

PRIORITY CHECKLISTS  
STANDARDS AND INSTRUMENTS  
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GOOD PRACTICES  
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MEASURING EFFECTIVENESS

**CleanGovBiz**  
Integrity in practice

## Tax administration: detecting corruption

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The CleanGovBiz Initiative supports governments, business and civil society in their efforts to build integrity and fight corruption. The initiative draws together existing instruments, reinforces their implementation, improves co-ordination among relevant players and monitors progress towards integrity.

The CleanGovBiz toolkit provides guidance on how corruption can best be tackled in different policy areas and offers access to relevant standards and instruments.

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## Tax administration: detecting corruption

Tax policy is often used to encourage or discourage certain behaviours and countering corruption is no exception. Similarly, tax administrations are increasingly involved not only in enforcing tax measures but also in the detection of possible crimes, particularly financial crimes. Why? Tax examiners are highly trained financial investigators and thousands of tax inspectors around the world routinely examine the financial affairs and transactions of millions of individuals, companies, partnerships, trusts, foundations and other taxpayers in the course of tax audits or other tax administration activities. They are thus ideally placed to detect and report suspicions of criminal activity such as payments of bribes to the appropriate authorities.

Countries have taken a range of tax related measures to strengthen both the legal framework and the practical administrative efforts to counter corruption. Where possible, a multi-agency approach to fight tax crimes, bribery and other crimes is an efficient option. The combined effect of the tax policy and administration steps described below is increased deterrence, detection, reporting and prosecution of corrupt activities.

## Priority checklist

1. Do tax systems explicitly **disallow tax deductions** for bribes to public officials?
2. Do **tax administrations raise awareness among taxpayers that bribes are not deductible?** Is this message disseminated through regular contacts with tax advisors and accountancy firms, through the organisation's website or other communications tools?
3. Do tax authorities **include corruption in their risk assessment and audit processes** and encourage tax examiners to carry out relevant **compliance checks?**
4. Do tax administrations provide **guidance and training to tax examiners** as to the types of payments that are deemed to constitute bribes and the actions to take when they suspect a bribe has been paid?
5. Are tax authorities authorised to **report suspicions of corruption** to the appropriate domestic law enforcement authorities?
6. Do tax administrations provide **guidance to tax examiners to facilitate reporting of suspicions of foreign bribery** arising out of the performance of their duties to the appropriate domestic law enforcement authorities?
7. Do tax treaties allow the **use of information provided by a treaty partner for tax purposes** to combat serious crimes such as corruption under certain circumstances?
8. Do tax authorities **use tax information sharing agreements** with other countries to obtain and provide information to determine whether a deducted payment constitutes a bribe?

## Implementation guidance

### 1. Do tax systems explicitly disallow tax deductions for bribes to public officials?

Tax systems should not condone the criminal conduct involved in bribery and corruption. Having explicit legislation to prohibit the tax deductibility of bribes increases the overall awareness within the business community of the illegality of bribing public officials and increases the cost of doing so. It sends a strong signal to the senior management of companies, corporate accountants and more generally to the accounting profession that bribes are not to be considered as ordinary deductible business expenses.

The 2009 OECD Recommendation of the Council on Tax Measures for further Combating Bribery of Foreign Public Officials in International Business Transactions recommends the non tax deductibility of bribes . Explicit legislation can also help businesses refuse solicitations from public officials to pay bribes in order to get a contract. In Norway, for example, the deductibility of bribes was expressly prohibited in 1995 and representatives from large Norwegian companies have confirmed that they are now very cautious about tracking all company disbursements when conducting business abroad. Explicit legislation also increases the overall awareness of the tax administration and in particular tax examiners during tax audits of the need to detect and disallow deductions for payments of bribes to foreign public officials in international business transactions and to report suspicious payments to the appropriate domestic law enforcement authorities in order to prosecute bribery.

