TECHNICAL NOTES AND MANUALS

Revenue Administration: Developing a Taxpayer Compliance Program

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Revenue Administration: Developing a Taxpayer Compliance Program

Prepared by Barrie Russell

This technical note addresses the following questions:

- How do countries improve tax compliance?
- What is a taxpayer compliance program?
- What is the value of a taxpayer compliance program?
- What are the steps in developing a taxpayer compliance program?
- How often should the taxpayer compliance program be updated?

I. How Do Countries Improve Tax Compliance?

Improving tax compliance requires long-term reform efforts, beginning with strengthening the organization and management of the revenue agency, implementing robust collection systems (e.g., payment and withholding systems) and building capacity in core tax administration functions (registration, filing and payment enforcement, debt collection, audit, taxpayer services, and processing of appeals). Reform of the legal framework and judiciary is also often required to ensure that the necessary powers, penalty regimes, and dispute resolution processes are in place. Increasingly, information and communications technology is playing a critical role in compliance management (e.g., through automatic gathering of third-party information as a by-product of natural business processes; use of electronic invoices to facilitate real-time transaction monitoring and verification; and analysis of revenue risks).

Reform priorities to improve tax compliance differ across countries and regions, reflecting variations in stages of development, administrative capacity, and scope of tax abuse. One size does not fit all, so reforms need to be tailored to each country's circumstances. The relatively wider tax gaps and lower revenue productivity of developing and emerging economies generally suggest potential for bigger revenue yields from compliance improvement initiatives. For these countries, getting the fundamentals of revenue administration in place (especially taxpayer service operations and effective audit and enforcement) should be the first step. For

Note: Barrie Russell is a former Deputy Commissioner of the Australian Taxation Office and is a member of the roster of tax administration experts maintained by the IMF's Fiscal Affairs Department.

more advanced countries, more sophisticated approaches to compliance management can be taken. In this regard, a number of countries are adopting comprehensive tax compliance strategies (often referred to as "compliance programs"), building on the work undertaken by pioneers in this area (Australia, for example, developed its first comprehensive compliance program in the early 1990s). This technical note outlines a broad approach to developing a compliance program; it is based on international experience and follows the broad model recommended by the Fiscal Affairs Department (FAD) in delivering revenue administration technical assistance to IMF member countries. At the end of the note, two recent examples of compliance programs are summarized (Brazil and Chile).

II. What Is a Taxpayer Compliance Program?

A taxpayer *compliance program* is a high level plan which brings together in a single document a description of the most significant compliance risks identified in the tax system and sets out the broad detail of how the revenue agency intends to respond to those risks. It does not attempt to cover every aspect of a revenue agency's operational activities. Compliance programs are commonly structured around major taxpayer segments (e.g., large businesses, medium-size enterprises, small and micro enterprises, and individuals) and address compliance risks relevant to these segments.

The great majority of revenue agencies have moved away from administrative assessment systems under which all or most tax returns are subjected to examination prior to the issue of assessments to taxpayers, to a system of self-assessment which relies on most taxpayers *voluntarily* complying with their obligations to register, keep proper records, file correct returns and pay tax on time without the intervention of a tax official. Successful self-assessment systems are underpinned by an administrative approach which recognizes that voluntary compliance will be optimized through an appropriate balance of taxpayer education and assistance, simple laws and procedures, and risk-based verification programs:

- *Taxpayer education and assistance programs*—help taxpayers and their advisors understand their obligations and entitlements (taxpayers cannot comply if they do not understand the tax laws and procedures).
- *Simple laws and procedures*—make it easier and less expensive for taxpayers to comply with their obligations and access their entitlements (taxpayers may not voluntarily comply if the tax system itself makes it too difficult or too expensive for them to meet their obligations).
- *Risk-based verification programs*—create a downside to poor compliance behavior by detecting and deterring noncompliance through use of risk management approaches (taxpayers are more likely to comply if they perceive a strong chance of detection and see blatant noncompliers being brought to account).

