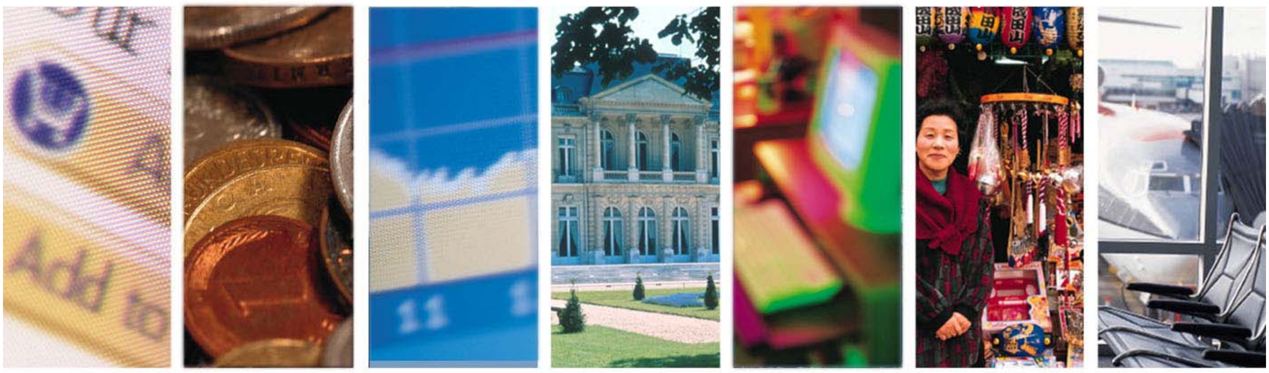
OECD

ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT



INFORMATION NOTE

Using Third Party Information Reports to Assist Taxpayers Meet their Return Filing Obligations— Country Experiences With the Use of Pre-populated Personal Tax Returns

Prepared by
Forum on Tax Administration
Taxpayer Services Sub-group

March 2006

CTPA

CENTRE FOR TAX POLICY AND ADMINISTRATION

TABLE OF CONTENTS

ABOUT THIS DOCUMENT

Purpose

This information note briefly describes the use of pre-populated returns that has become a feature of the personal income tax systems in countries in the Nordic region and elsewhere, particularly over the last decade or so.

Background

Since its establishment in July 2002, the Forum on Tax Administration, a subsidiary body of the OECD's Committee on Fiscal Affairs, has operated with the broadly stated mandate ………*to develop effective responses to current administrative issues in a collaborative way, and engage in exploratory dialogue on the strategic issues that may emerge in the medium to long term.* To carry out this mandate, the Forum's work is directly supported by two specialist Sub-groups—Compliance and Taxpayer Services (previously e-services)—that each carry out a program of work agreed by member countries.

The Taxpayer Services Sub-group exists to provide a forum for members to share experiences and knowledge of approaches to taxpayer service delivery, in particular through the use of modern technology. In this context, it is expected to: 1) periodically monitor and report on trends in taxpayer service delivery, with a particular focus on the development of electronic/online services; 2) examine ways to promote the uptake and use of electronic services by revenue bodies; 3) examine options for cross-border administrative simplification and consistency; and 4) assist, as appropriate, other groups of the CFA. In early 2005, it was agreed that the growing use and sophistication of arrangements involving the use of pre-populated returns was a major development worthy of closer examination and exchanges by the Subgroup. This information note is the initial by-product of work being undertaken concerning this topic.

Caveat

National revenue bodies face a varied environment within which to administer their taxation system. Jurisdictions differ in respect of their policy and legislative environment and their administrative practices and culture. As such, a standard approach to tax administration may be neither practical nor desirable in a particular instance.

The documents forming the OECD tax guidance series need to be interpreted with this in mind. Care should always be taken when considering a country's practices to fully appreciate the complex factors that have shaped a particular approach.