### **Examples of Legislation Prohibiting Deductions for Bribes**

#### **Japan**

Corporation Tax Law: Paragraph 5 of Article 55

“The amount of bribes (as specified in the Criminal Law and Unfair Competition Prevention Law) paid by a company to a domestic or foreign public official shall not be treated as deductible expenses when calculating that company’s taxable income.”

Income Tax Law: Paragraph 2 of Article 45

“The amount of bribes (as specified in the Criminal Law and Unfair Competition Prevention Law) paid by an individual to a domestic or foreign public official shall not be treated as deductible expenses when calculating that individual’s taxable income.”

#### **South Africa**

Section 23 (o) of the Income Tax Act provides as follows: No deductions shall in any case be made in respect of expenses incurred: (i) where the payment of that expenditure or the agreement or offer to make that payment constitutes an activity contemplated in Chapter 2 of the Prevention and Combating of Corrupt Activities Act, 2004 (Act No. 12 of 2004); or (ii) which constitutes a fine charged or penalty imposed as a result of an unlawful activity carried out in the Republic.

## **2. Do tax administrations raise awareness among taxpayers that bribes are not deductible?**

This message can be disseminated through regular contacts with tax advisors and accountancy firms, through the organisation’s website and publications.

Tax administrations often have forums where they discuss issues with representative bodies of tax advisers and accountancy firms. These can provide opportunities for raising such issues as the non-deductibility of bribe payments. Increasingly tax administrations use their public websites to provide advice – including preventive advice. A number of tax administrations have separate website channel dedicated to professional tax agents. They also publish advice booklets often with copies available online.

### United States Example

The United States Internal Revenue Service publishes advice to businesses on business expenses and clarifies the law on bribes and kickbacks. It states:

“Bribes and kickbacks. Engaging in the payment of bribes or kickbacks is a serious criminal matter. Such activity could result in criminal prosecution. Any payments that appear to have been made, either directly or indirectly, to an official or employee of any government or an agency or instrumentality of any government are not deductible for tax purposes and are in violation of the law.

Payments paid directly or indirectly to a person in violation of any federal or state law (but only if that state law is generally enforced, defined below) that provides for a criminal penalty or for the loss of a license or privilege to engage in a trade or business are also not allowed as a deduction for tax purposes.

Meaning of ‘generally enforced’ A state law is considered generally enforced unless it is never enforced or enforced only for infamous persons or persons whose violations are extraordinarily flagrant. For example, a state law is generally enforced unless proper reporting of a violation of the law results in enforcement only under unusual circumstances.

Kickbacks. A kickback is a payment for referring a client, patient, or customer. The common kickback situation occurs when money or property is given to someone as payment for influencing a third party to purchase from, use the services of, or otherwise deal with the person who pays the kickback. In many cases, the person whose business is being sought or enjoyed by the person who pays the kickback is not aware of the payment.

For example, the Yard Corporation is in the business of repairing ships. It engages in the practice of returning 10% of the repair bills as kickbacks to the captains and chief officers of the vessels it repairs. Although this practice is considered an ordinary and necessary expense of getting business, it is clearly a violation of a state law that is generally enforced. These expenditures are not deductible for tax purposes, whether or not the owners of the shipyard are subsequently prosecuted.”

*Source:* IRS publication 535: Business Expenses

#### Australia Example

The Australian Taxation Office publishes practical guidance for businesses to help them manage their tax obligations in the area of bribes and facilitation payments. The publication “Bribes and facilitation payments: A guide to managing your tax obligations” can be found at [www.ato.gov.au/content/00104079.htm](http://www.ato.gov.au/content/00104079.htm). The guidance suggests that company boards can put in place a code of conduct across the business relating to bribes; a strong internal audit function and audit committee, and act to rectify any relevant internal control weaknesses identified and reported to the board by external auditors.

#### Ireland Example

The Irish Revenue provides on its website links with guidance from a cross-departmental initiative established to raise awareness of bribery and corruption see [www.anticorruption.ie](http://www.anticorruption.ie).

