

## INTERNATIONAL TAX COMPLIANCE RISKS<sup>1</sup>

*Understanding and addressing international tax risks requires a comprehensive, end-to-end administrative approach.*

### Why is managing international tax compliance risks important?

Revenue mobilization is at the forefront of priorities for many countries. Understanding the potential risks to a country's tax base due to international tax issues is increasingly important in a globalized economy, despite the complexity that international tax continues to pose, now and with the emerging new rules on digital economy taxation. These risks can include arrangements such as those noted in Box 1 to minimize an entity's overall tax burden by shifting profits and exploiting jurisdictional differences in tax laws. Digitalization of the economy poses an additional risk that electronic sales of goods and services are not taxed in the country where the profits are generated.

### What is the impact of inadequately addressing international tax issues?

Significant negative consequences can occur as voluntary compliance can suffer if domestic taxpayers perceive that others are not paying the right amount of tax. This can not only reduce tax revenue but also threaten the community's perception of the fairness and integrity of the tax system. Foreign entities can also benefit from an unfair competitive advantage over domestic entities, which also threatens the level playing field needed for a healthy economic environment.







### How should international tax risks be balanced with other compliance risks?

Both international and domestic compliance risks should be evaluated, and the most severe risks to the tax base should be given priority for treatment. A standardized approach to identifying and quantifying the risks should be adopted using modern compliance risk management (CRM) approaches. Addressing international tax risks can be costly and time consuming but can produce significant revenue results. A quantification of the materiality of various compliance risks should guide decisions on resource allocation.

### What does a tax administration need to do to address international tax risks?

Building capacity to identify and address international tax risks requires a comprehensive approach involving all aspects of tax administration. The IMF has developed a methodology to evaluate a country's capacity in managing international tax risks and to measure progress toward good practice. Figure 1 outlines the six key tax administration areas that work together to effectively manage international tax risks.

**Figure 1. IMF's Framework for International Tax Administrative Strengthening (FITAS)**

	<b>People.</b> Staff with appropriate skills to effectively identify and address compliance risks.
	<b>Systems and Compliance Risk Management (CRM).</b> Systems and processes in place to support data analysis and international tax CRM.
	<b>Tools.</b> Access to analytical tools for risk assessment and audit support mechanisms.
	<b>Data.</b> Sufficient, appropriate data to facilitate international tax risk assessment and ability to protect data confidentiality.
	<b>Legislative Framework.</b> The necessary provisions are in domestic law to protect the domestic tax base.
	<b>Organization Structure and Governance.</b> Sufficient resources are in place, with management oversight of activities, along with efficient organizational arrangements.

For further information, see our [Revenue Portal](#). For capacity development support, contact IMF's Fiscal Affairs Department at [revenueportal@imf.org](mailto:revenueportal@imf.org).

#### Box 1. Examples of International Tax Compliance Risks

Transfer mis-pricing to shift profits
Misclassifying offshore payments to avoid Withholding Tax
Shifting capital gains to low tax jurisdictions
Using tax driven losses to limit source country tax
Creating artificial arrangements to get treaty benefits
Abusive business restructuring to shift profits
Contrived exploitation of jurisdictional differences
Artificial arrangements to inappropriately access tax incentives (e.g., credits, exemptions, holidays)

### Considerations as you start...

Invest in evaluating the existence and potential revenue loss from international tax compliance risks without delay. You may be able to request IMF assistance.

Building international tax capacity is a long-term process; however, not effectively addressing international tax risks poses reputational and revenue loss risks.

Get started with existing resources and capabilities and build as progress is made. Deliberate, incremental improvements over time will have a positive impact.

<sup>1</sup> The views expressed in this note are those of the authors and do not necessarily represent the views of the IMF, its Executive Board, or IMF management. It is intended to be used as a quick reference document to help promote understanding of this topic.