Box 1. Features of a Typical Taxpayer Compliance Program

- A compliance program is structured around the major taxpayer segments, typically: (1) individuals; (2) micro and small businesses; (3) medium-size businesses; (4) large businesses; (5) non-profit organizations; and (6) government organizations.
- For each taxpayer segment, the program summarizes the economic, revenue and business environment (e.g., number of taxpayers, nature of entities, total tax contribution, number of persons employed, and structural features).
- The program addresses the risks in each of the taxes administered in each taxpayer segment.
- The program outlines the headline compliance issues and the specific risks for each taxpayer segment, and describes how the revenue agency intends to respond to these issues and risks. Headline issues have an impact across more than one taxpayer segment and include, for example, the global economic crisis, informality, international profit shifting and abuse of tax havens.
- The program records the number and type of different service and control initiatives planned to be undertaken in the coming year within each taxpayer segment.
- Reporting against these commitments ensures that the planned activities are carried out and helps build community confidence in the administration of the tax system.

The purpose of a taxpayer compliance program is therefore to identify and respond to the most significant risks in the tax system through a range of measures aimed at the underlying causes of the noncompliant behavior. The objective is to achieve the widest possible impact on voluntary compliance across the taxpayer population. [1] Box 1 lists the features of a typical taxpayer compliance program.

III. What Is the Value of a Taxpayer Compliance Program?

Tax agencies are required to manage within a finite budget which is never enough to deal with all risks in the system at one time. As a result, they require an intelligence-led and evidenced-based methodology for identifying the most severe risks in the system and determining the most rational allocation of their resources. The development of a targeted compliance program on a cyclical basis allows a revenue agency to systematize its compliance risk identification, risk prioritization, and compliance strategy planning and delivery in a way that ensures a focus on the most significant issues and makes best use of available resources across competing functional departments. It also provides a transparent and defensible record of the process by which the revenue agency's compliance plans have been formulated (i.e., why resources have been devoted to particular risks in preference to others).

[1] Direct revenue from compliance activities (including audit) represents only a small proportion of total tax collections. In Australia, for example, direct audit revenue accounts for only around two percent of total tax collections each year.

Internal publication of the compliance program within the revenue agency provides important context for front-line delivery staff by clearly articulating the main risks in the system and the mix of strategies to be employed in managing them. Ideally, there should be a clear line-of-sight from the revenue agency's high level strategic plan down through all levels of operational plans to the team level. By ensuring clear linkages between each tier of the plans, managers and staff are better able to understand ***what*** they are required to do and ***why*** they are doing it, while the organization's statement of values informs staff about ***how*** they should approach their work. This can be a powerful motivational tool as well as providing a framework for better operational decision making.

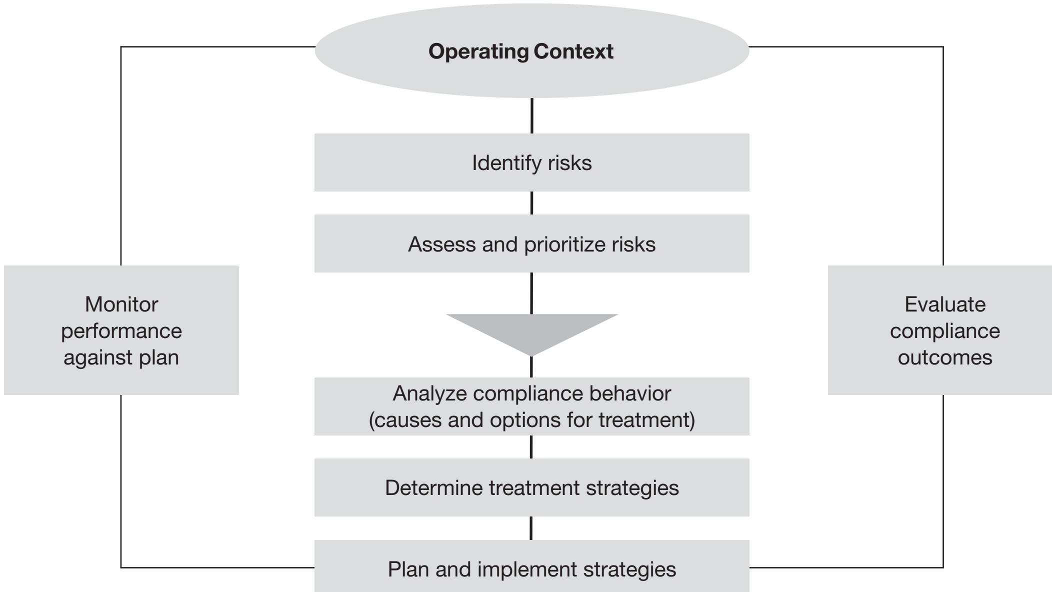
External publication of the compliance program enables the revenue agency to be open and transparent about compliance risks, and demonstrates to the government and broader community the rationale behind the deployment of its resources. This approach can generate significant media coverage of the revenue agency's concerns and intended actions – "free" publicity of this kind can significantly enhance the deterrent effect of the program. It enables people and businesses to understand the issues under scrutiny and helps them and their advisors manage their tax affairs more effectively, resulting in better overall compliance. It is also a mechanism for raising community awareness of the depth of compliance activities undertaken by the revenue agency and improving community confidence in the administration of the tax system. Documenting risks in the system in this way can also assist a revenue agency in lobbying the government for increased resources where the extent of identified severe risks is beyond its current capacities.

