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Cooperative compliance initiatives as a preventative mechanism

Quiñones, D.; Mosquera Valderrama, I.J.; Huiskers-Stoop, E.A.M.

Citation

Quiñones, D., Mosquera Valderrama, I. J., & Huiskers-Stoop, E. A. M. (2022). *Cooperative compliance initiatives as a preventative mechanism. Manual for the Control of International Tax Planning. 5. Tools for Combatting International Tax Planning* (pp. 1-59). Panamá: Centro Interamericano de Administraciones Tributarias (CIAT). Retrieved from <https://hdl.handle.net/1887/3513986>

Version: Publisher's Version

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Downloaded from: <https://hdl.handle.net/1887/3513986>

Note: To cite this publication please use the final published version (if applicable).

Manual

for the Control of International Tax Planning

5

Tools for Combating
International Tax Planning



5.5. Cooperative Compliance Initiatives as a Preventative Mechanism

Manual

for the Control of International Tax Planning

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Tools for Combatting International
Tax Planning

5.5. Cooperative Compliance Initiatives as a Preventative Mechanism

Diego Quiñones

Irma Mosquera

Esther-Huiskers Stoop

November, 2022

Manual for the Control of International Tax Planning

© 2022 Inter-American Center of Tax Administrations (CIAT)

ISBN:

978-9962-722-22-9

Diagramming:

CIAT Communication and Publications Coordination

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About the Authors



Diego Quiñones Cruz

Doctor of Law of the University of Oxford (where his thesis Determinants of Corporate Tax Behaviour and Cooperative Compliance was directed by Judith Freedman), LLM in International Taxation (Vanderbilt Scholar) and APCLB (Vogelstein Scholar) of New York University, Specialist in Tax Law of the Universidad del Rosario, Lawyer (cum laude) and Political Scientist of the Universidad de los Andes. Former partner of Quiñones Cruz Abogados. Former President of the Academic Commission of the Colombian Institute of Tax Law. Currently, member of the Tax Controversies and Risk Management team in Ernst & Young LLP (London, the United Kingdom). Professor and lecturer in Colombia and abroad and author of numerous publications in national and international journals and books. He holds the bar the New York State Bar and is Solicitor of the Higher Courts of England and Wales.



Irma Mosquera

Full Professor of Tax Law, Leiden Law School, University of Leiden (Netherlands). Jean Monnet Chair Holder EUTAXGOV (EU Tax Governance). Doctor (cum laude) University of Groningen (Netherlands) 2007. Her areas of expertise are international taxation and comparative tax law in developed and developing countries and more recently, information exchange and BEPS in developing countries. Principal Investigator of the international research project GLOBTAXGOV (Towards a new model of Global Tax Governance in International Tax Law). The overall objective of GLOBTAXGOV is to assess the feasibility and legitimacy of the current system of global tax governance and the role of the OECD and the EU in international tax legislation in 8 countries. GLOBTAXGOV receives funding from the EU H2020 and the ERC Research and Innovation Programme (Agreement No. 758671).



Esther Huiskers-Stoop

Assistant Professor Tax Law, Leiden Law School, Leiden University. Her current research interests lie in the promotion of tax compliance, internationally in the field of Cooperative Compliance and nationally in the field of Dutch. Horizontal Tax Monitoring. Esther Huiskers-Stoop has received two Master degrees in Law at the University of Amsterdam (Dutch law and Tax law, 1997). She worked for over five years as a tax advisor with KPMG Meijburg & Co in Amstelveen, Netherlands, in both national and international practice. During this time, she finalised the academic training for the Nederlandse Orde van Belastingadviseurs (2000). In addition, she worked for almost six years as a lawyer in the Dutch tax litigation practice of Jaeger Advocaten-belastingkundigen in Amsterdam. She has also finalised the academic training for the Nederlandse Orde van Advocaten (2004) and the lawyers training at the Court of Amsterdam (2005). From 2009, Esther was affiliated with the Erasmus School of Law in Rotterdam and in 2015 she finalised her PhD thesis on The Effectiveness of Horizontal Tax Monitoring.

Glossary

ADR	Alternative dispute resolution (mechanisms)
APA	Advanced Pricing Agreements
ARAR	Algemeen Rijksambtenarenreglement (“General Civil Service Regulations”)
ATAD	European Anti-Tax Avoidance Directive
BEPS	Base Erosion and Profit Shifting
BRR+	Business Risk Review (reforms)
CCM	Customer Compliance Manager
CSR	Corporate Social Responsibility
CIAT	Inter-American Center of Tax Administrations
DAC	Directive on Administrative Cooperation
EOI	Exchange of information (mechanisms)
EY	Ernst & Young Global Limited
FTA	(OECD) Forum on Tax Administration
HMRC	Her Majesty’s Revenue and Customs
HQ	(corporate) Headquarter
IT	Information technology
JITSIC	Joint International Task Force on Shared Intelligence and Collaboration
KAN	(Dutch) Kwaliteitscentrum Accountancy Nederland (“Quality Centre Accountancy Netherlands”)

LAPOP	Latin American Public Opinion Poll
MNE	Multinational enterprise
NGOs	Non-governmental organizations
NOAB	Nederlandse Orde van Administratie- en Belastingdeskundigen (“Dutch Association of Accountants and Tax Experts”)
NTCA	Netherlands Tax and Customs Administration
Novak	Nederlandse organisatie van accountantskantoren (“Dutch organisation of accountancy firms”)
RB	Nexia Register Belastingadviseurs (“Nexia Registered Tax Advisers”)
SRA	Samenwerkende Registeraccountants en Accountants-administratieconsulenten (“Cooperating Chartered Accountants and Accounting Consultants”)
TCF	Tax Control Framework
OECD	Organization for Economic Co-operation and Development

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5 Tools for Combating International Tax Planning

5.5. Cooperative Compliance Initiatives as a Preventative Mechanism

5.5.1. What are the objectives of cooperative compliance?

Cooperative compliance in general can be defined as “the establishment of a trust-based cooperative relationship between taxpayers and the tax authorities on the basis of voluntary tax compliance leading to the payment of the right amount of tax at the right time” (Huiskers-Stoop & Gribnau: 2019, pp.72)¹. The origins of cooperative compliance are found in the 2008 Report by the Organization for Economic Cooperation and Development (OECD) Forum on Tax Administration (FTA) on the Role of Tax Intermediaries (OECD: 2008, pp.5)². This study encouraged tax administrations to establish a relationship based on trust and cooperation with taxpayers (mainly large taxpayers) in order to tackle aggressive tax planning. At the same time, this Report encouraged the study of the role that tax intermediaries (tax advisors) play in the promotion of tax minimization arrangements.

The OECD Study stated that for tax administrations, it is important to understand the taxpayer’s activities and therefore, tax administrations need to establish risk management as a tool to identify and assess the risks presented by taxpayers or group of taxpayers (OECD: 2008, pp.5)³. This risk management relies on information, and therefore, tax administrations should encourage taxpayers to be transparent regarding their tax activities. Ordinarily, even in the absence of cooperative compliance, taxpayers are legally required to file tax returns that disclose a limited amount of information as required and to pay the tax due in time (OECD: 2008, pp.40). The tax authorities are legally allowed to question taxpayers about the tax returns they have filed, to obtain additional information, to adjust the amounts payable and to collect taxes. In this traditional relationship, there is no incentive to provide more tax information than is mandatory. Under an enhanced relationship based on cooperation and trust, this dynamic can be perfected (OECD: 2008, pp.5). These relationships are entered into voluntarily by taxpayers, and their voluntary and transparent regulatory compliance will be rewarded with more anticipated certainty and a reduction of (possible) subsequent tax audits, sanctions and prosecution (OECD: 2008, pp.40). For an enhanced relationship to exist, it is essential that tax authorities, taxpayers, and their financial and tax law specialists ‘start to trust each other’ and maintain that trust.

In 2013, the OECD FTA published a new report titled “Co-operative Compliance: A Framework – From Enhanced Relationship to Co-operative Compliance” (OECD: 2013)⁴. The report adopted the term cooperative compliance in order to make clear “that the approach is based on co-operation but with the purposes of assuring compliance” (OECD: 2013, pp.13). For the enhanced relationship addressed in the 2008 report, the approach was based more on transparency by the

taxpayer than on the voluntary fulfillment of legal obligations, and therefore, tax administrations were limited to the cooperation given by taxpayers and their tax advisors.

According to the 2013 report, the term cooperative compliance describes the concept of enhanced relationship more accurately “as it not only describes the process of co-operation but also demonstrates its goal as part of the revenue body’s compliance risk management strategy: compliance leading to payment of the right amount of tax at the right time” (OECD: 2013, pp.16). The report also states that “revenue bodies and businesses want greater certainty and to reduce risk and administrative costs” (OECD: 2013, pp.80).

According to this report there are two key elements of disclosure and transparency by taxpayers. First, a robust, reliable Tax Control Framework (TCF) (which can be described as an instrument of internal control specifically focussed on the tax function within a company) that gives the tax authorities assurance and enables the taxpayer to know which tax positions taken are uncertain or controversial, and second, “the willingness to disclose those positions voluntarily” (OECD: 2013, pp.20-21). As a result, the extent of reviews and audits of the tax returns submitted to the tax authorities can be reduced significantly. Because of the information disclosed by the taxpayer, the tax authorities may rely on the returns submitted to it and trust that uncertain tax positions and other “issues of doubt or difficulty in the tax positions taken in that return will be brought to its attention” (OECD: 2013, pp.62).

In 2016, the OECD FTA published follow-up guidance in its report on “Building Better Tax Control Frameworks”, regarding the quality of a TCF to manage tax control for (large) companies and tax authorities participating in a cooperative compliance relationship (OECD: 2016)⁵. Disclosure and transparency are key. The latter refers to the sharing of information about the internal control system and the implementation and effectiveness of the TCF, which enables the taxpayer to be aware and in control of the positions and issues that need to be disclosed (Huiskers-Stoop & Gribnau: 2019, pp. 77). Taxpayers who behave transparently and represent a ‘lower risk’ can reasonably expect the tax authorities to take a more cooperative approach, while taxpayers who are shown to represent a ‘significant risk’ in general can expect to attract greater scrutiny and enforcement attention (Huiskers-Stoop & Gribnau: 2019, pp. 74).

Even though the reports were made in the framework of the OECD FTA, which consist of 53 members mainly developed countries, the concept of enhanced relationship, and cooperative compliance have been also used by emerging and less developed countries including Inter-American Center of Tax Administrations (CIAT) member countries (Cremades et. al.: 2015)⁶.

For instance, in a comparative study carried out in 2015 by the CIAT in member countries of Latin America, the Caribbean, Africa and Asia, the different approaches from tax administration to initiatives in cooperative compliance were presented. This study into cooperative compliance by emerging and less developed countries provided a definition stating that “A cooperative compliance initiative arises from the relationship between the tax administration and the taxpayer, and endeavors to achieve significant improvements in the level of mutual transparency and consequently in the level of voluntary compliance, having as objective the reduction of compliance and or administrative costs, and if possible, the prevention of controversies in the juridical-tax relationship” (Cremades et. al.: 2015, pp.7).

For purposes of this Manual, the main features of the 2013 OECD report will be used. For cooperative compliance to be used, the tax administration and taxpayers need to be clear about what cooperative compliance can do (benefits) and what cooperative compliance cannot do (limitations). These two elements will be addressed below:

5.5.1.1. Benefits

Compliance programmes have the common aim of increasing trust in tax authorities and providing (high-quality) services in order to promote voluntary compliance (Huiskers-Stoop & Gribnau: 2019, pp. 101)⁷. Cooperative compliance can contribute to the tax administration as follows:

- To understand the business and the environment where taxpayers operate
- To understand and influence compliance behaviour by taxpayers
- To obtain more information, so that new management strategies can be developed by tax administrations for taxpayers' risk assessment
- To establish the equal treatment of taxpayers, so that the focus is not on improving the relationship with large taxpayers, but with taxpayers in general (individuals and business)⁸
- To provide guidance to the taxpayer and tax intermediary (tax advisor) in what can be regarded as aggressive tax planning structures
- To enhance transparency from the taxpayer by introducing a coordinated rather than an adversarial approach to the taxpayer
- To have less extensive audits and disputes by focusing only on a specific type of taxpayers/transactions based on the risk assessment of non-compliant, non-cooperative taxpayers
- To improve the allocation of financial and personnel resources by focusing only on a specific type of taxpayers/transactions based on the compliance risk assessment and the taxpayer's cooperative/uncooperative posture
- To provide greater certainty on how to treat tax structures based on a grey area of law or an undefined area of law.

Likewise, cooperative compliance can contribute to the taxpayer as follows:

- To obtain legal certainty regarding the taxpayers' tax positions
- To obtain legal certainty regarding tax structures/tax activities based on a grey or undefined area of law
- To facilitate the tax administration's understanding of the taxpayers' tax positions and tax control framework
- To contribute with information to the tax authorities, so that they have a complete picture to be used in the risk assessment and in the establishment of responsive risk management strategies

- To identify uncertain tax positions based on the tax administration's own risk assessment
- To establish a coordinated (collaborative) rather than an adversarial approach towards the tax administration
- To promote transparency in their tax activities as one of the elements of their business strategy
- To enhance the taxpayer's risk management frameworks (like a Tax Control Framework)
- To benefit from an earlier resolution of tax issues with less extensive audits and lower compliance costs
- To reduce – or limit the scope of - the tax disputes with the tax administration.

5.5.1.2. Limitations

One of the challenges of cooperative compliance is the change from adversarial to a coordinated relationship between tax administrations and taxpayers. This relationship should be based on transparency, mutual trust and understanding of the taxpayers' tax activities and the tax administration's position regarding such activities.

Even though these goals are legitimate, these goals can be achieved more successfully in countries where a good communication exists between taxpayers and the tax administration (e.g. the Netherlands, Australia). However, this is not yet the case in most developing countries where the relationship is marked by a more adversarial and hierarchical character. Therefore, in our view, a cooperative compliance programme may have several limitations.

First of all, for introducing cooperative compliance, a first step is to improve communication between tax administration and taxpayer, and to obtain a mutual level of understanding and trust. This **cannot** be achieved with cooperative compliance; this should be done before introducing a cooperative compliance programme.

Therefore, in jurisdictions where mutual trust is low before the introduction of cooperative compliance, the objective is not to remediate this situation immediately, but rather to incrementally improve the interaction between the parties, and, through successful cooperative exchanges, augment feelings of procedural fairness and voluntary compliance. Cooperative compliance, then, sets out a path for a gradual reduction of vertical regulation and an eventual scenario where horizontal regulation prevails.

While cooperative compliance can greatly diminish information asymmetries between the parties, it does not necessarily eliminate them. Therefore, it is recommended to supplement cooperative compliance with adequate safeguards designed to prevent the greater administrative discretion and interparty proximity from giving rise to selective disclosure or administrative impropriety.

In addition, cooperative compliance **should not** be an instrument only for large taxpayers, but it should be used by all taxpayers (individuals and business). Even though large taxpayers may be more involved in tax minimization arrangements that could be regarded as aggressive tax planning strategies by the tax administrations, the success of a compliance programme should be based on a neutral approach towards all taxpayers. Naturally, the limited availability of administrative resources means that cooperative compliance cannot be made available to

all taxpayers at the same time, and indeed the use of pilot programmes for gradual rollouts is a good practice; however, what should be clear is that, in principle, the philosophy of horizontality and mutual collaboration towards greater certainty should be applicable in all taxpayer-tax administration interactions.

Finally, cooperative compliance may contribute to reduce disputes, for instance, regarding the use of advanced pricing agreements (APA) in transfer pricing. However, the decisions regarding the tax liability of the taxpayers **cannot** be addressed in a cooperative compliance programme. Cooperative compliance is not meant to change the law, so that a different law applies to each taxpayer, what cooperative compliance does is that it provides a scenario for the parties to discuss their interpretation of the law, agree/disagree on the facts, and then commit to a specific treatment for a tax position. Certainly, the treatment that is agreed needs to be within the law (in accordance with the principle of legality - the Rule of Law).

