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Digitalization and other opportunities to improve tax administration

Secretariat note

Summary

Developing countries need to finance the spending necessary for sustainable development, with domestic revenue mobilization (DRM) critical to achieving that goal. In the quest to mobilize more resources to finance public expenditures for economic and social development, it is important that governments design effective tax systems that will facilitate the achievement of DRM. Well-planned, efficient, and equitable taxation helps to pursue economic growth, reduce inequalities, combat poverty, and provide social services. A key component of efficient tax systems is digitalization. Manual processes and procedures limit the efficiency of tax administrations and greater efficiency could be achieved by digitalizing these processes. Moreover, in an increasingly digitalized business environment, tax administrations need to digitalize their processes to effectively tax digitalized businesses.

This note highlights issues for consideration in assisting tax authorities to digitalize their operations and improve administration of taxes. This paper is *for decision* from the Committee on whether to advance work on digitalizing tax authorities and if so, whether to form a subcommittee with the mandate to provide guidance to developing countries in digitalisation and other opportunities for improving tax administration.

INTRODUCTION

1. Information and Communication Technology (ICT) has made technologies cheaper, more powerful, and widely standardized, improving business processes and bolstering innovation across all sectors of the economy. As a result of this, the economy has become digitalized, changing many business models and giving rise to new ones.

2. Tax administrations need to adopt some of these technologies, as they realise the benefit of doing so in keeping up with the changing business scene as well as effective taxation of the digitalised economy, which is slowly becoming the mainstream economy. The Covid-19 pandemic has accelerated this transformation and many businesses have had to become digitalized to remain relevant and afloat. Over the past years, tax administrations moved many of their processes online. A survey by the OECD Forum on Tax Administration (FTA)¹ completed by some of its members showed that this move allowed them to substitute in-person communication with a virtual or digital means during the crisis and shift a significant percentage of communications from paper to digital, in many cases 75% or more. This development was further reinforced during the crisis. While about half of the administrations considered their digital channels sufficient to deal with the increased demand, the others addressed shortcomings through introducing enhancements to existing services or by developing new services such as applications and virtual assistants.

3. For improved revenue collection, it is important for tax authorities to improve administrative efficiency. Use of information technology, enables the authorities achieve substantial efficiency gains. For countries beginning their digital transformation, AI-enabled data capture of paper-based records can speed up the digitalization and reliability of the data. Others find significant value through the simplification of procedures and matching of filing information with third-party data sets.

4. For more advanced tax administrations, the use of advanced analytics to identify underreporting will be a key value driver. In the current crisis, some administrations are also rethinking their balance between offsite and onsite audits. It also becomes easier to implement the one-stop-shop concept, making it easier for taxpayers to be tax compliant.

5. Further, it is important that tax authorities seek to minimize the compliance burden for taxpayers. A survey of 190 economies has shown that it is getting easier for people and businesses to pay taxes. There are now 106 economies using electronic filing systems, double the number in 2004². Digital technology is reducing the time spent on paying taxes, as well as the total number of individual payments taxpayers must make each year.

ISSUES

6. The Committee work in this area could explore ways of supporting developing countries in digitalization, as well as improving tax administration, starting with the provision of guidance for revenue authorities on how to develop a road map for digitalization. As a first step in digitalization, revenue authorities need to develop a road map for digitalization. It will

¹ Tax Administration: Digital Resilience in the COVID-19 Environment (reference document, PDF, webbook), published 21 April 2021

² <https://www.pwc.com/gx/en/services/tax/publications/paying-taxes-2020.html>

serve as a communication tool, a high-level document that helps articulate strategic thinking, the why behind both the goal and the plan for getting there. For better focus and to ensure that digitalization serves the desired purpose for the revenue authorities, it is important that they come up with a strategic plan that defines their goals or desired outcome and include the major steps or milestones needed to reach it.

7. This road map would need to be specific to each country's needs but incorporating an international outlook to ensure integration with the global tax scene. As part of the road map, it is important to incorporate an explicit element of time. The time required for each step towards full digitalization should be outlined, in line with the available resources and expected outcome.

8. The Committee's work should also aim at guidance on the areas of priority for digitalization. Which taxes, which processes for the said taxes and what part of the operations of the tax administration should be digitalised to maximise on the benefit in tax collection, based on examples of best practice from both developed and developing countries. This guidance should assist revenue Commissioners make decisions on areas of priority for digitalization as well as determine how to integrate these systems into a harmonious operation.

Committee guidance in this area could focus on the following issues:

Technical support

9. The support offered here starts from identifying what systems are appropriate for the country and their compatibility with existing systems, if any. This support further extends to capacity development in improving the skills of the tax authorities' staff, as well as options for the maintenance of the systems and equipment used, if any. ICT systems are also costly to procure, operate and maintain and hence the Committee can identify cost effective solutions for developing countries.

Data

10. At the core of digitalization of operations in revenue authorities is data. There are several considerations to be made with relation to data. Tax Authorities need to review the data available to them, in order to determine:

- i. What data they are holding,
- ii. The integrity and quality of this data,
- iii. Where and how this data is held,
- iv. What the Authority wants to do with this data, and
- v. Whether it is sufficient for the purpose identified.

