pressure on

both business premises and private dwellings and associated seizure of documents without a search warrant.[90]

As noted above, the grounds for review of the ATO's decisions under the AD(JR) Act, are largely limited to improper exercise of power or abuse of power, both of which are difficult for a taxpayer to prove. Important rights available to taxpayers are the common law right to client legal privilege, which is supported by an administrative right extending recognition of most aspects of privilege to accountants' working papers;[91] and protection of privacy and confidentiality of information.[92] However, there is no privilege against self-incrimination and[93] privilege does not extend to contractual and equitable obligations owed to third parties or spouses.[94]

The ATO uses information gathering extensively to support its compliance program and help it to manage the risk of non-compliance. It uses its search and seizure powers sparingly, concentrating on high risk taxpayers. This is an appropriate approach to managing the compliance framework and reinforces its attempt to balance the ex

compliance. Project Wickenby and the Serious Financial Crime Taskforce, described above, are consistent with this approach. As are the ATO's efforts to ensure that Australia's revenue base is not undermined by international tax fraud and evasion. Dirkis and Bondfield note this requires a range of international institutional bodies to 'develop complementary policy, administrative and legal responses', [97] if the international institutional framework is to work effectively 'to enhance and monitor tax information exchange'.[98]

Currently there are limited taxpayer rights and remedies in respect of information exchange. However, this is balanced in part by the limits on revenue authorities in their practical and legal ability 'to exercise the essential taxation administrative processes (such as information gathering) needed to counter cross border tax avoidance and evasion'.[99]

Australia's international tax treaties are supplemented by a significant number of taxation information exchange agreements based on the Organisation for Economic Cooperation and Development (OECD) process,[100] the Joint International Tax Shelter Information Centre Network, [101] and the Australia and US intergovernmental agreement to implement the US Foreign Account Tax Compliance Act.[102]

Most agreements contain some general protection, reflective of most OECD countries' and Australia's own requirements, for example, recognising the confidentiality of communications between a client and their admitted legal representative, and a right not to disclose trade secrets. The OECD has a comprehensive guide to the protection of information exchange for tax purposes.[103] However, they do not provide a taxpayer under investigation with any notification or appeal rights. They also offer the opportunity for the ATO to obtain significant quantities of data, often without the knowledge of the taxpayer or consequent recourse until it may be used.

While these measures are arguably important steps to protect the Australian revenue base, it does represent nonetheless an increasing commitment by the Australian Government and its agencies to transfer information to other jurisdictions. This in turn raises concerns that have yet to be fully considered and addressed.

The issues related to cross-border information exchange are not new. They were identified by Amparo Grau Ruiz in 2003, analysed extensively by Bentley in 2007,

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[97] Dirkis and Bondfield, above n 90, 127.

[98] Ibid.

[99] Ibid 122, citing the example, of *Jamieson v Commissioner for Internal Revenue* [2007] NSWSC 324 and Foreign Judgments Act 1991 (Cth), ss 3(1) and 5(4).

[100] Art 26 Model Tax Convention on Income and Capital, <http://www.oecd.org/tax/treaties/> at 11 June 2016, Convention on Mutual Administrative Assistance in Tax Matters <http://www.oecd.org/tax/exchange-of-tax-information/> at 11 June 2016, Global Forum on Transparency and Exchange of Information for Tax Purposes, <https://www.oecd.org/tax/transparency/> at 11 June 2016.

[101] Described at <http://www.oecd.org/tax/forum-on-tax-administration/ftajitsicnetwork.htm> at 11 June 2016.

[102] Signed on 28 April 2014, the ATO has published extensive guidance material as to its operation and the obligations of Australian Financial Institutions at <https://www.ato.gov.au/General/International-tax-agreements/In-detail/International-arrangements/FATCA-detailed-guwaidan> , (7s)4.3 v (g)2.6 (ai)-6 (l)-ab(an)-10.l (t)-

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confidence and self-assurance the ATO displays on issues of domestic taxation may give way to a less consistent approach to grey areas in transactions that cross borders.[109] Where the taxpayers involved are confined to large taxpayers with the resources to understand fully their own position, this does not necessarily give rise to increased antagonism.[110] On the other hand, where large groups of smaller business and individual taxpayers become part of a more uncertain tax environment, tensions 110

8. Provide mechanisms for monitoring, review and continuous improvement both at individual and systemic levels.

The ATO has an extensive and highly effective dispute resolution service designed to prevent most cases from escalating and resolves approximately 80% of disputes in this way, although both Mookhey and Jone argue that the system could be improved further.[136] When an issue does go to a court or tribunal, mandated alternative dispute resolution, which is part of the normal tribunal and court process, results in over 80% of matters being resolved without proceeding to a formal hearing.[137] Add to these the Inspector-General of Taxation's complaint handling powers (discussed above) and there is a comprehensive framework of arrangements already in place to give effect to an integrated legal and compliance framework that fosters early resolution of disputes.

When depicted in a pyramid similar to that used for the compliance framework, a legislative rights framework can be shown in Figure 3.

Figure 3: Legislative rights framework

[136] See <https://www.ato.gov.au/About-ATO/Access,-accountal5J 0 v3(A)13.3itys,

Mirroring ation of key influences on taxpayer behaviour shown in Figure 2, of key influences on taxpayer perception that drive trust in the tax de:[138]

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Figure 4

Thus far the calls for the legislation of taxpayer rights or for the Charter to be incorporated into a legal document have seemed unnecessary. International trends and potential challenges have highlighted two concerns: one related to the undermining of basic legal rights and the other related to the impact on taxpayer rights of government and revenue authority responses to th

eJournal of Tax Research (2016) vol 14, no.2, pp. 319-336

Tax disputes, litigation costs and access to tax justice

Binh Tran-Nam[1] and Michael Walpole[2]

In Australia, in addition to the Australian Taxation Office (ATO)'s internal review, there exists a comprehensive system of external tax dispute resolution involving the Administrative Appeals Tribunal (AAT) and the courts, and, to a lesser extent, a variety of governmental bodies. At the same time, there is anecdotal evidence that the litigation costs of taxpayers engaging in tax disputes can be very high especially if professional (legal, tax or accounting) assistance is employed. The existence of such high costs can act as a barrier to the effective accessibility of the external tax dispute resolution system and to the neutrality of the outcomes of such disputes (in the sense that taxpayers with greater resources may be able to obtain more favourable outcomes than taxpayers with lesser resources). This paper provides a comprehensive review of the current state of play and sets out a future agenda for research

Categories 2 and 4 generally refer to statutory rights, while 1 and 3 relate to administrative due process. The remedies of 1 and 3 are thus founded in administrative due process largely recognised in common law principles. Categories 2 and 4 are slightly different as they are based on rights established under the relevant statutes which allow, and set out the process for, review of decisions and the precise terms and extent of objections to assessment. They are thus statutory rights, but their scope and effect can overlap with rights available under administrative due process. Of these categories only 2 to 4 could result in litigation.

if, for a variety of reasons, taxpayers are discouraged or deterred from using those forums for dispute resolution. It is apparent the social costs of resolving tax disputes are high, especially from the taxpayer's perspective. Note that 'social costs' refer to costs borne by the society including those incurred by the taxpayer (litigation costs), ATO, AAT and the courts. While little systematic and reliable information about taxpayers' litigation costs is available, anecdotal evidence, based on plausible

assistance provided by the tribunal/courts to the taxpayers would, to some extent, redress the issue of effective accessibility being discussed. However, there is a limit to how much the tribunal/court can do to assist taxpayers whilst maintain their neutrality as required by law.

2.4 Accessibility and neutrality in a broader context

The accessibility and neutrality of independent tax dispute resolution should be placed in the broader context of socioeconomic changes in Australia, especially over the past 30 years. As a young nation, the notion of a 'fair go' has been enshrined in the Australian ethos. However, while data is limited, there is an agreement that income inequality in Australia has been on the rise since the 1980s.[24] Lack of access to and neutrality of independent tax dispute resolution accentuates this inequality. First, the inability of certain individuals to access an essential government service can be construed as a violation of social justice. Secondly, if tax dispute resolution is indeed not neutral between the 'haves' and the 'have-nots', then this may be regarded as a violation of distributive justice. Both undermine egalitarianism, a notion that many Australians continue to value.

Finally it is worthwhile to note that tax disputes are, in general, not socially wasteful from a pure economic point of view. This is because the outcomes of the disputes may help to clarify the tax law, especially in test cases sponsored by the ATO. In this case, while tax disputes will increase current operating costs of the tax system, it may reduce future tax operating costs. On the negative side, however, tax disputes may indeed sometimes increase future tax operating costs, for example, if unclear/testable

Indirectly related to the spirit of the study is a group of papers by Murphy,[27] Mookhey[28] and Jone.[29] From a compliance perspective, Murphy examined the relationship between procedural justice and tax non-compliance in order to design a more effective tax compliance framework. Mookhey and Jone evaluated the ATO's internal review system. While they found that the ATO dispute resolution model possesses much of the best-practice principles such as clear multi-step procedure and emphasis on negotiation, notification and consultation, the ATO model is still

There is also a paucity of international evidence on whether independent tax dispute resolution is accessible and the implications.[37] There is, however, a more substantial literature on the application of economic analysis to dispute resolution.[38] While these papers were concerned with legal disputes in general, their approaches and insights may be modified for analysing tax disputes. In a seminal work on the dynamics of litigation, Galanter[39] made an important distinction between one-shotter (OS) and repeat player (RP) in analysing whether the US legal system is eff1.6 (r)6P)3 (pl)6.3 (a)-1.7 (y)

Other potential sources of data are the various Australian studies on tax compliance costs.[42] Since taxpayers' compliance tasks are typically broken into activities, including tax dispute resolution, it should be, in principle at least, possible to derive estimates of taxpayers costs specifically related to tax dispute resolution. However, the send-out samples of taxpayers provided to the researchers by the ATO did not include any taxpayers who are currently disputing with the ATO. Thus the effective samples did not contain sufficient number of taxpayers who have been in dispute with

4.2 Advantages and disadvantages of ADR

Five major advantages of ADR have been identified in the literature:[48]

- reduced time in dispute
- reduced costs relating to the dispute resolution
- increased probability of settlement
- improved satisfaction among disputants with the outcome or manner in which the dispute is resolved
- increased compliance with agreed solutions.