5.5.2. What are the principles behind cooperative compliance?

Having referred to the benefits and limitations of cooperative compliance, this section addresses the principles behind this regulatory approach, with the objective of assisting readers in identifying the elements that identify this regulatory philosophy and distinguish it from other regulatory models. Acknowledging that there are various ways of understanding cooperative compliance (e.g. we have referred to the OECD and CIAT's own interpretation of the concept), for this chapter the authors propose using a modified version of the principles by Quiñones in his book on cooperative compliance and determinants of corporate tax behaviour (Quiñones:2020).

Fundamentally, cooperative compliance is a regulatory approach that is premised on the idea that taxpayers and the tax administration can trust each other to collaborate (voluntarily), seeking to achieve a shared compliance goal. The idea is that, unlike other regulatory strategies which are based on coercion and mandates from the authority that are imposed vertically on taxpayers, cooperative compliance assumes that most taxpayers are compliance-minded, and this means that both parties can be placed on a level standing (as equals), so that they can interact with each other horizontally, with the taxpayer disclosing uncertain tax positions, compliance strategies and tactics, and factors associated to its tax risk profile, and the administration revealing how it understands and intends to treat the taxpayer's positions, as well as its opinion regarding the taxpayer's tax risk management.

Through this transparent dialogue, the expectation is that taxpayers are able to acquire legal certainty in relation to their tax positions, administrative guidance in relation to their compliance profile and tax control frameworks, and depending on domestic regulations, provide an opportunity to settle or narrow down the scope of existing tax disputes. At the same time, cooperative compliance offers administrations the opportunity to acquire material information about the taxpayers' tax positions, their approach to tax compliance, and their tax control frameworks. This flow of information and keeping a permanent regulatory dialogue with the taxpayer enables the administration to acquire greater certainty about tax revenues, settle or narrow down tax disputes, obtain intelligence about contemporaneous tax practices and about compliance issues that taxpayers may be experiencing, and a stronger commercial understanding that enables the

administration to be more responsive in its regulation and more aware of the tax risks presented by each taxpayer.

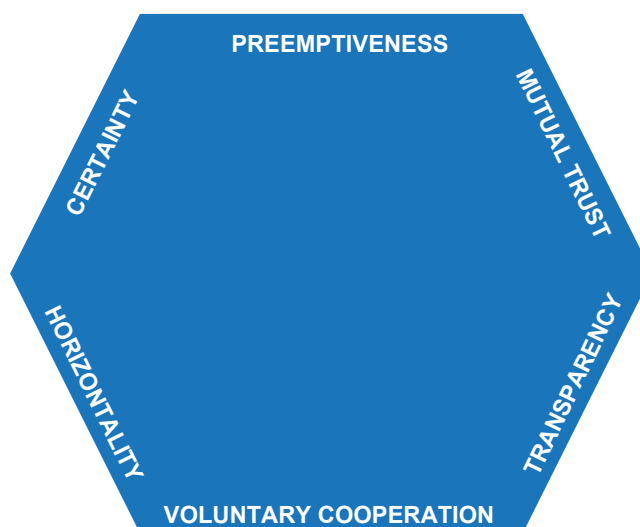
While cooperative compliance can include within the regulatory dialogue both current (open) and past tax positions, it is primarily meant to address tax uncertainties before they materialize, that is, before they create effects which are harder to rectify or act upon. The principle here is for the taxpayers and the administration to act proactively and prevent the materialization of risk, rather than acting reactively.

In summary, cooperative compliance is premised as a regulatory approach aimed at increasing overall tax compliance by means of greater voluntary compliance (achieved as a result of greater information that can be translated into a preemptive, risk-focused regulatory strategy, regulatory dialogue, compliance taxpayer-targeted assistance and interventions, and the benefits of increased taxpayer trust in the administration) and more resources being made available for coercive interventions, in the minority of cases where this would be necessary.

Visually, the main principles behind cooperative compliance could be thought of as a hexagonal representation, where all dimensions are equally important for the regulatory paradigm:

Figure 1

The principles behind cooperative compliance



Source: Elaborated by the authors, 2021.

In the following pages, each one of the six ‘principles’ enumerated above will be analyzed in the context of cooperative compliance.

5.5.2.1. Mutual Trust

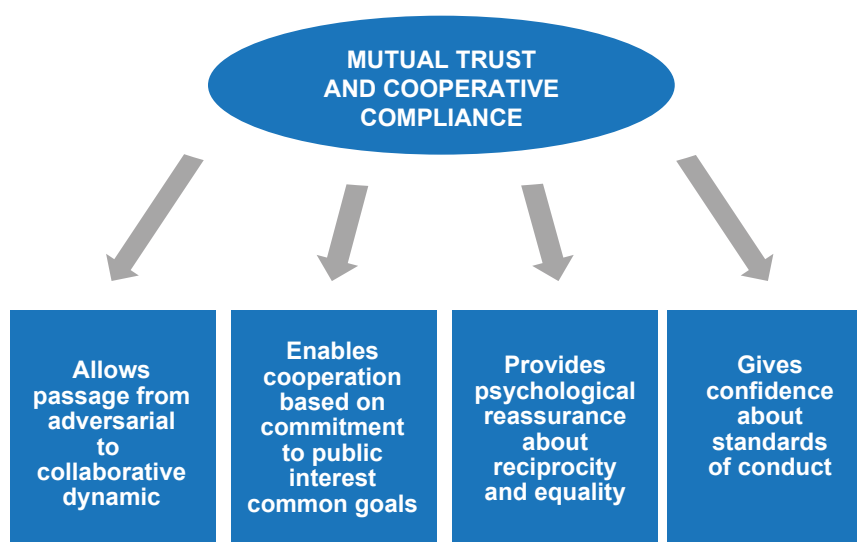
As has been demonstrated by research into the economic psychology of tax (e.g. Kirchler et.al: 2008), trust is an important determinant of tax compliance since it fuels voluntary compliance of taxpayers who feel emotionally comfortable with the administration, are more likely to see it as legitimate, and judge the interaction with the authority as fair.

In the case of cooperative compliance, trust, understood as the feeling that the other party will consistently act according to what is expected of them (predictability) under a specific standard, is a fundamental principle. Unlike traditional enforcement-based approaches to tax regulation, where distrust is the guiding principle (since the authority operates under a “cops and robbers” philosophy according to which the taxpayer is a utility maximiser that is constantly at risk of non-compliance), the existence of trust - which for cooperative compliance’s purposes has to be bilateral (mutual) - is necessary for the cooperative exchange to proceed efficiently.

There are multiple reasons behind the importance of trust for cooperative compliance, trust: i. Enables the passage from an adversarial approach to tax regulation into a collaborative one by allowing the parties to leave behind the idea that the other party is inherently suspicious, ii. Allows both the parties and external stakeholders to understand that the cooperation between taxpayers and the administration is based on an understanding that the parties’ actions are geared towards a common goal that serves the public interest (Wahl et.al: 2010), iii. Provides psychological reassurance to the parties’ belief that their own actions and efforts will be reciprocated by the other party (reciprocity) and that, in that sense, they are equals, and iv. Gives the parties confidence about the other party being expected to act as prescribed by specific standards of conduct (e.g. in a transparent manner, with empathy towards the other, striving towards efficiency, etc.) throughout the cooperative exchanges.

Figure 2

The importance of mutual trust for cooperative compliance



Source: Elaborated by the authors, 2021.

Cooperative compliance's reliance on trust does not mean that the parties assign trust blindly, since both parties' levels of trust have to be continuously nurtured, and, is conditional on the conduct displayed, meaning that behaviours by either party that deviate from expected procedural and substantive standards are likely to derail the cooperative exchange (Goslinga et al.: 2018, pp.19). If trustworthiness is absent, this type of regulation will not be effective, be it because the taxpayer withdraws from the scheme (where it is not mandatory) or ceases to collaborate, or because the administration, upon seeing evidence of unjustified, reiterated or highly material untrustworthy taxpayer conduct, reacts responsively, removing the taxpayer from the programme, or switching to more coercive regulatory approaches.

As for the standards of conduct that underly the notion of trust in a cooperative compliance setting, these standards are both procedural and substantive, meaning that the parties expect consistency from each other in acting transparently, respectfully (empathetically), and efficiently, but also both parties are expected to behave with compliance as the top objective, rather than tax minimization (taxpayers) or revenue maximization (tax administration).

In addition, mutual trust can be also seen as "informed trust". Informed trust depends on "reciprocal transparency" with regard to information provided by the tax administration and taxpayer (Huiskers-Stoop & Gribnau: 2019, pp. 67). The tax administration and taxpayers engage in actions designed to lead the other party to place trust in them, which in a tax context may consist of the exchange of information.

Finally, it is important to bear in mind that the role of trust in cooperative compliance is somewhat paradoxical, because mutual trust is needed for the approach to function, but at the same time, consistency in execution is expected to consolidate (and increase) mutual trust gradually as the parties move from calculated, single instance *reason-based trust* to habitual, unconscious *implicit* trust (Gangl et.al: 2015). Thus, in contexts like the ones often present in Latin America, where high levels of tax non-compliance and a contentious approach to tax regulation, couple with weak societal and institutional trust to mean that there are low levels of interparty trust to begin with, making the passage to cooperative compliance potentially more challenging. This point will be discussed further in the Chapter.

5.5.2.2. Voluntary Cooperation

Another key principle of cooperative compliance is voluntary cooperation. Unlike the traditional vertical supervision approach, which is based on the administration's ability to detect non-compliance and act as an enforcer, cooperative compliance is not based on coercive enforcement of tax compliance, but rather on voluntary compliance. This should not be confused with cooperative compliance lacking enforcement or deterrence, since these will still be present, as they are necessary to deal with those taxpayers that are not compliance-minded or who engage in a resistant or uncooperative *posture* (V. Braithwaite et.al: 2007) towards the administration. What it means is that the regulator starts from the premise that most taxpayers are compliance-minded and somewhat risk averse, and that, as a consequence, harnessing these taxpayers' own motivation to comply, their intrinsic motivations (Langham et.al: 2012), can prove more efficient as a regulatory strategy, than one primarily focused on coercive enforcement, since this would make sense only if most of the taxpayers are not compliance-minded.

Voluntary cooperation is essential for cooperative compliance because taxpayers are expected to disclose their material tax positions and the elements that aid the administration in assessing their risk profile without having been told what to disclose. This represents a departure from traditional, audit-based regulation, where the administration acts as an investigator, and is forced to uncover or command the taxpayer to disclose the information it seeks via information requests and audits/inspections. Thus, in cooperative compliance, the taxpayer assists the administration *motu proprio*, revealing information even in the absence of a legal mandate to do so. Since cooperative compliance is an eminently reciprocal relationship, the same principle applies to the administration, meaning that it is expected to act proactively, seeking to assist the taxpayer in achieving compliance even when the taxpayer has not filed a formal request or is outside a regulated official determination/assessment procedure.

The expectation, then, is that cooperative compliance uses the taxpayers' ability to self-regulate and its own ability to anticipate the taxpayers' compliance needs, to achieve higher compliance more efficiently and not being limited by the formalistic rigour sometimes attributable to a highly legalist regulatory approach.

5.5.2.3. The Philosophy of Horizontality

In line with the principle of voluntary cooperation, cooperative compliance is also guided by the idea of horizontality, which means that, in contrast to the traditional audit-based approach, where the administration is seen as an enforcer that is vertically situated above the taxpayer (based on its legal *imperium* and authority), and whose purpose it is to dictate compliance mandates, cooperative compliance sees the taxpayer and the administration as equal partners, working towards a common goal of compliance.

Both the taxpayer and the tax administration must be willing to understand each other. Mutual understanding can be described as "the willingness to put oneself in the other's place and to understand the other party's perspective" (Huiskers-Stoop & Gribnau: 2019, pp.85). It is, for instance, important that the tax administration understands the commercial interests of the company⁹.

While the differences in institutional composition, philosophy, and ancillary objectives (e.g. revenue maximization, tax burden optimization) remain, horizontality acknowledges that the parties can also find common ground in seeking to reduce their compliance/collection costs and in increasing legal certainty. Psychologically, the feeling that both parties are stakeholders, with reciprocal duties and rights, in a common enterprise (financing the State so that private parties, including taxpayers, can thrive¹⁰), fuels collaboration.

Since horizontality tends to be misconstrued with a renunciation of public power, or with the State 'caving-in' to private interests, it is necessary to emphasize that working as partners does not mean that the tax authority and the taxpayer have to agree regarding specific tax positions, or even the taxpayer's risk profile and corresponding regulatory treatment. What it means is that the parties work together to gather the most information possible regarding those positions and the taxpayer's tax function and try to agree on a path towards optimal compliance, and while this can reduce conflict or prevent it, it is likely that, given the complexity of tax law, disagreements will persist. What does change is that the parties' attitude towards discussing their tax positions and compliance strategies and tactics is no longer confrontational, meaning that differences

are to be discussed technically, efficiently, with commercial understanding, civility, and fairness, and this should lead to more agreements, narrowed-down disputes, and, occasionally, to an agreement to disagree and let a third party adjudicate conflict without the relationship breaking down.

Finally, as pointed out by Gribnau (Gribnau: 2015), the partnership present in cooperative compliance does not mean that the parties are legally equivalent, since the administration will always be endowed with the legal authorization to use coercive means to enforce compliance when cooperation is not forthcoming. Indeed, cooperative compliance does not entail a disappearance of deterrence and enforcement, since these persist as necessary tools both to penalize uncooperative non-compliance (something which is necessary to maintain taxpayer morale by showing taxpayers that non-compliance will be dealt with, and the notion of the authority as powerful) (Kogler et.al: 2013), and to dissuade compliant taxpayers from turning non-compliant themselves.

5.5.2.4. Certainty

Certainty is another one of the main principles behind cooperative compliance. This is the case because achieving certainty is one of the goals shared by both parties in the relationship, and the cooperative compliance regulatory dialogue (or exchange) can be seen as the means to reach it. Thus, legal certainty is an objective for this type of regulatory approach.

In the case of taxpayers, the expectation is that they agree to voluntarily disclose to the administration all of the information that might be material so that the tax administration can properly assess their risk profile and the legality of their tax positions, and consequently provide them with commitments in relation to the treatment that will be afforded to said positions, as well as to the taxpayer, in terms of the administration's regulatory approach (e.g. is the taxpayer going to be seen as low risk or high risk, with the consequences that might entail in terms of administrative intervention and legal benefits). In general terms, the administration is usually willing to reveal to the taxpayer how it interprets the taxpayers' positions and how it assesses the taxpayer's risk profile, in exchange for acquiring greater certainty regarding potential revenue, the scope of tax disputes, and the existing risks and compliance patterns (and the compliance strategies that the administration will need to implement). This greater predictability means both parties have an opportunity to be more efficient, be it in terms of collection efficiency, or in terms of compliance costs.

In terms of the determinants of tax behaviour, because of the impact taxes have on the taxpayer's finances, certainty is highly valued. This means that one of the strongest incentives that taxpayers have in terms of entering a cooperative compliance relationship, is increased tax certainty (De Simone et.al: 2013), and the benefits that come with it, such as a reduction in financial statement contingencies (such as the tax reserve account) and in the costs associated with tax disputes. For the administration, having more information about taxpayer strategies and tactics, as well as their uncertain tax positions, means that there is more clarity in the variables that lead to targeted or tailored administrative responses, and this increases the ability for the administration to dedicate (often scarce) resources efficiently.

While both parties expect legal certainty as an effect of the cooperative exchange, it must be clear from the onset that achieving certainty is not easy because of various factors: On the taxpayer's side, selective – rather than full – disclosure can be a risk where appropriate safeguards are not in place against letting taxpayers who are not sufficiently compliance-minded and risk-averse participate in the program¹¹. On the side of the administration, a lack of discipline can mean that the treatment of a tax position that was disclosed to the taxpayer is changed *ex post facto*, meaning that the taxpayer's legitimate expectations are broken. Additionally, both parties have to contend with the fact that the law can often be very complex and uncertain, so legal systems where the quality of the law is limited might not provide the parties with a real possibility to commit to an interpretation of the law that is mutually shared. Moreover, in systems where the law changes frequently, or where the judiciary or other organisms are active in challenging/overturning administrative acts, can also lead to overrides of the positions laid out in the cooperative exchange.

