WEST AFRICAN TAX ADMINISTRATION FORUM | FORUM DES ADMINISTRATIONS FISCALES OUEST AFRICAINES

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COMPLIANCE RISK MANAGEMENT FRAMEWORK

FOR TAX ADMINISTRATIONS IN WEST AFRICA

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ACRONYMS	
CCD	Commissioner for Customs Department
CDTD	Commissioner for Domestic Tax Department
CG	Commissioner General
CIT	Corporate Income Tax
CR	Compliance Risk
CRM	Compliance Risk Management
DTD	Domestic Tax Department
ES	Executive Secretary
EU	European Union
GST	Goods and Services Tax
ICT	Information and Communication Technology
IMF	International Monetary Fund
IRS	Internal Revenue Service
MDAs	Ministries, Departments and Agencies
MSME	Micro, Small and Medium Enterprises
MSMTD	Micro, Small and Medium Taxes Division
OECD	Organization for Economic Cooperation and Development
PAYE	Pay As You Earn
PIT	Personal Income Tax
RA	Revenue Authority
RPT	Real Property Tax
SDGs	Sustainable Development Goals
TADAT	Tax Administration Diagnosis Assessment Tool
TPS	Taxpayer Perception Survey
ToR	Terms of Reference
TPAF	Tax Policy Assessment Framework
UNDP	United Nations Development Programme
VAT	Value Added Tax
WATAF	West African Tax Administration Forum

1.0 INTRODUCTION

This Compliance Risk Management (CRM) Frameworkis intended for customization and implementation by West African Tax Administration Forum (WATAF)member revenue authorities (RAs). Its goals are to:

- Delineatea common language, methodology and tool for RAs in West Africa to establish and implement compliance risk management program that increases voluntary compliance and reducethe tax gap;
- Provide a systematic basis to accurately, consistently and timely identify, analyze, prioritize, treat and monitor risks that pose the greatest threats to RAs' objectives;
- Provide consistent and fair treatment of taxpayers in accordance with compliancebehaviour;
- Provide a rational basis for the allocation of limited resources to activities and areas that yield maximum returns; and
- Help achieve key performance measures and milestones.

This CRM framework is generallybased on the Global Institute of Risk Management ISO G31000 concepts, methodologies, principles and standards and the IMF and OECD compliance risk management literature. Compliance risk management is a systematic process of objective identification, analysis, evaluation, prioritization, treatment, monitoring and communication of threats and vulnerabilities that make it uncertain as to whether and when RAs will achieve their objectives[1].

The CRM framework consists of protocols, architecture and tools for establishing and implementing compliance risk management programs that increase voluntary compliance and reduce the tax gaps. The overarching objective of CRMis to achieve the widest possible impact on voluntary compliance across all taxpayer population by minimizing non-compliance and reducing the tax gaps. CRM has become pivotal to long-term strategic and annual operational planning in many RAs. Specifically, CRM has helped RAs achieve equal treatment of taxpayers; focus the burden of audit and enforcement on non-compliant taxpayers; make best use of available human, financial and technical resources; increase voluntary compliance level of taxpayers; allocate available resources to the levels of risks; and weigh the possibilities that a compliant taxpayer could become non-compliant.

Compliance risk refersto 'what could go wrong' in an RA's ability to meet its goals and objectives,particularly, the goal of fairly and transparently administering tax legislations

[1] G31000's definition of CRM

forpurposes of assessing, collecting, auditing, enforcing and accounting for tax revenues. A CRM is a systematic processthat involves seven (7) steps:

- Scanningthe external and internal environments
- Identifying taxpayer compliance risks
- Analyzing taxpayer compliance risks
- Evaluating taxpayer compliance risks
- Prioritizing taxpayer compliance risks
- Treating taxpayer compliance risks
- Monitoring treatment strategies and communicatingresults with relevant stakeholders

CRM consists of:(1) risk management protocols – use to define theobjectives of compliance risk management, the roles and responsibilities of stakeholders; (2) risk management strategy – use to define the philosophy, principles and standards of compliance risk management; (3) risk management architecture – use to design compliance risk management processes and procedures; and (4) risk management tools – use to implement compliance risk management strategies.

This CRM framework is intended for a typical West AfricanRA'slegal context, taxpayergroups, economicand political influences, human resource and technical capacity gaps and resource constraints that affect taxpayer compliance with tax legislations.The legal infrastructure, government revenue policies, public opinion and economic conditions constitute the external context that affects taxpayer compliance risks. Institutional and human resource capacity gaps, administrative issues and the ethical and behavioral dispositions such as corruption, bribery and conflict of interest constitute the internal context that affects taxpayer compliance risks. The internal contextposesserious national priority risk that affects most RAsinWest Africa.Institutional risks may be grouped as follows: policy risks, systems and procedures risks, infrastructure risks, data and recording risks and human resource capacity risks. Much of these risks are low hanging fruits that can be treated in full by RAs. For example, infrastructural inadequacies relating to supply of electricity can be addressed with standby generators. Human resource capacity gaps can be addressed by on-the-jobtraining of relevant personnel.

Taxpayer compliance risks are categorizedby turnover size, tax type, tax domain and taxpayer's location. Risks relating to turnover size are large, medium, small and micro. Risks relating to tax types are personal income tax, corporate income tax, capital gains tax, value added tax (goods and services tax) and real property tax. Risks relating totax domain are registration, filing, reporting and payment. Risk related to taxpayer's location are rural, urban and industrial areas.

Compliance riskmanagement consists of answeringfivefundamental questions: (1) What is happening?(2) How is it happening? (3) Where is it happening? (4) Who is responsible? and(5) Why are they doing it? Most compliance risks relating to the first question have to do with willful attempts by the more initiated taxpayers to engage in exaggerating costs and understating revenues and expanding the space of allowable exemptions under tax legislations. However, the bulk of non-compliant taxpayers in vast informal sector in West Africa fall under the other categories of those who lack knowledge about who, where, how and why to pay and those unwilling to pay.

While the choice of compliancerisk treatment strategies needsto be discerned on a country-by-country basis, general principles, language, standards and practices across countries are just as essential.This is achievable by distilling the tax types that determine maximum revenue collectible, presenting the realities and the sectors and activities that are resulting in leakages across the West African sub-region. This prognostic approach can equally be aggregated with a view to determining tax gap and mitigation efforts across RAs in West Africa.

2.0 THE COMPLIANCE RISK MANAGEMENT PROCESS

Tax administration is arguably one of the most difficult jobs in any society.The truth is, taxpayers cannot match their taxes directly to the benefits they receive. Not because they cannot see! The greatest risk to any RA is public perception about the tax system, its asdministration and the role of government.

For example, enforcing realty taxes on properties where there are no paved roads, schools, hospitals, utilities, security and the crime rates are high is a sort of a moral dilemma. When taxpayers perceived that the taxes they pay are used to fund lavish lifestyles of those in power and that the tax system itself is seen as unfair pose the greatest risk totax administration.

In an ideal law-abiding society, people and businesses would pay the taxes they owe. RAs would only facilitate citizens to carry out their responsibilities. That would be excellent,but no such society exists. Compliance with tax laws must therefore be created, cultivated, enforced and monitored in any society. The objective of compliance risk management is to enable RAs accomplish their mission by helping management make better decisions that achieve the optimal voluntary compliance through use of available resources.

2.1 STANDARD COMPLIANCE RISK MANAGEMENT PROCESS

The term 'compliance risk management' can have many different meanings but all have one thing in common: ‘A process that helps RAs treat compliance risks and provides a level of assurance and justification for management’s actions’ [2].Compliance risk management helps identify the different steps in a decision-making process that allows explicit and more educated decisions.

A standard compliance risk management is a systematic and structured process, consisting of seven well-defined steps:

- Establishing the context

Establishing the context involves scanning and reviewingthe internal and external environments to understand the tax laws and regulations, government policies, economic conditions, taxpayer groups, institutional capacities and ethical culture that influence RAs’ performance.

- Risk identification

Risk identification involves determining what is happening, where and whenfrom a myriad of sources categorized by tax domain (registration, filing, reporting and payment); by tax types (personal income tax, corporate income tax, capital gains tax, value added tax (goods and services tax), real property tax, etc.); by industries (service industry, manufacturing industry, entertainment industry, food and hospitality industry, etc.); by locations (rural area, urban area, industrial area, etc.); by taxpayer types (individuals, businesses, governments, non-governmental organizations, etc.); and by standard industrial classifications(manufacturing, distribution, wholesale and retail). There are generally two major approaches to risk identification: top-down approach and bottom-top approach.

- Risk analysis

Risk analysis involves breaking down each element of compliance risk to understandthe why’s and how’sa particular non-complaince behavior is happ ening. It seeks to determine the underlying motivations and attitudes of non-compliant behaviorscontributing to the greatest tax gap.

- Risk evaluation

Risk evaluation is the determination of possible effect of non-compliance behaviors on RAs’ obejectives. It involves determining the likelihood a nd consequences of non-compliance behaviors.

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[2] OECD (2014 Compliance Risk Management Compendium)

- Risk prioritization

Risk prioritization is the ranking of risks in a matrix based on a linear combination of likelihood and consequences of risks to determine the risks with the greatest impact on revenue and which risks should be treated.

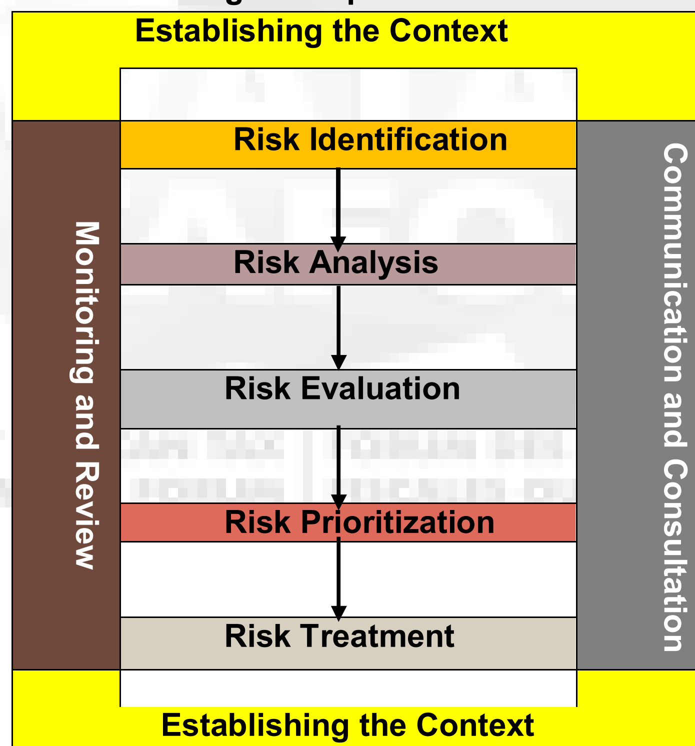
- Risk treatment

Risk treatment involves taking active steps and measures to reduce either the likelihood of risk occuring or the consequences or both. There are possibly four risk treatment strategies: (1) risk reduction (covering); (2) risk transfer (sharing); (3) risk avoidance (mitigation); and (4) risk acceptance (retention).

- Risk monitoring and communication

Risk monitoring and communication is a continual review of risk treatment strategies to determine how well the treatment strategies achieve desired results and communicate outcomes with relevant stakeholders and back into the entire compliance risk management chain.

Figure 1.1 - Compliance risk management process[3]



[3] Global Risk Management Institute G31000

2.2 ESTABLISHING THE CONTEXT

The operating context consists of the objectives, scope, strategies and the internal and external influences on RAs. Objectives define the general and specificgoals that RAs exist to achieve, typically the fair administration of tax legislations for purposes of assessing, collecting, auditing, enforcing and accounting for tax revenues. Scope defines the nature and extent of products and services offerred by RAs and geographical coverage and time period. Strategies are course of actions designed and implemented to achieve desired goals and objectives. Compliance risk management can only be implemented within the specific operating context in which the tax administration takes place.

Establishing the context sets the boundaries within which compliance risk management occur. The context needs to be continually scanned and monitored in an effort to detect changes that might consequentially affect compliance risks. In practice, many factors may directly bear on compliance risk management. For example:

- Limited financial resources may substantially affect capacity to deal with major compliance risks identified.
- Public perception of tax administration and the role of government may undermine public confidence in the tax administration.
- General economic performance and intrenational trade and commerce may affect taxpayers' ability to pay their tax obligations when due.
- Weaknesses or shortages in staff skills and capacities may seriously impede ability to deal with certain major compliance risks. etc.

Key factors in the operating context may include, but not limited to the following:

- RAs' objectives, strategies, policies, processes and procedures
- Internal stakeholders, including management and board
- External stakeholders, including major actors
- Cultural and socio-economic factors
- Laws and regulations directly or indierctly infuencing RAs
- Health of the economy
- Number and types of taxpayers
- Advances in information technology
- Globalization and protectionism
- Relationships, perceptions (us vs. them) attitude
- Public opinion, perceptions and expectations of major stakeholders

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- Management philosophy and operating style
- Efectiveness of control policies and procedures
- Employees' integrity and general conduct
- Level of independence and freedom from political interference
- Organizational capabilities, resources and technologies
- Political system, structure and stability of institutions. etc.

2.2.1 THE EXTERNAL ENVIRONMENT

The external and internal institutional context sets the stage for RAs identification and treatment of potential risks that impede achievement of goals and objectives. The context dictates how CRM program will be designed and carried out and the resources devoted to it (OECD 2004). The goal is to acquire knowledge of the external environment to provide intelligence on identifying, analyzing, evaluating, prioritizing and treating compliance risks. The key factors in the external environment that affect compliance risks include legislation, government policy, public opinion and economic conditions.