Inquiries and further information

Inquiries concerning any matters raised in this information note should be directed to Richard Highfield (Head, CTPA Tax Administration and Consumption Taxes Division), phone +33 1 4524 9463 or e-mail (richard.highfield@oecd.org).

SUMMARY

All revenue bodies are confronted with the goals of making it easier for taxpayers to comply with law (i.e., reducing their compliance burden), improving taxpayers' compliance and increasing administrative efficiency. This particularly applies to systems of personal income tax that in many OECD countries constitute the major revenue stream for governments and impose a range of obligations on the majority of citizens that comprise the taxpayer population.

Around 15 of 30 OECD countries impose a general requirement on all personal taxpayers to file an annual tax return. Thus, for these countries issues surrounding taxpayers' compliance burden, levels of compliance and administrative efficiency are key considerations in the overall design and operation of the tax system.

Particularly over the last decade, a small number of countries (six OECD and one non-OECD) have been perfecting arrangements on an incremental basis that transform the traditional business model for personal income tax administration, with potentially significant benefits for both taxpayers and governments.

Under these arrangements, described in this report as 'pre-populated returns', the revenue body, rather than the taxpayer, is the originator of tax returns for a majority of the personal income taxpayer population, using a large range of third-party information sources and other information held by it relevant to each taxpayer's tax affairs. In countries where these arrangements have been established on a comprehensive basis, pre-populated returns are sent to taxpayers in either paper form or electronically for their confirmation, or if necessary, to obtain any additional information required to enable a final assessment to be made.

While there are clearly limitations as to the extent to which complete and accurate pre-populated returns can be generated for the bulk of the taxpayer population, as described in this report considerable progress has and is being made in the countries concerned. Indeed, the success to date of these arrangements is encouraging a number of other countries to implement similar arrangements or to contemplate adopting this approach in the medium term.

This report briefly describes the use of pre-populated returns that has become a feature of the personal tax systems in a number of countries over the last decade or so. In doing so, it elaborates on a number of critical success factors for efficient and effective arrangements (e.g., comprehensive third-party reporting systems, high integrity taxpayer identifiers, compatible legislative framework, and effective use of technology), bearing in mind the objective of providing as many taxpayers as possible with a pre-filled return that is largely complete. Although not studied in detail, the report also outlines the potential benefits and costs arising from use of these arrangements.

INTRODUCTION

1. The report 'Survey of Trends in Taxpayer Service Delivery Using New Technologies' published by the Forum on Tax Administration's Taxpayer Services Sub-group in early 2005 made brief reference to the system of 'pre-populated returns' developed by countries in the Nordic region (i.e., Denmark, Estonia, Finland, Iceland, Norway, and Sweden) largely over the last 10 years.[1] In more recent times, a number of other countries (e.g., Chile and Spain) have started to implement identical or broadly similar arrangements while others have taken some small steps in this direction or have indicated an intention to do so.[2] Given the growing level of interest in this development, the Secretariat thought it useful to carry out a small study to ascertain the key features of these arrangements, the experiences and progress of individual revenue bodies in implementation of these approaches, and likely future developments.

2. This note briefly describes the use of pre-populated returns that has become a feature of the personal income tax system in the abovementioned countries. In doing so, it elaborates on a number of critical success factors for efficient and effective arrangements, bearing in mind the objective of providing as many taxpayers as possible with accurate and complete pre-populated returns. Although not studied in detail, the report also describes potential benefits and costs arising from use of these arrangements.

3. The Secretariat wishes to acknowledge the considerable assistance provided by revenue officials in Chile, Denmark, Estonia, Finland, Iceland, Norway, Spain and Sweden in providing critical information that has enabled this report to be prepared.

Background

4. In countries where personal income taxpayers are generally required to file annual tax returns, revenue authorities have till relatively recent times followed a fairly similar approach:

    - For most personal taxpayers, income tax is withheld at source (e.g., by employers) and/or paid by installments during the year of income.