5.5.2.5. Transparency

Transparency, understood as full disclosure between the parties, is a crucial principle of cooperative compliance because it enables parties (and external stakeholders) to realize that the regulatory dialogue that takes place as part of cooperative compliance is factually grounded, and that the mutual trust between parties is conditional on honesty. As with every other aspect of cooperative compliance, transparency is reciprocal: taxpayers are expected to voluntarily disclose all the information that could prove material for the administration to profile them and set up responsive regulation, as well as to define how it will treat a taxpayer's tax position. Simultaneously, the tax administration is expected to reveal to the taxpayer all the information necessary for them to understand how the administration profiles them and customizes their regulatory treatment, and all the information regarding the administration's interpretation of the taxpayer's tax positions and its response to them.

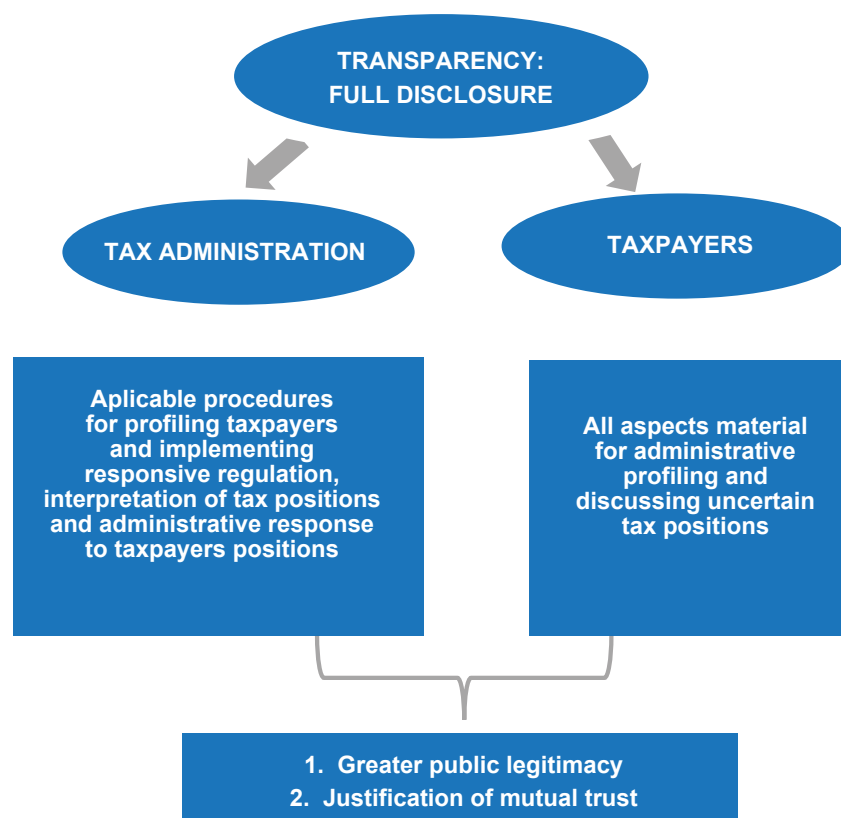
Fundamentally, transparency is meant to deal with the information asymmetry that characterizes the audit-based regulatory approach. In a traditional regulatory setting, the administration has limited knowledge about the taxpayer's affairs, and must rely on the information that must be legally disclosed in order to detect non-compliance and profile taxpayers. Similarly, taxpayers have limited information on how the administration interprets their circumstances and tax positions, and on how it will act in relation to them. These informational shortcomings mean that the decisions taken by both parties are imperfect.

Thus, rather than maintaining an antagonistic setup where asymmetry often harms the administration because of information asymmetry and, in the case of large corporate and high net worth taxpayers, because of differences in resources, and where taxpayers are operating on the premise of suppositions and probability calculations, horizontality allows the parties to implement regulation more effectively on the basis of shared information and shared resources.

Visually, the dynamic of reciprocal transparency in a cooperative compliance setting is as follows:

Figure 3

The dynamic of transparency in cooperative compliance

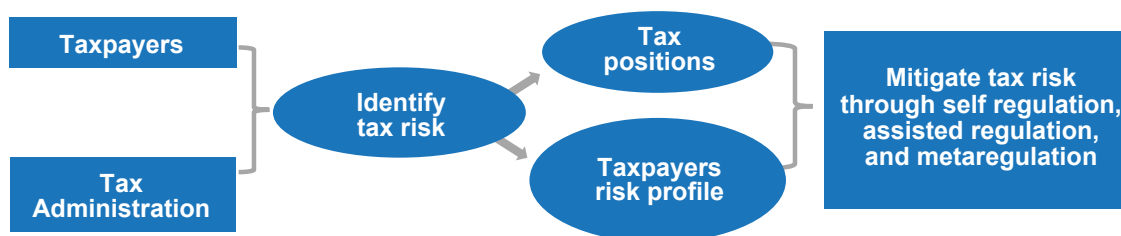


Source: Elaborated by the authors, 2021.

5.5.2.6. Focus on Preemptive Risk Control

A final principle that defines cooperative compliance is its focus on preemptive action and its commitment to risk-based regulation. In contrast to the traditional audit-based approach, which seeks to detect previous non-compliance and from that detection proceed with regulatory intervention, aimed both at penalization and tax recovery, cooperative compliance seeks to anticipate (preempt) non-compliance and prevent it, reduce it, or in the very least, be prepared for it. The idea is to avoid having to work as a reactive regulator, on the premise that it is less desirable to remedy non-compliance, than to target resources to prevent it, where possible.

The way in which the administration and the taxpayer prevent the materialization of tax risks is by using the regulatory dialogue provided by the cooperative exchange as a space for the parties to; i. identify risk (be it the risk of a tax position, or the comprehensive risk of non-compliance attributable to the taxpayer's tax control framework) and ii. discuss and agree strategies to mitigate/eliminate the risk before it has the chance to become a reality. It is this knowledge about risk and the use of differentiated regulatory strategies and tactics that allows the passage to responsive regulation (Black and Baldwin: 2010).

Figure 4**Risk control in cooperative compliance**

Source: Elaborated by the authors, 2021.

Naturally, this requires a commitment from the taxpayer to reveal uncertain tax positions before they have been implemented, and to fully disclose any elements that might assist the administration in understanding its tax risk profile. This means that taxpayers participating in cooperative compliance must be i. Risk aware (ideally by having robust tax control frameworks in place), and ii. Risk averse (willing to mitigate tax risk). For the administration, an adequate level of commercial understanding and the ability to manage tax risk through regulation must be coupled with technical tax knowledge to detect and address risk properly.

Using cooperative compliance as a risk regulation tool entails significant changes for both parties, because taxpayers have to upgrade their tax function to be able to detect possible non-compliance well before it happens and have to build a risk management system that allows them to provide assurance to the administration. For the administration, tax intelligence is refocused on detecting risks rather than on detecting tax deficiencies, and the role changes from that of an enforcer, to one of a compliance guide or partner, who assists taxpayers in managing risk (assisted regulation), and for those taxpayers who have proven they are capable of self-regulating, going towards metaregulation and acting as a prudent regulator (J. Braithwaite: 2003)

5.5.3. How Does Cooperative Compliance Operate?

The OECD and the CIAT have addressed the differences in the political and legislative environment where tax administrations operate, as well as the differences in their administrative practices and culture (OECD: 2013; Cremades et. al.: 2015, pp.6). For these reasons, a “standardized tax administration approach would not be in itself practical or desirable in a particular case” (Cremades et. al.: 2015, pp.6). These differences should be also taken into account in order to introduce a framework for cooperative compliance.

Before introducing a framework for cooperative compliance, it is important for the tax administrations to assess critically their relationship with the taxpayer, and to introduce measures to promote transparency and trust by the taxpayer and the administration.

Examples of these measures are for instance i. increasing training of the tax administration (including skills other than technical understanding of tax such as behavioral analysis and negotiation), ii. increasing personnel and technological resources for communication, and risk assessment, and iii. improving the quality of the risk assessment process in terms of transparency, and accountability.

In general, CIAT member countries have introduced some of these measures, but there are differences in the choices made by the countries (Cremades et. al.:2015, pp.18-19). Some countries may provide for more advanced technological tools (online cash registers, online self-servicing), whereas other countries are mainly focusing on communication with the taxpayer. For instance, by i. improving personalized communication, or ii. creating consultation tax channels with the tax administration on technical and procedural issues and iii. creating forums for interaction between tax administration and taxpayers. Both the tax administration and taxpayers are required “to adopt a solution-focused attitude, display empathy and listening skills, improve and maintain the mutual relationship, be decisive, and build up a relationship of trust” (Gribnau & Huiskers-Stoop: 2019).

Some of the tax administrations in the CIAT member countries have regarded the above mentioned measures as cooperative compliance, however, in our view these measures facilitate compliance and, in some cases, voluntary compliance by the taxpayer, but there are various other measures that are required for the efficient implementation of cooperative compliance, particularly in the context of CIAT member countries where vertical approaches have prevailed historically and there are contextual challenges in terms of resources, interparty trust, and voluntary compliance. These requirements will be addressed below.

5.5.3.1. Main requirements for cooperative compliance

For cooperative compliance to work, the tax administration needs to:

- i. Promote voluntary compliance by making easier for the taxpayer to get it right,
- ii. Prevent non-compliance by intervening at the point of the transaction and
- iii. Respond robustly to non-compliance by those who deliberately evade or avoid.

This approach, “promote, prevent and respond”, has been addressed by the representative of the tax administration in the United Kingdom; Her Majesty’s Revenue and Customs (HMRC) in the 2014 OECD Report¹². In our view, this approach can provide the main requirements for cooperative compliance that go beyond voluntary compliance. Certainly, each one of these requirements incorporates other aspects such as transparency, trust, commercial awareness, and responsiveness that have been described previously in this text, but the overall philosophy is to reach a point where the regulator can achieve these three objectives.

Furthermore, this approach to cooperative compliance may contribute to less disputes, less audits, and a better use of resources by the tax administration. By using this approach, tax audits will only occur at the end of the compliance process, as contentious issues are identified and resolved prior to tax filing by using the promote and prevent approach first (OECD: 2014, pp.18)¹³. By reducing the scope of tax disputes, not only do taxpayers acquire greater certainty

about their tax obligations, thus reducing the financial impact of tax contingencies, but also the administration acquires greater predictability about the magnitude of revenue and the areas where greater administrative interventions will be required.

5.5.3.2. Transparency and tax compliance outcomes

For cooperative compliance to effectively work, tax administrations need to make changes that go beyond communication and training of the tax administration. It is required that tax administrations think about what is needed to increase transparency by the taxpayer and how to improve transparency of the tax administration and of the tax system as a whole¹⁴. In as much as there is greater transparency from all the parties of the tax relationship, there is a positive impact in terms of societal perceptions of the legitimacy and fairness of the tax system and this, in turn, could increase voluntary compliance.

The first step is to identify the desired outcome of cooperative compliance taking also into account the limitations of the tax administration. In general, the OECD in 2014 stated that these outcomes are i. to collect the right amount of revenue, ii. to improve the voluntary compliance by taxpayers, and iii. to administer the tax system with integrity and confidence. It is important to reiterate that cooperative compliance always operates under the rule of law, and as such is not an enemy of the principle of legality. Any outcome of a cooperative exchange has to be compatible with existing tax laws.

However, in some countries especially developing countries, these outcomes may be limited, mainly due to the lack of resources, trust and understanding of the tax administration activities, as well as the focus on adversarial positions through audits and tax disputes before the court. If the focus has been on audits and tax disputes, then, the tax administration does not generate confidence for the taxpayer to participate in cooperative compliance initiatives. The fact that the achievement of these goals is not immediate, but rather gradual, does not diminish the value of the regulatory approach because any gains will still be an improvement vis á vis the status quo.

Therefore, each tax administration should identify their own tax compliance outcomes, and how these outcomes can also be reinforced by making changes in the tax administration system as a whole (and, ideally, in the tax legal system itself). One way could be to change their adversarial character, and to prevent disputes by being transparent regarding their audit practices¹⁵, or to be transparent about specific risk transactions that have been identified by the tax administration as possible non-tax compliant transactions.

5.5.3.3. Use of information to tackle tax aggressive tax planning

Cooperative compliance in general is not a standalone model as tax administrations complement its use with traditional (command and control) regulation in respect of non-compliant taxpayers (Huiskers-Stoop & Gribnau: 2019, pp.70). Thus, cooperative compliance is only one of the tools available to promote tax compliance. Tax administrations do not abandon traditional enforcement mechanisms, but “put them on hold when dealing with compliant taxpayers who engage in cooperative compliance”.

The identification of risk transactions or non-tax compliant transactions can be facilitated for instance by using the information received by the tax administration due to the exchange of information (on request, automatic and spontaneous) and the project to tackle Base Erosion and Profit Shifting (BEPS).

The introduction of the BEPS Project and its 15 Action points has increased information regarding exchange of rulings (BEPS Action 5), exchange of transfer pricing documentation (BEPS Action 13) and the exchange of aggressive tax planning structures (BEPS Action 12¹⁶). Therefore, one way to move towards compliance is for the tax administration to analyze this information and to identify possible risk transactions that can be subject to audit by the tax administration. This may not require so much effort, but it requires training of tax administrations on transfer pricing, aggressive tax planning structures and tax treaties in general.

This training is provided to some extent by regional tax organizations such as CIAT, the 'Tax Inspectors Without Borders' initiative, or others. The only thing that may be needed is to be transparent towards the taxpayer, on how this information is being used. That said, precisely one of the benefits of cooperative compliance is that taxpayers are under a broad expectation to disclose any information that can be material for the administration to assess their tax risk and that of their tax positions, so the information available under a cooperative compliance setting can go beyond that which is obtained under mandatory disclosure regimes.

5.5.4. How does Cooperative Compliance Differ from Traditional Vertical Supervision Approaches?

Having reviewed various features of cooperative compliance, from its objectives to the principles behind it and how the core cooperative exchange functions, this section presents a summary of how cooperative compliance, seen as a distinct regulatory approach, differs from other forms of regulation.

5.5.4.1. Cooperative compliance works horizontally

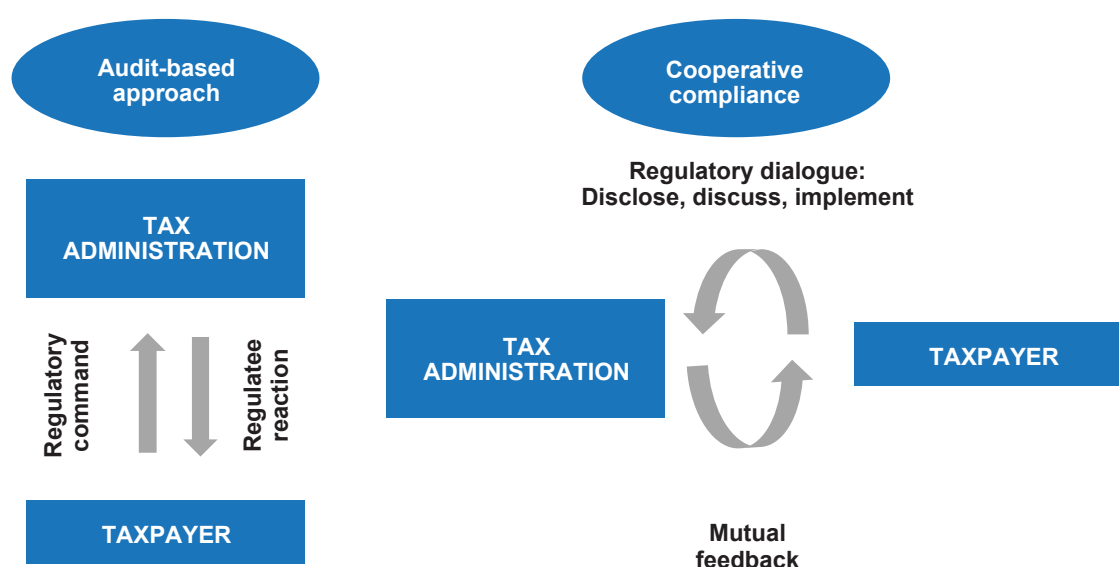
Cooperative compliance works horizontally, meaning that the regulator and the regulatee are placed on a level standing, and are seen as compliance partners. This represents an important departure from the traditional audit-based tax regulatory approach, where the relationship is vertical in nature, and the administration uses its legal authority to issue commands to the regulatee (the taxpayer). Unlike the climate generated by the vertical dynamic, which is characterized by suspicion and confrontation, cooperative compliance seeks to operate under what Wahl et.al (2010) denominate a "synergistic climate", where respectful dialogue is used to assist and guide regulatees, enhance interparty trust, and turn it into voluntary compliance gains.