The main disadvantage of ADR is that there is very limited opportunity for judicial review of an arbitrator's decision.

There is some Australian evidence suggesting that the above general advantages carry over to tax disputes. Sourdin and Shanks have recently provided an empirical analysis of the costs and benefits of ADR in taxation disputes.[49] They surveyed and analysed the experiences of ATO internal staff members, taxpayers, ADR practitioners, taxpayer representatives and ATO representatives who were involved in ADR processes in relation to taxation and superannuation disputes that took place

The modelling of the taxpayer's decision under approach (i) involves identifying the taxpayer's motive (maximising/minimising financial gains/losses), choices (settle before dispute, settle during dispute, or litigate with or without legal representation), and the consequences of each of these choices, which in turn depend on institutional factors (for example, legal costs are tax deductible or the AAT does not award costs to 'winners' while courts do award costs to 'winners'). There are several complications that need to be considered. For example, in addition to financial considerations, there are non-financial factors that cannot be easily captured quantitatively. Similarly, financial gains/losses can be either one-off or ongoing (especially if taxpayers seek clarity of the tax laws so that they can continue to engage in tax planning or make deduction claims in the future). These issues may be resolved by (i) incorporating a non-financial variable as a determinant of the taxpayer's objective function and (ii) formulating the taxpayer's motive as a multi-period objective function. Another relevant issue in this theoretical approach is the determination of the taxpayer's subjective probability of success in the AAT or the courts, which will depend, amongst other things, on whether or not professional assistance is engaged.

A more sophisticated approach is to take the role of the ATO into account and model the interaction between the ATO and the taxpayer as a game with mixed strategies (probabilistic approach to game theory). As previously reviewed, game theory has been applied with some success to the problem of paying taxes and auditing taxpayers[62] but not to tax dispute resolution. This study will develop a game with mixed strategies to capture the process of tax dispute resolution. A major challenge in so doing is how to incorporate the role of tax advisers in the game.

There will be no formal model developed for investigating the neutrality of independent tax dispute resolution. There will instead be a comprehensive legal analysis as to whether the ATO (as ultimate repeat player (RP)) or large businesses (as RPs with non-trivial bargaining power) enjoy a position of advantage over one-shotters (OSs) in tax dispute resolution. Further, a number of testable hypotheses will also be proposed. They are:

(i) *Alternative hypothesis A*: Costs to taxpayers and duration of tax disputes render access to independent tax dispute resolution ineffective

(ii) *Alternative hypothesis B*: Legal representation of taxpayers makes a difference in the outcomes of the disputes

(iii) *Alternative hypothesis C*: The ATO is more likely to lose against a RP than an OS

(iv) *Alternative hypothesis D*: The ATO is more likely to appeal losses against OSs (individuals, trustees, etc) than RPs (large or foreign companies)

(v) *Alternative hypothesis E*: RPs are more likely to appeal losses against the ATO than OSs.

[62] See, for example, M Graetz, J F Reinganum and L L Wilde, 'The Tax Compliance Game: Toward an Interactive Theory of Law Enforcement' (1986) 2(1) *Journal of Law, Economics and Organization* 1; B Erard andFgo ( )]T69 Tc -0.017 S1 (num)]TJ 0 Tc91 (ooTw 0.4 S1u2.9 (tE)-2.3 ()]TJ 0n72 0 Tds [(92 t]TJ 0innum)]T

5.3 Data collection

The study will utilise both primary and secondary data from a variety of sources. Secondary data will be sought from publicly available sources (such as annual reports of the ATO, the AAT, Federal Courts and the High Court) as well as unpublished sources, principally the ATO. In addition, primary data will also be collected from a variety of surveys and structured interviews of relevant stakeholders. Like most empirical studies, primary data collection represents a very challenging aspect of the study.

The proposed primary data collection is summarised in the following table.

Table 1: Primary data collection by hypothesis

Hypothesis	Primary data
A	Interviews of tax advisers who have represented either taxpayers or the ATO at hearings or trials Survey of taxpayers who have been in dispute of the ATO Small scale e-survey of ATO officers
B	Interviews of tax advisers, tribunal memberax161.7 (r)-3.9 (a)-1.7 (x161.

eJournal of Tax Research (2016) vol. 14, no. 2, pp 337-358

International experiences of tax simplifim4 (T)11.

the world. This was duly published (James, Sawyer & Budak, 2016) and this paper analyses the findings. The first stage of this study was to identify experts on the tax systems of particular countries who also had knowledge of issues involving complexity and simplification they would be willing to share. This was not always an easy process but eventually an authoritative group of experts was established who were willing to report on the tax simplification experiences in particular countries. They are listed in Table 1.

Table 1: Country Simplification Contributors

County	Contributor(s)
Australia	Binh Tran-Nam, University of New South Wales

However, even within this fairly specific framework, the expert contributions often varied considerably in the attention they gave to different issues and the actual experiences they examined. This is not surprising of course, not least because the political and socioeconomic environment within which tax systems operate often vary considerably between different countries. For instance, Sharkey (2016, p. 45) pointed out that the simplification of income tax in China is significantly different from most of the other countries represented in this study, essentially because the 'tax institution environment' is different. Nevertheless, the contributions also demonstrated that each country has significant challenges with tax complexity, tried different way to simplify taxation and achieved different degrees of success. The diversity of the experiences of these countries means a case study approach is the most appropriate method of analysis and perhaps the best way is to examine the experiences of the different countries is by the aspects listed above, starting with the simplification of tax systems.

2.1 The simplification of tax systems

Calls for tax simplification often focus on the tax system itself – the number of taxes, the tax bases, the exemptions and the structure of tax rates. However, the contributions from the 11 countries suggest that major simplification of tax systems is relatively rare.

2.4 Simplifying tax administration

There have been some major achievements in simplifying tax administration both in terms of limiting the numbers of tax returns issued in some countries and also in 'pre populating' (pre-filling) tax returns that are sent out. In the UK most taxpayers have not been required to complete an annual tax return since the introduction of the cumulative Pay-As-You-Earn system in 1944 which, at least in principle, withholds tax accurately from employment and some other income. New Zealand has also moved in this direction removing the requirement of individual taxpayers to submit annual returns. This is possible where their income is taxed at source, the relevant information is received from third parties and employee deductions are eliminated. Malaysia has also made a change in this respect so that employees with specified straightforward circumstances are no longer required to file tax returns (Singh, 2016).

aspects of the tax system and relatively few make a major impact on the tax system as a whole. It may therefore be helpful to consider a strategic approach to simplification and how it might assist in identifying unnecessary complexity.

3. A

3.2 Identify the aims of taxation

Taxation is used to support a range of government policies in addition to raising revenue to support public expenditure. It is used to redistribute income as well as encourage some activities while discouraging others. Identifying the aims of taxation is not, of course, sufficient to distinguish necessary from unnecessary tax complexity but it should be the starting point to examine whether the level of complexity is proportionate given the aims of taxation.

3.3 Consider different methods of achieving the aims

Taxation may not necessarily be the best way of achieving all the aims identified above. For example, tax expenditure describes the use of tax concessions to give a fiscal advantage to a particular activity or group of individuals rather than the more direct use of public expenditure (Surrey, 1973). If tax expenditures are being used as part of a policy of redistributing income their effectiveness will be seriously limited because, of cour

As Vickrey (1969, p. 736) suggested, complexity in the relevant legislation and

> underlying complexity due to the role played by the impact of policy Although underlying complexity can have an effect on the impact of complexity (i.e. by structuring a tax measure in a way that applies to more customers), how the measure is implemented can affect overall complexity (OTS, 2013, p. 1, emphasis added).

This component of the Complexity Index would have four measures:

1. Net average cost per taxpayer, incurred by taxpayers and HMRC
2. Number of taxpayers
3. Average ability of taxpayers
4. Avoidance risk

The Complexity Index was recognised by the OTS to be a work in progress needing further methodological refinement. For instance, determination of the weightings to the various factors could be developed through use of the Delphi technique (Evans & Collier, 2012). The Delphi technique was developed by Dalkey and Helmer (1963) at the Rand Corporation in the 1950s. It is a widely used and accepted method designed to achieve consensus of opinion of experts, within certain topic areas, on a significant issue. As a group communication process, through the debate and discussions on specific issue, the Delphi technique seeks to enable goal setting, policy investigation, and/or predicting the occurrence of future events

> i. Retaining the existing tax design but delivering it in a less complex way essentially by reducing operational complexity by, for example, writing legislation/guidance in a form that is easier to understand or removing unnecessary informational complexity.
>
> ii. Retaining the given aims of the tax system but trying to achieve these in a less complex way by reducing the unnecessary design complexity (p. 47, emphasis added).