IV. What Are the Steps in Developing a Compliance Program?

The standard risk management process model (see Figure 1) illustrates a structured approach to identifying risks, assigning priorities, developing responses and evaluating the impact of measures taken. It provides an appropriate framework for the development of an effective risk-based compliance program. The model also demonstrates the cyclical nature of the compliance planning process and that it is a learning system.

Step one: evaluate compliance outcomes. A compliance program is a high level business plan and like all planning processes should commence with an evaluation of the effectiveness of the previous plan. If this is the first attempt at developing an integrated compliance program, the evaluation should focus on the effectiveness of the separate function- based strategies adopted in the previous planning cycle. "Effectiveness" is the extent to which the actual outcomes achieved align with the desired outcomes articulated in the plan. Gaps should be analyzed to test if the shortfall was due to inappropriate strategies or poor delivery of activities, and the learning from this should be applied to future planning processes. External factors affecting achievement of the outcomes should also be considered so that the effectiveness of the organization's delivery of the plan can be differentiated from other influences. An

Figure 1: Risk Management Process Model



important element of this process is to test the viability of the performance indicators included in the previous plan—did they prove to be sufficiently specific, measurable, achievable, relevant and timed, and did they combine to provide sufficient evidence of success?

Step two: understand the operating context. Compliance risks and responses must be determined in the context of the revenue agency's broader objectives.[2] It is therefore critical that the organization's strategic plan includes clear statements of the organization's *mission, vision* and *values*. The *mission statement* sets out the fundamental purpose for which the organization exists; the *vision statement* describes the desired future state of the organization; and the *values statement* sets the behavioral context within which all of its activities should be framed. These foundation statements, together with the high level goals and objectives identified in the strategic plan, provide the operating context for the organization. Understanding this operating context helps position compliance risks within the broader socio-economic environment and helps ensure alignment of compliance strategies with the direction and values of the organization.

Step three: identify risks. Making sense of all compliance risks across the total revenue system is a daunting task; compliance programs are therefore increasingly developed around taxpayer segments. This approach allows for the taxpayer population to be divided into more

[2]It is important to note that compliance risk management takes place within the broader scope of a tax administration's total risk management activity, which will include an examination of other internal and external factors that might also represent risks to success such as competing government policy objectives, staff capabilities, sustainability of business systems, the legislative framework and the health of the economy.

manageable groups based on common characteristics and potential risks. A typical approach is to first segment the taxpayer population into businesses, individuals, government organizations and non-profit organizations, and then to further break each category down into more meaningful sub-segments based on, for example, location, size, age, entity type, or industry sector.

For each identified taxpayer segment, risks should then be identified using information gathered from a variety of sources, including:

- ✓ The current computerized risk analysis system
- ✓ Tax returns, financial statements, taxpayer information schedules and registration applications
- ✓ The audit program (results from audits can be a rich source of information)
- ✓ Oral and written taxpayer enquiries (these provide insights into problem areas, emerging issues, and taxpayer understanding and attitudes)
- ✓ Other tax administrations (developments in other countries with similar tax systems should be closely monitored)
- ✓ Customs, social security agencies, land title offices and other regulatory agencies
- ✓ Third-party intermediaries such as banks, credit card providers and stock exchanges
- ✓ Professional bodies and peak industry groups
- ✓ The general community

A common approach is to conduct both a "top-down" and "bottom-up" assessment of risks. Risks identified through the top-down approach tend to be at a strategic level and require extensive and carefully managed interventions. The top-down view will focus on significant issues (e.g., government policy initiatives) and highly visible risks (e.g., the informal economy). Risks identified through the bottom-up approach tend to be more operational and localized in nature and are often manageable as smaller stand alone projects.

