The relevance and sustainability of co-operative compliance models for tax in African countries

Authors: Eelco van der Enden and Kuralay Baisalbayeva, PwC Netherlands
Introduction
Tax authorities have always felt the pressure ‘to do more with less’ due to budget constraints and limited capacity within tax administrations; these issues are increasingly becoming a common challenge for many countries, but especially in the developing world. To improve their position, many countries have already incorporated a co-operative compliance model into their tax enforcement strategies, along with a traditional command-and-force manner. Co-operative compliance is a new way to effective tax compliance management based on transparency, ‘justified trust’ and a better understanding of the taxpayer’s business and risk profile. If properly designed and executed, it has proved capable of enabling tax authorities and taxpayers to build a sustainable tax compliance infrastructure.

In the previous edition of *Paying Taxes* we introduced the idea of co-operative compliance and its history. This paper investigates the relevance and sustainability of co-operative compliance models for tax in African countries. Given the culture and challenges faced by both businesses and the tax authorities in these countries, we suggest some practical measures that can enable the effective and efficient implementation of sustainable co-operative compliance models in Africa. Although co-operative compliance is generally targeted at large companies, often operating across country borders, the underlying principles are relevant for companies of all sizes.

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71 African tax administrations: a Dutch multinationals perspective. In a recent study by the Dutch Association of Investors for Sustainable Development (VBDO, 2015), tax directors of the Dutch listed companies have identified the following challenges to taxation in developing countries:
- Opportunistic / aggressive behaviour of local tax authorities towards MNEs;
- Overly hierarchical and bureaucratic tax organisation, difficult to get a single point of contact;
- Time-consuming and costly appeal procedures;
- Multi-interpretable, complex and fast-changing tax laws;
- Corruption within governmental bodies;
- Lack of capacity and skills of local tax authorities;
- Different perspectives, difficult to establish an open and transparent relationship with local tax authorities.
Businesses struggles to establish the right dialogue and good working relations with local tax authorities in many developing countries. However, MNEs are crucial for the financial development and economic sustainability of these countries with an estimated annual contribution of 750 billion dollars to local economies (UNCTAD, 2015). *Paying Taxes* refers to a medium sized enterprise, however we believe that the concepts outlined in this paper remain relevant.
Co-operative compliance – what, how and why?

The co-operative compliance concept can be best described as a means to effective tax compliance management based on mutual transparency, justified trust and a better understanding of the taxpayer’s business and risk profile. The objective is improved tax compliant behaviour – payment of the right amount of tax due on time, at lower costs of compliance for both tax administrations and businesses.

In 2006 the OECD’s Forum on Tax Administrations (FTA) concluded that tax authorities should have effective risk-management processes in place, enabling them to effectively allocate their resources to those taxpayers with a higher risk profile. Tax authorities were prompted to create solid relationships with taxpayers by:

- understanding the business based on commercial awareness,
- being impartial,
- acting in a proportionate manner,
- being prepared to be open (transparent), and
- being responsive.

In theory, if tax authorities could demonstrate these attributes, taxpayers from their side should be more likely to engage in “a relationship with revenue bodies based on co-operation and trust with both parties going beyond their statutory obligations” (OECD, Study into the Role of Tax Intermediaries, 2008, p. 5).

Since 2008 many tax authorities have implemented compliance risk management strategies and co-operative approaches to businesses. In addition, increased attention has been given to the concept of a ‘tax control framework’ (TCF) as a key tool to disclosure and transparency (OECD, Co-operative Compliance: A Framework – From Enhanced Relationship to Co-operative Compliance, 2013, p.13). In May 2013, the OECD published the report ‘Co-operative Compliance: A Framework, From Enhanced Relationship to Co-operative Compliance’, thus providing more practical guidance on how to achieve improved compliance. ‘How do I know as a tax administration that I can trust a tax payer?’ was a question that was raised by many tax officials. The trust element of the relationship between tax authorities and a taxpayer has to be justified. This justification can be found if a taxpayer has an internal control system in place that assures the accuracy and completeness of the tax returns submitted by the taxpayers. In other words, if the taxpayer has a functional TCF in place.

Co-operative compliance in African countries

This section is based on the results of a survey of telecommunications operators and PwC offices in Botswana, Cameroon, Democratic Republic of the Congo, Ghana, Kenya, Namibia, Nigeria and South Africa. The selection of countries from all over Africa represents a comprehensive approach to studying compliance practices on the African continent.