Sherwood (2015), then head of the OTS, in a UNSW Business School Thought Leadership Lecture in 2015, defined necessary complexity thus as 'minimum complexity needed to deliver the broad policy aim'. Examples offered by Sherwood include: political/social aims; economic aims; fairness; certainty; avoidance measures, and the like. On the other hand, Sherwood provided examples of unnecessary complexity as: 'poor policy design (for example, artificial boundaries); too many special cases; badly worded law; poor guidance; complicated and expensive processes, etc'. Within the UK, Sherwood pointed to examples of unnecessary complexity being the capital gains tax (CGT) taper relief, many badly targeted tax reliefs, and unclear VAT boundaries.

Further discussion that is directed at achieving consensus over what path(s) should be taken to reduce (unnecessary) tax complexity would be a positive further step to responding to Ulph's observation. In this regard we would suggest that the Delphi technique should be applied to moving the discussion forward towards a consensus, following which the data gathering and analysis process can begin in earnest.

are necessary or fundamental for the functioning of a successful tax system, and those which are unnecessary (and ought to be reduced or eliminated).

In this paper we focussed on the relevant factors and issues involved in classifying unavoidable and unnecessary complexity, not only with respect to legislation, but also tax policy and administrative systems. In identifying unnecessary complexity, we have explored the

Cooper, GS 1993, 'Themes and issues in tax simplification', Australian Tax Forum, vol. 10, pp. 417–60.

Dalkey, NC, & Helmer, O 1963, 'An experimental application of the Delphi method to the use of experts', Management Science, vol. 9, no. 3, pp. 458–67.

Devas, N, Delay, S & Hubbard, M 2001, 'Revenue authorities: are they the right vehicle for improved tax administration?' Public Administration and Development, vol. 21, no. 3, pp. 211–22.

European Commission 2006, Risk Management Guide for Tax Administrations <https://ec.europa.eu/taxation_customs/sites/taxation/files/docs/body/risk_management_guide_for_tax_administrations_en.pdf >

Evans, C & Collier, K 2012, 'The Delphi Technique', in L Oats (ed), Taxation: A Fieldwork Research Handbook, Routledge, London, pp. 228–41.

Evans C & Tran-Nam, B 2014, 'Towards the development of a tax system complexity index', Fiscal Studies, vol. 35, pp. 341–70.

Gibson, J 1990, The Politics and Economics of the Poll Tax: Mrs Thatcher's Downfall, EMAS, Cradley Heath.

Grant, RM 2015, Contemporary Strategy Analysis, 9th edn, Wiley.

Hall, RE & Rabushka, A 1983, Low Tax, Simple Tax, Flat Tax, McGraw Hill, New York.

Hall, RE & Rabushka, A 2007, The Flat Tax, 3rd edn, Hoover Press, Stanford.

James, S 2005, 'Tax Compliance Strategies to Tackle the Underground Economy' in C Bajada & F Schneider (eds), (,)Tj ( )Tj -0.013-0.002 (y)10.9 i Tw 6.033 0 Td iSi ( )Tj 0.03 (d)2]TJ /TT2x rs6 (e)-1.7 (

Ulph, D 2015, 'Measuring tax complexity', in C. Evans, R. Krever & P. Mellor (eds), Tax simplification, Wolters Kluwer, series on international taxation no 53, the Netherlands, pp. 41–53.

Vaillancourt, F & Bird, R 2016, 'Tax simplification in Canada: a journey not yet mapped', in S James, A Sawyer & T Budak (eds), The complexities of tax s

the revenue authorities to create a cross-border tax-induced debt bias which actually results in said tax base erosion.[9]

The current international tax framework incentivises the location of expenses in higher tax jurisdictions and income in lower tax jurisdictions as it can result in significant tax minimisation. Multinational enterprises (MNEs) can shift expenses to, and income from, soure1nd (m)19.2 (,)2 (s b20o)2 (8. (e1n)u13i.6 (e)11.2 ( )-s8.2 (ax)660

A significant gap in the literature is that thin capitalisation rules' impact on tax planning has only been analysed on a piecemeal basis, and studies have not yet adequately considered the impact of thin capitalisation rules on MNEs' investment decisions.

foreign tax relief, there is a tax incentive to adjust its behaviour to maximise overall deductions in higher-tax jurisdictions to minimise the group-wide tax liability and, in turn, the overall net profit after tax.

The author recognises that not all MNEs will fall within this category in practice. Accordingly, this study is only concerned with MNEs that are responsive to cross-border tax-induced distortions.

Assuming that MNEs which exhibit tax planning behaviour make tax decisions as a global group with the objective of minimising total tax payable worldwide.[34] Such tax planning is generally encouraged by tax professionals and is statutorily, administratively and judicially condoned.[35] In other words, such an MNE is 'tax-minimising', albeit with varying degrees of aggressiveness.

Accordingly, the behaviourally distortive effects of existing and proposed tax rules relating to cross-border intercompany activities are of primary concern in this study. Specifically, the focus of this paper is on MNE's cross-border intercompany transactions relating to passive or highly mobile income; specifically how tax distortions affect MNE decisions on the funding mix between intercompany financing, licensing and finance leasing activities.

As such, this paper proposes restricting the tax deductibility of these otherwise

Figure 1: Various types of intercompany payments

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Perhaps the most controversial aspect of the funding bias concept is that royalties are fungible. However, this paper does not suggest that all intercompany royalties are equivalent and fungible with other financing activities. Rather, the scope is limited to some categories of licenses or royalty financing ostensibly similar in their capacity to provide access to an underlying asset with the ability to provide a revenue str (termed 'royalties') but not dissimilar in operation to intercompany debt or equity financing or a finance lease.

It is noteworthy that, as observed by Van [n] historically, excess royalties were assumed by some OEEC delegates to be classified as

financial transactions … affiliated leasing transactions could replicate the consequences of related lending.[42] Nonetheless, Benshalom observes that the mobility of intercompany activities erodes the source jurisdiction's tax base from both the perspective of intangible and tangible manufacturing and merchandise activities.[43]

So, while the literature implicitly contains support for the proposition that cross-border

> global tax liabilities through external debt financing, but we cannot observe their using internal debt to generate interest deductions in high-tax countries and interest income in low-tax countries … intrafirm transactions are nontrivial and may even exceed the avoidance opportunities with third parties[47]

In the absence of a requirement to fully disclose their intercompany transactions in financial statements, cross-referencing the information reported to taxing authorities and reported in financial statements is a highly challenging task.[48] Further, if a subsidiary is a private company it does not even need to disclose comprehensive financial statements in the source jurisdiction.[49] Accordingly, this presents a gap in the literature.

Generally, quantitative evaluations are conducted utilising regression based evaluation methods and general equilibrium modelling. For example, there is a growing theoretical literature on the relationship between tax planning and investment locations, and its implications for tax policies.[50] There is also a rich literature which utilises empirical data in this context, extensively considering the relationship between MNE leverage and taxation with US, Canadian and European Union (particularly German) data.[51]

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[47] KS Markle and DA Shackelford, 'Cross-Country Comparisons of the Effects of Leverage, Intangible Assets, and Tax Havens on Corporate Income Taxes' (2012) 65 Tax Law Review 415, 417–32.

[48] Commentators such as De Simone and Stomberg observe that '[f]inancial reporting for income taxes is so complex that even sophisticated financial statement users often ignore detailed tax disclosures' and 'taxation is often viewed by the market as beyond meaningful analysis': De Simone L and Stomberg B, 'Do Investors Differentially Value Tax Avoidance of Income-Mobile Firms?' (Working Paper, University of Texas at Austin, June 2012), 2. Consolidated accounts undergo intercompany eliminations so are not helpful in this regard. While some MNEs provide some detail regarding their intercompany transactions in their segment reports, this is not a requirement across the board. See further, 'this large shift in pre-tax income without any corresponding change in revenues suggests the presence of significant intercompany payments—likely royalty payments attributable to the transfer of intellectual property into Ireland': K Balakrishnan, J Blouin and W Guay, 'Does Tax Aggressiveness Reduce Financial Reporting Transparency?' (Working Paper, Wharton School, University of Pennsylvania, 20 September 2011), 29.

[49] For example, in the financial year ending 2014, Google Australia Pty Ltd's disclosure omitted itemising over $35 million in expenses from its financial statement and the corresponding notes, not even categorising these expenses as 'COGS' and/or 'Other expenses'. Further, Google Australia Pty Ltd's intercompany financing activities were presumably classified as 'operating' activities, as the 'financing' section of the cash flow statement was entirely blank, with no details afforded in the notes.