2.2.1.1 LEGISLATIONS

Existing tax legislations are potential sources of compliance risks due to their prescriptive nature and contextual ambiguities. Generally, tax laws in Anglophone countries are modelled against that of the United Kingdom, perhaps with the single exception of Liberiaand those of Francophone countries are associated with the West African Economic and Monetary Union (WAEMU). In the former, the governance structure and tenure of executive management conform with the autonomous status of RAs that have enough latitude to conduct the day-to-day activities without significant political interference than in the later. Although this may hold for many RAs, in practice, it does not translate into being risk free on account of political interference on a case-by-case basis. Most RAs in West Africa are in some way or another still under the influence and supervision of their respective finance ministries.

Specifically, tax legislations must be probed to see risks imbeddedwithin them. For example, in most West African countries, tax legislations permit tax holidays under an enabling national investment code. These countries havetax laws that lead to revenue loss and therefore constitute potential sources of compliance risks, albeit, self-inflicted. These 'legislated' risks must be identified and treated accordi ngly.

Another cross-cutting issue legislated in West African tax legislations is withholding of taxes in a myriad of institutions which have intrinsic non-surrender risks. The proliferation of responsibility for holding government money is a source of risk that can lead to revenue loss. To close this loophole, relevant laws may be amended to enable RAs have more robust surrender arrangements with other government ministries, departments and agencies

that collect fees relating to passports, vehicle registration, driver's licenses, etc. The legal infrastructure must be combed for such risks and strategies devised to mitigate and minimize potential revenue loss.

2.2.1.2 GOVERNMENT POLICIES

Any government policy that has revenue loss implications, including how exemptions are granted under the tax legislations must always be scrutinized as part of the context of compliance risks. The starting point being the fiscal budget and its demand on RAs to match expenditures, given desired level of deficit financing. Government fiscal policies in many West African countries put tremendous pressure on RAs and that in many instances brings disagreements among the legislatures, ministries and RAs. There is, however, a mutually agreed budget target between the government and RA, a projection of receipts that serves as a target for the annual collections.

2.2.1.3 PUBLIC OPINION

Studies show that public confidence in the tax system and its administrators is a key motivating factor for taxpayer compliance. Modern RAs must seek to attain a high level of public confidence[4]. "Attitude and perception surveys of current and potential taxpayers may help to identify perceived weaknesses in the tax systemand enable RAs focus attention efficiently on high-risk categories of taxpayers" (NORAD 2012). An annual Taxpayer Perception Survey (TPS) administered by RAs is intended to elicit public opinion on the effectiveness of the services RAs renderto the public.

The TPS seeks to gauge public opinion about RAs by posing questions on access to and quality of the services offered. Respondents are asked to rate the effectiveness and usefulness of information and RA's support with regard to voluntary registration, filing, reporting and payment of taxes. Knowing one's customers (KYC) is a sine qua non for serving themwell and that is the aim of TPS.

The public perception of RAs can affect the compliance behavior of taxpayers and if strongly negative, even poison the interpersonal contacts between taxpayers and tax officials. Non-cooperation and unwillingness to give information are a couple of risks which can be motivated by 'dislike' perceptions.

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[4] Author's parenthesis

Figure 1.2 Public perception survey in the quality of the services of RA

Very High	High	Fair	Low
4	3	2	0

Figure 1.3 Sample questionnaire for availability of services

	Excellent	Good	Fair	Poor	Unavailable
	4	4	2	1	0
Services					
Information Products					
Internet services					
Help desks					
Telephone					
RA visibility					

Figure 1.4 Timeit takes to get to any of RA Offices

	Less than 10 mins	10 – 30 mins	30 mins – 1hr	1 – 2 hrs.	>2hrs
By Car					
Walking					

Figure 1.5 Medium usedto source information about taxes

	Very Useful	Fairly Useful	Not Useful
	2	1	0
Sources of information			
RA Website			
Email			
Telephony (SMS, Voice)			
Pamphlets			
Brochures			
Billboards			

Figure 1.6 RA's Tax Registration by level of simplicity

	Very Simple	Fairly Simple	Not Simple	Not Available/ Relevant
	1	2	3	0
Taxpayer registration				
Registration Information				
Registration Form				
Registration Process				

2.2.1.4 ECONOMIC CONDITIONS

Economic activity, as measured by gross domestic product (GDP) is a sine qua non for a sustainable increase in tax revenue. Central to the economic context in CRM is paying particular attention to the macroeconomic aggregates that point to a rise or fall in the fortunes of taxpayers. This includes GDP growth or if the data are available, disposable income; domestic price level - inflation; current account - movements in exports and imports; international commodity prices for the country's major exports and imports; stable international exchange of the local currency – the exchange rate; and, supported by reasonable international reserve cover – International reserve stock. The risks posed by a country's economic conditions is usually assessed by the International Monetary Fund (IMF) in the medium-term outlook that it publishes in the Article IV Consultations report with countries. CR analysis can readily extract credible economic risks from these and other sources instead of reinventing the wheel.

2.2.2 THE INTERNAL INSTITUTIONAL ENVIRONMENT

Influences and conditions internal to RAs are potential sources of compliance risks. The internal environment consists of the current state of compliance risk management, human resources and technical capacities and the integrity and ethical disposition of staff.

2.2.2.1 CURRENT STATE OF COMPLIANCE RISK MANAGEMENT

Many West AfricanRAs are aware of CRM as a tool for managing compliance risks consistent with international best practices. However, the current context shows that most RAs do not have a framework for compliance risk management.Theyneither havecompliance risk register, nor a systematic data-driven identification and quantification of specific risks, estimates of comparative compliance levels by tax type, economic sector and tax obligations[5]. Some RAs in East Africa, like those of Rwanda and Kenya have established formal systems of CRM that clearly identifies and analyzes risks based onpredefined selectivity criteria using taxpayers, institutional, policy and economic data.

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[5] TADAT assessment of RAs in West Africa

Liberia also has a CRM program that uses predefined selectivity criteria,but it lacks sufficient taxpayers, institutional, policy and economic data[6].

2.2.2.2 HUMAN AND TECHNICAL CAPACITIES

A potential source of compliance risks associated with the internal institutional environment in many West African RAs is the lack of appropriate human resource and technical capacities to effectively administer tax legislations. This risk consists of either limited number of staff needed to administer tax legislations or staff lack skills and competences necessaryto effectively perform their tasks or both.Thus, RAs are at the mercy of the sophisticated tax avoidance and evasion schemes by taxpayers. Revenue analysts, auditors and enforcers in many West African countries lack the appropriate knowledge and skills to perform their tasks.

In addition to the lack of appropriate staff and requisite knowledge and skills, many RAs in West Africa lack the technical infrastructure such as information technology hardware and software to facilitate the assessment, collection, audit, enforcement and accountability of tax revenues. Key aspect of this risk is that existing information technology systems are not fully used by RAs as a result of staff lack of understanding and ability to make full and effective use of existing systems.

2.2.2.3 INAPPROPRIATE STAFF BEHAVIOR

A major source of compliance risks in most West African RAs is the high rate of corruption, bribery and conflict of interest of staff particularly in audit and enforcement functions. Staff of RAs collude with taxpayers to understate incomes or overstate expenses for purposes of understating taxable profits. In the end, not only do RAs fail to meet revenue targets, but also affects governments' ability to provide basic social services to their people. The institution and implementation of professional ethics function that investigates staff misconduct arising from corruption, bribery and collusion with taxpayers is critical to managing these risks. RAs must conduct annual fraud risk assessment to determine staff who are susceptible to fraud and take active steps to reduce fraud risks. Some RAs have instituted lifestyle audits of staff in key functions. A complete and proprer understanding of factors in the operating context of RAs is necessary for an accurate, complete and reliable identification of compliance risks.

2.3 COMPLIANCE RISK IDENTIFICATION

[6] June 2019 IMF Article IV Staff Assessment report

Compliance risk identification is a systematic and objective recognition and description of potential events and vulnerabilities that pose threats to tax compliance objectives. Compliance risk identification can be a top-down techniques, such as macro analysis or bottom-up processes such as case-based risk identification. Appropriate understanding of the context and proper taxpayer segmentation are fundamental to achieving a thorough identification of compliance risks. Taxpayers can be segmented by:

- Tax type
- Legal status
- Industry
- Turnover
- Lifecycle
- Location

Compliance risk identification begins by determining the compliance gap – the difference between the potential compliance level and the actual compliance level. The aim of risk identification is to identify the specific risks that an RA must confront as comprehensively as possible, minimizing the possibility of oversight and facilitating subsequent in-depth analysis.

Compliance risks identification at the strategic level requires extensive and carefully managed interventions, whilst those at the operational level can be dealt with on a day-to-day basis. Consideration of existing tax legislations often represents the most appropriate place at which to begin identification of strategic risks. This needs to be supported by evidence-based policymaking, treatment strategies and quantification of revenue at risk. Most tax laws throughout West Africa are of a highly prescriptive nature and tend to cover all possible consequences. Unfortunately, it is rare to be able to conceive all possible situations that might arise based on the application of the law. It is therefore almost impossible to create a law that is both clear and entirely unambiguous. Ambiguity in the law provides scope for non-compliance as taxpayers seek to operate in those 'grey' areas of the law. There will always be taxpayers determined to identify and exploit the gaps in the law in their efforts to gain advantage. In addition, prescriptive legislation tends not to allow sufficient flexibility to keep pace with developments in the business community. Compliance risk identification often entails identifying matters that, if left untreated, could pose a risk to the long-term viability and sustainability of revenue collection[7].

At the case-based or operational level, the aim is to identify individual cases or taxpayers that represent specific examples of taxpayers who collectively make up the strategic level

[7] IMF FAD CRM Literature

risks that an RA is proposing to address. In case-based or operational system, the characteristics of selected taxpayer and account transactions are examined to produce an objective measure that reflects the comparative level of risk that is posed by that taxpayer relative to other taxpayers. Some case-based systems identify the type of risk involved and may estimate the amount of tax revenue that is at risk. However, on its own, the value of a single piece of data in determining a compliance risk is somewhat questionable. Most commonly, it is analyzed from the perspective of the individual taxpayer. However, it can also be analyzed from the perspective of an industry grouping, or from a socio-economic or even psychological perspective. Many RAs tend to segment taxpayer population into groups with similar characteristics and identify compliance risks at these segmentatation levels.

In order to ensure that the most significant risks are addressed, the strategic risk identification needs to occur before operational or case-based risks are identified. Just as environmental scanning sets the context within which strategic risks can be effectively identified, identification of strategic risks represents the context within which operational or case-based risk identification occurs. Strategic risk identification can be done through continuous accumulation of data that is progressively transformed into intelligence and knowledge. This data accumulation can often occur, in part, because of past operational risk treatments, the knowledge of taxpayers and the general economic trends. Analysis of anomalies is a useful way to ensure continuous improvement in the compliance risk identification process.

Finally, good channels of communication between risk strategists and frontline compliance staff are necessary to ensure validation and identification of risks. This two-way feedback process will enhance an overall compliance risk identification strategy.

2.3.1 TAX GAP ANALYSIS

Generally, an objectivethat cannot be measured cannot be achieved. RAs must measurecompliance risk by way of estimating the Tax Gap. A tax gap is the difference between the potential revenue that can be collected based on existingtax legislations and what actually gets collected in any given year. Even though there is currently no tax gap estimate for many West African RAs, departmental and divisional performance gaps are good approaches to estimate the global tax gap. In most cases, taxpayers are demarcated as (1) individuals; (2) small and micro businesses; (3) medium-size businesses; (4) large businesses; (5) non-profit organizations; and (6) government organizations. The thresholds demarcating these segments are usuallyturnover and nature of business operations, but vary from country to country. Basic tools such as appropriate templates, questionnaires, data and information sources can be used to estimate the tax gap. Compliance risks can be identified in the four taxpayers' compliance obligation s.

2.3.2 IDENTIFICATION OF REGISTRATION RISKS

Registration risk is any risk that causes a taxpayer who is required toregister not to be registered or a registered taxpayer is not properly registereddue to misclassification, inaccurate information or taxes for which a taxpayer should be registered for are not registered. Registration risk also includes a registration of individuals and companies who should not be registered in the tax database.

Taxpayer types that are susceptible to registration risks are individuals, small and medium size businesses and startups. The major reason for their lack of registration is the lack of information to enable them register. Registration risk is generally high for micro, small and medium size businesses but low for large businesses. Tax types that are susceptible to registration risks are capital gains tax, property tax and goods and services tax (value added tax). The general reason for high registration risk for these tax kinds is their indirect nature and timing of assessment and collection. The major industries with high registration risks in West African countries are the service, retail and food and hospitality industries due to the unstructured nature of these industries. A macro top-bottom approach followed by a case base method is most effective in identifying registration risks. That is, first identifying the population of taxpayers or tax types most susceptible to registration risk and then narrowingdown to individual taxpayers or tax types in that population can facilitate accurate and complete risks identification.

2.3.3 IDENTIFICATION OF FILING RISKS

Filing risk is any risk that causes taxpayerseither not to file tax returns on time or not to file at all. Because most micro, small and medium size businesses are unlikely to be registered, they also have higher rates of non-filers than large business enterprises. Tax types that are susceptible to filing risks are individuals, property tax and capital gains tax due to compliance costs to obligators. Many startup businesses are also prone to higher filing risks because of lack of appropriate information to comply with tax legislations. Most West African RAs lack clear strategy to assist micro, small, medium size and startups to comply with tax legislations. The net result is that these businesses become noncompliant even when they mature. The general method currently used by most RAs in West Africa is to perform a case base analysis of taxpayers who have not filed for a given period. This method is inherently inadequate as it focusses only on taxpayers currently registered in the tax database but does not address those that are not registered.