### **3. Do tax authorities include corruption in their risk assessment and audit processes and encourage tax examiners to carry out relevant compliance checks?**

As tax authorities have finite resources with which to fulfil their responsibilities they cannot audit every taxpayer or every issue. Therefore there is a need for risk assessment to be used in selecting cases for audit. Adding corruption to the risk assessment and audit process should focus tax examiners on identifying bribes during the examination of tax returns and encourage them to carry out relevant compliance checks. The education and training of tax auditors enables them to check transactions for tax assessment. These checks can also reveal indicators of criminal activities. In the process of reviewing the reality or economic justification of a transaction they can detect certain transactions which are unusual or suspicious and which may be indicative of tax evasion or bribery or other financial crime.

For example these may be fictitious deductions e.g. for alleged consultancy fees, the transfer of funds through a fictitious business, payments to a shell company or payments to entities in a non-cooperative tax haven. Bribe payments may also be disguised as payments for professional services or for travel and entertainment expenses or for salaries of fictitious employees. Such payments may eventually lead back to companies controlled by a politically exposed person (PEP).

For fictitious deductions one of the parties to corruption may open a bank account in a fictitious name as a conduit for converting checks to cash. Invoices printed in the fictitious business name are prepared as evidence of purchases. Checks issued to the fictitious business are deposited and then cash representing the bribe payment is withdrawn.

One method of indirect payments to public officials is by way of making payments to a law firm. In this instance, the lawyer acts merely as a conduit to which checks are issued for ostensible legal services rendered. The payments are deposited to the lawyer's trust accounts and disbursements made from those accounts to the public official or PEP. This method is also used through public relations, advertising, or accounting firms.

#### **Detection of the "Ivy" real estate fraud case through tax auditors in the Netherlands**

The "Ivy" real estate fraud case, the largest of its kind in the Netherlands revolves around bribery and fraudulent property deals involving dozens of construction and real estate companies as well as managers at Philips Pension Fund and the Rabo Property Fund. Over €200m were defrauded and EUR 160 million has been recovered by settlements and penalties, most of which has been returned to the aggrieved parties. It is called the Ivy case ('Klimop' in Dutch) because its tendrils spread like the plant and its roots have proven hard to find and eradicate. The case was uncovered by a tax auditor carrying out a normal audit who questioned some transactions which appeared to lack commercial reality. The methods used and the "red flags" they leave have been incorporated into awareness training for tax auditors.

**4. Do tax administrations provide guidance and training to tax examiners as to the types of payments that are deemed to constitute bribes and the actions to take when they suspect a bribe has been paid?**

Such guidance and training will sensitise examiners to the issue and enable them to better detect bribe payments, disallow any tax deductions taken for the payments and report the payments to the appropriate domestic law enforcement authorities. Guidance can be included in audit handbooks or manuals and in training programmes for auditors and examiners. The peer review examinations under the OECD Anti-Bribery Convention include checks that guidance has been provided for tax auditors.

The OECD *Bribery Awareness Handbook for Tax Examiners* provides tax examiners with information on the various bribery techniques used and the tools to detect and identify bribes. This tool has currently been translated into 18 languages, including Chinese French, German, Portuguese and Spanish and it is often used as a basis for the development of national guidelines.

Training is cascaded through tax administrations often based on a *train the trainers* seminar provided by OECD which combines awareness on money laundering and bribery. Participants learn how to teach tax examiners and tax auditors to identify possible cases of money laundering or bribery during the course of civil tax audits and examinations. They also acquire more advanced knowledge on detection techniques and additional resources to be able to give advice.

OECD *train the trainer* seminars are scheduled for 2012 to cover tax administrations in Sub-Saharan Africa, Eurasia, Latin America and Asia-Pacific and further events are being planned for subsequent years.