[50] Q Hong and M Smart, 'In Praise of Tax Havens: International Tax Planning and Foreign Direct Investment' (2010) 54(1) European Economic Review 82; see references cited therein, including: H Grubert and J Slemrod, 'The Effect of Taxes on Investment and Income Shifting to Puerto Rico' (1998) 80 Review of Economics and Statistics 365–73; A Haufler and G Schjelderup, 'Corporate Tax Systems and Cross-country Profit Shifting' (2000) 52 Oxford Economic Papers 306–25; J Mintz and M Smart M, 'Income Shifting, Investment, and Tax Competition: Theory and Evidence from Provincial Taxation in Canada' (2004) 88 Journal of Public Economics 1149–168; S Bucovetsky and A Haufler, Tax Competition When Firms Choose Their Organizational Form: Should Tax Loopholes For Multinationals Be Closed? (Technical Report 1625, CESifo, 2005); J Slemrod and JD Wilson, 'Tax Competition with Parasitic Tax H

Substantially less developed is the literature on the effect of taxation on leverage in a multilateral context, with 'nxn countries'[52]. Huizinga, Laeven and Nicodème present the primary exploration of whether MNEs make multilateral capital structure decisions based on the tax rates faced by various subsidiaries.

International tax

Figure 2: The modelled 'multiverse' of policy iterations and MNE tax aggressiveness

This hypothetical approach is preferable due to the accessibility issues associated with collecting various revenue authorities' corporate tax return data and the limitations of using accounting data. Even if accounting data was gathered through annual reports this approach is problematic given the difference between accounting profit and taxable income. Specifically, MNEs start with accounting profit and then make adjustments to accounting profit[61] to reach their taxable profit.[62] Accordingly, it is difficult to glean intercompany tax-related information from financial statements.

Further, these difficulties are exacerbated by recent amendments to the Corporations Act 2001, enacted 28 June 2010, which have removed the requirement for companies to include full unconsolidated parent entity financial statements in their group annual financial reports under Chapter 2M of the Corporations Act 2001 where consolidated financial statements are required.[63] This renders it even more difficult to discern intercompany tax-related information. Also, there is currently no requirement to produce 'general purpose' financial reports in subsidiary locations where the MNE determines that that subsidiary is not a 'reporting entity'. Further, given the gaps in reporting requirements and the fact that some items are off balance sheet to begin with, it is highly difficult to undertake a meaningful analysis of data from financial statements in this context. This is made more problematic by the absence of official

The remainder of this section outlines and justifies the optimisation model. Specifically, it expresses MNEs' decisions to utilise various conduit financing structures to minimise taxation for the overall group in the form of an algorithmic expression.

The optimisation model is developed using the IBM ILOG CPLEX for Microsoft Excel ('CPLEX') software.[65] Microsoft Excel is utilised to generate the data, delineate the parameters and display the solution in a multidimensional format, while the CPLEX software is used to express and solve the optimisation problem. Quantitative analysis facilitates a deeper understanding of the interplay of effects determining tax-induced distortions than may not be observable with a qualitative analysis alone.

The 'objective function' is to minimise the total tax payable by the MNE on global operations. The 'constraints' are the four groups of otherwise fungible intercompany debt and equity financing, licensing and finance leasing activities. The model can then be fine-tuned by overlaying various parameters.

Specifically, the hypothetical MNE modelled by this paper has entities in four jurisdictions; two high-tax jurisdictions (one capital exporter and one capital importer; specifically, a US parent and Australian subsidiary) and two low-tax jurisdictions (one non-treaty country and one treaty country, in Hong Kong and Singapore, respectively).[66]

Given its focus on intercompany funding options, this optimisation model focusses on funding constraints and regulatory limitations directly relevant to intercompany funding decisions; namely, withholding taxes, thin capitalisation rules and foreign tax credits. This ensures the model is complex and flexible enough to represent both funding structure decisions and regulations influencing these behavioural responses.

The baseline model in the optimisation problem consists of the current global tax framework and its treatment of fungible funding options. It is necessary to develop a baseline model because modelling in this area has not yet focussed on the fungibility of intercompany funding options. So far, the predominant focus in the literature has been on an economy-wide scale[67] with firms identified with, for example, one unit of

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[65] CPLEX is a sophisticated software appropriate for both building and solving optimisation problems, and for interfacing with Microsoft Excel; 'IBM® ILOG® CPLEX® for Microsoft® Excel is an extension to IBM ILOG CPLEX that allows you to use Microsoft Excel format to define your optimization problems and solve them. Thus a business user or educator who is already familiar with Excel can enter their optimization problems in that format and solve them, without having to learn a new interface or command language. CPLEX is a tool for solving linear optimization problems, commonly referred to as Linear Programming (LP) problems': IBM ILOG CPLEX V12.1 IBM ILOG CPLEX for Microsoft: Excel User's Manual, 12 <ftp://public.dhe.ibm.com/software/websphere/ilog/docs/optimization/cplex/cplex_excel_user.pdf>.

[66] In the Australian context, it appears that Singapore is a relatively more popular jurisdiction than other well-known low-tax jurisdictions such as Ireland in terms of the volume of intercompany payments made by Australian companies: E Butler and G Wilkins, 'Singapore, Ireland Top Havens For Multinational Tax Dodgers', Sydney Morning Herald (online), 1 May 2014 <http://www.smh.com.au/business/singapore-ireland-top-havens-for-multinational-tax-dodgers-20140430-37hzi.html>.

[67] See, for example, O Jacobs and S Spengel, 'The Effective Average Tax Burden in the European Union and the USA: A Computer-based Calculation and Comparison with the Model of the European Tax Analyzer' (ZEW Discussion Paper No 99-24, Centre for European Economic Research (ZEW) and University of Mannheim, September 1999).

capital with different firm types linked to different types of capital whereby MNEs dispose of as unit of mobile capital.[68] Even when the analysis is constrained to a

For ease of reference, the abbreviations used throughout the remainder of this section are summarised in Table 1 below:

Table 1: Abbreviations used in formulation of model

Abbreviations	
0 2 $ 6	Net profit before tax for company 'E' at the start of the period
0 2 $ 6	Net profit before tax for company 'E' at the end of the period
N	Headline corporate income tax rate in country 'E'
TTP	Total tax payable
N	The rate of return on debt financing from company 'E' to company 'F'
&	The balance of debt financing provided from company 'E' to company 'F'
+	The interest received by company 'E' (or, if negative, interest paid)
N	The rate of return on equity financing from company 'E' to company 'F'
'	The balance of equity financing provided from company 'E' to company 'F'
8	The dividends received by company 'E' (or, if negative, dividends paid)
N	The rate of return on licensing from company 'E' to company 'F'
%	The balance of licenses provided from company 'E'

Table 2: Overview of withholding tax rates between USA, Singapore, Australia and Hong Kong

Withholding tax rates				
	Interest	Dividends	Royalties	Finance lease payments

highlighted in bold. For example, assuming a high level of participation, the withholding tax rate of dividends from Co C and Co A would be zero percent. It is

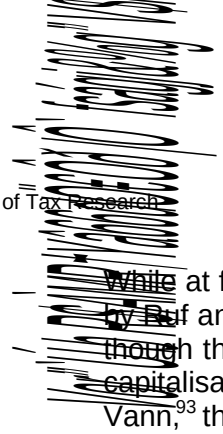
5.1 Variation 1: Tightening Australia's thin capitalisation rules

One of the most surprising findings in relation to the existing system is that the hypothetical MNE is indifferent to the existence and/or variation in thin capitalisation rules. This is because while thin capitalisation rules change the funding mix of entities within an MNE, the TTP remains unchanged.

Specifically, where this variation is modelled with NPBT increments between 0 and 100, the TTP remains the same for each increment of tax aggressiveness, such that the AETR is 26.50 per cent to 30.75 per cent regardless of whether thin capitalisation rules are tightened. In contrast, in the absence of any tax planning the AETR is 34.50 per cent for the hypothetical MNE. So, contrary to policymakers perception that thin capitalisation rules can be made more effective at restricting base erosion by simply tightened the debt-to-equity ratio, this model also finds no impact on TTP.

The model shows no change in TTP from tightening thin capitalisation rules from a debt-to-equity ratio of 3:1 to 1.5:1, as recently implemented by Tax and Superannuation Laws Amendment (2014 Measures No 4) Act (2014).

In addition, capital structure and both the quantum and direction of funds flow remains the same under so-called tightened thin capitalisation rules. In particular, the Australian subsidiary experiences no change in its funding mix between inbound-only, outbound-only, or both inbound/outbound rules. This result seem to be at odds with the literature that tightening thin capitalisation rules would impact MNEs' funding decisions. The a



While at first blush these results may appear unusual, the anecdotal research presented by Ruf and Schindler[91] anticipates this result. This finding is significant because even though there is a growing body of literature challenging the traditional belief that thin capitalisation rules protect the tax revenue base, including Ruf and Schindler[92] and Vann,[93] there is currently no empirical evidence that new FDI is simply financed at or around the debt-to-equity ratio limits set by thin capitalisation rules. Accordingly, this finding could have significant policy implications globally, especially given the worldwide popularity of implementing and tightening thin capitalisation rules.

5.2 Variation 2: Unilateral adoption of the OECD's BEPS recommendation

Shaviro noted that this strict reform would bring the US rules closer to the German earnings-stripping rules.[101] However, there was much opposition to this 'bifurcation' rule. C

rule in comparison to both the existing regime and the OECD's BEPS Recommendation is presented in below Figure 4.