2.3.4 IDENTIFICATION OF REPORTING RISKS

Reporting risk is any risk that causes taxpayers to misstate taxable profit, thereby misstating the applicable taxes payable. Reporting risk is also referred to as declaration risk, which

means that the risk is related to the amount of income and expenses declared by taxpayers. Taxpayers are most likely to underdeclare taxable profits either by understating income, overstating expenses or both than to overstate taxable profits. Therefore, attention must be directed at instances where taxpayers are most likely to understate income or overstate expenses. There are no particular reasons for reporting risks, but the general conclusion is that of economic or psychological reasons. Personal financial incentives and cash flow problems are general economic reasons for under declaration of taxes. Psychological reasons stem from the psychological state of taxpayers, including risk taking and possibility of not getting caught.

Large business enterprises are susceptible to reporting risks than small and medium size businesses due to their ability to use complex tax schemes to evade taxes. Tax types that are susceptible to reporting risks are personal income tax, capital gains tax and real property tax. Businesses in the financial services, food and hospitality, natural resource and retail are highly susceptible to reporting risks.

2.3.5 IDENTIFICTION OF PAYMENT RISKS

Payment risk is any risk that causes taxpayers either not to pay the correct taxes payable on time or not to pay taxes payable at all. Many RAs in West Africa have huge tax receivables as a result of poor collection and enforcement mechanisms as well as corruption in the systems. Small and medium size businesses are highly susceptible to payments risks because of cash flow problems and the financial incentives not to pay taxes. Taxes are used as source of funding new investments into the business. Tax types most susceptible to payment risks include corporate income tax, property tax and capital gains tax. Personal income tax is less susceptible to payment risks due to withholding mechanism in the form of 'pay as you earn' through withholding agents.In some West African countries, there are requirements for advance payments of corporate income taxes which makes it less susceptible to payment risks. However, advance corporate taxes are susceptible to declaration risks. Businesses that are experiencing cash flow problems may be highly susceptible to payment risks.

2.3.6 IDENTIFICATION OF INSTITUTIONAL RISKS

Institutional risk is any risk internal to RAs that affects their ability to effectively administer tax legislations for purposes of assessing and collecting the correct amount of taxes.

The primary goal of CRM is to increase voluntary compliance with the specific objectives to enhance taxpayer knowledge of tax laws, diversify, expand and upscale service delivery and attain a high level of public confidence. The basic question then is whether RAs have the programs, resources and capacities to achieve these objectives. The answer to this

questioncan be grouped into four categories: (1) policy, systems and procedures; (2) infrastructure; (3) human capacity; and (4) data and recording.

To identify internal risks, an assessment of these areas is required to identify weaknesses that pose limitations to RAs' ability to effectively ad minister tax legislations. This can be a control self-assessment where staff who actually do the work can narrate risk factors from their experiences to identify limitations and weaknesses actually existing in the systems.However, care must be taken to recognize that there is implicit bias in this approach, a tendency for staff to downplay risks associated with their own behavior. Therefore, to properly assess staff related risks such as corruption and potential strikes, third party sources must be assessed.

Analysis of internal risks concerns questions such as 'what is happening' and 'why are they doing it' as a third question of 'who is responsible' re sts ultimately with Management. RAs' policies concern with courses of actions or principles underlying those initiatives RAs can be addressed or adopted. Institutional risks also involve administrative issues as experienced by the functional departments such as Assessment, Accounting and Analysis (AAA), Enforcement and Audit.

Figure 1.7Identification of Institutional Risks[8]

No	Sources of risks	What is happening?	Why are they doing it?
	Systems and Procedures		
1			
2			
	Infrastructure		
1			
2			
	Data and Recording		
1			
2			
	Human Capacity		
1			
2			
	Administrative Issues		
1			
2			

[8] Adopted from the OECD

Figure 1.8 Compliance Risks by Internal and External Sector

Risk Number	Tax Domain	Description and Sources of Risks			
		Internal RA	Other Agencies	Private Sector	External
	Registration				
	Filling				
	Reporting				
	Payment				

Figure 1.9Risk identification tools and techniques[9]

[9] Adopted from the Fiscal Affairs Division of IMF

Knowledge		Transaction/ Case	Aggregated	Strategic
Knowledge	Intelligence	• Individual social/psychological behavior profile including client relationship management information • Intelligence gathering tolls – local knowledge and business intelligence • Rated using future probability of noncompliance	• Behavior based on industry, social/psychological profiles • Business intelligence – categorization and synthesis • Monitoring risk populations • Feedbacks from audit programs • Knowledge based on rules • Moderator/analyst capability	• Compliance context – strategic intelligence from environmental scans and scenarios • Senior executive considerations • Risk impact measured using reputation, costs of compliance and revenue
	Information	• Integrated databases – centralized case selection process • Taxpayers profiles of tax obligations • Success criteria – e.g. previous audit results, risk indicators/ratios, etc • Public information – e.g. utilities, law enforcement agencies • Rated using weighted attributes	• Whole of tax population profiles including views by segments • Tax issue profiles • Third party information used • Technology tools enabling data matching • Resources allocated by risk • Trend analysis • Confidence ranges/reliability indicators attached to risk ratings	• Macro-economic information, economic time series • Effective average tax rates • Multiple taxes profile • Corporate risk culture
	Data	• using tax return data • Processing checks – e.g. high risk refunds or credits • Paper-based selection methods	• Industry tax profiles • Technology tools enabling case selection based on tax data – e.g. data warehouse • Comprehensive risk coverage including register, file, report, payment, etc. • Deviations from populations norms	• Data mining • Automated exception cases • Macro level statistical analysis • Neural networks
		Transaction/ Case	**Aggregated**	**Strategic**
		Focus		

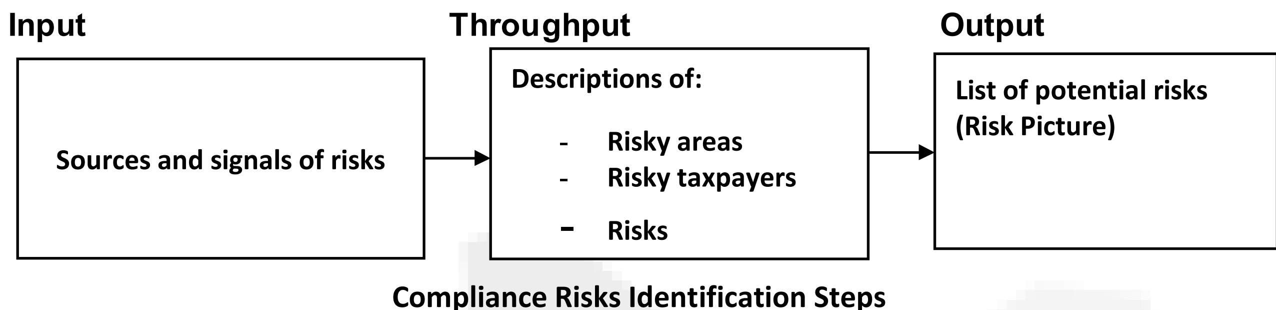
Figure 1.10 Taxpayer Compliance Risks by Tax Segment

ID	Tax Domain	Risk Description	Large	Medium	Small	Micro
	Registration					
	Filing					
	Reporting/Declaration					
	Payment					

Figure 1.11 Taxpayer Compliance Risks by Tax Type

ID	Tax Domain	Risk Description	CIT	PIT	VAT/GST	RPT	Excise and Other
	Registration						

	Filing						
	Reporting/Declaration						
	Payment						



Compliance Risks Identification Steps

2.4 COMPLIANCE RISK ANALYSIS

Compliance risk analysis is the systematic breakdown and examination of detailed taxpayers information to discover patterns and common characteristics giving rise to compliance risks. The number and category of risks and risky taxpayersare analyzed and grouped according to similar characteristics. Finding out what is occurring and who is doing it is not enough. Risk analysis answers the why question - what is the motivation behind the non-compliant behavior in specific areas.This is important because it contributes to evaluation and the choice of the most efficient and effective risk treatment strategies. For example, if the reason for non-compliance is the complexity of a specific part of the tax legislation, a possible treatment strategy may be simplification of the legislation and tax education. Risk analysis is done on the bases of data gathered from different sources:

- Economic and tax data, for example, data about the economic growth, average wages;
- Data supplied by taxpayers, for example, tax return(s);
- Data acquired by RAs, for example, audit results, last compliance reports, tax returns filed late;
- Data supplied by a third party, for example, a bank statement, divorce settlements;
- Information from other law enforcement agencies; and
- Information available on the Internet, companies registry, etc.

During the analysis, the risks are examined in order to discover essential components and features. Risk analysis is performed by logically manipulating and matching data, human knowledge and intelligence. Data put together results in information that gives meaning. Knowledge is a deeper understanding of this information. It is like a big jigsaw puzzle. The data are the pieces. When put together with the picture, information arises. With the

understanding of the meaning of the picture, knowledge is born. Data on their own have no practical 'value'. They get their value by being compar ed or related with others, often referred to as data matching. In compliance riskanalysis, specific knowledge is necessary and the use of techniques such as data mining and data warehousing require knowledge of electronic data processor.

Advances in information technology mean that the possibilities in this area is wide open. Unfortunately, many RAs in West Africa make little or no effective use of the huge volume of data in their possession.Compliance risk can also be analyzed at the operational, case by case level where frontline personnel examine detailed documents and data filed by taxpayers. Traditionally, when looking at registration risk, for example, the aim of RAs has been to ensure that anyone making taxable income is identified and registered at the appropriate time. However, a case base method is unlikely to identify those unregistered taxpayers.

For example, when registering new taxpayers, RAsmust compare new applicants with such items as:

- Other registrations at the same postal code
- Known addresses
- Beneficial owners
- Known associates
- Board members and executive management
- Mobile phones
- Bank accounts
- Suspect databases
- Credit reference agencies
- Other government department data, etc.

Early contact with taxpayers to establish that they exist can be considered in an attempt to thwart fraud. Most businesses in huge tax debts are susceptible to reregistration. Notwithstanding this, there are strategies for treating potential risks even before a taxpayer becomes registered. These will include the provision of clear and helpful advice and education, a prevention rather than cure approach. Except for advice and education regarding filing, payment and declaration risks, intervention can only take place when the possibility of a risk materializes and that is after registration.

There are several opportunities for risk analysis. When returns from a taxpayer are received, it is possible to carry out a number of 'rule based' checks:

- The inter-relationship of different figures on the return can be checked to test both accuracy and the credibility of the income, expenses, assets and liabilities declared;

- The return received can be compared with previous returns submitted by that taxpayer to highlight apparent inconsistencies;
- Comparisons can be made with other taxpayers who have a similar profile (size, type of trade, markup, assets, liabilities, income, expenses, etc.); and,
- Comparisons with industry, norms and standards.

These checks are particularly useful when a tax refund or credit is being claimed. The results of any check will inform the decision process on the type of action needed to address the perceived risk. Sometimes the sources for analysis are not structured. In that case, the analysis has to be carried out as soon as possible after the data are obtained.

In the end, risk analysis results in the knowledge about one or more of the following areas:

- The characteristics of the taxpayers involved
- The reasons for taxpayer behavior
- The likelihood or frequency of the risk occurrence
- The indicators/ selection rules and parameters
- The consequences on tax collections
- The trend, i.e. whether the risk is becoming more or less severe
- Possible treatment strategies
- Cost of treatment
- The impact on the RAs' objectives.

2.4.1 ANALYSIS OF REGISTRATION RISKS

Registration risk can be grouped into two main categories: (1) Taxpayers that are required toregister but are not registered; and (2) taxpayers that are registered but are not properly registered in the tax database. Taxpayers in the first category operate mostly in the informal sector of the economy. A large percentage of taxpayer population in West Africa operates in the informal sector. As a result, a large percentage of taxpayers are not registered in the tax database. Many fast food, artistic, retail and furniture businesses operate mostly in the informal sector of economies of West Africa. Micro, small and medium size businesses are more susceptible to registration risks due to their lack of education, complexities and ambiguities in existing tax legislations and willful and deliberate failure to comply with the laws.

The second categoryof registration risks relates to: (1) taxpayers whose information has been wrongly captured in the tax database; taxpayers whose information is incomplete; and (3) taxpayers whose appropriate tax accounts have not been created in the tax database. Taxpayers information may be wrongly captured in the tax database becaue of lack of proper review of data input into the system and lack of proper supervision of data entry staff. The major reasons for incomplete taxpayers' information are lack of education on the required information and deliberate failure of taxpayers to provide the necessary information. Lastly, appropriate taxpayers' accounts may no t be created due to lack of

knowledge of data entry staff to request and input the relevant taxpayers' infornation, incomplete information provided by taxpayers or both.

2.4.2 ANALYSIS OF FILING RISKS

Filing risks can be analyzed into two major categories: (1) Late filers and (2) non-filers. In addition, late filers can be grouped into aging whereby RAs can segment into time intervals taken for taxpayers to file from the due date to the date of actual filing. Non-filers can also be grouped into never-filers and stop-filers. Never-filers are taxpayers who have never filed tax returns since the beginning of business operation or from the date of registration with RAs. Stop-filers are a form of late filers. These are taxpayers who once filed tax returns but have stopped filing for more than one calendar year or a time period established by RAs. Large business enterprises are unlikely to be non-filers but are mostly likely to be late filers. On the other hand, micro, small and medium size businesses are susceptible to non-filing. The general motivations for small and medium size non-filers are compliance costs and lack of appropriate education.