Under a horizontal regulatory approach, instead of mandates and commands, most regulatees are expected to operate out of their own volition, be it because they have implemented a degree of self-regulation, or because they implement the suggestions that have been agreed with the regulator. Indeed, unlike a traditional audit-based approach, the regulator does not wait to receive a command from the authority, but rather seeks to engage with it proactively, and then execute disclosed or agreed upon compliance strategies and tactics. Rather than a dynamic where the

regulator assesses the situation unilaterally (with all the defects of information asymmetry), issues a regulatory command, and then decides whether coercive enforcement is necessary depending on the regulatee's reaction, cooperative compliance works in a more circular fashion, with the parties assessing the situation jointly, proposing regulatory alternatives, giving each other feedback, and then deciding on a mutually agreed course of action, or, where this is not possible, issuing commands that are already targeted, knowing the regulatee's position. This dialogue, in which the tax function of the taxpayer effectively becomes a compliance partner of the administration, is very different from the model where these two are rivals:

Figure 5

Cooperative compliance horizontal dynamics



Source: Elaborated by the authors, 2021.

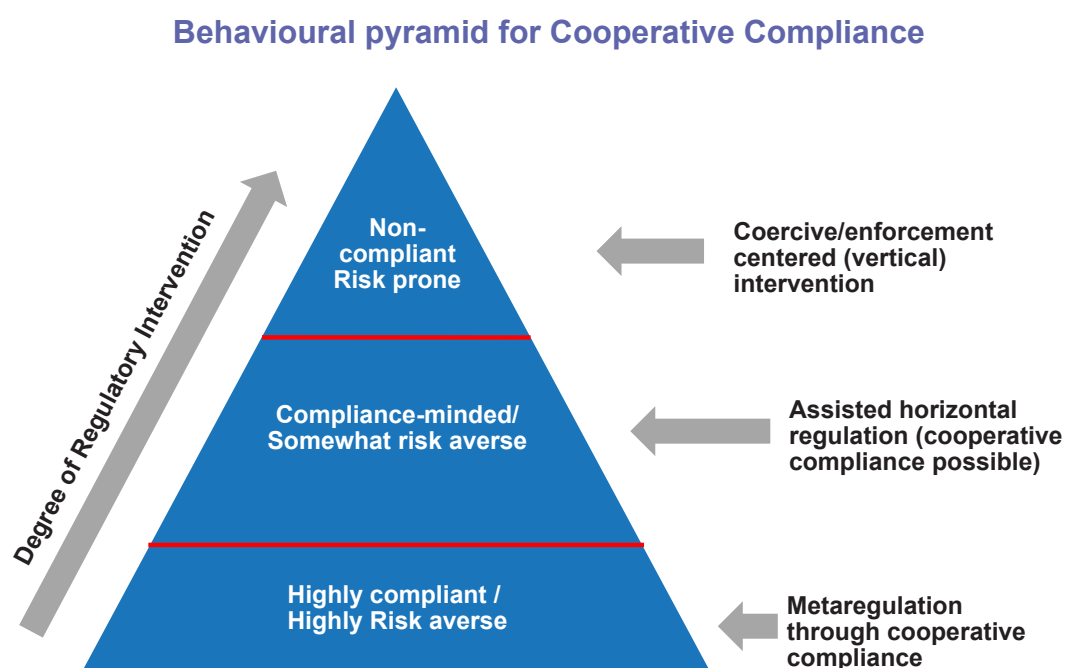
5.5.4.2. Cooperative compliance relies on responsive regulation

As was explained previously, cooperative compliance relies on the greater proximity between the regulator and the regulatee to acquire more information about the former and use it as a tool to implement regulatory strategies that are specifically tailored to that regulatee's tax risk profile (which incorporates their compliance history, structural characteristics, and risk management practices) and their unique array of tax positions.

This customization of regulatory interventions represents an advantage in terms of regulatory efficiency (because the regulator has more information on which regulatees require greater intervention than others and can assign scarce resources correspondingly), and can translate itself into greater voluntary compliance by enhancing the regulatee's perception that the regulator listens to their concerns, knows them, and acts accordingly (all aspects that affect procedural fairness, and through it, trust in the regulator).

While cooperative compliance differs from traditional regulatory approaches in its consideration of the average regulatee as inherently compliance minded and risk averse, per opposition to potentially non-compliant and opportunistically risky, by no means does it presume that all regulatees will comply, since it is still understood that a fraction of taxpayers will be uncooperative, risk-prone, or will produce non-compliant results. What is different is that rather than seeing the regulatees as a homogenous population, cooperative compliance, like other forms of responsive regulation, works on the basis that most of the regulatees are compliance minded, and increasingly smaller segments of the regulatees will be less compliant. This is represented by Braithwaite's idea of the "regulatory pyramid" (J. Braithwaite: 2003). For tax purposes, this means that cooperative compliance offers the potential for the tax administration to tailor regulatory efforts and work under multi-tier systems, with intervention inversely proportional to compliance and/or tax risk. An example of how the pyramid might look under a multi-tiered cooperative compliance system is presented next:

Figure 6.



Source: Elaborated by the authors, 2021.

It is important to bear in mind that responsive regulation means the regulator has the ability to constantly reassess its regulatory responses to changes in the regulatee's profile; as such, a specific taxpayer can go in and out of cooperative compliance programmes depending on their compliance behaviour and tax control frameworks, and even within cooperative compliance, the regulator's intervention and focus can shift from a more interventionist guided compliance (e.g. for taxpayers who are compliance minded but need to improve their tax control frameworks), to a high-level regulation where the tax administration focuses on periodically assessing whether the taxpayer has been prudent in its self-regulation. In this last variant, which would require

sophisticated, risk averse and highly compliant taxpayers, and is therefore unlikely to exist in the early years of a cooperative compliance regulatory approach, the administration uses cooperative exchanges only to discuss uncertain tax positions as and if they arise, and to discuss how the taxpayer's self-regulated tax control frameworks are operating.

5.5.4.3. Cooperative compliance relies on risk control

As explained previously, cooperative compliance is a regulatory approach that is premised on the regulator and the taxpayer addressing tax compliance proactively and not reactively. This means that rather than focusing on materialized non-compliance, cooperative compliance focuses on addressing the risk of non-compliance in order to attempt to prevent it from materializing. This is a significant departure from the audit-based approach, that relies on detecting and penalizing materialized non-compliance. Focusing on risk does not mean that cooperative compliance cannot be used to address existing (materialized) non-compliance, since there are different cooperative compliance regimes that do allow for the parties to discuss closed tax positions as part of the cooperative dialogue, and certainly cooperative compliance can assist in solving existing disputes expeditiously without having to resort to litigation or Alternative Dispute Resolution (ADR) mechanisms. However, the ideal is that the parties' full, transparent disclosure and collaborative attitude allows them to identify possible risks and resolve them before they turn into a dispute.

A crucial element required for a risk-based regulatory approach, that is also necessary for responsive regulation, is the ability for the regulator (the tax administration) to understand the regulatee's compliance conduct and their characteristics associated to risk profiles. In cooperative compliance, this is achieved by a combination of administrative commercial awareness (also known as business understanding) and using subsidiarity and voluntary disclosure for the taxpayer to reveal risks autonomously. In the case of commercial understanding, the expectation is that the administration invests in learning about the taxpayer's business, so that they can more easily identify tax risks and compliance challenges, and then discuss these with the taxpayer. As for subsidiarity, the principle is that the taxpayer is the best positioned to know about compliance challenges, weaknesses and strengths of the tax control framework, and uncertain tax positions, so the regulatee is expected to voluntarily disclose these aspects, thus allowing the regulator to identify them and attempt to address them in tandem with the regulatee.

In addition, it is important that the regulator understands the circumstances in which financial and tax law specialists act (Huiskers-Stoop & Gribnau: 2019, pp.85). These specialists must entertain good relationships with their client on the one hand, and with the tax administration on the other. This implies the parties' willingness to "enter into discussion about for instance the cause of mistakes (and the best way to redress them) and about the measures necessary to prevent mistakes from being made in the future".

There is a direct link between commercial awareness and the administration's ability to detect risky areas or tax positions that are more uncertain and are therefore more likely to entail non-compliance challenges. This is particularly true in highly specialized or regulated industries (e.g. extractives, pharma, finance, digital services), where special tax and accountancy provisions are applicable, and where commercial transactions are often complex. Furthermore, commercial awareness is highly important when addressing situations of aggressive tax planning or tax abuse because the commerciality (or lack thereof) and the artificiality of a transaction/tax position are

key factors or hallmarks. The problem here is that, while commercial awareness is necessary to optimize cooperative compliance, and to enhance interparty trust and voluntary compliance, it requires for the regulator to invest significant resources in training or hiring industry specialists and maintaining them as dedicated taxpayer or taxpayer sector officers. This can be challenging for resource-limited administrations.

Naturally, risk-based tax regulation is not a panacea and comes with a set of problems of its own (Quiñones: 2020, pp. 153-205), it offers efficiency gains and responsiveness, but it can also confuse the risk of non-compliance with actual non-compliance, thus endangering the principle of legality. Similarly, it can lead the tax administration to believe that non-compliance stems from taxpayers' not sharing the administration's interpretation of the law, rather than the law as it is (in essence, how it would be determined to apply if taken to court). This could translate into undesirable instances of overcompliance. Finally, regulating as a function of risk requires that care be placed into calibrating risk predominantly based on taxpayer behaviour, rather than on structural factors, since the risk associated to the latter can be mitigated by taxpayer behaviour, and taxpayers with highly complex structures can still be highly compliant and risk averse.

5.5.5. What are the potential advantages and risks of cooperative compliance in the context of developing nations?

As has been recognized by various policy-making institutions and academics, trying to implement a specific regulatory policy in different jurisdictions raises the risk of incurring in a legal transplant, where a “one-size-fits-all” approach leads to the belief that copying what has been implemented successfully elsewhere will necessarily work equally well in another jurisdiction, regardless of contextual differences. With this in mind, this section of the chapter is devoted to heading the call made, among others, by CIAT (Cremades et. al.: 2015, pp.6-7)., about the need to acknowledge the legal, administrative, cultural, political, and socioeconomic features present in the Regions under the scope of CIAT and identify the advantages or challenges that commonalities in these regional features raise in relation to implementing cooperative compliance.

While the panorama in developing nations like many of those belonging to CIAT presents many challenges in this area, the limited availability at present of fully-fledged cooperative compliance programmes and different conditions surrounding tax compliance and tax administration in this type of jurisdictions also make cooperative compliance particularly attractive for taxpayers and tax administrations alike. Even though initiating the implementation of regulatory policies that may not be familiar or long-standing requires that jurisdictions overcome various hurdles and that significant investments are undertaken, acknowledging these challenges should not deter policymakers and stakeholders from embracing cooperative compliance, since this regulatory approach's potential benefits are substantial and can lead to sustained improvements in voluntary tax compliance.

5.5.5.1. The advantages of cooperative compliance in the context of developing nations

5.5.5.1.1. High levels of litigiousness

The **high levels of litigiousness** present in many jurisdictions throughout the CIAT-sphere provide an incentive for the implementation of cooperative compliance because both taxpayers and tax administrations can see that the experimental treatment (cooperative compliance) could lead to significant gains in terms of compliance costs and a refreshed working relationship between the parties. In essence, where the status quo has traditionally been characterized by a confrontational approach to tax compliance, regulatory approaches like cooperative compliance, which are based on the premise of a collaborative, non-adversarial relationship, have a heightened attractiveness because they represent a departure from practices that can have negative effects on compliance. For example, high levels of litigiousness or a relationship centered on tax disputes can lead to interparty distrust, perceptions of procedural unfairness, resistant or disengaged attitudes towards compliance, and can create an unhealthy dependence on a detect-dispute-penalize dynamic that foregoes voluntary compliance, overburdens tax courts, and displaces (limited) administrative resources towards tax dispute management to the detriment of other administrative functions. Similarly, for taxpayers, the availability of a cooperative compliance programme can be seen as an opportunity to reduce tax compliance costs associated with tax dispute management (e.g., attorney fees and the cost of complying with intrusive administrative audits).

5.5.5.1.2. Highly complex tax systems that are characterized by frequent normative changes

Many of the jurisdictions covered by CIAT have **highly complex tax systems that are characterized by frequent normative changes**. This is both an advantage and an obstacle for cooperative compliance. In terms of the advantage offered, the existence of complex and ever-changing tax rules means that both taxpayers and the administration have a marked incentive to cooperate with the objective of gaining more tax certainty, either through agreements on the interpretation of the law, or by agreeing to disagree, meaning identifying each party's differences in relation to the interpretation of the law and what the consequences of the assuming tax positions based on that difference are.

Greater certainty is associated with a greater predictability of the tax function, and this in turn improves the efficiency of corporate tax functions and the efficiency of the administration in terms of having more certainty about revenue flows and areas where tax investigations and disputes will remain necessary. The point here is that where the status quo (absent cooperative compliance) offers high levels of certainty, investing in cooperative compliance appears to be less attractive because it is seen as unnecessary, whereas the existence of high levels of uncertainty acts as a driver to push forward with innovative alternatives, including cooperative compliance.

The downside to having highly complex and fast-changing tax systems is that it might make cooperative dialogues less productive in terms of reaching agreements because the underlying

tax rules are too uncertain for the parties to be able to reach a shared understanding. Similarly, companies and the tax administration might be reluctant to engage in programmes that are meant to work over the mid and long term and constant changes in the rules might render the agreements reached in one period inapplicable to subsequent periods.

Finally, a high frequency of normative changes (legal instability) might deter taxpayers from participating in cooperative compliance programmes and disclosing their information voluntarily because they fear that the structure and rules of the cooperative compliance programme might also be subject to change and that the benefits associated with their participation might not materialize. Thus, while high uncertainty can be used as an incentive to initiate cooperative compliance and gives it momentum, it is clear that once the programme is running, the administration needs to work with policymakers to try to reduce the pace at which rules change and their complexity so that the programme remains attractive.

5.5.5.2. The challenges of cooperative compliance in the context of developing nations

5.5.5.2.1. Changing the culture of regulators and regulatees

One of the challenges present in developing nations is the fact that longstanding practices both for the tax administration and for taxpayers are based on tax compliance under an adversarial tradition and on an understanding of compliance that is reactive and not based on risk identification and mitigation.

For the administration, having operated under an adversarial scheme for many years means that the change to a regulatory approach based on horizontality and collaboration (partnership) is difficult because it requires a complete change in the way in which the regulator sees its role in the compliance equation (from a coercive enforcer and inquisitor (through audit) to a compliance facilitator and prudential regulator. As with any process of institutional change, it is to be expected that administrative personnel who has been trained and operating under a detect, punish, and deter approach displays some resistance to a shift where the objective is not primarily to punish, but rather to assist the taxpayer in improving their compliance, and enforcement is reserved for recalcitrant taxpayers.

Additionally, tax administration officials that are accustomed to work under a reactive dynamic (audit closed tax periods, detect non-compliance and penalize/force adjustments) might find it complicated to transition to a scheme where their role is proactive and based on identifying tax risks and working together with the taxpayer to prevent their materialization.

Since cooperative compliance is a two-way (Reciprocal) dynamic, it must be taken into account that regulatees (taxpayers) also face important challenges in terms of the transformation of their tax culture. Indeed, corporate tax departments also need to shift towards a more proactive, risk-based, compliance role, and, despite past experiences, start to view the administration as a partner, rather than an adversary. This cultural change is fundamental to ensure adequate risk identification and management and to ensure that the transparency required by cooperative compliance is satisfied so that voluntary disclosure is provided, even where the administration or a judge has not demanded the release of a specific piece of tax information.