---

1 The first use of pre-populated returns was by Denmark in 1988. Sweden introduced its arrangements in 1994, while other Nordic region countries followed in the late 1990's/early 2000's.

2 **Singapore** introduced a very limited form of pre-populated returns early in 2005 which involves volunteering employers and a small number of information sources (i.e. wages, dividends and donations). Given its initial narrow scope and being the first year of introduction, Singapore was not approached to participate in the survey.

From July 2005**, Australia's** taxpayers had on-line access via the Australian Taxation Office (ATO) to limited third party information to assist them prepare their tax returns. From this time, taxpayers filing electronically and in receipt of payments from Centrelink, the government's welfare payment agency, were able to access payment information online through the ATO's e-tax (electronic filing) capability. Similarly, they also had online access to medical expenditure information from the government's Health Insurance Commission via e-tax when preparing their return.

France also conducted in 2005 a pilot test of a very limited form of a pre-populated return involving one department (i.e. district) of around 500,000 taxpayers. According to French officials and media reports the pilot was very successful, both from viewpoint of taxpayers and the tax administration. A decision on wider implementation of the concept was announced in January 2006 indicating the intention to broaden the use of prepopulated returns, albeit still on a limited basis, for all employee and retiree taxpayers.

- Taxpayers are provided general information concerning the tax system and their obligations under the law to assist them (or their representatives) prepare their annual tax returns.

- Returns submitted by taxpayers are processed by the revenue body applying either assessment or self-assessment principles, generally with limited checking, and a formal assessment notice is issued to the taxpayer along with details of any further amounts payable or refundable, after taking account of taxes already paid.

- Information reported by third parties (e.g., employers and financial institutions) under the law is processed for matching with tax records to detect cases of inaccurate returns or return non-filing.

- Actions are taken (e.g., office audits, correspondence inquiries) to examine suspected cases of unreported income, and if needed, to issue reassessments, and to obtain outstanding tax returns; taxpayers may also seek amendments to their returns after discovering any errors.

5. In countries where these sorts of arrangements have been and are still being applied, the processes for capturing and matching large volumes of third party income reports with tax records have been highly effective in detecting unreported income and have resulted in the collection of substantial amounts of additional tax revenue. On the downside, detecting tax non-compliance in this way presents additional work for revenue bodies—reported discrepancies have to be verified and, where appropriate, assessments need to be amended. In practice, this verification work often takes place well after original assessment notices have been sent to taxpayers meaning that the overall cycle of activities required for any one fiscal year is quite lengthy (i.e. , up to 3 years in elapsed time). All of this involves administrative costs for the revenue body and additional actions for taxpayers and/or their representatives, and is often resented by those taxpayers who felt their tax obligations for the year concerned had already been finalised.

6. Over the last decade or so, countries in the Nordic region, and more recently in Chile and Spain, have fundamentally reformed this approach by making third party information available to taxpayers 'upfront', at the return preparation stage. In this way, taxpayers are assisted directly and significantly in meeting their tax return filing obligations and the need to amend assessments, particularly resulting from taxpayers' unintended errors, is greatly reduced. In practice, these arrangements are described by a variety of terms such as 'pre-populated returns', 'pre-filled returns', or 'tax proposals'. In this report, the term 'pre-populated returns' is used hereafter to describe all of these arrangements.

Methodology and Scope

7. To carry out this work, a short survey questionnaire was developed by the Secretariat in collaboration with the Norwegian Tax Directorate, and subsequently referred to the five other Nordic countries known to be using pre-populated returns (or conceptually similar arrangements). Chile and Spain were later included in the survey on discovering that the revenue bodies in these countries had established similar arrangements. A summary of the responses received from all countries is set out at Annex 1.

8. The survey and this report are not intended to represent an exhaustive study of this development. Rather, the objective has been to gather sufficient information to give observers an overview of how these arrangements work in practice, and an indication of the level of maturity of the pre-populated return systems used by the respective

revenue bodies, the progress achieved to date, critical success factors, and some of the lessons learned to date. Subject to agreement by the Forum's Bureau, the Taxpayer Services Sub-group will undertake further study in this area in order to gather more detailed information for member countries.