2.4.3 ANALYSIS OF REPORTING RISKS

Reporting risks can be analyzed in terms of understatement of income and overstatement of expenses through deliberate manipulation of information or errors in the preparation and presentation of information. Reporting risks constitute the greatest compliance risks to RAs in West Africa[10]. Reporting risks can be analyzed in terms of the susceptibility for taxpayers to manipulate income and expenses or the use of wrong tax legislations and rates applicable to taxpayers. Large businesses and businesses that are having cash flow problems may be susceptible to income and expense manipulation. This deliberate manipulation of taxable profits is generally the cause of tax evasion in most West African countries. Reporting risks due to wrong application of laws and appropriate rates are caused by lack of tax education and occur mainly within the micro, small and medium size business enterprises. Businesses operating in the financial services, natural resources and complex business operations are susceptible to reporting risks.

2.4.4 ANALYSIS OF PAYMENT RISKS

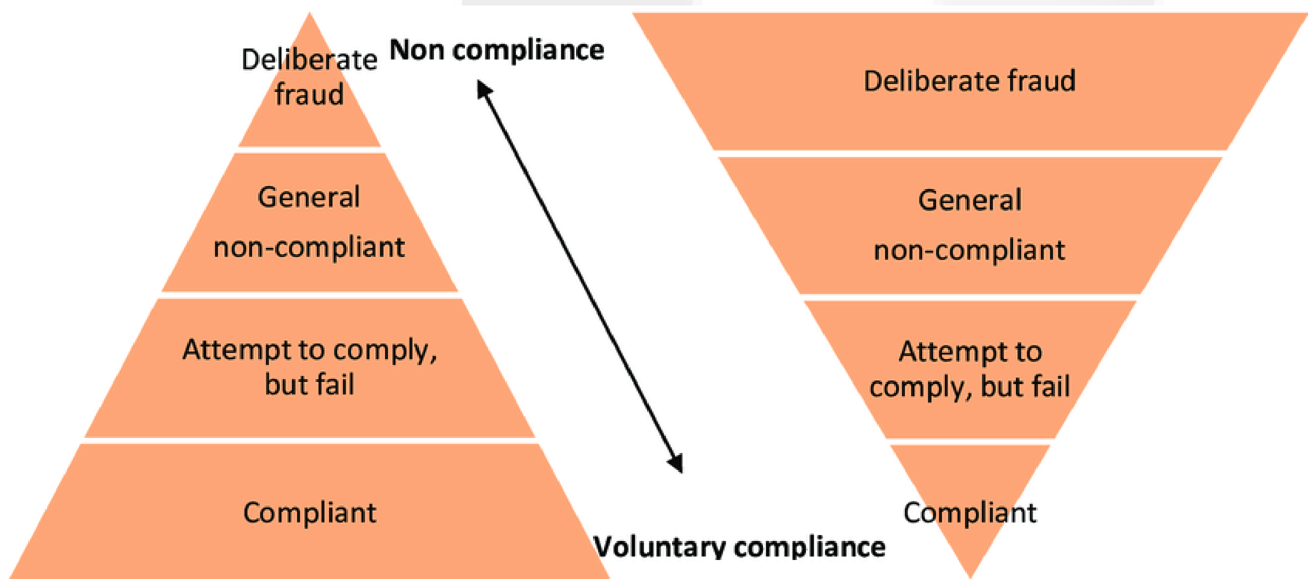
Payment risks can be analyzed in terms of late payment and nonpayment of taxes payable. Tax types that are susceptible to late payment are corporate income tax, capital gains tax and goods and services tax (value added tax) and occur mainly within micro, small and

[10] TADAT assessment of RAs in West Africa

medium size businesses. Tax types that are susceptible to nonpayment of taxes are property tax, capital gains tax and personal income tax for unregistered individuals. The major reason for late payment for large business enterprises is cash flow problems. However, psychological motivations may also account for late payment of taxes by these categories of taxpayers. Some taxpayers who refuse to pay taxes do so by willful and deliberate attempt to evade taxes. The main reasons for these taxpayers are the financial gain and the possibility of getting away with it.

2.5 ANALYSIS OF TAXPAYER COMPLIANCE BEHAVIOR

Analyzing Taxpayers' behavior is critical to design ingappropriate treatment strategies to treat compliance risks. The standard compliance behavior model divides taxpayers' compliance into four general attitudes to compliance constituted by those: (1) Compliant; (2) Attempt to comply but fail; (3) General non-compliant; and(4) 'Deliberate fraud[11].



A critical step is to locate the taxpayer on the compliance pyramid to elicit an appropriate mitigation strategy summarized in figure 1.12:

Figure 1.12 Taxpayer Attitude and Compliance Strategy

Risk Level	Taxpayer Behavior/Attitude	Compliance Strategy
High	Deliberate fraud	Use force of law

[11] Adopted from OECD model

Moderately High	General non-compliant	Deter with detection
Moderately Low	Attempt to comply but fail	Assist to comply
Low	Compliant	Make it easy

The basic assumption is that the bulk of taxpayers at the base of the pyramid constitutethose 'Willing to do the right thing' which sh ould be addressed by 'making it easy' for them to comply. Given the preponderance of compliance risks in the informal sector of economies in West Africa, the go-to strategy for the bulk of non-compliance risks is 'making it easy to comply' referred to as preventative enforceme nt, education on who, why, when and how to pay taxes.

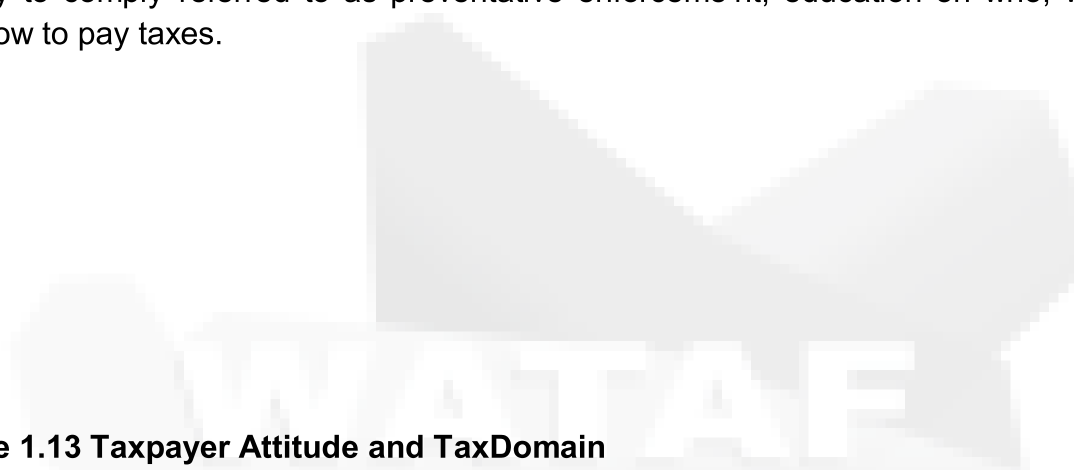


Figure 1.13 Taxpayer Attitude and TaxDomain

Risk Number	Tax Domain	Compliant	Attempt to comply but fail	Don't want to comply	Have decided not to comply
	Registration				
	Filing				
	Reporting				
	Payment				

Analysis of compliance behavior shows the results of sampling taxpayers with regard to each risk in the register and the dominant compliance behavior associated with it. Risks such as failure to register may show multiple compliance behaviors which would require different mitigating strategies and treatments. A further narrowing down of mitigation options may be needed to engender a successful strategy.

The identified risks are analyzed for significance by the following segmentation:

- Taxpayers by tax domain – registration, filing, reporting and payment.
- Taxpayers by tax segment, micro, small, medium and large taxpayers and taxes collected by each segment by tax type.
- Taxpayers by tax type – corporate income tax, personal income tax, value addedtax (goods and services), capital gains tax and property tax.
- Taxpayers by location – geographical demarcation of the segmented risks will bring to the fore shared characteristics of risks such as ready physical access to tax services
- Taxpayers by standard industry classification– manufacturers, distributors, wholesalers and retailers.

A complete picture of the identified risks is formed by juxtaposing the risks with the base data on the grouping above. It allows for 'cluster risk ranking' with regard to tax segment, geography, tax domain, tax types and economic sector. Such categorizations permit generalized approaches to risk treatment. For example, large taxpayers in the mining sector may be prone to false reporting through tax avoidance scheme by way of transfer pricing.

Compliance risk management should not be a stand-alone activity, separate from the main activities and processes of RAs. Compliance risk management should be part of the responsibilities of all levels of management, from board and executive management to line management and floor employees. It should be an integral part of all processes, including strategic planning, project and change management processes. Compliance risk management helps managers make informed decisions about the operations of an RA. The value derived from this help is indispensable to achieving the mission and objectives of RAs.

More than ever before, compliance risk management is taking center stage in the daily operations of RAs. It has yielded unprecedented increase in the level of voluntary compliance. Embedding risk management into tax administrations involves deliberate steps to gather, analyze and develop knowledge and intelligence of taxpayers and third party data. The knowledge and intelligence developed can be used to induce voluntary compliance together with other appropriate methods to enforce compliance with tax legislations. This provides opportunities for RAs to trump taxpayers in an ever increasing complex business environment.

Embedding risk management in RAs involves the following activities:

- Establishing an intelligence framework
- Gathering and analyzing taxpayers data
- Developing knowledge about taxpayers
- Analyzing compliance behavior
- Understanding influences on taxpayers' behavior

- Recognizing drivers of taxpayers' compliance behavior

2.5.1 ESTABLISHING INTELLIGENCE FRAMEWORK

An intelligence framework is a structured knowledge and understanding that allows RAs to perfectly predict taxpayers' compliance behavior.An intel ligence is the highest level of knowledge and understanding about a subject matter that allows an individual to make accurate, complete and reliable prediction regarding that subject matter. An intelligence framework is like fitting a jigsaw puzzle together to discover the image that lies behind the puzzle. By fitting fragmented taxpayers data together, RAs can learn a great deal about taxpayers' behaviors in ways that they are able topredict future compliance behavior with reasonable certainty.

Developing an intelligence framework takes great deal of time, effort and resources but the payoffs far exceed those resources. An effective intelligence framework answers the following questions, called the 5WHs:

- What is happening
- Who is doing it
- Why is it happening
- How is it happening
- Where is it happening
- When is it happening

Figure 1.14 Intelligence Framework

Unit Level	Information and Intelligence		
Micro Level	International trade and commerce	Prices of produce on the world market	Free trade vs protectionism
	Health of local economy	Government regulations	Socio-cultural factors
Business and Micro Level	Compliance history and credit rating	Capital structure, liquidity and profitability	Corporate governance framework
	Nature, sizes and complexity of business	Business competitiveness and intensity	Management integrity and operating style
	Business formality and ownership interest	Household income and purchasing power	Level of automation and use of high tech.

2.5.2 GATHERING TAXPAYER DATA

The first step in building an intelligence framework is gathering, grouping and analyzing data. The first sources of data are those of taxpayers, such as:

- Business registration
- Beneficial owners
- Tax registration
- Property registration (if any)
- Tax return records
- Financial statements
- Court records, if any
- Key partners and associates
- Key customers and suppliers
- Registered address, contact number and contact person
- Credit rating and history of compliance with laws and regulations
- Bank records
- Scope of operation
- Major shareholders
- Previous audit results (if any)
- Board and executive management composition. etc.

Other sources of data include:

- Power and utility companies
- Other government departments
- Company registry
- Law enforcement agencies
- Other revenue authorities
- Foreign governments
- Trade associations
- Import and export statistics
- Industry and market data. etc.

2.5.3 DEVELOPING KNOWLEDGE OF TAXPAYERS

Gathering taxpayers' data is not sufficient and provides no benefit to RAs. The data must be grouped, analyzed and structured in ways that provide discernable patterns that explain current and future compliance behavior. Data must be captured and stored in a format that allows logical manipulations using appropriate data extraction, analysis and matching tools and techniques.

For example, annual turnover can be compared with industry average, economic data or those of competitors to uncover possible false declaration of turnover. Import records can be matched against cost of sales and compared with industry average to determine whether cost of sales is deliberately overstated or understated. Economic data can be compared with cash flow forecast and bank records to determine whether a taxpayer will be able to settle existing tax debts.

Data can also be triangulated. For example, matching data from company registry against property registry, financial statements and tax filings may expose possible tax fraud or money laundering scheme. Accurate, complete and reliable knowledge of taxpayers is indispensable to RAs.

RAs need to build and retain knowledge, skills, expertise and competencies which can be translated to such knowledge and intelligence. The use of advanced information technology, data warehouse and data extraction, analysis tools and techniques is equally important to RAs.

2.5.4 ANALYZING COMPLIANCE BEHAVIOR

As businesses become more and more complex, it is imperative for RAs to adapt and keep pace with new developments. Understanding taxpayers compliance behavior is not a guesswork. Several indicators of compliance behavior are now supported by robust empirical research. Both economic and non-economic explanations of compliance behavior have predictive force.

Taxpayers adopt a range of motivational postures in their response to the demands of RAs. The tax system itself, both law and administration can be a shaper of taxpayers' compliance behavior.Research has identified two broad approaches to the problem of compliance[12]. The first stems from an economic rationality perspective and has been developed using economic analysis. The second is concerned with wider behavioral issues and draws from concepts in psychology and sociology of taxpayers.

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[12] Research done by IMF's Fiscal Affairs Division

Economic factors:

- **Financial burden -**There appears to be a relationship between the amount of tax owed and taxpayers compliance behavior. For instance, if a taxpayer has tax liability that can easily be paid, the taxpayer may be willing to pay. However, if the liability is large, potentially threatening the viability of the business, the owner may avoid paying at all or may try to adjust the data reported so as to incur a smaller, but incorrect, tax liability.