There is no single "right" way to approach the risk identification process; standard practice is to consider the risk environment through a range of "lenses"— e.g., taxpayer segments; industry segments; revenue types (i.e., Personal Income Tax, Company Income Tax, Value Added Tax, etc.); and core tax obligations (i.e., record keeping, registration, filing, correct declarations, and payment). This multi-lens approach helps refine the risks and locate them within more specific taxpayer groupings. The various sub-segments can also be "sliced and diced" to develop more highly targeted analyses of risk, e.g., the risk of *poor record keeping for VAT purposes by small businesses* engaged in providing *concreting services to householders.*

This risk identification process will result in a pool of identified risks for each taxpayer segment or sub-segment. Identified risks should be captured in a formal "risk register" which describes each risk and the nature of the threat that it poses to the revenue system (e.g., impact on revenue, government policy goals, community confidence, or reputation of the revenue agency).

Figure 2: Typical Risk Rating Matrix

Consequence/ Likelihood	Insignificant	Minor	Moderate	Major	Insignificant
Remote	Negligible	Negligible	Low	Low	Significant
Unlikely	Negligible	Low	Low	Significant	High
Possible	Negligible	Low	Significant	High	High
Likely	Low	Significant	High	High	Extreme
Almost Certain	Low	Significant	High	Extreme	Extreme

Step four: assess and prioritize the risks. In the context of a limited operating budget, decisions will need to be made on how to rank the risk pool in terms of priority. Identified risks must therefore be assessed and prioritized in a structured manner to ensure that the revenue agency's scarce resources are applied in the most effective way to improve voluntary compliance. Central to the process of assessing and prioritizing risks is the need for a sound framework within which compliance risks can be comparatively assessed in a repeatable manner. This can be done using a risk rating matrix of the kind shown in Figure 2 which considers both the likelihood of an event/risk occurring and the consequence of that event/risk. It is important to note that "consequence" should not be measured in revenue terms alone. The impact on the integrity of the tax system overall, and on the level of community confidence in the administration of the tax system should also be considered.

Decisions on the level of investment required to mitigate each risk must be made in the context of the number of serious risks identified, their relative estimated impact on the revenue system, and the operating budget available to the revenue agency. The aim is to achieve a reasonable balance of risk management across all market segments with all of the most serious risks under active management. At a minimum, all risks rated as "extreme" or "high" should be under active management. For the less serious risks, a watching brief may be applied to ensure that any further erosion of compliance in these areas is quickly identified and reconsidered.

Step five: analyze compliance behavior. Priority risks must then be analyzed to identify the drivers and attitudes underlying noncompliant behaviors and to determine the appropriate mix of responses from the revenue agency. An approach now used by many revenue administrations involves the use of a compliance model—see Figure 3.[3] This model provides a struc-

[3]This compliance model was first developed by the Australian National University in partnership with the Australian Taxation Office, and later endorsed by the OECD.

tured way to better understand what motivates people to comply, or not comply. It recognizes that taxpayers are not a homogenous group, and that their circumstances can change over time. Importantly, it provides revenue agencies with insights into factors that influence different compliance behaviors, and assists them in deciding what interventions to make.

The Compliance Model is in two parts:

- The left side of the model recognizes that a wide variety of factors influence taxpayer behavior. This includes business, industry, sociological, economic and psychological factors, all of which influence whether a person chooses to meet their obligations, and
- The right side of the model reflects the different taxpayer attitudes to compliance, and the corresponding compliance strategy that best responds to each particular attitude.

The model advocates a deeper understanding of motivation, circumstances and characteristics so that enforcement and other actions can be tailored to promote better compliance. With the right responses and interventions revenue agencies can influence taxpayer behavior in a positive way. The ultimate aim is to influence as many taxpayers as possible to move down the pyramid into the ***willing to do the right thing zone***.