**OECD Bribery Awareness Handbook**

This handbook provides tax examiners with information on the various bribery techniques used and the tools to detect and identify bribes. The OECD Bribery Awareness Handbook for Tax Examiners is now available in 18 languages and is in active use in many countries: [www.oecd.org/ctp/nobribes](http://www.oecd.org/ctp/nobribes).

For more information on training: [ctp.contact@oecd.org](mailto:ctp.contact@oecd.org).

## 5. Are tax authorities authorised to report suspicions of corruption to the appropriate domestic law enforcement authorities?

Historically, information obtained by tax authorities could only be used for tax administration purposes. Domestic law generally prevents a tax administration from disclosing taxpayer-specific information to any person not directly involved in the administration of that taxpayer's tax affairs. The rationale for this policy was that it would encourage voluntary compliance with the tax laws.

More recently, with the challenges posed by the globalisation of the economy and the increasing sophistication of financial crimes, policymakers have recognised that sharing of certain tax information with law enforcement authorities can improve the detection and sanctioning of serious crimes like corruption. Countries therefore establish an effective legal and administrative framework that facilitates the reporting by tax authorities of suspicions of corruption arising out of the performance of their duties to the appropriate domestic law enforcement authority. The Oslo Dialogue is an international forum for promoting whole of government approaches to tackling economic crime. A report on models of inter-agency cooperation will be published mid 2012.

Tax administrations have established gateways between the relevant organisations to ensure that sensitive taxpayer information is exchanged securely and legally.

### **Legal gateway with police forces in UK's tax administration**

The UK's HM Revenue and Customs has a legal gateway for sharing information with the police and certain other enforcement authorities in the Anti-Terrorism, Crime and Security Act (ATCSA) 2001. This gateway allows the disclosure of information which will be used for the purposes of a criminal investigation or proceedings, or for the initiation or termination of an investigation or proceedings. If a tax examiner uncovers information about criminal activity in the course of work, they should consider disclosing it to the police through this gateway.

Relevant links: [www.hmrc.gov.uk/manuals/bimmanual/BIM43155.htm](http://www.hmrc.gov.uk/manuals/bimmanual/BIM43155.htm).

### **Horizontal intelligence centres for information exchange**

One OECD country has developed a series of intelligence centres at a national and at regional levels where officials from the tax administration, the police, the customs and other relevant agencies sit in the same room to enable instantaneous exchange of information. Each officer has access to their agency's databases and they are able to pool information into a common database for analysis. The intelligence centre has access to a wide variety of tools including tax audits and surveillance.

### **From tax evasion to bribery**

Following the discovery of tax deductions for the cost of vehicles which appeared to be for non-business use, the tax administration of an OECD country carried out a full audit of two related companies. This audit uncovered payment documents with the names of diplomatic representatives of three other countries. This audit uncovered documents that revealed payments to diplomatic representatives of three foreign countries. The companies were penalised for tax evasion and the case was reported to the prosecution authorities. The director of the two companies was subsequently found guilty of bribery of foreign public officials and received a 3-year suspended prison sentence and a substantial fine.

## **6. Do tax administrations provide guidance to tax examiners to facilitate reporting of suspicions of foreign bribery (arising out of the performance of their duties) to the appropriate domestic law enforcement authorities?**

Clear procedures setting out the circumstances under which suspicious payments may be reported to other law enforcement agencies or authorities should be provided to tax examiners. The tax examiner will pass the information on their suspicions to the relevant official in the tax administration responsible for cooperation with other law enforcement agencies.

The obligation for tax examiners to report bribes they have identified to their domestic criminal law enforcement authorities will depend on the legal system of their respective countries. In some countries the tax administration is required to

give information to police, prosecution administration and to courts when the bribe concerns a case where there is suspicion of a tax crime. In other countries this is not the case. When information is in the hands of the criminal law enforcement authorities, they may pass it on to their counterpart in another country on the basis of an international agreement on mutual judicial assistance.