- **The cost of compliance** – Taxpayers appear to have a number of common costs of having to comply with their tax obligations over and above the actual amount of tax they pay. These include the time taken to complete requirements, the costs of having to rely on accountants and the indirect costs associated with the complexity of tax legislations. These can include psychological costs such as stress that comes from not being certain that they have met all the tax rules or even knowing what those rules are.

- **Disincentives** – Investigations into the impact of deterrents, such as financial penalties and threats of prosecutions, suggest that they may have a limited effect on compliance behavior of taxpayers. However, those who are compliant want those who are non-compliant to be punished. If RAs do not deter non-compliant taxpayers with heavy penalties and prosecutions, those who are complaint will have disincentives to comply.

- **Incentives** – Giving taxpayers incentives for compliance may have a positive effect on compliance behavior by becoming more compliant. For example, giving a taxpayer an extended tax clearance certificate or special recognition at a national event may induce both compliant and non-compliant taxpayers to comply.

Behavioral factors:

- **Individual differences** – While many taxpayers comply with their tax obligations, some do not. Individual factors influencing behavior include gender, age, education level, moral compass, industry, personality, circumstances and personal assessment of risks.

- **Perceived inequality** – Taxpayers who believe that the tax system is unfair or who have personal experience of unfair treatment are less likely to comply compared with those who think that the tax system is fair.

- **Perception of minimum risk** – If a taxpayer has the opportunity not to comply and thinks that there is only a minimum risk of being detected, he or she will take the risk

of non-compliance. This presumably accounts for the greater under-reporting of certain types of income in West Africa. RAs in West Africa generally lack the capacity to detect non-compliant taxpayers. For example, salary and wage income is highly visible to RAs because of third party reporting. However, other forms of income may be much less visible and therefore subject to more creative accounting.

- **Risk taking** – Some taxpayers view tax avoidance as a game to be played and won. They like to test their skills in avoiding their obligations and avoiding being caught. The perceived fairness of RAs is important in inducing tax compliance. In addition, RAs must timely detect and punish those who take the risk to evade taxes because they rationalize tax avoidance as a game to be played and won.

2.5.5 INFLUENCES ON TAXPAYERS BEHAVIOR

It would be impossible, if not pointless to attempt to list all the different factors that go together to influence the attitudes and behavior of taxpayers. What can be done is to provide a model for thinking about those factors, a model that allows RAs categorize the factors in a consistent manner and form to aid them in understanding taxpayers' compliance behavior.

This model[13] is very useful for RAs to apply in their settings to understand why taxpayers behave the way they do and for effective and efficient treatment strategies. There are five general categories under which the factors can be grouped:

- Business profile
- Industry profile
- Sociological factors
- Economic factors
- Psychological factors

Business profile:

- Structure – sole trader, partnership, company, trust, etc.
- Size and age of the business

[13] Model developed by IMF's Fiscal Affairs Division

- The types of activities it carries out
- Focus – local versus international
- Its financial data – capital investment, profitability, liquidity; capital structure, etc.
- Key customers and suppliers
- Its business intermediaries. etc.

Industry profile:

- The definition and size of industry
- Major participants in the industry
- Profit margins
- Cost structures
- Industry regulations
- Working patterns
- Level of competition
- Seasonal factors
- Technology and infrastructure. etc.

Sociological factors:

- Socio-cultural norms
- Ethic background
- Attitude to government
- Age, gender and level of experience
- Educational level
- Social group. etc.

Economic factors:

- Investment
- Health of the economy
- Demographic interest rates
- The tax system
- Government policies
- International influence
- Inflation
- Market conditions. etc.

Psychological factors:

- Greed
- Attitude to risk
- Fear and trust
- Values and philosophy
- Fairness and equity
- Moral compass
- Opportunity to evade. etc.

2.5.6 DRIVERS OF COMPLIANCE BEHAVIOR

There is no easy answer to what influences taxpayer behavior toward either compliance or non-compliance. Research suggests that several factors combined to cause taxpayers to adopt sets of values, beliefs and attitudes that can be described as motivational postures[14]. These postures, two broadly non-compliant and two broadly compliant, characterize the way taxpayers relate to RAs and the tax systems:

- **The disengaged** - These are taxpayers who have decided not to comply. Taxpayers with this attitude either deliberately evade their responsibilities or choose to opt out. Cynicism about the tax system is usually matched by cynicism about the role of government.

- **Resisters** – The attitude of resistance characterizes confrontation. The system is seen as an oppressive, burdensome and inflexible. This attitude characterizes taxpayers who do not comply but who will if they can be persuaded that their concerns are being addressed.

- **Triers** – More positive is the attitude of those who are basically willing to comply but who have difficulty in doing so and dont always succeed. Th ey may have difficulty understanding or meeting their obligations, but their expectation is that, in any dispute, trust and cooperation will prevail.

- **Supporters** – The attitude here is one of willingness to do the right thing. There is a conscious commitment to supporting the system and accepting and managing its demands. There is an acceptance of the legitimacy of the role of tax officers and belief that they are fundamentally trustworthy.

It is important to realize that any taxpayer is capable of adopting any of the attitudes described at different times. It is also possible to adopt all of the attitudes simultaneously in

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[14] A literature by IMF Fiscal Affairs Division

relation to different issues. The attitudes are not fixed characteristics of a person or group, but reflect the interaction between the person or group and those that impose demands upon them. The value of this model is that it contributes to a deeper understanding of taxpayer behavior and lays the groundwork for the development of targeted strategies which encourage the motivation to do the right thing and constrain the motivation to resist or evade compliance. Understanding the general theory of taxpayers' motivation can help RAs shape and manage compliance program in a strategic way.

In the same way, understanding the factors that drive specific compliance behavior is essential to guide the selection of appropriate treatment strategies. Taking time to analyze compliance behavior assists RAs in addressing the cause of the non-compliance rather than the symptom, thereby achieving the long-term compliance outcome.

For example, over claiming business expenses or failure to report accurately may be the non-compliant behavior that is observed and needs to be addressed. However, the driver of the behavior may be the taxpayer's need to increase cash flow in an attempt to remain competitive in the business environment where competitors routinely under-report their business income or deal in cash.

Alternatively, the driver may be taxpayer's perception th at the tax rates are too high and the desire to recoup some money as compensation. In a situation such as this, treating the behavior (the symptom) will only have an impact on the affected taxpayer and even then only for a limited period of time. Moreover, the taxpayer concerned may actually feel hard done to have been singled out for attention when those around get away with the same behavior. This may in turn simply serve to fuel feeling of resentment to the tax system and provoke further acts of non-compliance.

Thus, looking for the underlying cause of the behavior and selecting appropriate strategies to address it could account for a difference in outcomes between short-term, isolated compliance or even aggravated non-compliance and long-term sustainable compliance.

It should not automatically be assumed that the target taxpayer is able to change behavior of its own accord. This is the reason why an RA must understand where the cause of the behavior problem lies. For example, the behavior of the target taxpayer may be to always submit tax returns late (failure to file).

Further analysis and investigation might determine the cause to be third party entities (say an accounting firm) not making necessary information available to the target population in a timely fashion. In this situation, penalizing the target taxpayer for its behavior is not going to fix the underlying systemic problem. A more effective strategy would be to work with the

third party information providers (the accounting firm) to improve the timeliness of their information provision.

Good compliance outcomes begin with good legislations. Laws that are clear and unambiguous with regards to their intent and interpretation provide a solid base upon which to build administrative compliance program and compliance risk management. Difficult or ambiguous laws create increased opportunities for taxpayers to behave in ways that were unintended by the laws. In many ways, good laws underpinRAs' ability to deliver procedural fairness in the conduct of tax administrations.If taxpayers perceive the laws to be unjust and inappropriate according to taxpayers mores, then, inevitably, there is an increased risk of non-compliant behavior.

Tax administration begins with the laws in place. The laws representa component of the context or environment in which RAs operateand it is from this environmental context that RAs discern the compliance risks associated with the administration of the laws.The challenge for RAs is to administer the laws in a manner that sustains taxpayers' confidence in their administration. To that end, the manner of administration must commensurate with the level of exposure to compliance risks. Any compliance imposition on taxpayers or sub-section of taxpayers needs to be acceptable in accordance with taxpayers' expectations. In general, the compliance costs to taxpayers associated with administration must be appropriate. Otherwise, it will create dissatisfaction and therefore lead to a decrease in taxpayers' compliance.

Figure 1.15 Taxpayer Compliance Risks by Tax Domain

No	Tax Domain	What is happening?	Why are they doing it?
	Registration Risks		
	Filing Risks		
	Reporting Risks		
	Payment Risks		

Figure 1.16 Taxpayer Compliance Risks by Tax Domain and Segment

ID	Tax Domain	Risk Description	Large	Medium	Small	Micro
	Registration					
	Filing					
	Reporting/Declaration					
	Payment					

Figure 1.17 Taxpayer Compliance Risks by Tax Domain and Tax Type

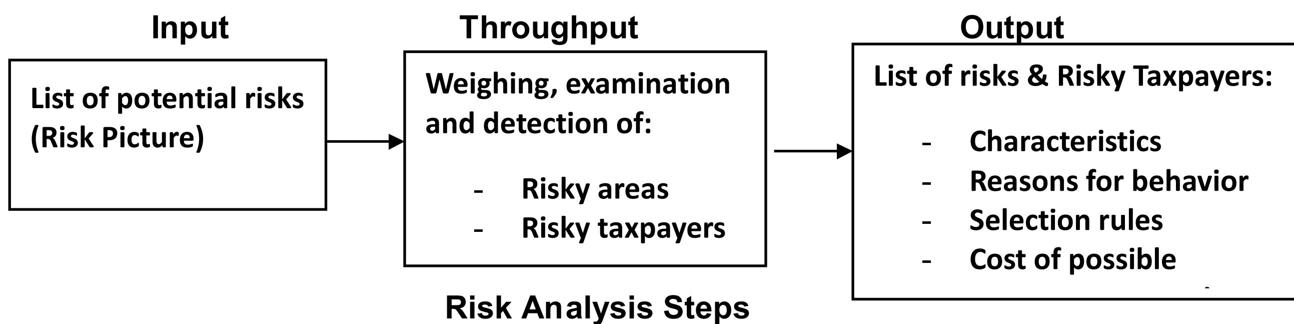
ID	Tax Domain	Risk Description	CIT	PIT	VAT/GST	RPT	Excise and Other
	Registration						
	Filing						
	Reporting/Declaration						
	Payment						

Figure 1.18 Taxpayer Behavior Analysis – Motivational Factors

Risk ID	Risk Description	Business	Industry	Economic	Social	Psychological

Figure 1.19 Taxpayer Behavior Analysis – Attitudes to Compliance

Risk ID	Risk Description	Willing to do things right	Trying to but not successful all the time	Do not want to comply	Decided not to comply



Risk Analysis Steps

2.6 COMPLIANCERISK EVALUATION

Compliance risk evaluation is a systematic process of objectivemeasurementof likelihood, consequences and severity of risks identified and analyzed. The central goal of risk evaluation is to facilitate informed and evidence-based decisions about the likelihood of a risk occuring and the consequences if the risk occurs as well as effectivetreatment strategies given available resources. Each compliance risk is evaluated to determine the likelihood of the risk occuring and the consequences on revenue collection if the risk occurs. There are five likelihood measures: (1) Rare; (2) Unlikely; (3) Possible; (4) Likely; and (5) Almost certain.

(1) The occurrence of a risk is rare if it is extremely unusual that the risk will occure; (2)The occurrence of a risk is unlikely if it is improbable that the risk will occur; (3) The occurrence of a risk is possible if it is conceivable for the risk to occur; (4) The occurrence of a risk is likely if it is probable for the risk to occur; (5) And the occurrence of a risk is almost certain if it is most likely than not for the risk to not occur.

Figure 1.20 Likelihood Measure

Risk Ranking	Likelihood measures	Ilustrative definitions to help determine the likelihood rating	
		Subjective definitions	Objective definitions
1	Rare	May occur in exceptional circumstances	Likely to occur once in 25-50 years
2	Unlikely	Could occur at some time	Likely to occur once in 10-24 years
3	Possible	Might occur at some time	Likely to occur once in the next 3 years
4	Likely	Will probably occur in most circumstances	Like to occur more than once in the next 3 years
5	Almost certain	Is expected to occur in most circumstances	Likely to occur this year or at frequent intervals.

Each likelihood measure can be subjectively or objectively determined depending on the availability of data to compute the probability distribution of each event.

Figure 1.21 Consequence Measure

Risk Criteria	Consequence Rating				
	1- Low	**2- Medium**	**3 - High**	**4 - Very High**	**5 - Extreme**
Revenue Risks	Variation of ……				
	Less than $50 m	Between $51 and $250 m	Between $251 and $500 m	Between $501 and $1b	More than $1b

Consequence measure can be determined based on the materiality of monetary loss that would result if a risk occurs. This monetary amount accounts for the tax gap that would occur at each given level of risk.

2.6.1 EVALUATION OF REGISTRATION RISKS

Registration risks can be evaluated by measuring the likelihood that taxpayers require to register will not be registered or taxpayers registered in the tax database are not properly registered and the potential revenue loss that would occur if either of the two scenarios occurs. Because the lack of registration means a hundred percent revenue loss, even a small number of unregistered large taxpayers could lead to significant revenue loss. Registration risk is unlikely to occur among large taxpayers but likely or almost certain to occur among micro, small, medium size and startup businesses. Tax types that are likely to be unregistered are property tax, personal income tax and goods and serviecs (value added tax). Because these tax types as well as small and medium size businesses account for the largest percentage of taxpayers in West Africa, registration risk remains the greatest risk to RAs in West Africa[15].