5.5.5.2.2. Dealing with limited organizational resources

As was explained in 5.5.2., transitioning from a traditional audit-based approach to a cooperative compliance approach requires significant transformations both for the taxpayer and for the tax administration. In the case of the tax administration, the need for increased business knowledge (Commercial awareness) means that generalist profiles will have to be replaced by tax officials that specialize in specific industries. Additionally, the horizontal dynamic of cooperative compliance dialogues benefits from the existence of single-point-of-contact officials that act as a dedicated channel for specific taxpayers, and this means that administrations, which often have limited resources at their disposal, have to invest heavily in recruitment and training, and also have to remove tax officials from their generalist roles to the more specialized roles, all of which leaves a void in their previous functions. Furthermore, as is the case with other initiatives like exchange of information (EOI) and mandatory disclosure mechanisms, the onset of cooperative compliance and the associated taxpayer voluntary disclosures means that the tax administrations in developing nations, that sometimes struggle with information technology (IT) resources, will have to improve their ability, both in terms of human and machine resources to interpret and make use of the troves of information provided by taxpayers (Braithwaite: 2006, pp.884)¹⁷. While the expectation is that the greater responsiveness and reduced information asymmetry resulting from cooperative compliance allow administrations to work more efficiently, thus compensating for any resource allocations towards cooperative compliance functions, it is likely that results take time to materialize, and this means that returns for the additional investments are not immediately seen. Thus, tax administrations need to be ready to engage in investments that have a mid-long term return panorama but an immediate or short-term need for resources, and the reality is that it is not easy to convince policymakers to allocate resources out of constrained public budgets when the results, for example, in terms of increased voluntary compliance, are likely to take time to become evident, even beyond the current electoral cycle. Therefore, in the case of developing nations it is important to focalize any available international aid towards obtaining the administrative resources required to implement cooperative compliance.

In the case of taxpayers, organizational resource constraints can also be an issue because the need to produce information to disclose to the tax administration preemptively (before filings) consumes the resources of tax teams but also of other corporate teams that are supposed to provide information internally to the tax team (for example, legal teams, general accountancy and finance teams, commercial teams, etc.). This means that in addition to having to allocate resources to cooperative compliance dialogues and information disclosure, tax teams and corporations as a whole also have to devote resources to achieving a better coordination between tax and non-tax teams, both to be able to keep the tax function apprised of any details needed to detect and mitigate tax risks, but also to ensure that any agreement reached with the administration is fully executed by the taxpayer's organization. While not all corporations present in developing nations are resource-constrained, it is likely that organizations that outsource their tax function or that rely on corporate headquarters (HQs) or back-office centers for tax functions will need to alter their resource allocation dynamics.

Because tax administrations in developing nations do not always have abundant resources at their disposal, hiring new staff is not necessarily an option, so intensive internal training and assistance from other administrations that are already experienced with cooperative compliance is likely to be required. As is the case for administrations, corporate tax departments are likely

to need to update their skillset to include skills such as risk management and negotiation, and, where available (for example, in the case of multinationals) they can benefit from partnering with the tax departments of other units in the corporate group that come from jurisdictions where cooperative compliance has been operating for a longer time. Like with administrations, it can be envisioned that corporate tax departments would have to ask for additional resources even if the additional investment would not yield immediate or short-term results, and this involves complicated intra-group negotiations.

A final resource-related issue which must be taken into account in the context of developing nations is resource asymmetry between the tax administration and large corporate taxpayers. Indeed, with certain exceptions where tax administrations in developing nations under CIAT's sphere (e.g. Brazil, Chile, Mexico, Colombia, Argentina, Perú, Ecuador) are somewhat well-resourced in a relative comparison to the tax departments of large corporations, many other tax administrations have lower levels of resources at their disposal (financial resources, human resources, etc.). While cooperative compliance's disclosure is meant to reduce information asymmetry, differences in resources can translate into the perception by corporate taxpayers that the administration's power is limited, something which has been evidenced to alter voluntary tax compliance and which can, for example, lead to undesirable phenomena such as selective disclosure, where taxpayers participating in the programme attempt to exploit administrative weaknesses by disclosing only the most favorable information or whatever is deemed to aid them strategically.

5.5.5.2.3. High levels of corruption

As can be seen in different sources, such as Transparency International's Corruption Perception Index (Transparency International: 2019)¹⁸, many developing countries share the unfortunate contextual characteristic of exhibiting high levels of corruption (be it perceived or materialized). This represents a fundamental challenge for implementing cooperative compliance because high levels of perceived corruption can be associated with lower levels of interparty trust and, as was explained earlier in this chapter, trust is necessary for the cooperative exchange to function efficiently. If the parties to the cooperative relationship see each other as untrustworthy, they are less likely to perform the functions expected of them and collaborate in a satisfactory manner.

On the other hand, if the perceptions of corruption also coincide with high levels of actual corruption, there is a risk that the proximity and horizontality offered by cooperative compliance are exploited by self-interested parties that instrumentalize the cooperative dialogue by means of regulatory capture, where the regulator is privately captured in order to produce results contrary to the public interest.

The challenge then, is to devise mechanisms that allow cooperative dialogues to take place without providing an opportunity for tax officials to be coopted into using the programme's greater administrative discretion to reach agreements that are contrary to the rule of law. Naturally, dealing with corruption goes far beyond the context of tax administrations and taxpayers, and there are multiple contextual issues that need to be addressed.

However, the focus here is to create internal mechanisms like tax official rotation or selective auditing that reduce the opportunity for regulatory capture to take place, but which are not

so burdensome that they jeopardize the programme's efficiency or its ability to deliver legal certainty (see section 5.5.5.3. below). Having mechanisms in place to prevent corruption is necessary not only for the program to produce adequate results which respect applicable laws and regulations, but also to improve the public legitimacy of the initiatives, something which represents a challenge in and of itself.

5.5.5.2.4. Legitimacy issues associated to the perception of preferential treatment

A challenge for the implementation of cooperative compliance in the countries under CIAT's sphere is the possibility that cooperative compliance is equated by different actors with an unjustified preferential treatment for those who are able to participate in the programme.

While this has proven to be a challenge in multiple jurisdictions that have implemented cooperative compliance, regardless of their contextual circumstances (see Quiñones: 2020), the concern here is that the high levels of citizen dissatisfaction with the provision of public goods and services present¹⁹ in many of the countries that make up CIAT's membership and the high levels of inequality often present in these jurisdictions (e.g. as measured by their Gini coefficients) combine with other factors to strengthen a perception that cooperative compliance represents a breach to the principle of equal treatment under the law.

This issue, which in other latitudes has translated into cooperative compliance wrongly being equated with "sweetheart deals", has the potential to derail the program and even erode voluntary compliance among non-participating taxpayers if the fundamental misperceptions about what cooperative compliance can do and how it operates are not corrected.

Fundamentally, it is necessary for those jurisdictions interested in implementing the program to enact comprehensive tax education initiatives so that different actors (Citizens, civil society groups, non-governmental organizations [NGOs], politicians, etc.) are shown that cooperative compliance does not accept (and cannot) lead to outcomes contrary to the rule of the law, and that, while cooperative compliance can lead to differential treatment for participating taxpayers, this treatment is justified because these taxpayers engage in a level of voluntary disclosure that goes beyond what is legally required and that the administration's interaction with taxpayers is mediated by risk profiling and responsiveness, so that the treatment received by taxpayers should always be a function of their compliance behaviour and their amenability to the program, objectively evaluated. Thus, it is important to communicate the fact that the benefits attached to cooperative compliance are not granted arbitrarily, but rather as a result of tangible actions by participating taxpayers that are different to those expected of non-participating taxpayers, and that while participating can lead to benefits it also subjects participants to heightened, preemptive scrutiny, and requires participants to undertake considerable investments. Furthermore, the limited availability of public resources and relatively low levels of tax compliance often present in countries in Latin America, Africa, and the Caribbean should be also be seen as factors that require authorities to embrace regulatory approaches like cooperative compliance, which are based on increasing compliance and collection efficiency, and which are expected to assist the administration in better allocating its resources so that both participants and non-participants can benefit from more targeted regulation.

Within the tax administration, it is possible that there are internal clashes between supporters of cooperative compliance and those who (erroneously) see it as too lenient on taxpayers and as giving away power. These internal conflicts are more likely to happen in jurisdictions where the staff in tax administration has been operating under a command-and-control approach for many years, and where contextual circumstances such as low levels of compliance, high levels of crime, and/or high levels of informality have led to “hardened” inspectors that only feel comfortable with coercive measures. As with other challenges, a good approach to tackle this problem is to increase administrative training and, if possible, pairing administrations with the staff from other jurisdictions’ administrations that are experienced with cooperative compliance and which, ideally, come from similar contexts (Braithwaite: 2006, pp.892)²⁰.

Additionally, if all actors are not given accurate information about how the programme operates and what it can and cannot do, and about the measures taken to prevent corruption within the programme (some of which were discussed earlier in this text), there is a risk that other state actors (e.g. ombudsmen, control organisms, the Legislative, the Judiciary) also view the programme as illegitimate and attack it or prevent it from functioning effectively. For that reason it would be advisable to involve other state (and non-state actors) in the programme (Braithwaite, 2006: pp.888)²¹.

Finally, it should be noted that legitimacy can also become a concern when participants themselves begin to see the programme as unfair or inefficient (e.g. when legal certainty is not being provided in a timely fashion, when the administration is not being truly responsive, or when agreed-upon positions are disregarded), or when extended public perceptions of the programme as illegitimate make participants shy away from it in an attempt to prevent reputational damage. Thus, in addition to informing all stakeholders about the programme’s true nature, it is important that tax administrations constantly ask for feedback from participants (both taxpayers and personnel from the administration working in the programme) in order to be able to quickly anticipate problems and/or provide solutions before parties lose faith.

5.5.5.2.5. Excessive legalism

A challenge to cooperative compliance which can be foreseen in relation to many of the jurisdictions under CIAT’s sphere is excessive legalism, understood as an overly legalistic view of the way in which the tax administration should exercise its functions. This issue, which is connected to legal systems which rely heavily on codification and statutory or reglementary instruments over and above other sources of law, can represent problems for cooperative compliance because it can lead to a restrictive view of the administration’s discretionality and to a reliance on the codification of cooperative exchanges that can lead to excessive bureaucracy, thus reducing the model’s efficiency and possibly legal certainty (when the belief that every aspect no matter how minor should be pre-ordained in the law and that all of the administration’s actions (or omissions) are subject to administrative and/or judicial challenge).

Since cooperative compliance relies on preemptive regulation and on real-time dialogues between regulators and regulatees, and responsiveness mandates that the solutions and positions offered by the administration are customized so that they answer to each regulatee’s specific profile, reliance on legal principles and doctrines associated with traditional administrative law

paradigms that focus on restricting the power of the administration (Something which makes sense under a command and control hierarchical approach) might stifle the program's dynamics.

Taking into account what was explained in previous sections in relation to corruption and legitimacy, the difficulty here is in striking the right balance between transparency and accountability (both of which are desirable in relation to any public policy), and the need for there to be enough legal certainty in relation to the agreements reached as a result of cooperative exchanges so that taxpayers feel that their disclosure has been adequately reciprocated. Therefore, while it is understandable and appropriate that different aspects of the cooperative compliance regime are enshrined in the law, and that cooperative compliance outcomes which are arbitrary and clash with public interest can be subjected to judicial review, it is necessary to trust the administration to be able to exercise its discretion appropriately, in a way which enables it to provide the efficient, legal certainty that participants require.

5.5.5.3. Evaluating cooperative compliance as a public policy

A final challenge to be outlined in relation to implementing cooperative compliance is that of evaluating cooperative compliance as a public policy. Indeed, the experience of many of the jurisdictions that pioneered cooperative compliance (e.g. The Netherlands, Ireland, the United Kingdom, etc.), shows that evaluating cooperative compliance is a difficult process, not only because finding the right benchmarks to evaluate outcomes is complicated when the program's goals are mid to long term making it very hard to establish a causal relationship between a regulatory approach and indicators like tax revenue and revenue efficiency, but also because the type of results and the scope of evaluation that different stakeholders have in mind are not necessarily compatible. Although some studies do exist that show that parts of cooperative compliance programmes work for both tax administrations and participating taxpayers, more empirical research is needed into the benefits of these programmes²².

For starters, some of cooperative compliance's goals, like increasing voluntary compliance by building interparty trust, improving taxpayer risk awareness and controls, improving administrative commercial understanding, etc. are normally not measured quantitatively, but rather qualitatively, and stakeholders often find qualitative evaluation less convincing because of a mistaken belief that only quantitative indicators are empirically valid. Moreover, many of cooperative compliance's features are associated with improvements in the compliance process (litigiousness, taxpayer satisfaction, reduction of information asymmetries, etc.), rather than the outcome of the process (e.g. how much revenue was obtained and how many resources were spent by the administration vs. revenue obtained).

Additionally, while it is foreseeable that stakeholders, particularly politicians and those in different State roles will want results in the short term, the implementation of cooperative compliance, particularly where it represents a break from a longstanding command and control model, will be likely to produce results in the mid and long term, rather than in the short term. As with other long-term public policies, this means that cooperative compliance could face attacks by the government and/or politicians in jurisdictions where policies are more dependent on electoral cycles and where resource constraints increase the pressure for quick results.

5.5.6. Cooperative compliance around the world

This Section provides a short comparison of some of the cooperative compliance frameworks around the world. For this comparison, the framework of the Netherlands, the United Kingdom, and Russia will be provided. In the Netherlands, this framework is called “horizontal monitoring”, in Russia “tax monitoring” and in the United Kingdom “Compliance Risk Rating”.

As highlighted by the OECD in scholarship (Russo: 2020; Pemberton & Majdanska: 2016²³) and OECD reports²⁴, countries have made different choices when introducing a cooperative compliance framework. These choices influence the design and implementation of the framework. Some of the reasons for these choices, can be found in the way that the tax system and the tax administration has been designed. But also, some other reasons may be the limitations of developing countries when introducing a cooperative compliance framework.

Some of these limitations are the lack of resources, trust and understanding of the tax administration activities, as well as the focus of tax administrations and taxpayers on adversarial positions through audits and tax disputes before the courts (see Section 5.5.1.2. and 5.5.3.2. above).

In our comparison we will address the following elements found in the countries of study. These elements have been also addressed in several articles providing comparison among countries (Pemberton & Majdanska: 2016) or analyzing a specific country (Martini et al.: 2021)²⁵. Therefore, for the reader, we are providing a short description of some of these elements, so that it is clear the differences among the countries of study.

Design of the framework

- Objectives of the framework: To improve compliance by the taxpayer, to carry out tax monitoring by the tax administration, to provide certainty to the taxpayer by means of providing a reasoned opinion by the tax administration to participants of the cooperative compliance framework, among others.
- Cooperative compliance framework as a standalone measure or as part of a program for instance a compliance risk management strategy by the tax administration.
- Cooperative compliance needs to be regulated by law, vs. cooperative compliance is based on tax administration policy (i.e. discretionary power of the tax administration).
- Validity of the cooperative compliance framework: To apply every year, or for a longer specific period of time.
- The scope of the framework open to all tax issues, or limited to some tax issues (e.g., excluding transfer pricing).
- Beneficiaries of the framework: all taxpayers, only large taxpayers with specific threshold, excluding high risk taxpayers, and taxpayers from all sectors or only from some sectors.
- Introduction of pilot projects.

Implementation framework

- Taxpayers required to introduce a Tax Control Framework (or not)
- Possibility to introduce a cooperative compliance agreement (or covenant) between the tax administration and taxpayer

Organizational changes

- Changes to the tax administration: introduction of a specific cooperative compliance division or use of large business taxpayer's division, to rotate tax officials participating in cooperative compliance, and to provide training to tax officials regarding risk management, auditing, etc.

5.5.6.1. Design of the framework

In general, the countries addressed in this comparison differ in the design of the framework for cooperative compliance.

In the Netherlands and the United Kingdom, the cooperative compliance frameworks are based on **tax administration policy** (Russo: 2020, pp.272) and are part of a Programme i.e., the Netherlands' Horizontal Monitoring model (NTCA: 2013; 2016)²⁶ and the United Kingdom's Tax Compliance Risk Management System²⁷. In contrast, in Russia, this framework has been designed as a **legislative measure** which started first as a pilot project in 2012, and thereafter incorporated in the Tax Code in 2014. At the time of writing, this Framework is in "the process of being further extended under Federal Law of 13 August 2020" (Martini et. al.: 2021, pp.29)²⁸.