The OECD [Bribery Awareness Handbook](#) provides a template form for tax examiners to report bribes identified, which can be adapted to country needs. It is useful if the tax administration sets up a monitoring system of bribes identified during tax examinations. Use of the template form would aid the gathering of information for monitoring purposes. Tax examiners could send the information collected on bribes identified in order to build a data base to be used for statistics purposes as well as for identifying trends and to assist in the audit plan.

#### **Tax office guidelines on bribery in Australia**

The Australian Taxation Office has developed guidelines for their staff based on the *OECD Bribery Awareness Handbook for Tax Examiners*. These “tax office guidelines for understanding and dealing with the bribery of Australian and foreign public officials” form part of the instruction manuals for tax staff and include instructions on referring suspicions to the police as well as useful additional information that can help in dealing with such cases. More information on the Australian tax office guidelines can be found on the website of the Australian Taxation Office: <http://www.ato.gov.au/content/81908.htm>

The Australian Tax Office advises its tax officers that if they encounter “a transaction they suspect may be a bribe to an Australian or foreign public official, it is imperative that the information be referred, at the earliest opportunity, to the Serious Non-Compliance business line.” An authorised officer in that section will seek, within the requirements of the legislation, to disseminate the information to the Australian Federal Police.

### **Tax assessment handbook in Norway**

The Norwegian Directorate for Taxes *Tax Assessment Handbook* includes provisions on corruption offences. In 2010, the Directorate also established a Working Group to provide training sessions for its tax examiners and tax lawyers on the detection of bribery and corruption. This training is based on case experiences as well as the *OECD Bribery Awareness Handbook*. Cross-departmental training also takes place and includes police and customs officers.

## **7. Do tax authorities use tax information sharing agreements with other countries to obtain and provide information to determine whether a deducted payment constitutes a bribe?**

Increasingly, financial crimes are committed using layered transactions involving offshore entities and accounts. In order to follow the financial trail, it therefore becomes necessary to **obtain information from abroad**. **There are over 3600 bilateral tax treaties worldwide, numerous bilateral tax information exchange agreements and also multilateral agreements** for administrative assistance in tax matters that can be used to obtain information from abroad. Many of these agreements can also be used to spontaneously provide information to a treaty partner about possible non-compliance with the tax law.

For example, you can imagine a tax auditor who has suspicions about a series of transactions with an offshore company and is not satisfied by answers from the taxpayer. He suspects that the offshore company may be a front for a slush fund and wants to determine whether it is a shell entity. He can make a request under the relevant treaty or convention to the jurisdiction where the entity is resident for information on the beneficial ownership of the company. This information may also be relevant to determining whether payments to that company may constitute a bribe.

### OECD Manual on Information Exchange

The Manual provides practical assistance to officials dealing with exchange of information for tax purposes and is used in designing or revising national manuals. It has been developed with the input of both member and non-member countries. It provides guidance to tax officials in carrying out exchange of information in order to improve the efficiency of such exchanges. It covers the legal bases for exchanges, clarifies the use of exchanges in criminal tax cases and provides legal, technical and practical advice on all forms of exchange – the main ones being exchange on request, spontaneous exchange and automatic exchange.

Simultaneous tax examinations may be another tool to identify bribes to foreign public officials. The 1992 *OECD Model Agreement for the Undertaking of Simultaneous Tax Examinations* states, “The main purpose of simultaneous tax examination is inter alia: To determine a taxpayer’s correct liability in cases where: (...) unreported income, money laundering, kickbacks, bribes, illegal payments, etc. are identified”.

The Exchange of Information manual is available on the OECD website at [www.oecd.org/ctp/eoi/manual](http://www.oecd.org/ctp/eoi/manual)

## 8. Do tax treaties allow the use of information provided by a treaty partner for tax purposes to combat serious crimes such as corruption?