[15] TADAT assessment of RAs in West Africa

2.6.2 EVALUATION OF FILING RISKS

Filing risks can be evaluated by measuring the likelihood that taxpayers who are required to file will not file on time or will not file at all and the potential revenue loss that would occur if taxpayers file late or do not file at all. Filing risks are likely to occur among micro, small, medium size and startup businesses. The objective of filing is to facilitate validation of declaration through audits and reviews of taxpayers’ de claration (reporting) of taxable profit. Filing risk affects the ability of RAs to fairly and transparently assess and collect the correct amount of lawful revenue. Tax types that are almost certain to be susceptible to filing risk are personal income tax, goods and services tax (value added tax) and capital gains tax. Micro, small, medium size and startup businesses are likely to be susceptible to filing risk. Retailers, artistic, food and hospitality businesses are also certain to be late or nonfilers.

2.6.3 EVALUATION OF REPORTING RISKS

Reporting risks can be evaluated by measuring the likelihood that taxpayers will engage in false declaration and the potential revenue loss if they falsely declare taxable profits. Reporting risk due to lack of understanding of tax legislations is lower than those of taxpayers that willfully manipulate income and expenses for purposes of tax evasion. Taxpayers that are most likely to engage in false reporting are those in industries such as food and hospitality, mining and natural resource, manufacturing and financial services sectors. Because of the high probability that these taxpayers will falsely declare income and expenses, they represent the greatest reporting risk to RAs in West Africa. West Africa is rich in natural resources but the benefits of these resources do not trickle down to citizens because a large percentage of companies operating in this sector are foreign owned. The only benefit derived from resources are the taxes companies in the sector pay. Becauseof the high rate of tax evasion in the sector, West African countries benefit little or nothing from theirnatrural resources.

2.6.4 EVALUATION OF PAYMENT RISKS

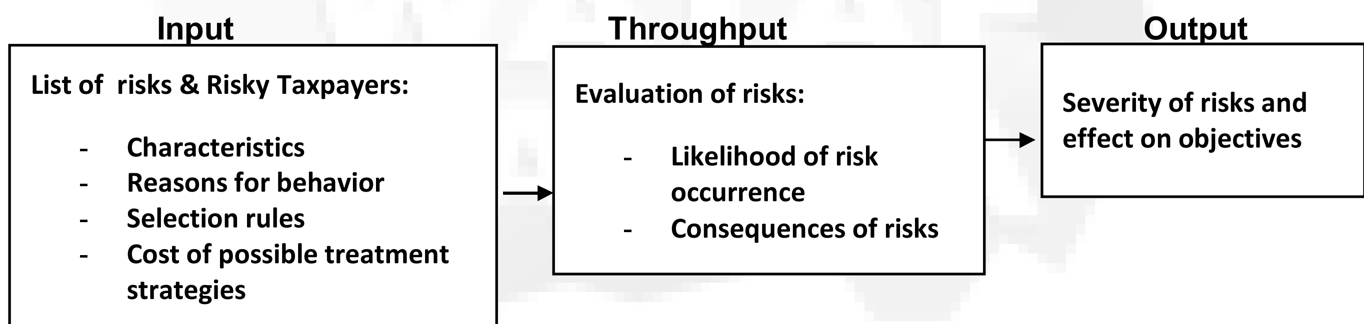
Payment risks can be evaluated by measuring the likelihood that taxpayers will not pay their full tax obligationswhen due or they will not pay their tax obligations at all and the potential revenue loss that result if this likelihood occurs. Payment risk is generally high for taxpayers having cash flow problems and during difficult economic times. Payment risk is also high for taxpayers who are likely to engage in deliberate and willful fraud of the tax system. Tax types that have high likelihood of payment risks are property tax, capital gains tax, goods and services tax (value added tax) and personal income tax in jurisdictions that have no

withholding regime. Tax types with the greatest potential for revenue loss are property tax and capital gains tax.

Evaluation of compliance risks is based an assessment of the likelihood and impact of risks on RAs' goals and objectives. It involves a quantitative evaluation oftaxpayers' data and the realization of any potential risk that would result in revenue loss and constitutes an impediment to the achievement of RAs' goals and objective s. Data that are relevant in payment risks evaluation may include general economic data of particular sector of the economy, cash flow forecast and long term profitability of taxpayers.

Figure 1.22 Taxpayer Compliance Risks by Tax Domain and Tax Type

ID	Tax Domain	Risk Description	CIT	PIT	VAT/GST	RPT	Excise and Other
	Registration						
	Filing						
	Reporting/Declaration						
	Payment						



Risk Evaluation Steps

2.7 COMPLIANCERISK PRIORITIZATION

Risk prioritization is the ranking of risks in terms of likelihood and consequences and determining which risks pose the greatest threats to revenue collection and deciding which risks shoud be treated subject to available resources. In practice, the prioritization requires the consequences and likelihood assessments to be brought together in linear pairing in an attempt to determine a relative rating (severity) of the risks. The likelihood – consequence matrix has twenty five (5 x 5) possibilities. Each likelihood is paired with all possible consequence and vice versa. The worst possible scenario is when a risk that is almost

certain to occur has an extremely high revenue loss. Registration risk related to taxpayers in the informal sector falls in this category. For example, this scenario also occurs when large taxpayers are actively engaged in tax fraud or when a large proportion of micro, small and medium taxpayers are not registered. On the other hand, the least harmful state is where a risk which is rare to occur has a low impact on revenue collection. For instance, this scenario occurs when a taxpayer or taxpayer group who are compliant and their total contribution to revenue collection is insignificant.

Having established the characteristics of the risks, prioritization involves selection criteria (impact on revenue, RA objectives, government policy and public opinion, discussed above) which inform consequences and likelihood (the chance that the risk materializes) as well as ranking through a standard risk rating matrix. To further buttress the answers on 'why they are doing it' which facilitates treatment of the risks, motivations behind taxpayer's behavior must be assessed. Those risks with the highest scores on the selection criteria are accorded the highest priority ranking for treatment purposes and allocation of resources.

Many software-based data mining tools are now available formeasuring likelihood (probabilities) and consequence(impact) of risk based on scenario simulation using real world data. In the absence of detailed reliable taxpayer data, approximations may be used to develop a ranking matrix. Likelihood measures are: 1-Rare, 2-Unlikely, 3-Possible, 4-Likely, 5-Almost certain and consequence measures are: 1- Low, 2-Medium, 3-High, 4-Very high, 5-Extreme.These two criteria are juxtaposed by way of a risk rating matrix to arrive at a priority ranking on the scale: Severe, High, Significant, Low and Negligible.

A risk which is likely to occur and has high impact on revenue collection is considered as severe risk. On the other hand, a risk which is rare to occur but has a high impact on revenue collection is considered as high risk. Any combination of likelihood and consequence measures can be assessed to derive the likely effect on an RA's objectives. Prioritization of risks is the first best step to taking proactive measures to treat risks that pose the greatest threats to objectives and survival of RAs. Risk prioritization must be an evidence-based process that includes both quantitative and qualitative measures.

Figure 1.23 Risk Prioritization Matrix

Consequence	Extreme	High	High	Severe	Severe	Severe
	Very high	High	High	High	Severe	Severe
	High	Significant	High	High	Severe	Severe
	Medium	Low	Significant	High	High	Severe
	Low	Negligible	Low	Significant	High	High

		Rare	Unlikely	Possible	Likely	Almost certain
	Likelihood					

It might be tempting to think that classification of identified risks according to a carefully constructed risk rating matrix is the end of the risk management process. However, such confidence would be premature: risk prioritization cannot be reduced to an objective, mathematical science. The initial rating must be revisited and confirmed following consideration of other relevant, perhaps contextual and qualitative issues. In addition, compliance risk management is an iterative process and any one step in the process is influenced by other steps. The context of organizations continually changes. This will lead to changes in risks. Some risks maychange and new risks may emerge.

The likelihood and consequence measures permit the ranking of risks so that the extreme cases characterized by “Almost Certain Likelihood”and “Extreme Consequence” would constitute the highest priority, going diagonally by order of priority to“Rare Likelihood” and“Low Consequence”.

The results of risk prioritization permit a further characterization by risk type which in turn leads to apportioning responsibility within the structure of RAs. Headline risks and risks with extreme priority take on a strategic character affecting the entire RA and therefore requiring immediate treatment and monitoring at the highest level, the Board and Commissioner General. The next tier pertains to sectoral risks that require the attention of departmental heads, while those risks at the case-by-case level demand corrective interventions at the divisional and operational levels. The desired outcomes, strategies and monitoring framework that facilitate the treatment of risks at various levels are discussed after a greater insight into the behavior of taxpayers related to the prioritized risks.

2.7.1 PRIORITIZATION OF REGISTRATION RISKS

Registration risks can be prioritized by matching the likelihood that taxpayers will be unregistered or incorrectly registered against the possible consequence on revenue collection and then determining which combinations posed the greatest filing risks based on the probability of risk occurring and the consequence if the risk occurs. Registration risks should be prioritized for taxpayers that are likely to be unregistered and have high revenue loss. Even though the consequence of revenue loss from large taxpayers is extremely high, the likelihood that a large taxpayer will be unregistered will be rare. On the other hand, it is likely that micro, small, medium and startup businesses will not be registered but as an individual taxpayer, the revenue loss may be low but when the total informal sector is taken into consideration, the revenue loss will be extremely high. That is why RAs in West Africa should pay keen attention to registration risks posed by micro, small, medium and startup

businesses. Likewise, registration risk is more likely to occur among property tax but on an individual basis, the consequence on revenue loss is low. However, because property tax represents a large percentage of tax base, registration risk among property tax may be assessed as high. The same is true with personal income tax, goods and services tax (value added tax) and capital gains tax.

2.7.2 PRIORITIZATION OF FILING RISKS

Filing risks can be prioritized by matching each likelihood that taxpayers will not file on time or may not file at all against the possible consequence on revenue collection and determining the combinations that pose the greatest filing risks to RAs based on the evaluation of likelihood of risk occurring and the consequence if the risk occurs.

Filing risk is more likely to occur among small, medium and startup businesses and the corresponding consequence on revenue collection could be high. Therefore, these businesses posed the greatest filing risks to RAs in West Africa where a large percentage of them operate in the informal sector. Filing risk is also likely to occur among individual natural persons and the impact on revenue collection is also high. Tax types among which filing risk is likely to occur include goods and services tax (value added tax) and capital gains tax.

2.7.3 PRIORITIZATION OF REPORTING RISKS

Reporting risks can be prioritized by matching each likelihood that taxpayers will falsely report income and expenses against the potential consequence on revenue collection and determining the combinations that pose the greatest reporting risk to RAs based on evaluation of likelihood of risk occurring and the consequence if the risk occurs.

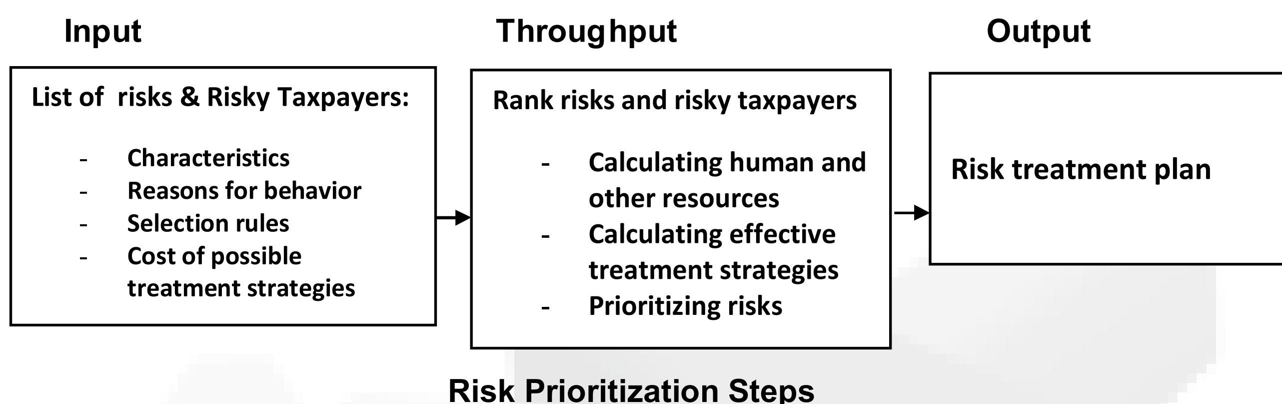
Reporting risk is likely to occur among taxpayers operating in complex industries such as natural resource, telecom, financial services and manufacturing. The consequence on revenue collection is also high. Thus, reporting risk is extremely high among taxpayers operating in these industries. Reporting risk is also likely to occur among taxpayers who take excessive risk for purposes of obtaining financial gains. Reporting risk is more likely to occur among micro, small, medium and startup businesses and the consequence on revenue is also correspondingly high. Micro, small, medium and startup businesses pose significant reporting risks to RAs in West Africa.

2.7.4 PRIORITIZATION OF PAYMENT RISKS

Payment risks can be prioritized by matching each likelihood that taxpayers will not pay their full amount of taxes payable when due or will not pay at all against the potential consequence on revenue collection and determining the combinations that pose the

greatest payment risks to RAs based on evaluation of likelihood of risk occurring and the consequence if the risk occurs.

Payment risk is likely to occur among taxpayers having cash flow problems. RAs must pay keen attention to payment risks relating to large taxpayers and tax types that are susceptible to cyclical changes. Retail and startup businesses have high likelihood of payment risks occurring but the consequence on revenue may be low. Real property, goods and services tax (value added tax) and personal income tax have high probability of payment risks and theconsequence on revenue could be extremely high.