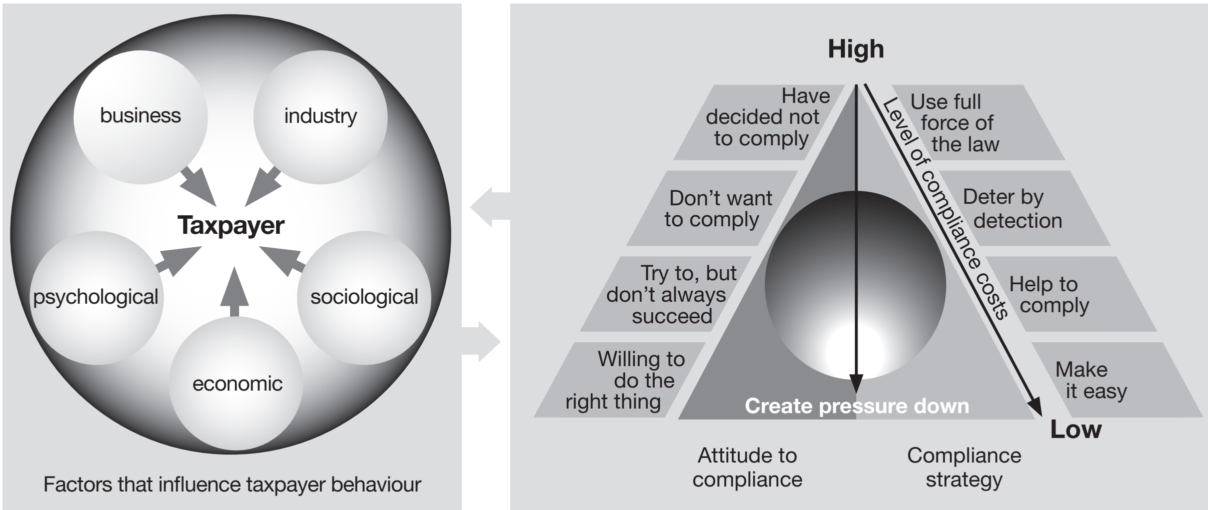
Analyzing compliance behavior in this way will assist revenue agencies to address the actual causes of noncompliance rather than the symptoms. For example, under-reporting of business income may be the noncompliant behavior observed, but the driver of that behavior may be the taxpayer's need to increase cash flow in an attempt to remain competitive in a business environment where competitors routinely under report income or deal in cash. Alternatively, the driver may be the taxpayer's belief that tax rates are too high and/or unfairly applied to his personal circumstances. Treating the behavior (the symptom) will only impact the affected taxpayer and only for a limited time.[4] Understanding the underlying causes of the behavior, and developing appropriate strategies to address them, is much more likely to achieve sustainable long-term compliance.

It is important to note that the aim is not necessarily to remove identified risks completely, but rather to mitigate them to a level of risk that is acceptable. For example, there will always be elements of the cash economy in any tax system as the cost of eliminating it completely is prohibitive and would require administrative actions unacceptable to the community. The aim is therefore to manage the identified risks down to a level that is acceptable to the government and the community.

Lower ranked risks should be monitored on a regular basis to identify potential changes in circumstances. The risk rankings should also drive future investment decisions for the revenue agency should there be a change (up or down) in the resources available for compliance management.

[4]Audits in these circumstances can actually have a negative impact on longer term compliance if the taxpayer concerned feels that he has been unfairly singled out for attention while others get away with the same behavior.

Figure 3: Compliance Model



Step six: determine treatment strategies. Revenue agency responses to mitigate priority risks should be developed in the context of the allocated resources and should be documented to reflect a logical thinking process that includes a description of the desired outcomes and how effectiveness will be evaluated.

Treatment strategies must be considered in a holistic way. Initiatives for improving service, reducing compliance costs and verifying compliance should not be developed independently within functional departments; piecemeal approaches can result in duplication of effort and poor sequencing of inter-related activities. The treatment strategies must address the underlying causes of noncompliance in a rational way. For example, audits are not the best response to noncompliance caused by ignorance of the law; taxpayer education is not the best response to deliberate evasion; and imposition of strong penalties may not be appropriate where voluntary compliance with obligations is made difficult by inadequate administrative policies and procedures.

The treatment strategies should aim for the optimal mix of responses (e.g., education, assistance, improved law and procedures, audit and enforcement) to achieve the widest possible impact on voluntary compliance across the taxpayer population. To ensure that outcomes are sustainable, possible unintended consequences should be anticipated and strategies identified to address these.[5] A checklist of factors to be considered in developing and implementing effective integrated treatment strategies is set out in Box 2.