Not only domestic information but also foreign source information may be relevant in the fight to counter corruption. For this reason countries should consider allowing the use of information received from their treaty partners to be shared with law enforcement authorities to counter corruption provided this is allowed under the laws of the supplying state and that the supplying state agrees to this use. This enables the tax administration under certain circumstances to pass on the information to law enforcement in a similar way to their passing on suspicions based on information held or obtained domestically

A growing number of bilateral tax treaties contain such provisions allowing tax authorities to share relevant information with other law enforcement agencies (see e.g. those between Austria and Mexico, Bulgaria and Germany, Mexico and

Switzerland, and Norway and Slovenia). A number of Tax Information Exchange Agreements (TIEAs) also include such provisions.

Within the European Union, the new Directive on Administrative Cooperation in the Field of Taxation (2011/16/EU) includes language in Article 16.2 allowing tax authorities of a Member State to share relevant information with other law enforcement agencies provided it obtains the permission of the competent authority of the Member State communicating information, subject to certain conditions.

The Multilateral Convention on Mutual Administrative Assistance in Tax Matters, which is a global instrument for international cooperation on tax matters, also contains such a provision. The Convention has already been signed by 32 countries with more expected to sign in the near future.

#### **Information sharing on corruption in the Multilateral Convention on Mutual Administrative Assistance in Tax Matters**

The Convention on Mutual Administrative Assistance in Tax Matters was jointly developed by the Council of Europe and the OECD. Open for signature to OECD member states since 1988 it has been amended in 2010 to bring it in line with the international standard on exchange of information for tax purposes and to open it to all countries. All countries can now ratify the Convention.

The Convention allows that the information obtained under the Convention can be given to other authorities, e.g. law enforcement authorities to counteract corruption, money laundering and terrorism financing. This is subject to certain conditions: information received by a Party may only be used for other purposes when (i) such information may be used for such other purposes under the laws of the supplying Party and (ii) the competent authority of the supplying Party authorises such use. Moreover, information provided by a Party to another Party may be transmitted to a third Party, if this is authorised by the competent authority of the first Party (Article 22.4).

See [www.oecd.org/ctp/eoi/mutual](http://www.oecd.org/ctp/eoi/mutual)

## Further Resources

### OECD

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#### INSTRUMENTS AND STANDARDS

[OECD Recommendation on the Tax Deductibility of Bribes to Foreign Public Officials 1996](#)

[OECD Recommendation on Tax Measures for Further Combating Bribery of Foreign Public Officials in International Business Transactions](#)

[OECD Recommendation to Facilitate Co-operation between Tax and Other Law Enforcement Authorities to Combat Serious Crimes](#)

#### TOOLS, GUIDANCE, MANUALS

##### [OECD Bribery Awareness Handbook for Tax Examiners](#)

This handbook provides tax examiners with information on the various bribery techniques used and the tools to detect and identify bribes. The Handbook is available in 18 languages at [www.oecd.org/ctp/nobribes](http://www.oecd.org/ctp/nobribes).

##### [Money Laundering Awareness Handbook for Tax Examiners and Tax Auditors](#)

A companion handbook on money laundering awareness also has relevant information and is available at [www.oecd.org/ctp/taxcrimes/laundrying](http://www.oecd.org/ctp/taxcrimes/laundrying).

##### [Practical guidance on exchange of tax information](#)

The OECD maintains a comprehensive online manual giving practical guidance on all aspects of exchange of tax information. This is available at [www.oecd.org/ctp/eoi/manual](http://www.oecd.org/ctp/eoi/manual).

## REVIEWS AND CASE STUDIES

The OECD reviews the implementation of the [Anti-Bribery Convention](#) and produces country reports on the implementation including the legislation and practice in respect of tax deductibility of bribes and other tax measures to combat bribery.

The [Exchange of Tax Information Portal](#) is an initiative of the Global Forum on Transparency and Exchange of Information for Tax Purposes. It gives an overview of bilateral agreements providing for exchange of tax information and provides detailed peer reviews of global forum members in respect of the legal and regulatory framework for the exchange of information in tax matters and the implementation of the standard on transparency and exchange of information in practice.

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