To date, only one of the surveyed countries has incorporated a co-operative compliance model in its risk management strategies – South Africa. The South African Revenue Service has introduced a formal co-operative compliance program – ‘taxpayers engagement strategy’. It involves compliance enforcement activities to mitigate prioritised risks and adjust the audit strategy depending on the taxpayer’s compliance profile. Whilst Botswana, Kenya and Namibia have taken steps to enhance the relationships with some taxpayers, still a majority of tax authorities in African countries perform detailed testing of almost all underlying records of the tax returns and rely on the taxpayer’s audited financial statements to a certain extent.

The survey respondents identified the following specific challenges in complying with their tax obligations:

- lack of suitably qualified and experienced tax officials;
- poor quality record keeping at the tax authority;
- delays in tax assessments and audits, obtaining clarifications and responses to issues;
- burdensome tax system, time demanding for preparation and submission of tax returns;
- lack of IT infrastructure at the tax authorities;
- lack of transparent guidelines from the tax authorities;
- high rate of tax evasion;
- no timely revision of tax legislation.

72 The OECD Forum on Tax Administration (FTA) for Commissioners from 45 OECD and non-OECD countries, including every member of the G20, was created in 2002 with the aim to improve taxpayer services and tax compliance by helping tax administrations increase the efficiency, effectiveness and fairness of tax administration and reduce the costs of compliance. See OECD / FTA website http://www.oecd.org/site/ctpfta/
Faced with these challenges many businesses struggle to establish the right dialogue and good working relations with local tax authorities. However, businesses are crucial for the financial development and economic sustainability of African countries. If tax authorities want to improve their relations with businesses, as well as assure their proper tax compliance, introducing a co-operative compliance model could be an effective solution. A number of suggestions for how to apply the co-operative compliance models in practice are provided below.

**Suggestions for African countries on co-operative compliance models**

1. **Set up clear measurable key performance indicators**
   Defined measurement parameters will enable the tax authorities to evaluate its effectiveness afterwards. This could for example be measured in terms of reduced compliance costs and hours.23

2. **Define the benefits for taxpayers – quid pro quo**
   Co-operative compliance requires ultimate transparency and providing information beyond formal legal obligations. Taxpayers should know what the benefits are and which value add it derives in return from the tax authorities, e.g. lower costs of compliance and/or greater certainty on tax positions.

3. **Define the concept of trust – Tax Control Framework**
   A TCF is the basis for establishing an open dialogue and justified trust between tax authorities and taxpayers. The focus of the TCF is “to be … able to detect, document and report any relevant tax risks to the revenue body in a timely way” (OECD, *Co-operative Compliance: A Framework – From Enhanced Relationship to Co-operative Compliance*, 2013, p.59).

4. **Define an auditing standard for TCF**
   A TCF should be auditable and based on clearly defined and communicated standards or guiding principles. There may be a need for additional certainty – assurance on the reliability of the taxpayer’s ‘in control’ statement, e.g. by auditing TCF on the basis of existing internationally recognised auditing standards.

5. **Managing disputes within co-operative compliance programs**
   If disputes arise, co-operative compliance helps ensure that disputes are managed in the most effective and efficient way. It is also very important to demonstrate impartial treatment of all taxpayers within and outside co-operative compliance relations.

6. **Enable tax authorities employees**
   It is of great importance to train tax administration employees on the co-operative compliance concept. It is based on a broad ‘system’ type of approach and it involves understanding business processes and assessing the TCF, including the quality of the technological infrastructure; these are not within most tax administrations’ traditional data testing approach.

7. **Leverage on technology to ensure compliance**
   Many tax authorities are beginning to understand the value of leveraging technology to achieve compliant behaviour in the most efficient way. As shown by the sustained falls in the *Paying Taxes* time to comply and payments sub-indicators, taxpayers are increasingly using advanced digital self-services, which make it easier and more efficient to comply with tax obligations.

**Conclusion**

The search for new and effective ways to assure tax compliance is becoming a common issue for many countries worldwide. In African countries, capacity building of tax authorities and domestic resource mobilisation are among the top priorities for many economies. Taking steps to create a culture that builds on the principles of co-operative compliance may be a way forward for many African countries, with the potential to instigate pilot projects using the co-operative compliance model.

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23 *Paying Taxes* identifies the time to comply with tax systems in 189 economies.
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