The differences in the way that cooperative compliance programs have been introduced (based on tax administration policy or by law) also influences the **discretionary power** of the tax administration. This discretionary power can be defined as the "elbow room" that a tax administration has to "efficiently set up the taxation process in view of scarce enforcement resources and the different characteristics and risk profiles of taxpayers" (Huiskers-Stoop & Gribnau: 2019, pp.68).

For instance, in the Netherlands and the United Kingdom, the tax administration has discretionary power to undertake acts in relation to their responsibility for the "collection and management" of taxes which also includes the enforcement powers under which the cooperative compliance framework exists (Huiskers-Stoop & Gribnau: 2019, pp.68).

In Russia, the cooperative compliance is regulated by law, and therefore, the changes to the framework need to be in accordance with the principle of legality, and throughout amendment to the Russian Tax Code provisions addressing "tax monitoring" (art. 105.26 - art. 105.31)²⁹. This is the case in the current (proposed) draft Federal Law mentioned above. However, there have been also administrative instructions to provide "detailed guidance and clarifications regarding the tax monitoring regime" (Martini et al.: 2021, pp.34).

In general, in all 3 countries of study, the cooperative compliance framework has been established to address **large taxpayers**, but in the Netherlands, it is also possible for small companies and high net worth individuals to benefit of cooperative compliance, not directly but mainly through arrangements between tax administration and tax/financial advisor (NTCA: 2016). In the Netherlands it is possible to conclude individual agreements (covenant) with service providers (e.g. tax/financial advisers) or umbrella organizations of these service providers (e.g. Dutch Association of Accountants, Dutch association of tax lawyers and tax advisors)³⁰.

In the Netherlands, one of the elements included in this cooperative compliance framework is the risk, and therefore, **high-risk taxpayers** are to a large extent excluded from this framework. Dutch taxpayers must be willing and able to comply with the tax laws and regulations (Stevens et. al.: 2012, pp.41). In the United Kingdom, in addition to non-risk taxpayers (low risk taxpayers under the Business Risk Review³¹+ [BRR]), there is a classification of moderate, moderate-high or high-risk taxpayers. Non-low risk taxpayers are subject to a business risk review every year, unlike low-risk taxpayers which are subject to a business risk review every 3 years (HMRC: 2019). The fact that in Russia, the risk factor has been excluded from the framework, making it possible (in principle) for high-risk taxpayers to also apply for cooperative compliance³².

The **objectives** of cooperative compliance for the tax administration also differ among the 3 countries of study. In the Netherlands and the United Kingdom, the objective is to enhance self-regulation (achieving compliance and also tax risk mitigation) and to establish a trusted relationship with compliant taxpayers by means of introducing a shared responsibility between compliant taxpayers and tax administrations. In Russia, the focus of tax administration is to facilitate monitoring by tax administration of large taxpayers by “having access to the company’s accounting and tax data in real time” (ITR: 2021)³³.

The **objectives** of cooperative compliance for the taxpayer of the cooperative compliance framework are also different between countries. In the Netherlands and the United Kingdom, the taxpayer when participating in cooperative compliance aims to develop a relationship with the tax administration based on reciprocal trust, understanding and transparency. In the Netherlands reciprocal trust should be seen as “informed trust” as opposed to “blind trust”. Informed trust depends on reciprocal transparency with regard to information provided by the tax administration and taxpayer (Huiskers-Stoop & Gribnau: 2019, pp. 85).

In the case of the United Kingdom, the aim is also to improve the administration’s commercial awareness and business knowledge and acquire greater insight about the taxpayer’s drivers so as to be able to provide responsive regulation, understood as proportional administrative responses to identified risks and the ability to provide clarity to taxpayers about the scope and process by which tax disputes (if existing) will be addressed (HMRC: 2019). Broadly speaking, the idea is that low-risk taxpayers will face a less intrusive regulator and be more autonomous,

whereas taxpayers in other risk categories will face proportionately more frequent and more intense regulatory intervention.

In the Netherlands, the taxpayers aim to obtain - in exchange for voluntarily providing relevant tax information - fiscal certainty about their tax liability in advance and are in principle “no longer subject to time and effort-consuming tax audits, sanctions and prosecution afterwards” (Huiskers-Stoop & Gribnau: 2019, pp. 67). Whereas in Russia the aim is to obtain certainty from the tax administration in the taxpayer’s activities throughout reasoned opinions (art. 105.30 Tax Code).

In the Netherlands cooperative compliance is called horizontal monitoring and it is applicable to the levying of all Dutch national taxes and the collection thereof (Huiskers-Stoop & Gribnau: 2019, pp. 86). To qualify for horizontal monitoring, taxpayers should be subject to one or more Dutch national taxes. The tax cooperation based on horizontal monitoring, subsequently, refers to all national taxes to which the taxpayer is subject.

The cooperative compliance programme in Russia **excludes** transfer pricing and outstanding legacy issues (Pemberton & Majdanksa: 2016, pp.597). The Tax Code states that “When conducting tax monitoring a tax authority shall not have the right to send to an organization a reasoned opinion on matters relating to the checking of prices used by the organization in controlled transactions for conformity to market price” (art. 105.30 (10)) (EY).

Finally, in Russia, taxpayers are required **to apply** every year for tax monitoring. However, this is current in process of being changed by means of the draft amendment Law of 13 August 2020. In the United Kingdom it depends on the type of taxpayer (non- risk, moderate, moderate high, high-risk taxpayers). In the Netherlands, the tax agreement (*covenant*) between tax administration and taxpayers (large³⁴ or small and medium taxpayers (NTCA: 2021)³⁵ state that the validity of the horizontal monitoring is for an indefinite period, but that it will be reviewed periodically by the underlying taxpayer and the tax administration³⁶.

The above-mentioned elements are also summarized in the following table:

Table 1.

Comparison of elements in cooperative compliance frameworks

Element	The Netherlands	The United Kingdom	Russia
Tax administration Programme or Statutory Law	Part of Horizontal Monitoring Model	Tax Compliance Risk Management System (including the BRR+)	Law: Russian Tax Code and administrative regulations(guidance)
Discretionary power	Yes	Yes	No
Pilot Project	Yes (in 2005 for large taxpayers and 2008 for medium-sized business (Stevens et. al.: 2012) ³⁷)	No. However, the BRR served as a first model that was then revamped with the BRR+ in 2019.	Yes (in 2012)
Taxpayers	Large taxpayers (and in exceptional cases high net worth) directly and small companies indirectly through arrangements with tax/financial intermediaries	Large corporate taxpayers	Large taxpayers
High-risk taxpayers	No	Yes, specific distinction between low-risk vs. moderate, moderate-high and high-risk taxpayers.	Yes (risk factor excluded)
Objectives	Tax Administration: To enhance self-regulation, and to establish a trusted relationship with compliant taxpayers. Taxpayer: reciprocal (informed) trust, understanding and transparency	Tax Administration: To enhance self-regulation, and to establish a trusted relationship with compliant taxpayers. Align tax with “genuine commercial activities” Taxpayer: reciprocal trust, understanding and transparency, certainty and risk working	Tax Administration: To facilitate monitoring by tax administration: Access to company’s accounting and tax data in real time. Taxpayer: Certainty: to obtain a reasoned opinion from the tax administration
Scope of application	All national tax issues	All tax issues	Exclude transfer pricing issues
Validity compliance arrangement	Indefinitely with periodical reviews	Low Risk 3 years, and Non-Low Risk every year	Every year

Source: Table elaborated by the authors.

5.5.6.2. Implementation of the framework

In the **Netherlands**, in order to implement horizontal monitoring the taxpayer and tax administration will need to sign an agreement (*covenant*). The covenant contains agreements which go beyond actual statutory rights and obligations. These additional covenant obligations have no basis in public law. The covenant therefore has a somewhat “hybrid character, merging public and private law obligations” (Huiskers-Stoop & Gribnau: 2019, pp.79). This hybrid character makes private law on top of public law applicable.

By classifying the *covenant* as a private agreement, the additional obligations not only bind the Dutch tax administration but also the taxpayers (Huiskers-Stoop & Gribnau: 2019, pp.86). By signing a covenant both parties agree to cooperate based on mutual trust, understanding and transparency in order to pursue correct tax assessments (Gribnau & Huiskers-Stoop: 2019)³⁸. Past tax problems must be resolved before the covenant is signed. In addition, the internal control system of the participating companies has to meet the requirements of the Tax Control Framework. The Dutch tax administration subsequently ‘trusts’ the information that emerges from this system.

In addition, horizontal monitoring “deals with the way in which parties cooperate in the taxation process - the process from the completion of possible tax-relevant transactions up to the filing of the tax return and issuing of the tax assessment - and not with the amount of the tax liability” (Huiskers-Stoop & Gribnau: 2019, pp.69). Horizontal monitoring should therefore not be confused with for instance the Dutch ruling practice, under which “advance agreements can be made about the position of the Dutch tax administration on international tax structures (e.g. international holding and financing activities)”.

In **the United Kingdom**, the Tax Compliance Risk Management Process allows the taxpayer (large business) to work together with the tax administration to identify and mitigate their compliance tax risk. This process also includes a Business Risk Review that will result in the identification of the taxpayer as low risk (first category) or moderate risk, moderate-high risk or high risk (second category). According to the outcome of the risk, there will be a specific tax compliance risk management process for each taxpayer (Risk working). Thus, whereas low risk taxpayers will see contact maintained to update information, it would be expected that HMRC would not normally initiate targeted interventions and challenges, whereas risky taxpayers will be subject to intense risk interventions with specialist teams and HMRC-taxpayer Board interactions designed to alter the taxpayer’s behaviour and steer it towards lower levels of risk (HMRC: 2019).

In **Russia**, the focus of tax monitoring is on information being requested by tax administration, and the requirement for the taxpayer to provide such information. In this process, “if inconsistencies are found in the details contained in documents (information) submitted or inconsistencies are found between information submitted by the organization and information contained in documents in the possession of the tax authorities, the tax authority shall notify the organization of this with a request to present necessary explanations within five days or to make appropriate adjustments within ten days. In the event that, after examining explanations presented by an organization or where none are presented, a tax authority finds evidence that taxes, levies, and insurance contributions have been incorrectly calculated (withheld) or have not been paid (remitted) in full or on time, the tax authority shall be obliged to prepare a reasoned opinion in accordance with the procedure laid down in Article 105.30 of this Code” (art. 105.29) (EY).

Unlike the Netherlands and the United Kingdom, there is not a differentiated type of tax treatment (large vs small taxpayer, low risk vs. non-low-risk taxpayer). Some of the reasons behind this could be that, as mentioned in section 5.5.6.1 above, in Russia, cooperative compliance is applicable only to large taxpayers, and the element of risk is not included as one of the factors that determines participation in a cooperative compliance programme.

5.5.6.3. Organizational changes

As was explained in the previous section, public perceptions of compliance strategies of tax administrations should not be underestimated (Huiskers-Stoop & Gribnau: 2019, pp.101). The cooperative compliance model and its goals should therefore be “properly explained and understood by citizens”. The focus on “reciprocal cooperation and mutual trust, understanding and transparency could otherwise be misperceived”. Misinformed citizens might associate cooperative compliance with “corruption and sweetheart deals” between taxpayers and the tax authorities. This would eventually erode trust in the tax authorities and also increase the likelihood that the programme and its participants (both taxpayers and the tax administration) would be attacked by various stakeholders, something which could stall the programme or lead participants to withdraw (Quiñones: 2020, Section 4.4.5).

Therefore, when setting up the cooperative framework, it is important both to carry out wide programmes designed to communicate to different stakeholders how the programme operates (its conditions for participations, objectives, dynamics, boundaries, etc.), and undertake organizational changes within the tax administration in order to increase transparency, communication and trust between the tax administration and the taxpayer. Some of these changes have been already addressed in Section 5.6.3. above (e.g. increasing training of tax officials, increasing personnel and technological resources for communication, and risk assessment, and improving the quality of the risk assessment process in terms of transparency, and accountability).

In all 3 countries of study, there is a large taxpayer unit of the tax administration. In the United Kingdom, participation in the programme is automatic, but will differ depending on the risk assessment and the opinions of the Customer Compliance Manager (CCM) and the countersigning officer. In Russia, the taxpayer needs to apply to the unit where the taxpayer is registered. In the Netherlands, however, since the cooperative compliance can also be applicable to small and medium enterprises), the application should be made to the Netherlands Tax and Customs Administration (NTCA).

In addition, in the Netherlands in the 2012 Report by the Committee Horizontal Monitoring Tax and Customs Administration stated the need for NTCA to introduce measures to prevent the “risk of attachment” i.e. tax administration staff risk of losing their ability to form objective opinions.

At that time, the Committee reported that a policy of that nature was not currently visible or explicit. Therefore, the Committee stated that “the Tax and Customs Administration needs to remain continually alert to the risk of attachment. Non-professional relationships increase the risk of corruption. The Committee advocates an adequate accommodating policy, for example the rotation of staff, reviews of the quality of dossiers, or the separation of duties” (Stevens et al.: 2012, pp.51).

To the authors’ knowledge no specific measures have been taken by the NTCA to prevent this “risk of attachment”. In a recent article, by one of the members of the Committee (van der Hel.: 2019)³⁹ reference was made to the need for more transparency in order to explain what entails horizontal monitoring, what are the agreements made, and how the objective of the monitoring is safeguarded (van der Hel.: 2019).

In Russia, as addressed by Martini et al, in addition to the internal Code of Conduct for tax inspectors, there is a rotation of tax inspectors to prevent the risk of corruption and non-objective tax evaluation. However, the practical application of this rotation faces some challenges since “in

order to ensure rotation in respect of files on a regular basis, the tax office has to be well-equipped in terms of human resources. Not all tax offices are in a position to do so, especially smaller tax departments, i.e. those within small cities where the tax inspectors are overloaded and such rotation is not possible. In big cities, however, such as Moscow, St Petersburg, Novosibirsk, Ekaterinburg, Kazan, etc., rotation is feasible. There is no official data as to whether or not there is a regular rotation of tax inspectors on files subject to tax monitoring” (Martini et al.: 2021, pp.38).

In the United Kingdom, this risk of attachment has been addressed by the introduction of countersigning officers (be it a CCM Tax Professional Manager or another CCM) as part of the Business Risk Review (BRR)+ reforms (HMRC: 2019). Additionally, there is a Compliance Operational Guidance that provides the fundamental principles, framework, and values within which all civil servants must work including the principles of integrity honesty, impartiality and objectivity (HMRC:2021)⁴⁰.

Unlike Russia and the United Kingdom, this Code of Conduct has not yet been introduced in the Netherlands, however, there are specific provisions in the General Civil Servant Regulations (ARAR *Algemeen Rijksambtenarenreglement*) in force until 31 December 2019. One relevant provision in the ARAR was art. 50 addressing the behaviour of the “good” civil servant. This reference to good civil servant has been included in article 6 of the Law for Civil Servants (Ambtenarenwet) that replaced the ARAR⁴¹.

In 2009, the Ministry of Finance and the Dutch tax administration published a leaflet addressing the integrity of the Dutch tax administration including the references to the ARAR. Recently in 2020, an appeal has been made by taxpayers and tax scholars in the Netherlands to have a Code of Conduct for the tax administration⁴², as well as a Code of Conduct (Tax Governance) for taxpayers (Gribnau et al.: 2020)⁴³.

Therefore, we can conclude that in order to prevent the “risk of attachment”, corruption and lack of objectivity, countries will need to include organizational changes to their tax administrations. These changes can be introduced in a General Code of Conduct for all civil servants, but there should be also a specific section addressing Tax Officials, or alternatively as in Russia, there could be an Internal Code of Conduct for Tax Inspectors. In all cases the rotation of tax officials dealing with cooperative compliance could be a good measure for countries when introducing a cooperative compliance framework. However, as explained in section 5.5.5, there is a need to balance protections against corruptions like the rotations of taxpayer-dedicated tax administration officials with the need to allow sufficient time for the investment made in having that official acquire greater business knowledge and for the taxpayers to fully communicate their challenges and tax practices to that official. The need to take into account economic and business cycles and to perform appropriate longitudinal studies (for example, in transfer pricing matters), suggests that dedicated tax officials should not be rotated before they’ve been with the same taxpayer for three to five years. Furthermore, in order for the administration not to lose the specialised knowledge acquired by these officers, it is a good idea to rotate them between different taxpayers but within the same sector that they have already become specialised in.