Risk Prioritization Steps

2.8 COMPLIANCERISK TREATMENT

Compliance risk treatment refers to specific actions and strategies taken by RAs to mitigate the potential likelihood and consequences of risks by reducing the likelihood of risk occuring or impact if the risk occurs or both. Very often an optimum result is gained with the combination of risk treatments. This is the kernel of risk management: knowing how to allocate resources in the most efficient way to get an optimal result. Compliance risk treament involves specifically addressing the 5WHs questions: (1) What is happening?; (2) When is it happening?; (3) Where is it heppening?; (4) Who is doing it?; (5) Why are they doing it?; and (6) How are they doing it?

There are generally four risk treatment strategies:

- Risk avoidance (mitigation) strategy means RAs do not undertake any activity or make any decision which poses the risk;
- Risk transfer (sharing) strategy means that the activity that poses risks is transferred to a third party;
- Risk acceptance (retention) strategy means RAs undertake the activity which poses risk by informed decisions; and

- Risk covering (reduction) strategy means RAs take steps to reduce the likelihood or consequences of specific risk.

Decisions about which risks to treat and which to monitor will potentially be determined by the following:

- Internal capability of RAs
- Availability of effective treatment strategy
- Availability of effective capability to implement the treatment
- Risk rating and risk level
- The rate of risk migration or risk rating deterioration
- The current return of treatment (recover revenue this year)
- The ongoing return of treatment (recover revenue in every year into the future)
- Public perceptions of administration around the risk
- The cost and benefits of proposed treatments
- The wider context of the risks as a group

The ideal treatment option depends on the location of the taxpayer on the spectrum of the compliance pyramid. Clearly, provision of help and advice is not appropriate to a fraudster, nor is full investigation for a compliant taxpayer. Risk reduction is possible in a number of ways:

- Limiting opportunities
- Reducing unintentional errors
- Reducing intentional errors.

Limiting opportunities means making it impossible to make mistakes:

- Legislation – simplify, assist, inform, discuss, amend, standard allowances, thresholds, authorization, special schemes, etc.
- Technical solutions - filing electronic tax return, validity checks,etc.
- Consultation and agreements – with tax practitioners, relevant sectors, individual taxpayers, etc.

Reducing unintentional errors means making it difficult to make mistakes:

- Understandable legislation and tax forms – clear legislations, simplify tax forms, consistency in elements, pre-filled tax forms, etc.
- Information and guidance – accessible and understandable support information, public notices, media campaigns, advance ruling, etc.

- Encouragement and support – easy contacts such as website, telephone, help desk office; helping hand; etc.

Reducing intentional errors means making it risky to make mistakes:

- Increasing perceived probability of detection
- Creating a third party interest
- Written contract
- Contact by telephone
- Invitation for voluntary disclosure
- Partial desk test/examination
- Complete desk test/examination
- Desk audit
- On site visits
- Partial audit
- Full audit
- Criminal investigation and prosecution.

Organizational risk factors –Internal conditions and constraints sometimes pose significant compliance risks to RAs. The following are some of the conditions that limit the ability of RAs to effectively adminsiter tax legislations:

- Lack of human resource capacity and skills
- Lack of efficiency and effectiveness in the processes and procedures
- Lack of clear lines of communication and responsibility of key stakeholders
- Inadequate IT infrastructure and IT skills
- Failure to identify severe risks and inappropriate strategies
- Internal communication breakdown among key stakeholders
- Bad leadership – no tone at the top
- Lack of adequate staff incentives and welfare package
- Inappropriate behavior – staff corruption, fraud, bad attitude towards taxpayers. etc.

RAs must apply proactive risk treatment strategies that facilitate an effective compliance risk management:

- Build confidence
- Act with fairness and integrity
- Deal with taxpayers and issues directly, respectfully and fairly
- Pursue a flexible and customized approach
- Make taxpayers' obligations clear
- Make it easy to comply
- Exercise sanctions when appropriate
- Make power, authority, responsibility and activity visible
- Provide incentives

- Bolster integrity through identifier, withholding and reporting systems
- Promote effective record -keeping
- Promote openness and accountability
- Build partnerships
- Escalate severity of enforcement
- Take actions that are consistent with words (talk the talk and walk the talk). etc.

2.8.1 TREATMENT OF REGISTRATION RISKS

Registration risks constitute the greatest tax compliance risks to RAs in West Africa[16]. Registration risks can be treated based on a clear understanding of the nature and elements of risks: The 5WHs (What, When, Where, Who, Why and How) and the resources available to RAs. Analysis, evalaution and prioritization of risks assistRAs to clearly understand the motivation, severity and priority of each risk. This helps RAs take appropriate measures to treat risks in the most cost efficient manner. Registration risks can be divided into two categories: (1) Those taxpayers that are required toregister but are not registered and (2) those taxpayers that are registered but are not properly registered in the tax database.

Registration risks can be treated based on taxpayer segmentation, taxpayer type, tax type, taxpayer location and taxpayer industry classification. A large percentage of unregistered taxppayers in West Africa operate in the informal sectors and are largely micro, small and medium size businesses. As stated in the registration risk analysis, the only two possibilities for taxpayers to be unregistered are ignorance of the tax legislations and deliberate tax evasion. Ignorance of the law can be attributed to lack of tax education and poor visibility of RAs' services. When the compliance cost to taxpayers is high, the probability of non-compliance will correspondingly be high. On the other hand, registration risks due to improper taxpayer registration can be attributed to lack of staff skills, lack of complete taxpayer information, lack of supervision of data entry staff or lack of appropriate reviews of tax accounts before they are permanently saved in the tax database.

Registration risks due to deliberate fraud can be attributed to weaknesses in the tax legislations to criminalize and prosecute violators, lack of robust taxpayer compliance program or lack of resources and capacity for RAs to comprehensively administer tax legislations. Many tax legislations in the West African subregion lack proper mechanisms to criminalize and prosecute taxpayers who refused to register. At the same time, West African RAs lack adequate human capacity and financial resources to institute and implement a robust compliance risk management program. A major treatment of registration risks related to micro, small, medium and startup business enterprises is through directed and frequent tax education program and a simplified registration requirements and forms that facilitate compliance. Some RAs have adopted mobile registration of micro, small and medium size businesses operating in the informal sector. This constitutes a proactive step to

[16]TADAT assessment of RAs in West Africa.

reach out and register taxpayers that consider registration as a compliance cost and lack the knowledge as to who and where to register.

Figure 1.24 Key Registration Risks and Likely Treatment Strategies

Registration risks	Likely reasons	Possible treatments
Taxpayers required to register but are not registered	Lack of tax education to create awarenessabout who, where and how to to register	Conduct tax education of high risk taxpayers, tax segment and geographical location
	Poor visibility of RA's services such as tax office, technology such internet availability	Create visibility through tax offices, mobile tax registration and online registration services
	Lack of robust CRM to effectively identify and deal with risks	Institute and implement robust CRM program that proactively identify and deal with registration risks
	Deliberate tax evasion	Strenghten existing laws and create disincentives through prosecution and hash penalties
Taxpayers registered are not properly registered in the taxpayer database	Incomplete taxpayer information	Simplify registration requirements and forms and provide opportunity for stages of registration
	Lack of supervision and review of data entry staff	Provide timely supervision and review of data entry staff
	Lack of appropriate layers of review of data before accounts are permanently saved	Provide a minimum of two layers of reviews of data entered into the taxpayer database
	Lack of skills and competencies of data entry staff	Provide training and job skills to data entry staff and create opportunity for pre-filled fields

2.8.2 TREATMENT OF FILING RISKS

Filing risks can be treated by addressing the reasonsgiving rise tothe risks. Understanding the reasons for any riskis the basic first step for giving appropriate treatment to the risk. Filing risks for small, medium size and startup businesses can be attributed to either high compliance costs, complexity of filing forms, lack of appropriate education or any combinations of these. Filing risks for large business enterprises can be largely attributed to deliberate and willful attempt to circumvent tax legislations. Filing risks for natural persons are commonly due to lack of education and the high compliance costs. Filing risks can also be due to lack of visibility of RA's services such as lack of b usiness office or the lack of appropriate technology to facilitate filing.

Filing risks ralated to stop-filers and nonfilers are commonly due to taxpayers going out of business, high compliance costs or deliberate attempt to violate tax legislations. Taxpayers who are not registered in the tax database are most likely to be nonfilers.

Figure 1.25Key Filing Risks and Likely Treatment Strategies

Filing risks	Likely reasons	Possible treatments
Late filing	High compliance costs required for taxpayers to prepare and submit returns	Reduce compliance costs through liberalization of services
	Complexity of filing forms that inhibit timely preparation and presentation of returns	Simplify tax return forms and synchronize forms to reduce the number of forms
	Poor visibility of services such as tax office and technology	Create visibility through tax offices and online filing services
Stop-filing	Taxpayer gone out of business	Validate nonexistence of taxpayers and remove from taxpayer database
	Taxpayer changed business name for purposes of tax evasion	Locate and penalize taxpayers. Make it difficult for existing businesses to reregister as new businesses by matching beneficial owners, directors, management, etc.
	High compliance costs required for taxpayers to prepare and submit returns	Reduce compliance costs through liberalization of services
	Complexity of filing forms that inhibit timely preparation and presentation of returns	Simplify tax return forms and synchronize forms to reduce the number of forms
	Poor visibility of RA's services such as tax office	Create visibility through tax offices and online filing

Filing risks	Likely reasons	Possible treatments
	and technology	services
	Deliberate failure to file for purposes of tax evasion	Create disincentives through prosecution and hash penalties for noncompliance
Nonfiling	Lack of tax education to create awareness of requirement to timely file	Create awareness through tax education of key taxpayer groups and sectors
	High compliance costs required for taxpayers to prepare and submit returns	Reduce compliance costs through liberalization of services
	Complexity of filing forms that inhibit timely preparation and presentation of returns	Simplify tax return forms and synchronize forms to reduce the number of forms
	Poor visibility of RA's services such as tax office and technology	Create visibility through tax offices and online filing services
	Deliberate failure to file for purposes of tax evasion	Create disincentives through prosecution and hash penalties for noncompliance

2.8.3 TREATMENT OF REPORTING RISKS

Reporting risks can be treated by making it difficult (reducing the likelihood) for taxpayers to falsely report income and expenses, increasing likelihood of detection or penalizing taxpayers that deliberately manipulate taxable profits. Reporting risks are most common among startup businesses, taxpayers operating in complex industries and taxpayers experiencing cashflow problems. Reporting risks may alsobe high (other things being equal) when the economy is not performing and businesses are not making sufficient incomes to cover their costs. Large size businesses are more likely than not to misrepresent taxable profits than small and medium size businesses. Taxpayers are more likely to falsely report direct taxes than they will with indirect taxes. However, for the fact that most indirect taxes are correlated to direct taxes, there is always an incentive to falsely report both direct and indirect taxes.

Reporting risks can generally be classified as either intentional or unintentional misrepersentation of taxable profits. Reproting risks due to unintentional misrepresentation of taxable profits are commonly due to complexity of tax legislations, unintentional calculation errors and lack of tax of expertise to collate and present tax information.

Figure 1.26 Key Reporting Risks and Likely Treatment Strategies

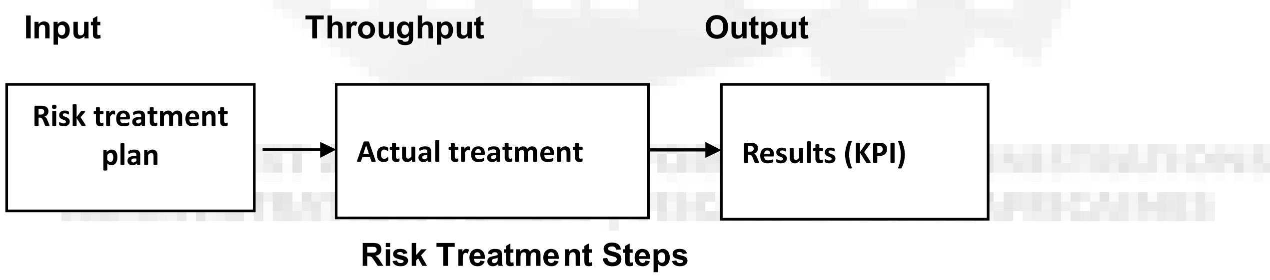
Reporting risks	Likely reasons	Possible treatments
Unintentional misrepresentation of taxable profits	Misrepresentation due to complexity and/or ambiguity of tax legislations	Simplify tax legislations andtax forms
	Lack of expertise to collate and accurately report taxable profits	Conduct tax clinics for specific taxpayers and sectors with high risks of reporting risks
	Unintentional errors due to calculation of numbers or misapplications of tax legislations	Make it difficult to make mistakes through prefilled forms and simplify tax legislations and forms
Intentional misrepresentation of taxable profits	Intentional misstatement of taxable profits through misrepersentation of income and expenses	Create disincentives through fines, penalties and prosecution
	Intentional misrepresentation of taxable profits through misapplication of tax legislations	Create disincentives through fines, penalties and prosecution

2.8.4 TREATMENT OF PAYMENT RISKS

Payment risks can be treated by reducing the likelihood of late payment (or nonpayment) of taxes and the consequence on total revenue collection. Late payment risks are most common among small, medium size and startup businesses than they are for large taxpayers. Likewise, payment risks are higher for taxpayers experiencing cash flows and during bad economic period than otherwise. Payment risks can be divided into two categories: (1) late payment and (2) nonpayment of taxes. Large taxpayers are likely to fall in the first category than in the second category. On the other hand, small, medium size and startup businesses are liekly to fall in the second category than in the first category.Tax types that are at high payment risks are personal income tax, goods and services tax (value added tax) and capital gains tax.