Evaluation Criteria

9. There are number of obvious criteria against which systems of pre-populated returns can be evaluated, for example, the burden on taxpayers, compliance levels and efficiency.

10. At its most rudimentary level, the use of pre-populated tax returns is intended principally to relieve the bulk of personal taxpayers who have obligations to file annual tax returns from the burden of having to complete these tax returns. This "burden" can include taxpayers' personal time in locating and storing records and preparing returns, the costs of professional preparers where these services might otherwise have been used, and the time involved in dealing with errors when they arise. Such "costs" are difficult to measure accurately but potentially are quite significant in a relative sense given the size of the taxpayer populations targeted in most countries.

11. Pre-populated returns also directly impact the levels of compliance achieved by taxpayers in a number of ways. Most significantly, such returns by their very design will include information concerning taxpayers' liabilities that might not otherwise have been reported by them. In addition, the process of sending pre-populated returns serves as a reminder to taxpayers of the need to complete their filing obligations and thus may reduce the level of follow-up action otherwise required by the revenue body.

12. Revenue bodies can also benefit from use of pre-populated returns through lower administrative costs as they largely replace the need to mount post-assessment checking programs used with traditional approaches. However, the extent of this benefit will depend on a range of factors - the size of the targeted population, the rate of usage of pre-populated returns by taxpayers, the rate of adjustment required to these returns, and the level of automation and self-assessment applied to this aspect of the overall arrangements.

13. Assisting taxpayers in these ways also may increase respect for the revenue body as, compared to traditional approaches, the availability of pre-populated returns is likely to be viewed by most taxpayers as a genuine and personalised service that was not previously available.

14. These are all relevant considerations in appraising efficacy of the arrangements, vis-à-vis traditional return filing, processing and post-assessment matching arrangements.

DESCRIPTION OF ARRANGEMENTS IN PLACE

15. Set out hereunder is a summary of the key features of the arrangements observed in practice, along with a number of metrics pointing to the coverage and relative success being achieved with these arrangements.

Overview of common arrangements

16. Revenue bodies in the Nordic region have collaborated closely in the development of systems of pre-populated returns and, as a result, there are many common features in the arrangements in place. An overview of the process in practice is depicted in Figure 1. However, surveyed countries are at different stages in their automation of the overall process meaning that the benefits being achieved vary somewhat from country to country. Chile and Spain have established similar arrangements and, as described hereunder and in Annex 1, they too are at different stages of development.

Tax withholdings at source (steps 1 and 2 - Figure 1)

- All countries place emphasis on ensuring that that the amount of tax withheld at source for each taxpayer approximates to his/her end-of year liability. As a result, end-of-year refunds, particularly for employee taxpayers, tend to be relatively small, and there is no strong incentive for taxpayers to file returns early seeking large refunds of overpaid tax. This is a critical issue for the countries concerned as it takes from 6 to 12 weeks to make pre-populated returns available to taxpayers.

- With the exception of Estonia which uses a system of flat rate withholding, precise withholdings are achieved in practice through arrangements that require the revenue body to compute all employees" individual tax rates using historical assessment data, and to advise this information to employers and/or employees for withholding purposes.[3] Also relevant here is the withholding of tax at source on interest income, which is applied in 4 of the 6 Nordic countries and in Spain.

---

3 This might be viewed as an additional step in the pre-populated return arrangements; other countries such as Australia, Canada, and the USA are not required to administer a system of personalized withholding rates with employers for their employees; in these countries, employers are only required to apply set schedules that take broad account of a taxpayer's circumstances. As a result, withholdings are less precise and average refunds tend to be much higher. With relatively larger refunds, many taxpayers file returns very soon after the end of the fiscal year to obtain their refund entitlements which they expect to be made fairly promptly.