11. Over and above the data that the authority holds, it is important to determine whether there are linkages to other databases that may be required. For example, data on beneficial ownership of companies from company registries, or personal data from National Registration Authorities, government payment portals for service providers and other databases that are relevant to tax administration. Identifying the vital linkages will ensure that the data held and accessible to tax authorities is useful and serves the purpose of effective taxation.

12. Data governance is also an issue that the Committee can assist developing countries to address. It is important to ensure that there is effective data governance in tax authorities for the data to be consistent, usable, have integrity and be well secured. Towards this end, a data

governance framework would be important so that there are rules and procedures for the collection, storage and use of data. As data privacy regulations gain wide usage and acceptance, organizations must put in place safeguards to ensure that their data is consistent, trustworthy, and not misused. The Committee work in this area could support developing countries in the development of a data governance framework.

Technology

13. Identifying the right type of technology for the Tax Authority's needs and circumstances is vital. The right technology will be determined by a country's IT landscape and infrastructure. The kind of technology that a country settles on for digitalization of its operations must be consistent with the access its populace has, to the chosen technology. In many developing countries, the informal sector makes up a major percentage of the economic activity and therefore the technology adopted must seek to incorporate the unique nature of informal businesses. The technology must be easy to access and use, at minimal cost. A case in point is use of mobile phones to make payments, receive payments, access financial services etc. The Committee in assisting developing countries could provide guidance in identification of the most appropriate technology for their economies.

Digitalization of processes

14. The Committee's work in this area could entail examining the various processes in tax administration to determine the level of digitalisation and the tools to employ to achieve this digitalization.

- Taxpayer recruitment and tax base expansion. For a country's revenue to keep growing, it is important to recruit taxpayers and expand the tax base to ensure there's equitable sharing of the tax burden within a country. Digitalization of this process may involve use of artificial intelligence (AI) to collect and analyse data from various economic activities, as well as facilitate self-registration for new taxpayers. Data capture using AI technology of paper records is the first step towards digitalisation and it ensures that the data the authority has in their system is reliable and accurate. The work here could include providing guidance on the use of AI as well as capacity development.
- E-filing. Most tax authorities have now included e-filing as part of their processes. This has been especially useful during the Covid-19 pandemic, when manual filing has all but been eliminated due to safety concerns, for both the staff and taxpayers. Simplifying this process is critical to promote compliance. Data collection through use of AI is one way through which this process could be simplified, where the data collected is used for pre-population of returns for taxpayers, and all that is left for the taxpayer to do is verify and confirm the information on the return.
- Compliance Checks, Refunds processing and Audit. In the current crisis, administrations are leaning more towards offsite audits as opposed to the previous onsite audits. Remote working has seen a rise in off-site audits and checks for many tax authorities. Simplifying procedures and matching filing information with third party data sets comes in handy for tax authorities in these circumstances. For more advanced tax administrations, the use of advanced analytics to identify underreporting is a key value driver. This has also improved risk profiling, and authorities are better placed to make more targeted interventions. The Committee's practical guidance would assist developing countries to establish these systems.

Improving Tax transparency

15. Digitalization of tax authorities could also enhance transparency and trust in the tax system. Establishing electronic platforms for tax registration, filing, payment, and dispute resolution make processes clear for citizens, provide assurances that tax payments end up in an actual government account, and reduce the risk of officials abusing their discretion. Implementation of technologies provides researchers, think tanks, or any citizen the ability to independently analyse tax data without having access to personally identifiable information. This will provide for unprecedented transparency.

RECOMMENDATION

16. The Committee membership is diverse with a mix of experts from developed and developing countries allowing for broader sharing of experiences and expertise. The Committee can draw from the work and expertise of other organizations, while still maintaining an independent view that address the specific needs and priorities of developing countries.

17. Against this backdrop and presentation of issues, it is proposed that the Committee should form a Subcommittee on Digitalization and Improvement of Tax Administration, which would cover digitalization of tax administrations as well as related issues.

18. This subcommittee would be mandated to give guidance on the issues highlighted, as well as other areas for improving tax administration. Among the key deliverables would be developing a road map for digitalization of revenue authorities that would guide developing countries in their efforts at digitalization. Digitalization would be the main initial focus, but the Subcommittee could also have a role in identifying other opportunities to improve tax administration.

19. A possible mandate for a Subcommittee on Increasing Tax Transparency could read as follows:

“The Subcommittee is mandated to address the issue of Digitalization and Improvement of Tax Administration by;

- a.) Developing a road map for digitalization of revenue authorities which will include guidance on
 - Identifying the priority areas for digitalisation and the appropriate taxes.
 - Identifying the relevant technology and appropriate systems based on best practice from developed and developing countries.
 - Simplification of tax systems and procedures to make them user friendly for taxpayers after digitalisation.
 - Identifying the relevant skills necessary for digitalization, and any gaps on the skill level required
 - Future proofing the tax system
- b.) Providing guidance on the development of a data governance framework that considers the best use of available data and identifies gaps in the availability of quality data.
- c.) Proposing means of monitoring technological developments to identify relevant enhancements to the tax system

d.) Proposing other means of improving tax administration.”

20. The Subcommittee membership could include international organizations that have supported developing countries in digitalization, representatives from tech organizations and academia, as well as other stakeholders both government and non-government who would add value to this work.