Figure 4: Results of modelling the OECD's Recommendation and an Extended

the unilateral and multilateral implementation of the OECD's BEPS Recommendation, with both reforms resulting in an increase in the tax payable by the MNE, most markedly for the most tax aggressive MNEs. However, the most noteworthy finding in this paper is that an extended thin capitalisation rule is more effective at protecting a jurisdiction's tax revenue base than the OECD's BEPS Recommendation.

While the implementation of the OECD's BEPS Recommendation results in an improvement to tax revenue base protection, the improvement is only marginal and the reform ceases to deliver any improvement in tax revenue outcomes for the majority of MNEs (who are assumed to not be tax aggressive). On the other hand, an extended thin capitalisation rule delivers a significant improvement to tax revenue base protection, partic-10.3 (t (l)7 (pr)-3.l(ot)6.y (v)10.9 (f)-3.o6 (r)-43 (t)-4.6 ((e)-1.63 (m)17.c

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1. INTRODUCTION

History indicates that tax compliance behaviour remains problematic around the globe (Chau and Leung, 2009; McKerchar and Evans, 2009; OECD, 2012a). Several strategies have been introduced and developed to address this issue (OECD, 2012a). Due mainly to inconsistent findings that have emerged from the economic deterrence approach (Andreoni, Erard & Feinstein, 1998; Kirchler et al., 2010), recent developments in compliance strategies have emphasised the importance of psychological and behavioural factors (Congdon, Kling & Mullainathan, 2009; James, 2012; Kirchler, 2007; Kirchler, Kogler

2. LITERATURE AND THEORETICAL FRAMEWORK

2.1 Corruption and perceptions of corruption

2.1.1 Corruption

Corruption is an ongoing global issue (Shleifer and Vishny, 1993; Transparency International, 2015) and is recognised as a major impediment in preventing economic development in many areas of the world (Blackburn, Bose & Haque, 2010; Wilhelm, 2002).

As a social phenomenon, the concept of corruption does not operate in a vacuum. Its meaning largely depends upon the specific social and political contexts in which it is applied (Brown, 2006).[6] Social rules as well as moral views may also interrelate and vary significantly among different cultures and societies; as a result, an action could be a common courtesy in one society, but in a different context it could be considered as corrupt practice (Melgar, Rossi & Smith, 2010; Philp, 2006). Specifically, in the Indonesian context, apart from its political and economic situation, cultural aspects

unintentionally non-compliant; (iii) accidentally or unintentionally compliant and (iv) deliberately or intentionally non-compliant.

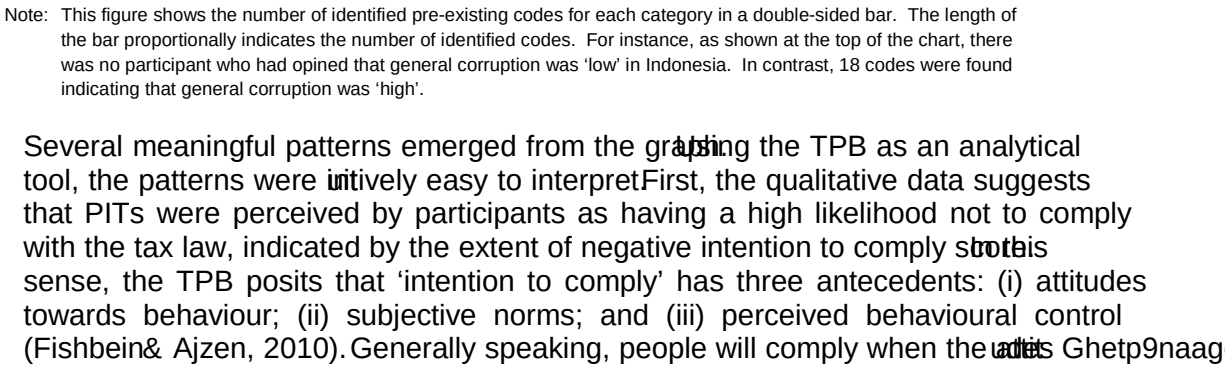
It is apparent that two related aspects need to be taken account in examining tax compliance behaviour: intention and outcome (see, for example, Antonides and Robben, 1995; Ibid, 2015; Long and Swingen, 1991; McKerchar, 2003; Langham, Paulsen & Hartel, 2012; Tran-Nam, 2003; World Bank, 2015).[16] While the outcomes of compliance behaviour vary, intention can be reasonably considered as the accurate proxy for the performed behaviour (Antonides & Robben, 1995; Lewis, 1982, 15

3. RESEARCH METHODS Š POPULATION AND DATA COLLECTION

This study employs both the qualitative and quantitative paradigms in a sequential priority model of *'qual ÆQUANT'* to enhance research method capabilities and to improve the quality of the research findings[25]. In the first phase, in-depth interviews are used to clarify, modify, and develop more robust observed independent and dependent variables in the design of the questionnaires from theoretical perspectives. This is then followed by an extensive survey to explain the structural patterns, through numeric measurement, of relationships among the variables of perceptions of corruption and the prescribed TPB constructs through quantitative analysis. As high-risk human research ethics approval, covering the research design for both the

total of 272 assigned codes were identified from the transcribed interview data. To provide an easier description of the findings, a representation of the assigned codes was converted into clustered bar charts and depicted in Figure 2.

Figure 2: Diagrammatic interpretation of qualitative findings



Note: This figure shows the number of identified pre-existing codes for each category in a double-sided bar. The length of the bar proportionally indicates the number of identified codes. For instance, as shown at the top of the chart, there was no participant who had opined that general corruption was 'low' in Indonesia. In contrast, 18 codes were found indicating that general corruption was 'high'.

Several meaningful patterns emerged from the graphs. Using the TPB as an analytical tool, the patterns were intuitively easy to interpret. First, the qualitative data suggests that PITs were perceived by participants as having a high likelihood not to comply with the tax law, indicated by the extent of negative intention to comply scores. In this sense, the TPB posits that 'intention to comply' has three antecedents: (i) attitudes towards behaviour; (ii) subjective norms; and (iii) perceived behavioural control (Fishbein & Ajzen, 2010). Generally speaking, people will comply when the audit risk is adequately managed

Figure 3: Hypothetical relationships between perceptions of pervasive corruption and poor level of tax compliance arising from qualitative findings

4.2 Results of phase two: Survey instrument

4.2.1 Representativeness test

received additional income. Further, roughly four per cent of employed PITs (seven respondents) have reported that they did not earn income in 2014.

In terms of the amount of income being underreported in the annual tax returns, the data indicated that 44 per cent of self-employed PITs had underreported between 50 per cent and 100 per cent of their actual income. Surprisingly, no respondent from employed PITs who received additional income other than from employment reported their additional income in the annual tax return. X {à, F ’gFóFó£Aq {ÁÓ’F QqFdc 1• ¦p–•! –

In modelling the channel of causality, the results previously presented in Section

H4: the negative

forms of corruption on the level of reported income. Accordingly, the second test was performed on full models only.

It was found that while all types of perceptions of corruption had negative effects on intention to correctly report actual income in the partial models, perceptions of petty corruption and perceptions of petty tax corruption had insignificant effects in the full models. In terms of levels of reported income, it was found that three out of five types of perceptions of corruption seemed to have significant negative effects on the level of reported income: general corruption, grand corruption and grand tax corruption. Perceptions of grand corruption was the most influential with -0.073, followed by perceptions of grand tax corruption with -0.071 and perceptions of general corruption at the least with -0.034. Based on these findings, the null hypothesis H_0 can be rejected.

4.2.10 Summary of findings

PGC Æ ATB, PTC Æ ATB respectively), while only one influential relationship and one partly influential relationship were found in H2 (that is, PCO Æ SNO and GTC Æ SNO). Attitudes, subjective norms and perceived behavioural control towards tax underreporting were found to be negatively influential upon respondents' intention to report actual income, which in turn were related to the level of reported income (TCB). The effect of perceived behavioural control over tax underreporting (PBC) seemed to be fully mediated by intention to report actual income (ITC) as there was no statistically significant relationship was found between PBC and TCB. In terms of score of (direct) effect, it was found that the effect of ITC upon TCB was strongest with path coefficient greater than 0.55. In the second place was the effect of ATB upon ITC, with scores ranging from 0.400 to 0.455.