Figure 1.27Key Payment Risks and Likely Treatment Strategies

Payment risks	Likely reasons	Possible treatments
Late payment of taxes	Taxpayer is experiencing cash flow problems	Make payment plans and/or stipualations with taxpayer
	Poor visibility of services such as tax office and technology	Create visibility through tax offices and online payment services
	Deliberate failure to pay taxes for purposes of tax evasion	Create disincentives through prosecution and hash penalties for noncompliance
	Technical issues that prevent taxpayers from paying taxes on due dates	Work with taxpayers to resolve such technical issues
Nonpayment of taxes	Lack of tax education to create awareness and obligation to pay taxes	Conduct tax education of high risk taxpayers, tax segment and geographical location
	Poor visibility of services such as tax office, technology	Create visibility through tax offices, mobile and online payment services
	Taxpayer is experiencing cash flow problems	Make installment payment plans and/or stipulations with taxpayer
	Deliberate failure to pay taxes for purposes of tax evasion	Create disincentives through prosecution and hash penalties for non-compliance



Risk Treatment Steps

2.9 COMPLIANCE RISK MONITORING AND REVIEW

Compliance risk monitoring is a continual check to determine the suitability, adequacy and effectiveness of risk treatment strategies.Monitoring can be applied as a risk management framework, risk management process or risk management control. It is important to note that risk treatment strategies may lead to new risks. For example, reputational risk posed by

the transfer of a function to a third party. There should be periodic review of performance to appraise accountability and responsibility of all stakeholders. The results of risk monitoring and review are fed back into the risk management continuous loop and the cycle of risk identification through to risk treatment revolves.

2.10 COMMUNICATION AND CONSULTATION

Throughout the risk management process, internal and external communication and consultation with relevant stakeholders is important for effective compliance risk management. Internally, risk and control information should be communicated with responsible parties to help them make informed decisions in carrying out their responsibilities. Consultation with external stakeholders helps to get their involvement and participation in the risk identification and possible treatment strategies.

3.0 ESTABLISHING A COMPLIANCE RISK MANAGEMENT PROGRAM

Compliance risk management has its own common set of assumptions, concepts, principles, standards, practices , protocols and tools that together form the compliance risk management discipline. It is imperative for RAs and risk management practitioners to understand and use these fundamental tenets in their practice of risk management.A compliance risk management system is a series of coordinated organizational arrangements, structures, relationships, processes and procedures that are designed and embedded into the organization's strategic and operatio nal policies and practices.

3.1 COMPLIANCE RISK MANAGEMENT PRINCIPLES

The principles of risk management provide a sound basis (intention and purpose) for establishing and implementing an effective compliance risk management system. The Institute of Global Risk Management (G31000) has established the following compliance risk management principles:

- Compliance risk management creates and protects value – Compliance risk management should contribute to the demonstrable achievement of objectives and improvement of performance in, for example, tax compliance, human health and safety, security, legal and regulatory compliance, public acceptance, environmental protection, product quality, project management; efficiency in operations, corporate governance and reputation.

- Compliance risk management is an integral part of all organizational processes – Compliance risk management should not be a stand-alone activity that is separate from the main activities and processes of RAs. Risk management is part of the

responsibilities of management and an integral part of all organizational processes, including strategic planning, project management and change management processes.

- Compliance risk management is part of decision-making – Compliance risk management should help decision makers make informed choices, prioritize actions and distinguish among alternative courses of actions.

- Compliance risk management explicitly addresses uncertainty – Compliance risk management should explicitly take account of uncertainty, the nature of that uncertainty and how it can be addressed.

- Compliance risk management is systematic, structured and timely – Compliance risk management should be a systematic, structured and timely approach to dealing with internal and external threats and vulnerabilities to the organization's objectives and should contribute to efficiency, consistent, comparable and reliable results.

- Compliance risk management is based on the best available information – The inputs to compliance risk management process are based on information sources such as historical data, experience, stakeholders' feedback, observa tions, forecasts and expert judgement. However, decision makers should be aware of and take into account any limitations of the data or modelling used or the possibility of divergence among experts.

- Compliance risk management is transparent and inclusive – Appropriate, full and timely involvement of all stakeholders and in particular, decision makers at all levels within and outside of the organization is required to ensure that risk management remains relevant and up-to-date. Involvement also allows stakeholders to be properly represented, informed and to have their views taken into account in determining risk criteria and risk treatments.

- Compliance risk management is tailored – Compliance risk management should be aligned with the organization's internal and external contexts and risk profile.

- Compliance risk management is dynamic, iterative and responsive to change – Compliance risk management should continually sense and respond to change. As external and internal events occur, context and knowledge change, monitoring and review of compliance risk take place, new risks emerge, some change and others disappear.

- Compliance risk management facilitates continual improvement of the RAs – RAs should develop and implement strategies to improve their risk management maturity alongside all other aspects of their organizations.

3.2 COMPLIANCE RISK MANAGEMENT FRAMEWORK

While the principles provide the bases for establishing and implementing effective compliance risk management system, the framework provides the system and structure that are integrated into the RA's policies, processes and procedures. The framework consists of architecture, strategy, protocols and tools.

Compliance risk management framework has four inter-related stages:

1. Plan:

    - Identify intended benefits of compliance risk management initiatives and gain board support
    - Plan the scope of compliance risk management initiatives and develop common language of risk
    - Establish common compliance risk management strategy, framework and roles and responsibilities.

2. Implement:

    - Adopt suitable compliance risk management tools and an agreed risk classification system
    - Establish risk benchmark (risk criteria) and undertake risk assessment
    - Determine risk appetite and risk tolerance levels and evaluate the existing controls.

3. Measure:

    - Evaluate effectiveness of existing controls and introduce improvements
    - Embed risk-awareness culture and align compliance risk management with other activities in the organization.

4. Learn:

- Monitor and review risk performance indicators to measure compliance risk management contribution
- Report risk performance in line with obligations and monitor improvement.

3.2.1 COMPLIANCE RISKMANAGEMENT ARCHITECTURE

Compliance risk management architecture consists of the following elements:

- Committee and terms of reference – There should be structured risk governing bodies at the board and executive management levels to provide oversight, direction and supervision over compliance risk management.
- Roles and responsibilities – There should be clear roles and responsibilities for all responsible parties in the compliance risk management process.
- Internal reporting requirements – Management and board should establish clear reporting requirement and responsibility for individuals to provide accountability of their actions and use of resources.
- External reporting controls – There should be clear controls in place for disseminating information to outside parties subject to confidentiality and data privacy policies.
- Compliance risk management assurance arrangement – The board and executive management should establish a system that provides independent check and assurance on the adequacy and effectiveness of the compliance risk management process.

3.2.2 COMPLIANCE RISKMANAGEMENT STRATEGY

Compliance risk management strategy consists of the following elements:

- Risk management philosophy – The board and executive management should form a system of shared beliefs and attitudes that characterize how compliance risks and compliance risk management are viewed in the organization.
- Arrangements for embedding compliance risk management – Compliance risk management should be embedded into the RA's processes, procedures, activities and responsibilities.

- Compliance risk appetite and risk attitude – The board and executive management should set and communicate the organization's compliance risk appetite (the level of risk) that the organization is willing to accept and risk attitude (behavior) toward risk.
- Benchmark tests for significance – The compliance risk management policy and strategy should have thresholds for determining the significance and severity of risks.
- Specific risk statements and policies – The compliance risk management framework should have rules for specific risk categories.
- Compliance risk assessment techniques – The compliance risk management framework should have established methodologies for compliance risk identification, analysis and evaluation.
- Compliance risk priorities for the present year – The board and executive management should set and communicate compliance risk management priorities for each year.

3.2.3 RISK MANAGEMENT PROTOCOLS

Compliance risk management protocols consist of the following elements:

- Tools and techniques – RAs should have appropriate risk management tools, for example, computer software applications, data mining tools and common techniques.
- Compliance risk classification system – RAs should establish common risk classification system based on the nature and severity of risks.
- Compliance risk assessment procedures – RAs should establish common risk assessment procedures such as data analysis, interviews, questionnaires, surveys, focus group, research, etc.
- Compliance risk control rules and procedures – Compliance risk management polices should establish control rules and procedures for carrying out risk treatments.
- Responding to incidents, issues and events – There should be clear to-do-list of activities to perform in case of emergencies, etc.
- Documentation and record keeping – Compliance management policy should establish the nature and form of documents and records to be maintained in electronic or manual form.

- Training and communication – Staff at all levels of RAs should have periodic compliance risk management training. Important compliance risk management tips and messages should be communicated to all staff within the organization on a regular basis.
- Audit and assurance procedures and protocols – Compliance risk management system should have clear documented audit trail and procedures for audit and assurance purposes.
- Reporting, disclosures and certification – RAs should have documented reporting and disclosure policies. Compliance risk management certification at the entity and individual levels is important.

3.2.4 COMPLIANCE RISK MANAGEMENT TOOLS

The fundamental tool to compliance risk management is the human capacity with the competences, expertise and risk-awareness culture. Every risk management tool is useful in so far as there is accompanying knowledge, skills, awareness and competences to adopt and use those tools. A large proportion of compliance risk is identified, analyzed and treated through human interactions. RAs therefore need personnel with the right knowledge, skills and attitude to effectively manage risk . The lack of such knowledge, skills and attitude poses potential risk to RAs.

Compliance risk management is based on information science (data, information and intelligence) and the creation and use of information is an essential tool for compliance risk management. Another fundamental tool for compliance risk management is a database – a data warehouse and data extraction and analysis tools and techniques to analyze, translate and effectively use taxpayers information.

There are many bespoke and off-the-shelf data extraction and analysis software available for use in compliance risk management. RAs need to build data warehouse that seamlessly interfaces all data across the organization to enable data mining, matching and logical manipulations.

3.3 COMPLIANCE RISKMANAGEMENT POLICIES AND GUIDELINES

West African RAs need to develop a common compliance risk management language that is consistent across institutions and countries. The role of compliance risk management policy is to lay the foundation for such common language. A compliance risk management policy is

a statement of overall intentions, direction and scope of compliance risk management initiatives[17].

A compliance risk management guideline specifies the step-by-step procedure for the interpretation and implementation of compliance risk management policies. Guidelines define the implementation modalities of policies and a logical classification and proposition that are actionable within the context of RAs.

A compliance risk register[18] is a tool for capturing compliance risks and actions to manage each compliance risk. The register must be regularly updated to add new risks and remove risks that no longer exist. The risk register is a summary of the compliance risk management process use to continually monitor risks and events in the internal and external environments.

Figure 1.28 Sample of Compliance Risk Register

Compliance Risk Register							
Risk ID	**Date identified**	**Risk description**	**Likelihood of risk occuring**	**Impact if risk occures**	**Severity of risk**	**Risk owner**	**Risk treatment strategies**
102	April 5, 2017	Incomplete tax returns filing by many start-ups	High	High	Severe	Taxpayer Services	Tax education
146	Aug. 27, 2018	Tax returns not thoroughly analyzed	Medium	High	High	Human Resource Services	Data analytics training for analysts
76	July 20, 2018	Multiple TINs for taxpayers on the tax register.	Low	Medium	High	Special Project Team	Data Cleansing Project

3.4 RECOMMENDED LESSONS FOR REVENUE AUTHORITIES

[17] Adopted from Global Risk Management Institute

[18] OECD Compliance Risk Register

RAs must allocate limited resources in the mostcost efficient ways to optimize results in the midst of internal and external influences. They must assess and treat risks to the achievement of objectives using a systematic and disciplined approach. Compliance risk management helps management make informed decisions and provides assurance that objectives are being achieved[19]. The following principles are important lessons for RAs to implement in their effort to instill and improve voluntary compliance with the tax laws:

- RAs must establish compliance risk management system which provides reasonable assurance that objectives are being achieved.
- Compliance risk management provides a structured basis for strategic thinking with a focus on key drivers of performance.
- RAs must understand the reasons for non-compliance behavior and promote diversity in the treatments of compliance risks.
- Compliance risk management provides better outcomes and improves compliance with tax laws, leading to increased tax collections and improved taxpayer service.
- Compliance risk management provides a stronger foundation for evidence-based evaluation of taxpayers compliance with tax legislations.
- RAs must have clear documented compliance risk management policies, processes and procedures.
- RAs must use appropriate tools, techniques and protocols that are necessary for effective risk management.
- RAs must maintain a register of all risks and have clear treatment strategy for each risk and update the register as changes occur in the internal and external environment.
- Successful RAs are those with the greatest proportion of voluntary compliance.
- RAs must have clear description of roles and responsibilities in their risk management process.
- RAs must understand economic and psychological drivers of taxpayers' compliance behavior.
- Tax laws must be clear and unambiguous in regards to their intent and interpretation.

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[19] Recommended lessons espoused by OECD

- RAs must be perceived as being fair in administering the laws to sustain confidence in the tax system and its administration.
- Embedding risk management in tax administration and the use of intelligence framework provide new opportunities for RAs to increase compliance with tax legislations.
- RAs must establish data warehouse that seamlessly interfaces all data across the organization and use appropriate data extraction, analysis and matching tools and techniques to understand and make effective use of data.
- RAs must hire and retain appropriate human resource capacity with the appropriate competences, expertise, knowledge, skills and risk-awareness culture to effectively manage risks to objectives.
- Risk and control information must be communicated to appropriate persons or group of persons to help them make informed decision in carrying out their responsibilities.
- Compliance risk management should be inclusive and involve the participation of everyone in RAs.
- Staff at all levels of RAs must have periodic risk management training. Important risk management tips and messages must be communicated to all staff within the organization on a regular basis.
- The board and executive management must form and promote a system of shared beliefs, vision and attitudes that characterize how risks and risk management are viewed in RAs.

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