5.5.7. Pathways to cooperative compliance (18 building blocks)

Cooperative compliance is a regulatory approach that is premised on the idea that taxpayers and the tax administration can trust each other to collaborate (voluntarily), seeking to achieve a shared compliance goal.

Tax administrations considering implementing a cooperative compliance programme, will need to evaluate the changes that will need to take place: i. before, ii. during the design and iii. after the introduction of the cooperative compliance programme. These changes may be different among CIAT countries, and therefore, a self-evaluation by each tax administration will need to take place before introducing a cooperative compliance programme.

Based on the above, we distinguish 18 building blocks to pave the way to a cooperative compliance approach:

5.5.7.1. Before introducing cooperative compliance

Changes in the tax administration and its relationship with taxpayers

1. **Improve communication between tax administration and taxpayer** and obtain a mutual level of understanding and trust. In most developing countries the relationship is marked by a more adversarial and hierarchical relationship. This change in communication and dealing with each other should be done before introducing a cooperative compliance programme. It is important for the tax administrations to assess critically their relationship with the taxpayer, and to introduce measures to promote transparency and trust by the taxpayer and the administration. Examples of these measures are, for instance i. increasing training of the tax administration (including skills other than technical understanding of tax such as behavioral analysis and negotiation), ii. increasing personnel and technological resources for communication, and risk assessment, and iii. improving the quality of the risk assessment process in terms of proper weighing of behavioral and structural risk factors with measures taken to mitigate risk, transparency, and accountability.
2. Cooperative compliance requires that tax administrations will have to **improve their ability**, both in terms of human and machine resources, **to interpret and make use of the troves of information provided by taxpayers**. In the case of AI and “machine learning”, while technology can be highly useful in detecting behavioral patterns and risks, and these insights can be very important for producing more responsive regulation, both in a coercive/vertical and in a cooperative/horizontal setting, human processing is required in order to understand why these behaviors are taking place and how to intervene in order to change them. In this regard, since cooperative compliance requires a deep understanding of the administration about the characteristics of regulatees, it is suggested that behavioral analysis units are established prior to initiating cooperative compliance exchanges, so that the tax administration has a better comprehension ab initio about the determinants that drive taxpayer conduct in their jurisdictions and about

the best ways to address regulatees. Tax administrations need to be ready to engage in investments that have a mid-long term return panorama but an immediate or short-term need for resources.

3. Cooperative compliance requires **commercial awareness, to enhance interparty trust and voluntary compliance**. Additionally, high levels of commercial awareness are necessary in order for the administration to be able to detect tax risks proactively, provide timely legal certainty about complex matters, and prevent taxpayer selective disclosure or regulatory capture. As such, it is necessary to tax administrations to invest in training existing personnel or hiring industry specialists in order to have a base of inspectors that can later (once the program is operational) act as dedicated taxpayer or taxpayer sector officers. This can be a significant challenge in developing countries, where scarce resources often lead to generalist profiles, so it is advisable that countries interested in moving towards cooperative compliance make sure that they have sufficient specialized personnel to make cooperative compliance truly responsive and fluid.
4. Before cooperative compliance can initiate, it is important for the administration to **redefine its organizational framework and prepare all the internal guidelines** necessary for the program to operate efficiently and without interruptions once it is in place. This involves aspects such as establishing how taxpayer specific or sector specific officers will operate (how they will rotate, their powers, who they answer to, how they coordinate with other teams), to establishing the parameters for risk weighing and behavioral analysis that will be used later to determine who will participate in the program and how the administration will respond to different types of participants or even recalcitrant taxpayers. Moreover, to prevent the 'risk of attachment', corruption and a lack of objectivity, cooperative compliance requires that countries introduce preventative mechanisms and model conduct standards for their tax administrations. For example, these can be introduced in a General Code of Conduct for all civil servants, where there should be also a specific section addressing Tax Officials, or, alternatively, in an Internal Code of Conduct for Tax Inspectors.
5. In line with establishing a new organizational framework and administrative guidelines, a key step for cooperative compliance in developing nations that needs to take place prior to implementation is **setting up the legal framework** that will be necessary for the program to operate in the future. Based on the strong tradition of legalism that is present in many CIAT jurisdictions, this is a step that is of the utmost importance, since it can be expected that any ambiguities or lacunae in the legal framework will lead to litigation once the program is operational, and it is also to be expected that taxpayers who are accustomed to working in jurisdictions where administrative discretion is highly regulated but where there are high levels of legal uncertainty, will only accede to participating in the programme if the regulatory exchanges, the procedural aspects of the admission and participation in the program, and the binding nature of the agreements reached after the exchanges are all clearly defined in the law and are understood to be safe from unilateral modifications or overrides. Naturally, the legal framework will change depending on each jurisdiction's specific legal traditions, but the two aspects which are more likely to cause disputes and/or jeopardize the program are i. the administration's faculties as part of the exchanges (and in terms of admitting or expelling from the program), and ii. The binding nature of the outcomes of exchanges under the light of legal certainty and

legitimate expectations, but also taking into account the need to create a framework to deal with cases of corruption or egregious deviation from applicable tax laws.

Improving understanding of cooperative compliance

6. In addition to the steps described above, and which are focused on preparing the tax administration for successfully implementing cooperative compliance, it is also advised that jurisdictions interested in applying this type of regulation also dedicate themselves to **communicating to the various stakeholders prior to the start** of the programme what cooperative compliance actually involves, so that views that would eventually create challenges to the programme's legitimacy are addressed preemptively and that the resistance of different stakeholders is diminished or eliminated before it can erode the program's functioning. Among others, key messages that need to be transmitted to the public, the administration, politicians, potential participants, the academia, and other stakeholders include.
7. That cooperative compliance does not allow for the parties to alter the content of the law in relation to **tax liability**. Cooperative compliance is about how parties deal with each other in the context of taxation that has been stipulated in the law. It provides a scenario for the parties to discuss their interpretation of the law, agree/disagree on facts, and then commit to a specific treatment for a tax position, always within the letter of the law. Understanding this point will prevent future scenarios where cooperative compliance is confused with "sweetheart deals" or regulatory capture and where non-participating taxpayers feel like there is a different legal system for participants, thus becoming less compliant.
8. That offering cooperative compliance should **not be confused with lacking enforcement or deterrence**. These will still be present, as they are necessary to deal with those taxpayers that are not compliance-minded or who engage in a resistant or uncooperative posture towards the tax administration. However, most taxpayers are compliance minded. This message is essential both to preserve voluntary compliance among all taxpayers (who must not feel that non-compliance is lightly treated), and to signal that cooperative compliance, as a part of a responsive regulatory strategy, frees resources for coercive interventions, which will be applied in a more targeted fashion, rather than indiscriminately. Because it is possible that a portion of the tax administration's personnel (particularly those who belong to divisions most accustomed to investigating and prosecuting criminally or administratively or where there are high levels of non-compliance) are reluctant to embrace cooperative compliance, it is essential to dispel the idea that cooperative compliance prevents the administration from penalizing non-compliance.
9. That cooperative compliance is about **changing the parties' attitude towards discussing their tax positions and compliance strategies**. This should no longer be confrontational, meaning that differences are to be discussed technically, efficiently, with commercial understanding, civility, and fairness, and this should lead to more agreements, narrowed-down disputes, and, occasionally, to an agreement to disagree and let a third party adjudicate conflict without the relationship breaking down. It is important that taxpayers and tax officials understand that implementing cooperative

compliance will require profound relational changes and that this also involves greater transparency (even when not required by law) to prevent selective disclosure.

10. Cooperative compliance requires that tax administrations communicate (also to wider society) that **benefits attached to cooperative compliance are not granted arbitrarily**, but rather as a result of tangible actions by participating taxpayers that are different to those expected of non-participating taxpayers. This means that, while participating can lead to benefits, it also subjects participants to heightened, preemptive scrutiny, and requires participants to undertake considerable investments.
11. Cooperative compliance requires a complete **change to a regulatory approach based on horizontality and collaboration (partnership)**. This requires a complete change in the way in which the regulator sees its role in the compliance equation; from a coercive enforcer and inquisitor (through audit) to a compliance facilitator and prudential regulator. Because many tax administrations have traditionally operated under a vertical enforcement model, there is a need for extensive retraining and internal consultations so that everyone in the administration has a unified position in relation to cooperative compliance and the implementation is not jeopardized by internal divisions. Taxpayers and other stakeholders need to see that the administration is fully on board so that they can participate in cooperative compliance willingly and committedly. Naturally, the change to the regulatory approach also takes place at the taxpayer level, since taxpayers have to leave behind a contentious model based on strategic calculation and selective disclosure and shift towards openness and collaboration.
12. The experience of many jurisdictions that have implemented cooperative compliance tells us that this approach works best when, prior to its implementation, the administration, interested stakeholders and potential participants (taxpayers) **undergo extensive consultations** that allow all parties to reach understand each other's expectations in relation to the model, hear their objections and suggestions, and, where possible, align the regulatory design to each jurisdiction's specific factors (for example, cultural practices, resource availability, legal frameworks, economic make-up, etc.). Indeed, pre-launch consultations are a useful tool in preventing that regulatory policies are transplanted to specific jurisdictions without having regard to the differences existing in the adopting jurisdiction and the jurisdiction/s where the model was devised. This is a fundamental point to bear in mind in the CIAT context.
13. A final aspect that is very important before introducing cooperative compliance is to perform a **real-life** test using a limited number of participants. These pilots provide an ideal mechanism to assess the parties' readiness to engage in cooperative compliance, detect any obstacles and unforeseen factors, and calibrate the legal and administrative framework accordingly. Similarly, the results of the pilot phase can be used to devise evaluation indicators, as evidence for policy makers and funders, and as a hands-on training exercise for both parties. Moreover, in the context of countries like many of those under CIAT's sphere, where cooperative compliance would be a pioneering experience, pilots offer the possibility for the tax administration and for participating taxpayers to be assisted by "mentors", tax administrations and corporate tax departments from other jurisdictions (in the case of multinational enterprises [MNEs], usually other corporate tax departments within the same corporate group) who have experienced cooperative compliance in the past. At the conclusion of the pilot, it is expected that all stakeholders

will have sufficient empirical data to assess whether proceeding with cooperative compliance is advisable in that specific jurisdiction, and, if so, what changes should be undertaken.

5.5.7.2. When introducing cooperative compliance

14. Cooperative compliance requires tax administrations to **think about** what is needed to **increase transparency** by the taxpayer and how to **improve transparency** of the tax administration and of the tax system as a whole. Greater transparency of the tax relationship has a positive impact in terms of societal perceptions of the legitimacy and fairness of the tax system. For tax administrations, this involves understanding that releasing information about risk weighing and legal interpretation is not waiving administrative power, and for taxpayers this involves understanding that acknowledging uncertainty about the interpretation of the law or about its application to specific contexts should not translate into tax controversies and/or penalties, provided that risks are identified proactively and all material information is disclosed as part of the cooperative exchange.
15. Cooperative compliance should, in principle, be based on a **neutral approach towards all taxpayers**. It should not be an instrument only for large taxpayers. Of course, in the context of jurisdictions that might have scarce resources available, this means that cooperative compliance should be seen as an incremental program, with smaller groups of participants in the beginning, and gradual expansions as the exchanges become more institutionalized, more results are obtained, positive evaluations start to come in, and greater experience with the model leads to efficiency gains. The idea here is that, while it is easier and advisable to begin with the largest taxpayers that have more complex tax needs, have more resources to operationalize cooperative exchanges, and who represent a greater revenue potential, cooperative compliance can work with any type of taxpayer once the model is more mature.

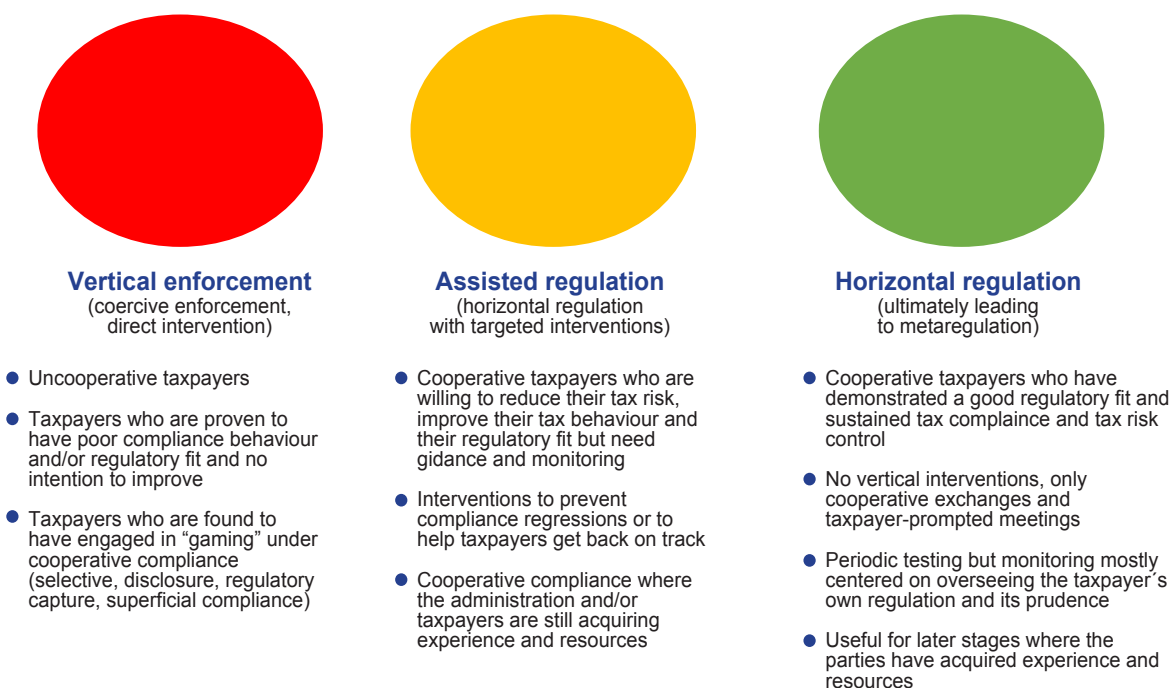
5.5.7.3. After introducing cooperative compliance

16. Once cooperative compliance is operational, the administration needs to assess the tax risk of potential participants and current participants as well as their “fit” to this type of regulation⁴⁴ and their actual tax behaviour. Based on taxpayer assessments on these dimensions, the administration can apply targeted regulation that is aimed to be responsive, both in relation to participation and non-participation in cooperative compliance, and to the shape of participation within cooperative compliance. This can be synthesized into a “traffic light” model, that sees cooperative compliance as incrementally horizontal as risk diminishes and regulatory fit increases. For example, within cooperative compliance, those taxpayers that are assessed as most risky and/or less amenable to the model can require assisted regulation with more vertical supervision until they are able to proceed a more horizontal tier. In later tiers, cooperative compliance may lead to **metaregulation and ultimately the tax administration operating as a prudent regulator**. Using cooperative compliance as a risk regulation tool entails that taxpayers have to upgrade their tax function to be able to detect possible non-compliance well before it happens and have to build a risk management system that allows them to

provide assurance to the administration. In a situation of proven capability of self-regulation, the administration may focus on detecting risks rather than on detecting tax deficiencies. Because cooperative compliance should be properly responsive, it is important to understand that it is not a unidirectional process, so it is possible that taxpayers who were progressing devolve or fully disengage. In these cases, the taxpayer should be brought down to a lower tier, but the administration should try to understand the reasons behind this lack of progress and assist the taxpayer to go back on track. In the case of recalcitrant or uncooperative taxpayers, targeted vertical enforcement should remain the approach. In low income and mid income countries, the advantage of a tiered system is that it allows for the program to advance to higher stages (towards metaregulation) not only as a function of taxpayer behaviour, but also as a function of the accumulated experience and the resources made available to both parties.

Figure 7

Cooperative compliance under a traffic light tiered system



Source: Elaborated by the authors, 2021.