[5]For example, an audit crack-down on unregistered itinerant farm workers may have a negative impact on farm output if not carefully managed.

Box 2. Factors to be Considered in Developing Integrated Treatment Strategies

Identify and analyze the compliance risk

- What exactly is the risk and who is affected by it?
- What are the underlying causes of the noncompliant behavior?
- To what extent are the current law and/or administrative systems a causal factor in the non-compliance?
- What judgment has been made about how the compliance attitudes of the risk population have been formed (i.e., how have they been affected by business, industry, social, economic or psychological factors)?
- Has this judgment been validated through engagement with taxpayers and their advisors?

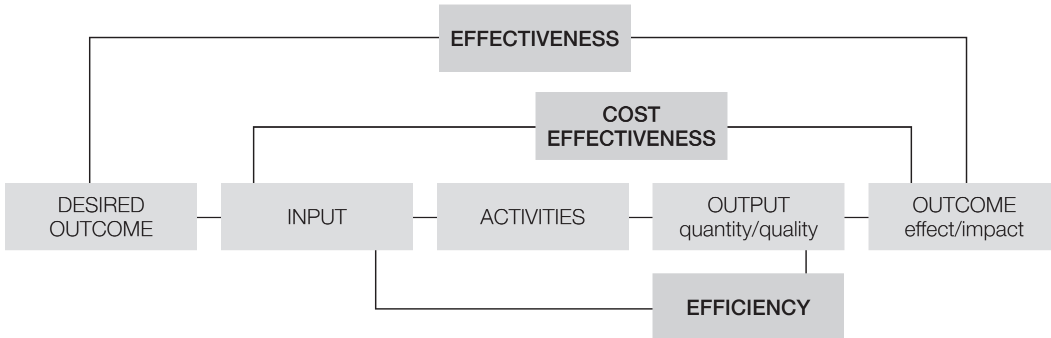
Plan and implement the treatment strategy

- Has the desired outcome of the treatment strategy been clearly articulated and have success criteria been identified?
- Is the revenue agency's interpretation of the law understood and accepted? Does the revenue agency need to clarify and/or communicate its position?
- Can the revenue agency improve the ease and/or cost of compliance for affected taxpayers by providing educational material or self help tools such as industry benchmarks or on-line calculators?
- How can the revenue agency identify and assist those taxpayers within the risk population who are trying to comply? Can the revenue agency provide them with the time they need to get their affairs in order?
- Are the revenue agency's internal risk and intelligence capabilities adequate to detect instances of this type of non-compliance for case selection purposes?
- Does the revenue agency staff have the skills and support tools to conduct effective audit and enforcement activities where necessary?
- Are there any underlying causes of the noncompliant behavior that are not addressed by the treatment strategy?
- Are there any unintended consequences which are likely to arise as a result of the treatment strategy?

Evaluate the effectiveness of the treatment strategy

- What do the effectiveness indicators show about the impact the treatment strategy has had?
- What has been learned and how will it influence future planning?

Figure 4: Strategy Evaluation Model



Examples of compliance strategies are provided at the end of this note. The first example (Box 3) describes the approach taken by Brazil to combat tax avoidance schemes associated with transfer pricing and tax havens. The second example (Box 4) illustrates the approach taken by the Internal Revenue Service of Chile to tackle false VAT invoices.

Clearly identifying all of the desired outcomes will assist in determining the goals for success, and will help to ensure the compliance strategies are working towards those outcomes. Success must be defined in terms of specific goals that represent the desired new behaviors or positive changes in community confidence. These success goals must be expressed in measurable terms. It is important to note the difference between effectiveness indicators and efficiency indicators. The strategy evaluation model in Figure 4 demonstrates the difference between *effectiveness, cost effectiveness* and *efficiency* measures. While it is important to retain objective measures of efficiency and cost effectiveness, the ultimate measure of success is in determining whether the compliance strategies implemented have had a positive impact on voluntary compliance.