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World Bank 2015

APPENDIX

1. Model A -full (modified)

2. Model B -full (modified)

3. Model C -full (modified)

4. Model A -partial (modified)

5. Model B -partial (modified)

6. Model C (modified)

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The applicability of the OTS Complexity Index to comparative analysis between countries: Australia, New Zealand, Turkey, and the UK

Tamer Budak[1] and Simon James[2]

Abstract

Tax systems world-wide are becoming more complex for a variety of reasons. Countries such as Australia, New Zealand (NZ) and the UK have attempted to simplify their taxes but with limited success. The Complexity Index produced by the Office of Tax Simplification (OTS) in the UK is an important contribution in this field. This paper considers general issues in relation to complexity and simplificat

3. Trans-pacific partnership countries: comparative trade and economic analysis[5]
4. Comparative analysis of firm demographics and survival: micro-level evidence for the OECD countries[6]
5. Financing democracy: funding of political parties and election campaigns and the risk of policy capture[7]
6. Languages in education and training: final country comparative analysis[8]
7. A comparative analysis of health policy performance in 43 European countries[9]
8. Why are saving rates so different across countries? an international comparative analysis[10]
9. A comparative analysis of the structure of tax systems in industrial countries[11]
10. Paying taxes 2016: The global picture[12]
11. Are stock prices related to the political uncertainty index in OECD countries? Evidence from the bootstrap panel causality test.[13]

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3. THE DEFINITION OF TAX COMPLEXITY OR SIMPLIFICATION

Although tax complexity is a much debated topic, defining or measuring what is meant by complexity is difficult and a serious barrier to tax simplification.[14] To arrive at a definition of 'complexity' is not an easy task. Most scholars do not define tax complexity but they have listed and categorised some characteristics that contribute to complexity. For instance, Slemrod lists four main dimensions of tax complexity: enforceability, predictability, difficulty and manipulability. He also provides a description of tax complexity as the sum of compliance costs or the total resource cost and administrative costs incurred in complying with the system's requirements. Thlty (f)11.9 chlty (ft.7(ta)1.554 0 Td [(H)3.6 (e)0.8Se3 (d [(hlty (flahlty (ft3 (ta

complexity index,[43] and contributions such as Tran-Nam and Evans' combination of the axiomatic and statistical approaches,[44] and Borrego, Loo, Lopes and Ferreira's General Tax Complexity Index[45] related to the measurement of complexity in specific countries and around the world. These valuable studies have made important progress in improving methods of calculating complexity in order to make comparative analyses but much remains to be done.

4.1 The Progressive Policy Institute (PPI)

In 2010, the US President's Economic Recovery Advisory Board Report noted that the level of tax system complexity is very high. This complexity generates substantial costs for affected taxpayers and represents both time and money that taxpayers spend every year to prepare and file their taxes. It was estimated that taxpayers spend 6.7 billion hours and incur substantial expenses in meeting their federal income tax filing obligations. These costs are approximately equal to one percent of GDP yearly (or about $140 billion in 2008). These taxpayers' costs are also estimated at more than 12 times the IRS budget.[46]

The Progressive Policy Institute (PPI) reported a study ranking the tax systems of all 50 US states plus the District of Columbia (the State Tax Complexity Index). The index calculates tax complexity with regard to the number of tax expenditures in the tax code for each state revenue system. In other words, PPI has prepared an index of tax complexity based on the number of tax expenditures offered by each state. Several states do not provide complete reports on tax expenditure data. These non-transparent states received the highest ranking in the survey because producing a thorough list of tax expenditures is a key first stage in reducing complexity. Several relevant conclusions were drawn from the data summarised in Table 1 below:

1. All tax systems suffer from too much complexity

2. The type of tax structure does not define the level of complexity. Complex tax systems exist in states with progressive income taxes, states with a flat rate income tax, as well as states with no income tax. Tax complexity is everywhere in the US

3. Decreasing tax complexity through removing tax expenditures can finance lower tax rates and rise fairness because their benefits commonly go to higher income individuals and businesses[47]

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[42] PricewaterhouseCoopers International Limited, Paying Taxes 2013 ((2013) <http://www.pwc.com/gx/en/paying-taxes/assets/pwc-paying-taxes2013-full-report.pdf>.

[43] Jones et al., above n 29.

[44] Binh Tran-Nam and Chris Evans, 'Towards the Development of a Tax System Complexity Index' (2014) 35(3) Fiscal Studies 341-70.

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[47] Weinstein, above n 41.

Table 1: State Tax System Complexity Index: Complexity as measured by tax expenditures

State	Range of Tax Expenditures	Rank	State	Range of Tax Expenditures	Rank
Alabama	N/A	1	Rhode Island	200 to 250	24
Florida	N/A	1	Texas	200 to 250	24
Indiana	N/A	1	Colorado	150 to 200	29
Nevada	N/A	1	Connecticut	150 to 200	29
New Hampshire	N/A	1	Michigan	150 to 200	29
South Dakota	N/A	1	Missouri	150 to200	29
Wyoming	N/A	1	North Dakota	150 to 200	29
Washington	550 to 600	8	South Carolina	150 to 200	29
Louisiana	450 to 500	9	Vermont	150 to 200	29
Oklahoma	450 to 500	9	Virginia	150 to 200	29
Arizona	400 to 450	11	California	100 to 150	37
New York	400to 450	11	Hawaii	100 to 150	37

On the basis of these findings there does not seem to be a significant link between the level of tax expenditures, the tax structure, and complexity as measured by the OTS Complexity Index.

This ranking has been criticised by Tran-Nam and Evans.[52] Even though the PwC Paying Taxes ranking ensures an appropriate method for the international comparison, its usefulness as an index of overall tax complexity appears to be limited for a number of reasons as follows:

1. The indicator of the total tax rate is calculated as a tax burden instead of tax complex 0 Td [(o)10.9 (f)-4 (o3 >s4s)4 (l)-4.6 ( )-4.6 (houg)10.8 (h t)TJ 0.002 T

The aggregation formula is much simpler and a multiplication factor is included to extend the index to give scores between 1 and 10:

$$[(Y^1 + Z^1 + \ldots n^1)/4]*10$$

where 'n[1]' represents a normalised indicator, a score of 10 means the most complex tax possible and a score of 0 the least complex. As mentioned above, the OTS Complexity Index is made up of two main complexity indexes. One is the Underlying Complexity Index, which contains policy complexity, legislative complexity, and operational complexity. The other is the Resource Index.

They have contributed to the complexity literature and mainly focused on the construction of a tax complexity of a specific country at a particular time. Moreover, it has to be said that it was overambitious to put together a single index number for the entirety of a tax system. Their approach was based upon a combination of the test and statistical approaches in index number theory. The proposed index possesses certain desirable properties, which limit the functional form of the index formula. The statistical method was also used in a manner that the index formula was derived as a measure of central tendency.

Evans and Tran-Nam have considered two indexes, one devoted to business taxpayers and the other for personal taxpayers. A combination of the test and statistical method was considered to be the most appropriate approach. However, the index designed was not [illegible]

2 affects 10,000 to 100,000 taxpayers; and it continues up to 5, which impacts on 10 million and above taxpayers (for example, VAT and income tax).[61]

Comparative data for the four countries were collected from the Australian Government official website,[62] Nllan27 (d)2 (G)16.6 (o26 (v)-2.8 ((r)-6 (n26 (m)-9.1 e(n26 tl)-2.(

not been separated out between different taxes but it is noticeable that, as might be expected, the aggregate impact of VAT/GST is usually lower than for income tax.

Taking the Underlying Complexity Index together with the Resource Impact Index, Turkey has the lowest score for the former and the highest for the latter. There are also significant differences for the other three countries with the Underlying Complexity Index though they are much closer together regarding the Resource Impact

administration costs per 100 units of net revenue collection comes from

heart of this process which inevitably encourages progress and brings considerable benefit to the wider public. It is obvious that there is a need for fundamental changes in tax simplification culture.

7. ANNEX

Table 6: The UK Data (2014)

Table 9: Standardised Indicators for Turkey

	Underlying Complexity Index			Resource Impact Index	
	Policy Complexity		Legislative Complexity	Average resource cost	Aggregate impact
Taxes	Numbers of exemptions plus th[redacted]	Changes to legislation (since 2000)	The Gunning Fog		

Tc 0 c 0 -2.23Tw 2

Table 13: Indexes for Turkey

	Income Tax	VAT	Total Underlying Complexity[69]

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The relationship between principles and policy in tax administration: Lessons from the United Kingdom capital gains tax regime with particular reference to a proposal for a capital gains tax for New Zealand

Simon James[1] and Andrew Maples[2]

Abstract

It is unusual to find a tax in operation which does not represent a compromise between tax principles, policy and administrative considerations. However, the third of these, tax administration, often does not receive the attention it should as proposals for tax reform are developed. This paper examines one particular case, the possibility that attempts to introduce a capital gains tax (CGT) in New Zealand (NZ) have been unsuccessful because the right balance between the three dimensions of tax reform has not been achieved and that for this and other possible reforms each of these aspects should be given the appropriate consideration. New Zealand does not currently have a comprehensive CGT. In fact, political commentators have long said that the enactment of a CGT in NZ would be 'political suicide'. The reasons for such antipathy towards a CGT are not entirely clear especially given the successful implementation and operation of CGT in many jurisdictions, including the United Kingdom (UK). However, sentiment towards a CGT in NZ appears to have softened more recently. Perhaps sensing this rise in support, the centre-left New Zealand Labour Party in the 2011 and 2014 general elections unsuccessfully campaigned on, inter alia, introducing a comprehensive CGT. It is unclear what part the CGT proposal played in its defeat in both elections with other factors in play. However, noting that the CGT policy may have alienated voters in the 2014 election, Labour Party leader, Mr Andrew Little has indicated that reform of the NZ tax system, including a possible CGT, would not be made 'without going to the people first and getting a mandate to do so'.3 Accordingly, the electorate support for a CGT, and its design (including the administration of the tax), will be crucial for its political viability in NZ; hence the rationale for this paper. The paper finds that the UK CGT is a very robust tax but has never taken a pure form based only on the principles of good tax design. Indeed its success in tax policy terms has been largely accounted for by pragmatic modifications over the years to accommodate the different and changing political and economic pressures applying to modern tax systems. The paper concludes that a more pragmatic approach could lead to the design of a CGT that may gain the broad support of the NZ electorate and also be as enduring as it has been in the UK.