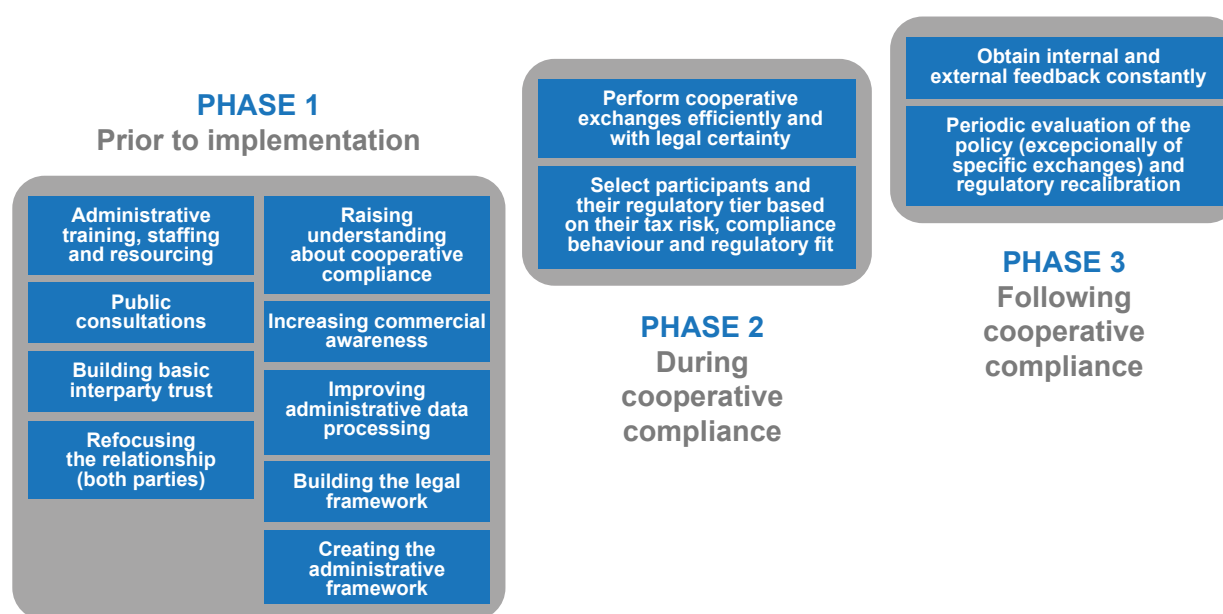
17. Cooperative compliance **should be supplemented with adequate safeguards** designed to prevent the greater administrative discretion and interparty proximity from giving rise to selective disclosure or administrative impropriety. In countries where litigation is customary, cooperative compliance must be protected from excessive unnecessary judicial review and from political manipulation. While it is possible that

providing for an exceptional instance to review cooperative compliance agreements may be necessary to maintain accountability, this instance should be purely technical, not political and, in order to protect legal certainty (which is at the core of this model) it should only allow for reversals or modifications of agreements if a legal process carried out by tax experts finds that there was a breach of applicable laws by either party (e.g. by not revealing material information or if the administration went ultra vires against the public interest).

18. As with any other public policy, and particularly with a responsive regulation, cooperative compliance should be subject to periodic evaluation to prevent it from becoming a static model. This means that is essential for all the parties participating in cooperative compliance to provide feedback constantly, so that policymakers have the appropriate information to evaluate how the program is working and calibrate the policy accordingly. The result of these evaluations is necessary not only to keep the policy updated, but also to make the policy accountable, show the program's societal benefits, and to justify funding decisions.

Figure 8

Steps towards cooperative compliance



Source: Elaborated by the authors, 2021.

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End notes

- 1 Cooperative Compliance and the Dutch Horizontal Monitoring Model.” (Available at: <https://ssrn.com/abstract=3333347>).
- 2 Study into the Role of Tax Intermediaries.” (Available at: <http://www.oecd.org/tax/administration/39882938.pdf>)
- 3 “Risk management relies on information, which makes it important to encourage disclosure from taxpayers. This means revenue bodies need to operate using the following five attributes when dealing with all taxpayers: understanding based on commercial awareness; impartiality; proportionality; openness (disclosure and transparency); and responsiveness”.
- 4 “Co-operative Compliance: A Framework: From Enhanced Relationship to Co-operative Compliance.” (Available at: <https://www.oecd.org/tax/co-operative-compliance-a-framework-9789264200852-en.htm>).
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- 7 The Authors refer too Enachescu & Kirchler, 2018: “The Slippery Slope Framework of Tax Behaviour: Reviewed and Revised”.
- 8 The expansion of cooperative compliance will inevitably be gradual, and it will require administrative investment of (limited) resources, so the use of pilots and phased roll outs is recommended.
- 9 And indeed, this administrative awareness regarding the taxpayers’ commercial operation is also a key aspect to ensure that cooperative compliance is truly a responsive regulation (Quiñones: 2020).
- 10 Essentially, Feld and Frey’s notion of the tax psychological contract (Feld & Frey: 2007, pp. 102).
- 11 For a case where the adequacy of disclosure in the context of a cooperative compliance setting was brought into question, see the UK’s GE case. (GE v HMRC, 2020).
- 12 OECD, 2014: “Measure for Tax compliance Outcomes a Practical Guide.” (Available at: <http://www.oecd.org/tax/administration/measures-of-tax-compliance-outcomes-9789264223233-en.htm>).
- 13 Refers to “Co-operative compliance a Framework from enhanced relationship to cooperative compliance” (OECD 2013) & “Right from the Start: Influencing the Compliance environment for SMEs” (OECD, 2012).
- 14 Schoueri & Barbosa have stated that the notion of transparency ‘should be extended to the state itself and to covering the tax system as a whole’. For Schoueri and Barbosa transparency ‘should be used as mechanism for the creation of a mature relationship between state and citizen, and the result is that taxpayers feel part of the community and therefore involved in the process of granting states the means for their activities’. (Schoueri & Barbosa: 2013, pp. 677–678).

- 15 Naturally, there is apprehension about revealing the specificities of audit rules. However, what is necessary is disclosure about the variables involved in those rules (so that taxpayers can use them as benchmarks or risk management guides), but not necessarily each variable's specific weight in an audit equation. In any case, while the administration could be said to be "taking a gamble" by disclosing information to taxpayers, the same can be said for taxpayers, since they are disclosing voluntary more than what they would be legally required to do.
- 16 Taking into account the differences in the way that each jurisdiction has implemented this Action (e.g. the information available to the administration is different in a jurisdiction subject to ATAD and the DAC than in a jurisdiction where there is no mandatory disclosure).
- 17 "Responsive Regulation is an approach designed in developed economies. (...) Responsive Regulation does require a big stick at the peak of an enforcement pyramid and big sticks are expensive, as well as demanding upon state capacities in other ways".
- 18 Available at: <https://www.transparency.org/en/cpi/2019/index/nzl>
- 19 While dissatisfaction perceptions vary across countries and in relation to specific public goods and services, sources like the Latin American Public Opinion Poll (LAPOP, data repository available via in <https://www.vanderbilt.edu/lapop/request-datasets.php>) and the Latinobarómetro (data repository available via <https://www.latinobarometro.org/latContents.jsp>) do evidence region-wide trends of general dissatisfaction or low relative satisfaction and trust. Other itemized studies like the IDB's quality and satisfaction in public services also reveal low levels of satisfaction. For example, Lupu et. al. (2020) revealed levels of satisfaction with public health services which were often in the 30 and 40 per cent in various countries of Latin America (See: Lupu et. al.: "Are We Achieving the Sustainable Development Goals?: Using Americas Barometer Data to Measure Progress in the Americas." (Lupu et. al., 2020)).
- 20 "The answer proffered is to network. It is that weaker actors can become stronger by networking with other weaker actors".
- 21 "Because states are at great risk of capture and corruption by businesses, even greater risk where regulatory bureaucrats are poor, Ayres and Braithwaite argue for the central importance of third parties, particularly NGOs, to be directly involved in regulatory enforcement oversight (Ayres & Braithwaite, 1992, chap. 3)".
- 22 See for instance Eberhartinger & Zieser (2020). The effects of Co-operative Compliance on Firms' Tax Risk, Tax Risk Management and Compliance Costs: "Results show that firms in horizontal monitoring perceive a significantly higher increase in tax certainty, which is associated with significant relative decreases in tax risk and compliance costs"; Siglé (2019). The effects of Co-operative Compliance programs.: "A modern tax administration must include a trust-based regulatory approach in its compliance risk management strategy for large businesses. A so-called Co-operative Compliance program (CCP) – such as horizontal monitoring in the Netherlands – increases tax certainty and reduces aggressive tax practices"; Huiskers-Stoop (2015). De effectiviteit van horizontaal belastingtoezicht. Een fiscaal-juridische en empirische analyse (The effectiveness of Horizontal Tax Monitoring. Tax Law and Empirical Analysis): "It is likely that horizontal monitoring, compared to traditional monitoring, leads to better tax compliance, greater fiscal certainty, reduction of tax compliance costs and a better relationship with the tax authorities."

- 23 See Russo: 2020: “Co-operative Compliance and the OECD’s International Compliance Assurance Programme”; Pemberton & Majdanksa: 2016: “Can cooperative compliance help developing countries address the challenges of the OECD G20 Base Erosion and Profit Shifting Initiative”.
- 24 See Section 5.5.1. above.
- 25 Martini et. al.: 2021: “Russia - An Analysis of the Russian Tax Monitoring Programme in Light of the OECD Concept of Cooperative Tax Compliance and the Experience of Other Countries”.
- 26 See Netherlands Tax and Custom Administration (NTCA), 2013: “Supervision Large Business in the Netherlands.” & NTCA, 2016: “Guide Horizontal Monitoring Tax service providers.” In 2018 the Dutch Tax Administration started a further development of the Horizontal Monitoring model, which was introduced in 2005, in order to come up with concrete improvement proposals in the light of the overall strategy toolkit of the Dutch tax administration. In this modernization, the initial principles remain - like interactive and responsive dealing with taxpayers on the basis of mutual trust, understanding and transparency - but the national guidance will be aligned with the international developments on cooperative compliance. Renewed guidance is expected in mid-2021.
- 27 HMRC, 2019: “HMRC internal manual - Tax Compliance Risk Management”.
- 28 “These changes are intended to improve tax monitoring by promoting a higher degree of interactions between taxpayers and tax administrations, further digitalization, real-time access to information and broader access to tax monitoring”.
- 29 See the translation of the Russian tax code: https://assets.ey.com/content/dam/ey-sites/ey-com/en_ru/topics/tax/tax-code/ey-tax-code-part-one-section-v-2.pdf (EY)
- 30 In Dutch Kwaliteitscentrum Accountancy Nederland (KAN); Nederlandse Orde van Administratie- en Belastingdeskundigen (NOAB); Nederlandse organisatie van accountantskantoren (Novak); Nexia Register Belastingadviseurs (RB); Samenwerkende Registeraccountants en Accountants-administratieconsulenten (SRA) See https://www.belastingdienst.nl/wps/wcm/connect/bldcontentnl/belastingdienst/intermediairs/toezicht/convenanten/convenanten_horizontaal_toezicht/koepelorganisaties/koepelorganisaties & https://www.belastingdienst.nl/wps/wcm/connect/bldcontentnl/belastingdienst/intermediairs/toezicht/horizontaal_toezicht/mkb/koepelorganisaties/koepelorganisaties
- 31 For an overview of some of the issues that led HMRC to review its original BRR program and introduce the BRR+, see Quiñones et al., 2020, pp. 153.
- 32 According to Martini et al. Risk profile is not listed, as a reason to deny an application. Therefore, although unlikely, it should be possible for a high-risk large company to apply for, and be accepted into, the tax monitoring programme”. (Martini et. al.: 2021, pp. 35).
- 33 Russia: Tax monitoring becomes popular in Russia. (Available at: <https://www.internationaltaxreview.com/article/b1f7n2f16c3gkm/russia-tax-monitoring-becomes-popular-in-russia>).
- 34 See information in English on horizontal monitoring and agreement at. https://www.belastingdienst.nl/wps/wcm/connect/bldcontenten/themaoverstijgend/brochures_and_publications/supervision_large_business_in_the_netherlands.

- 35 Available at: https://download.belastingdienst.nl/belastingdienst/docs/stand_fiscaaldienstverlenersconv_al8231z3ed.pdf (NTCA: 2021).
- 36 The Dutch tax authorities will publish new policy on Horizontal Monitoring in mid-2021, in which the duration of the covenants will be limited in time.
- 37 “Tax Supervision Made to Measure: Flexible when possible, strict where necessary.” Available at: https://download.belastingdienst.nl/belastingdienst/docs/tax_supervision_made_to_measure_tz0151z1fdeng.pdf
- 38 “Promotion of Tax Compliance: Cooperative Compliance and the Dutch Horizontal Monitoring Model.” Available at: <https://leidenlawblog.nl/articles/promotion-of-tax-compliance-cooperative-compliance-and-the-dutch-horizontal>.
- 39 Horizontaal toezicht: evalueren is noodzaak..” (Available at: <https://www.toezine.nl/artikel/309/horizontaal-toezicht-evalueren-is-noodzaak/>)
- 40 “HMRC internal manual - Compliance Operational Guidance.” (Available at: <https://www.gov.uk/hmrc-internal-manuals/compliance-operational-guidance/cog11210>).
- 41 As of 1 January 2020, this Regulations have been replaced by a Law for civil servants (Ambtenarenwet 2017) See: <https://wetten.overheid.nl/BWBR0001947/2020-01-01> (Overheid, 2020).
- 42 Available at: <https://fd.nl/economie-politiek/1368844/fiscale-experts-pleiten-voor-gedragscode-belastingdienst>. (fd, 2021).
- 43 Essaybundel ‘Tax Governance, maatschappelijke verantwoordelijkheid en ethiek. Tijd voor een code?’ (Available at: <https://www.rijksoverheid.nl/actueel/nieuws/2020/12/18/essaybundel-tax-governance-code-gepubliceerd>)
- 44 This is what Quiñones calls “amenability”. (Quiñones: 2020)

Manual for the Control of International Tax Planning

General Structure

1. Introduction, Scope, and Objective

2. International Tax Planning

3. Harmful International Tax Planning: Common Behaviours and Mechanisms to Identify Them

- 3.1. Thin-capitalization and other international financing operations
- 3.2. Transfer pricing manipulation
- 3.3. Tax treaty abuse
- 3.4. Abuse of domestic rules
- 3.5. Hybrids
- 3.6. Business restructuring
- 3.7. Tax residency
- 3.8. Permanent establishments and commissionaire arrangements
- 3.9. Use of legal structures for concealment purposes, tax havens, and harmful tax regimes
- 3.10. Triangulation
- 3.11. Transfer of intangibles
- 3.12. Payments for technical assistance, royalties, interests, dividends, and service fees
- 3.13. Leasing operations
- 3.14. Improper contractual allocation of risk
- 3.15. Artificial fragmentation of contracts
- 3.16. Artificial generation of losses and artificial allocation of costs
- 3.17. Misuse of special purpose entities (also known as financial vehicle corporations)
- 3.18. Profit shifting
- 3.19. Tax compliance risks by companies operating in the digital economy

4. Containment Measures for International Tax Planning

- 4.1. General anti avoidance rules: domestic and international

- 4.2. Specific anti avoidance rules: domestic and international
- 4.3. Anti hybrid regimes
- 4.4. Ability to disregard or recharacterize transactions
- 4.5. Rules relating to international tax transparency
- 4.6. Rules limiting tax base erosion through financial instruments
- 4.7. Transfer pricing regulations
- 4.8. Anti tax haven rules
- 4.9. Measures to contain misconduct by promoters of tax planning schemes
- 4.10. Mechanisms to prevent abuse involving transactions of commodities and raw materials
- 4.11. Measures to contain avoidance or evasion by companies operating in the digital economy
- 4.12. Measures to contain the abuse of permanent establishments and commission agents

5. Tools for Combating International Tax Planning

- 5.1. Special information regimes, development and maintenance of databases: information obligations for taxpayers carrying out international operations
- 5.2. Mechanisms to identify risks
- 5.3. International cooperation
- 5.4. Initiatives regarding corporate responsibility and fiscal governance
- 5.5. Cooperative compliance initiatives as a preventative mechanism
- 5.6. Procedures to prevent abuse by companies operating in the digital economy
- 5.7. Taxation of Cryptocurrencies
- 5.8. Advanced Pricing Agreements (APA)

6. Other administrative issues

- 6.1. Audit of multinational enterprises and entities with international operations