A suite of performance indicators is likely to be needed for each treatment strategy as a single indicator will unlikely provide sufficient information to assess the overall effectiveness of the strategy. But there should also be a limit to the number of indicators—if there are too many indicators it is unlikely that the necessary monitoring and evaluation will occur. While indicators are not definitive measures, collectively they should be able to demonstrate whether the strategy goals are being met. The indicators must be specific, measurable, achievable, relevant, and timed. The set of indicators to be used for evaluation must also be able to be supported by the revenue agency's business systems, and be obtainable at reasonable cost.

To enable comparisons before and after implementation of the treatment strategies, it is important to establish the baseline prior to implementation. If baseline data is not available, data from the first year of implementation may be used as the starting point for measuring the impact of the treatment strategies in future years.

Box 3. Combating Tax Avoidance Relating to International Transactions in Brazil

Background: Following the opening of the economy in the early 1990s, Brazil experienced a rise in the volume of international transactions. With this, a variety of tax avoidance schemes emerged involving transfer pricing, triangular operations through tax havens, and other offshore arrangements (at the time, profits of Brazilian companies abroad were not taxed at home).

Building a comprehensive strategy to combat tax abuse associated with international transactions. Given the nature and complexity of the problem, an integrated strategy was developed including:

- ***Tax policy improvements:*** Adoption of new legislation specifically dealing with: transfer pricing rules; transactions with tax heavens and tax-favorable jurisdictions (including the introduction of a clear objective rule to define such jurisdictions); and the introduction of worldwide taxation criteria.
- ***Institutional Strengthening:*** Establishment of specialized units within the organizational structure of the revenue agency (Receita Federal). In particular: (a) a special Office on International Affairs (OIA) responsible for administering and auditing multinational corporations and taxpayers involved with substantial international transactions (this was based in São Paulo close to the main taxpayers); (b) an Investigation and Intelligence Department (IID), responsible for investigating and detecting tax crimes, including those related to international financing and money laundering; and (c) four Tax Attaché offices located in Argentina, Uruguay, Paraguay and the US to provide services and gather information on international transactions of Brazilian taxpayers.
- ***New Information Systems:*** Development of new sources of information on international transactions, including customs operations, including: (a) integrated information systems on foreign trade (e.g., SISCOMEX, which provides a global view of the taxpayer's operations and networks); (b) development of new customs information systems based on risk management; coordination and information exchange across federal agencies, including the Central Bank which controls currency exchange flows, and the Council on Financial Activities Control; and (c) introduction of new fields on the corporate tax return specifically designed to gather information on such transactions.
- ***Internal recruitment and training:*** OIA and IID officers were recruited based on a specific skill profile, including language skills, accounting, and auditing of large corporations. Receita Federal offered specialized training, including participation in training programs offered by the IRS Criminal Investigation Unit.
- ***Networking and partnerships with key stakeholders in Brazil and abroad.*** An extensive pool of stakeholders was consulted on the need to strengthen the prosecution process. For example, (a) multinationals and key private sector representatives were invited to participate in the process of lawmaking and drafting of regulations (they helped define objective methods for the transfer pricing rules); (b) a series of seminars and conferences was organized to raise awareness and to prepare taxpayers for the new legislation; (c) extensive work to explain and alert judges from the administrative tribunal and judicial branch about the importance of enforcing the new law and prosecuting offenders, and the need to focus more on tax law interpretation.; and (d) partnering with tax administrations internationally and exchanging information (for example, signing an information exchange treaty with Argentina).

Box 4. Improving VAT Compliance and Tackling Fake Invoices in Chile

Background: VAT is a major tax in Chile, yielding around 50 percent of total tax revenue. Early surveys indicated very high VAT noncompliance rates. The tax department responded with differentiated strategies to tackle the problem, resulting in a reduction in the VAT gap during the 1990s from 28 to around 20 percent. Notwithstanding the successful campaign, a critical weakness remained—the use of fake invoices.