Keywords: capital gains tax, tax administration, tax policy, tax principles, sustainability, tax compliance

1. I

However, the country is unusual among Organisation for Economic Development and Cooperation (OECD) countries as it does not have a comprehensive capital gains tax (CGT).[19] Rather, certain specified capital gains are taxed in the *Income Tax Act 2007* (NZ). Despite various committees considering the implementation of a CGT in NZ, admittedly with differing conclusions,[20] and overseas bodies such as the OECD[21] noting the benefits of a CGT for the NZ economy, there has been a longstanding antipathy against adopting the tax. While more recently sentiment may have softened among some business leaders and politicians,[22] more will be required in order for any

equity and efficiency. An understanding of the antipathy toward the tax in NZ, and whether Labour's proposals contain the right balance between policy, principles and administration, may aid in the development of a CGT policy in NZ.

In fact, at first sight, one of the difficulties with the various committee reports considering the introduction of a CGT in NZ as well as Labour's recent proposals is that administrative issues have been insufficiently addressed and as a consequence seen as insurmountable.[32] Huang and Elliffe posit that:

> The reason historically that New Zealand does not have a CGT is not because New Zealand policymakers fail to recognise the benefits of such a form of taxation, but because they have been overawed by the perceived problems and cost associated with it. In looking at the history of this tax

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New Zealand's experience with another new form of taxation—the goods and services tax—has been very positive[39] partly because it did not face serious administrative concerns. The emphasis of the policy design of the GST strongly focussed on simplicity with equity concerns being dealt with outside the GST itself (via the welfare transfer system).[40] As a consequence the GST is economically very efficient. This positive experience with a comparatively 'pure' tax, with its few exemptions,

centre-left parties, it is probable that Labour will drive the policy design of any future CGT. The 2011 and 2014 policy statements are currently the best indication of the shape of such a tax at this point and no doubt will inform the development of any future policy. It is clear from a reading of the policy statements that they are the product of much research and analysis (even though essentially produced as part of Labour's election manifesto). Second, and related to the first point, of the politicamhou(x a)9.ec.N

> forward to a point which many did not believe was possible six months ago. This new tax will provide a background of equity and fair play for his work.
>
> Moreover, there is no doubt that the present immunity from tax of capital gains has given a powerful incentive to the skilful manipulator of which he has taken full advantage to avoid tax by various devices which turn what is really taxable income into tax-free capital gains. We shall only make headway against avoidance of this sort when capital gains are also taxed. [61]

So, in theory at least, the economic principles of efficiency and equity suggest there is a straightforward case for treating all capital gains as income but there is also the third criterion mentioned above of administrative considerations. Needless to say, there would be practical difficulties in taxing capital gains in precisely the same way as other income. The first and most obvious difficulty concerns capital gains which arise only through increases in the price level. Such nominal gains do not, of course, increase an individual's real spending power and should not in principle be counted as income.

A second problem is that, in theory, CGT should be levied on an accruals basis. In practice this would involve the valuation of capital assets for each tax year, so imposing a considerable administrative burden. It would also involve the risk that individuals might be forced to liquidate assets in order to pay the tax which might involve undesirable outcomes regarding business assets. In the UK, CGT avoids such problems because it is levied on a realisation basis. However, this also presents challenges. Taxpayers might find themselves 'locked in', in the sense they have an incentive to postpone payment of the tax by not realising the asset even when it might otherwise be economically efficient to do so. Also, because assets are realised in uneven lumps, it is difficult to make the tax progressive. This difficulty may be aggravated because capital gains, whether realised or not, may occur irregularly.

Valuation can also be a consideration. Even with the realisation basis, it is necessary to determine the value of the asset when acquired and when realised. This will often be a straightforward exercise—it will simply be the value agreed between third party buyers and sellers. For other transactions, such as the sale of an asset originally received by way of gift, determining the value of the asset (in this case when received) may be more difficult.

3.2 The United Kingdom experience

Although there had been previous attempts to tax certain types of capital gains, especially from l

Capital gains accruing to incorporated companies are also taxed but by corporation tax on their gains rather than CGT.

Although there have been several different ways of taxing a chargeable gain, the calculation of the gain itself has remained much the same. As one might expect, this is basically the sale proceeds less the purchase cost. One way in which the gain may work out to be smaller than at first expected is due to the sensible treatment of expenses. Those paid at acquisition are added to the original costs; those paid at disposal are deducted from the proceeds.

4. LESSONS FROM THE UNITED KINGDOM

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4.1 Labour's capital gains tax policy—an iis

basis with few, if any exemptions.[70] This form of CGT has been rejected by various NZ committees, let alone other countries including the UK, as unworkable. Second, (and the approach favoured by the authors) is that it could be based on a pragmatic approach which, considering broader tax administration, tax policy and design principles, departs from the comprehensive concept of income. Compromise and trade-off will be required under such an approach but hopefully will lead to a tax that is politically sustainable. Such an approach is contrary to that adopted by the GST where the policy design strongly focussed on simplicity but will be necessary for the successful implementation of a CGT.[71]

Labour's policy has taken certain administrative issues into consideration. As noted, the CGT would be levied on a realisation basis and will thus avoid both the burden of valuing assets annually and the potentially negative cash flow impact on taxpayer's required to fund an accruals-based tax. The policy trade-off will be the potential 'lock-in' of assets. Further, the tax base is not indexed for inflation. In a period of low

	UK	NZ
	Can be carried backwards for gains at death.	Panel to consider upper limit for offset of losses.
Treatment of gains at death	No CGT but rollover provisions for heirs and taxable at market value on realisation.	No CGT but rollover provisions for heirs and taxable at market value on realisation.
Treatment of gifts	Gifts subject to CGT unless to spouse, partner, civil partner or charity.	Gifts subject to CGT. Rollover where assets transferred between a couple in relationship break-up.
Private residence exempt?	Yes	Yes
Personal property exempt?	Yes—CGT on disposal of personal possession for £6,000 or more (eg jewellery, paintings, antiques, coins and stamps, sets of things such as matching vases or chessmen). No CGT on motor vehicles unless used for busi 9 Tc uynn BT 0.002 Tc 0.237 Tw -2.3 (36.4 58p8)1.9	

and Davey's NZ study.[77] There are two very practical tax administration impacts from the introduction of a tax-free threshold. First, it 'has the advantage of

As a consequence, and as indicated in Section 4.2, the authors favour a separate CGT with a tax-free threshold. This will ensure a level of progressivity with the CGT. Multiple CGT rates could also be introduced depending on the strength of the equity concerns to be addressed by the CGT. However, in addition to the complexity and tax administration issues noted above, differential rates could also encourage manipulation to avoid the higher rate(s). Therefore any decision to include more than one CGT rate will require careful consideration. on.3371lpu]TJac 0.165s ca23.6503c 0.165 6.9 (w

whether investment in such collectables is to be encouraged. As a tax policy consideration, arguably these are generally not the types of assets that a nation wants

the administration of the tax. Despite this a UK approach to 'collectables' can be justified when the focus is on tax policy and tax principles.

An alternative approach to address the concerns over determining who is (or is not) a dealer, would be to treat all gains from the disposal of personal property as ordinary income subject to income tax. While this would remove the boundary issues referred to above, and therefore positively impact on one aspect of the administration of the tax, in the absence of a tax-free threshold for ordinary income, this treatment would also impose compliance costs on taxpayers deriving small gains and administrative costs for Inland Revenue. This, in turn, would undermine the political sustainability of any such measure.

4.7 'Remember the little fella'—business concessions

The 2014 policy statement proposes the exemption of '[s]mall business assets, up to a maximum of $250,000, sold for retirement, where the owner is above a certain age (e.g. 55) has held the business for 15 years and has been working in the business'.[122] The term 'small business' is not defined. This and other details would be considered

acquired within 3 years of the disposal of the original assets. Further, under the Gift Hold-Over relief, no CGT arises where business assets are given away or sold for less than they are worth.

Evans and Sandford argue on equitable grounds that rollover 'provisions need to exist where involuntary disposals occur (compulsory acquisitions, corporate takeovers and mergers, destruction of assets through natural disasters, etc)'.[131] Similarly, on efficiency grounds they argue 'for deferral of the capital gain where taxpayers are rolling the proceeds of the disposal of one asset into a bigger asset, in order to grow a business'.[132]

Aside from Evans and Sandford's arguments in favour of the very specific

BBLR and its consequential focus on simplicity and broad coverage will therefore be required. It is clear from a consideration of the UK CGT regime that it introduces significant additional complexity into the tax system, due in part to policymakers introducing specific concessions. While in a 'pure' system such exemptions and concessions should be limited to minimise complexity and opportunities for tax planning, from an administration perspective there are a strong arguments for some relief, such as a tax-free threshold, to reduce compliance and administrative costs.

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should keep in mind Gammie's caution: '[a CGT] is a compromise, and, as is so often the case with a compromise, it functions badly and pleases no one'.[136]

The near future would be an ideal opportunity to implement a CGT in NZ as the Inland Revenue has embarked on the Business Transformation programme (referred to in Section 4.0). This 10-year programme[137]

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To shame or not to shame: That is the question

Kalmen Datt[1]

Abstract

This paper evaluates the naming and shaming of large corporations and concludes that such a response is unhelpful and counterproductive. The author argues that the only effective response to tax planning schemes is to enact effective laws that capture the income sought to be taxed.

Without the media, naming and shaming would not be effective. Naming and shaming campaigns appear to be a (deliberate?) misconception of the tax laws. 'Avoidance' is given an indeterminate and open-ended meaning. The media is not sufficiently versed in the tax laws to make an expert judgement of avoidance. It is not their role to punish extra-curially without any legal basis for assigning blame/guilt.

Keywords: Naming and shaming; tax planning; avoidance; effective legislation and Google.

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1. INTRODUCTION

This article evaluates the approach that the media, activists and politicians take to the manner in which large Australian and multinational corporations structure either themselves or individual transactions to ensure they limit their tax liability.[2] The response is to name and shame the entities concerned.

This article concludes that naming and shaming is unhelpful, counterproductive and

When shaming occurs there is some form of conscious manipulation of an entity with the purpose of obtaining some desired but different result to that about which [12]

[13]

Braithwaite and Drahos believe that naming and shaming may cause corporations to take steps to determine personal responsibility and '[put] things right'.

[14] According to them this is a relatively cheap remedy an d it could reflect society's moral outrage at the conduct.15 They contend that if the corporation is named, then internal compliance

[16]

systems go to work to define personal responsib

complaint has been made.

The learned judge in the above extract was commenting on the injustice of a penalty being imposed on different entities for the essentially the same act. With naming and shaming a penalty may be imposed for no wrongful conduct, but if such wrongful conduct were found to exist there would be a double penalty on the same party first in being shamed and second the penalty imposed by the court or regulator.

Grabosky and Shover, although referring to criminal conduct, consider that the refusal to acknowledge the criminality of conduct is one of the sharpest distinguishing characteristics of 'white-collar' criminals. Ways of mobilising public indignation to combat this is something worthy of consideration, to induce those targeted to acknowledge their wrong and to take steps to make amends.[19]

Shame can occur without the publicity of being publicly named. Grasmick and Bursik describe shame as the feeling of guilt one experiences after having committed a wrong; it is a self-imposed punishment.[20] The greater the wrong committed, the greater is the prospect and extent of the feeling of shame.[21] Grasmick and Bursik found, after surveying a number of respondents, that the prospect of feeling shame inhibited tax cheating.[22]

when criminal charges have been laid and made public because the public ascribes real meaning to cases in which criminal conduct is alleged by the state. This has

than $8.4 billion of tax.[39] Although not directly alleging wrongful conduct on the part of the corporations named in the report the inference (incorrectly) drawn is that these companies either have been guilty of what is referred to as 'aggressive corporate tax avoidance' or 'aggressive tax avoidance' or 'tax aggressive behaviour' or 'aggressive tax minimisation practices' . The meaning of these terms is never explained.

The fact that a corporation pays little or no tax in Australia means nothing without reference to the particular circumstances of that corporation and how the tax laws impact on its various transactions. Notwithstanding the foregoing, the report advocates that these corporations be named and shamed. It states:

> Disclosure and transparency of corporate tax practices needs to be increased. Greater public awareness of aggressive tax avoidance will provide an incentive to Australian corporations to be less tax aggressive. Tax dodging practices, when exposed, will damage corporate reputations and may increase regulatory and financial risks. Responsible companies should not wait for inevitable changes to the rules before deciding to act.[40]

This report was given headline treatment in the media. Examples include: Aston and Wilkins[41] who describe the main findings of the report and then give some views that do not agree with the conclusions reached; and Shorten and AAP where the results of the report are extensively reported.[42]

It is the media that gives credence to misleading claims about the tax affairs of corporations by politicians and activists rather than objectively and accurately reporting on their tax affairs. Reality and candour appear to be of little consequence.

Tulberg argues that corporations are vulnerable to media power and that the solution is one of appeasement to avoid being a target and to protect the value of the company brand.[43] According to Tulberg, there is an absolute right or wrong and the media are the sole arbiters on these issues, irrespective of whether their views are correct. It is often difficult to respond to such attacks in a way that resonates with the public.

There would appear to be little or no accountability on the part of the media, politicians or activists as to the accuracy and truth of what they publish or disseminate. Simply to make broad unsubstantiated allegations is not acceptable conduct from elected representatives who have the power to enact effective laws that capture within the tax net that income which is currently not assessable. Similarly the media may be abusiher

Silverman, referring to the media states:

> Then there is the question of accountability. Kipling's resonant description of the press as the guardian of "power without responsibility
>
> [illegible]
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3. I

> Google funnelled £6 billion through Bermuda last year, halving its 2011 tax bill and paying £1 billion less to government coffers.
>
> The company paid £6 million in UK tax last year, funnelling 80 per cent of its global revenue through the tiny island of Bermuda, twice as much as three years ago.[63]

BBC News Magazine on 21 May 2013 reports:

> In a report published on Monday, the committee's chairwoman Margaret Hodge said the level of tax taken from some multinational firms was "outrageous" and that HM Revenue and Customs needed to be "more aggressive and assertive in confronting corporate tax avoidance".[64]

The Register of 14 June 2013 states:

> British MPs have demanded that the government act to revamp the tax structure after damning revelations about Google's corporate payments structure in the country.[65]

The Telegraph

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The use of CAATTs in tax axS</M6>]TJS</ED>63

1 2

Abstract
This article presents a comparative study of the state-of-the-art kemenkeu.go.id

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1. INTRODUCTION

programs, activities, and processes of an individual and a group of individuals in their natural settings. A case study is bound by time and activities which define the scope of the research (Bhattacharya, 2008; Creswell, 2009; Yin, 2009).

According to Creswell (2009), research design is also concerned with methods; the means through which data is collected and analysed to construct an interpretation of the object of study. In this study, the data was sourced from documentary materials around the implementation of CAATTs issued by each of the tax authorities as well as published by consulting firms, research institutions and media releases. Bowen (2009) defines document analysis as a systematic procedure for examining electronic and print documents to reveal empirical research findings.

More specifically, the study used comparative institutional analysis (hereinafter 'CIA') as a frame of reference in collecting, transforming, analysing, and interpreting the data. Referring to Bowen (2009), document analysis can be part of (or incorporated with) other types of data analysis techniques. In this regard, we combined document analysis and CIA. CIA is one method available for comparative tax research. It uses a technique that combines tax problem, tax model, and tax mechanism; a pattern suggested by Garbarino (2009). The relationship between the three as a data analysis technique is determined by combining them with the core elements of CIA as follows:

1. determining the tax problem, in which case how the use of CAATTs influence tax audits
2. determining the tax model, which is the amount of available institutional choices with regards to tools and audit techniques including regulations surrounding CAATTs
3. determining the tax mechanism, which refers to the working rules or the selected institution for exchange. In this regard, it transpires in how the tax authority eventually determine the tax audit procedures which should use CAATTs.

Detailed explanations on CIA are presented in section 4.

This study follows the analytical framework in Debreceny et al. (2005) which uses qualitative methods to examine the extent to which generalised audit software has been utilised in banking sectors. The paper begins with a description on the sequential steps of conducting CIA for the purpose of comparative tax research (Garbarino, 2009). The detailed steps are important to illustrate the trilogy of tax

Tax authority	Description issued by the

In response to the variety of institutional roles and positions, Williamson (1998) suggests four levels of social analysis to differentiate institutional roles and positions based on the level of durability and maturity. These four levels distinguish one form

form of fiscal institution. Tax audits and CAATTs are both the selected institutions to realise the expected social interactions, that is, tax compliance. Building upon Williamson (1998), CAATTs can be positioned as a configuration shown in Figure 1. CAATTs in this setting are situated within level 3 and 4 which afford a discussion on institutional choices and the most relevant mechanism options available to the environment.

Figure 1: Choice of CAATTs and tax administration in four levels of social analysis—adapted from Williamson (1998)

From a conceptual and practical perspective, CAATTs use in audits is a response to the ubiquity of enterprise information systems which produce digital audit trails. Such a response manifests in the handling of digital audit trails from data test techniques to continuous auditing. Hardware-wise, CAATTs can take place in the

introduction of SAFT will place a burden on taxpayers in their efforts to meet the requirements of the standardised data format.

Based on the above, the authors propose some important criteria to compare how those tax authorities apply CAATTs in their tax audit

techniques so long as the implementation does not temper the taxpayers' running of business while being audited.

4. The relative position of digital forensics in the landscape of CAATTs use in tax audits. Tax audits have the potential to reveal fraud. This would require further treatment in the form of investigative audits. Questions remain on how the transition from CAATTs use in tax audit can be facilitated

	unzip/uncompress), number of records, length of records. • If company cannot deliver accounting system files where transactions are primarily recorded, tax auditors alternatively request reporting files or list files. Accounting systems create reporting files and transaction lists associated with the general ledger and journal receivable and accounts payable[6].	
Germany	Not specifically described	Direct access (Z1): Auditor has the right to independently access the taxpayer's computer systems which contain tax relevant data by using a user role that has been set up for the auditor The taxpayer has to provide the hardware een software so that the auditor can inspect the data

		analysis techniques			

Additional information:

The term tax-related data has not been defined nor specified respectively within the scope of the legal provisions for data access. The statutory record retention requirements and the data access refer to the documents mentioned in § 147 Sect. 1 AO

- Accounts and records, inventories, financial statements, management reports, opening balance sheet as well as the.6 (s)-2.3 e0078>Tj /s

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