Tackling the country's tax avoidance and tax fraud: an enhanced governmental priority in the 2000's. The new government that took office at the beginning of 2000 embraced an anti-tax evasion plan proposed by the tax department which included an integrated suite of measures to combat the use of fake invoices. The government embraced this plan as a critical tool for raising revenue to finance its social reform agenda. The new measures included:

- ***Tax policy changes:*** New laws closed several loopholes in the income tax and VAT legislation which were identified by the tax department during audits and compliance control operations.
- ***Increased institutional capacity:*** The number of tax auditors was increased and organizational changes were made to strengthen capacity in specialized tax avoidance activities; a specialized task-force was created in the legal department of the tax office headquarters—the anti-fake invoices prosecution unit—with delegates in each regional office to quickly prosecute fake-invoice cases detected through audit activities.
- ***Stronger sanctions:*** The tax procedures code was modified to better define and penalize tax avoidance related to clandestine commerce and use and trafficking of fake invoices.
- ***Improved procedures:*** New administrative procedures to detect and penalize the use of fake-invoices were implemented; tighter procedures were introduced to authorize the use of paper invoices by taxpayers; and intensified cooperation was established with the Police, National Prosecution Office, and Justice Department to execute the new prosecution powers.
- ***Public awareness campaigns:*** Media campaigns were launched to build community intolerance of tax evasion and to publicize successful prosecution of offenders.

A paradigm shift in the use of invoices. Building on the success of the measures described above (the VAT gap dropped to around 15 percent by 2005), the tax department in a joint strategy with the private sector spearheaded a paradigm shift by introducing electronic invoices (e-invoices) to replace paper invoices. E-invoicing is aligned to the e-commerce platform of the country and provides tighter control and greater security over transactions, and facilitates monitoring and verification by the tax department. Initially targeted at large taxpayers, this initiative represents a structural response to the problem of fake-invoices and will substantially reduce tax avoidance once the system is rolled-out to the broader business population.

Step seven: document the process. The entire process of developing the compliance program—from risk identification to strategy implementation—should be documented. The record should include:

- all risks identified for intervention and their priority ranking
- the nature and timing of the planned interventions
- resources allocated to particular activities
- the name of the officer or area accountable for delivery of each strategy
- efficiency indicators
- quality indicators
- effectiveness indicators
- arrangements for monitoring and evaluating progress

Step eight: monitor performance and evaluate outcomes. Strong governance arrangements must be instituted to monitor and evaluate the implementation of the compliance program. Regular reports (at least quarterly) on progress with implementation of the treatment strategies should be monitored at a very senior level in the revenue agency. These reports should cover both performance issues (i.e., have planned activities been delivered on time and within budget?) and conformance issues (i.e., has the organization met its legal obligations and lived its values in its delivery of the activities?). These regular reports should be complemented by more immediate exception reporting where major risks to delivery emerge. Managers should be encouraged to report potential exceptions as early as possible to optimize available time to take remedial action.

The final critical step involves evaluating the effectiveness of the treatment strategies and documenting and reporting the findings in a way that informs the decision makers. Effectiveness is the extent to which the actual outcomes align with the desired outcomes. Any shortfalls should be analyzed and the learning applied to future planning processes.

V. How Often Should the Compliance Program be Updated?

A full review and refresh of the compliance program should be conducted on an annual basis as an integral part of the revenue agency's strategic and operational planning cycle. However, this annual timeframe should not preclude the planning and delivery of longer term treatment strategies, particularly where endemic risks such as the cash economy are involved. Treatment strategies to manage these types of risks will span several years and will therefore be a consistent feature of the revenue agency's compliance programs over the medium to long term.

Like any business plan, the compliance program should be actively monitored and reviewed throughout each planning cycle to take account of emerging risks. For example, the emergence of a major unanticipated shock to the system such as the global economic crisis would clearly require a review and reset of the compliance program to take account of the changed operating environment.

VI. Key Points for Tax Administration Design

A properly structured compliance program promotes best use of available resources by ensuring a focus on the most significant risks in the system and facilitating better integration of activities across functional departments. It also provides important contextual information for operational staff and represents a transparent and defensible record of the process through which the revenue agency's compliance plans have been formulated.

The development of a taxpayer compliance program is a difficult administrative challenge, particularly for revenue agencies with limited experience in sophisticated risk analysis and compliance strategy development techniques. It will require a significant commitment of time and resources across all areas of the administration. The establishment of a high level Compliance Risk Management Committee to sponsor and manage the process is recommended. All of the key functional departments should be represented at a senior level on the committee which should, in turn, be supported by a permanent secretariat to provide expert support in preparing agendas, coordinating meetings, recording decisions, maintaining the formal risk register, and monitoring progress with action items etc. The committee will also generate a significant amount of work that will need to be done by working parties out of session. This will include design work to refine the organization's risk management approach and coordination activities to support the development and documentation of integrated treatment strategies.

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