FIGURE 1

Overview of pre-populated tax return systems used by Nordic region countries

(NB: The fiscal year is the calendar year in all surveyed countries.)

TIMELINES*	KEY STEPS
BY DECEMBER (before fiscal year)	1. EMPLOYERS ARE ADVISED BY REVENUE BODY OF EACH EMPLOYEE's WITHHOLDING RATE, ETC.
THROUGHOUT FISCAL YEAR	2. WITHHOLDING AGENTS & TAXPAYERS MAKE REGULAR PAYMENTS IN INCOME YEAR
BY END-JANUARY (after fiscal year)	3. EMPLOYERS AND OTHER 3RD PARTIES REPORT INFORMATION TO REVENUE BODY
FROM MID-JANUARY TO MID-MARCH	4. REVENUE BODY VALIDATES INFORMATION REPORTS & PREPARES PREPOPULATED RETURNS
FROM MID-MARCH TO MID- APRIL	5. REVENUE BODY SENDS PREPOPULATED RETURNS TO TAXPAYERS, OR MAKES THEM AVAILABLE ON THE INTERNET, FOR CHECKING
FROM MID-MARCH TO MID-MAY	6. TAXPAYERS REVIEW THEIR PREPOPULATED RETURNS & EITHER CONFIRM COMPLETENESS OR ADVISE ANY CHANGES
FROM APRIL	7. REVENUE BODY CHECKS TAXPAYERS' RETURN INFORMATION AND UPDATE RECORDS IF NEEDED
FROM MAY	8. IF NECESSARY, FURTHER INQUIRIES ARE MADE OF THE TAXPAYER BY THE REVENUE BODY
FROM MAY	9. FINAL ASSESSMENT NOTICES, REFUNDS AND OR BILLS SENT TO TAXPAYERS
BY DECEMBER	ALL RETURNS PROCESSED BY REVENUE BODY

*TIMELINES MAY VARY SLIGHTLY FROM COUNTRY TO COUNTRY

Information reporting obligations and practices of third parties (Step 3 - Figure 1)

- All countries have comprehensive systems requiring third parties to report income, asset and deduction-related information. Concerning income-related information, this typically includes wages and other employment-related payments (e.g., bonuses, severance payments), employee fringe benefits, interest, dividends, pensions, and insurance payments. Concerning assets, there are reporting obligations covering the sales and purchases of capital assets that are/may be relevant to computations for capital gains tax purposes. In relation to tax deductions, information reporting requirements typically extend to gifts, union fees, home mortgage interest, contributions to unemployment insurance and retirement savings plans, and child care expenses.

- As a result of the reporting requirements described, the volume of information reports per taxpayer, on average, is quite substantial (e.g., Denmark—20 and Spain—29).

- Third parties are obligated to identify related payee/payer parties using the system of citizen identification numbers that is a common feature of all countries included in the survey.

- Third parties face strict and timely end-of-year reporting obligations under the law with final information reports typically required within 3-4 weeks after the end of the relevant fiscal year.

- All countries have made considerable progress in establishing comprehensive electronic reporting arrangements with third parties, with a number citing reporting rates well over 90 percent; in a number of countries, this high rate of electronic reporting appears to have resulted from the introduction of mandatory reporting obligations.

Processing of third-party information reports by tax body (Step 4 - Figure 1)

- Revenue bodies are at varying stages of development in automating all of the processes involved in the preparation of pre-populated returns, meaning that the time-cycles involved (i.e. , from the end of the fiscal year to the issue date of pre-populated returns) varies considerably. Estonia, the smallest country surveyed, is able to finalise the preparation of pre-populated returns roughly within 6 weeks of the year-end,[4] while the periods in other countries vary from 7-10 weeks after the end of the fiscal year. Denmark has recently reported that from around 1 February 2006 (i.e., one month after the end of its fiscal year) taxpayers will have access via the internet to pre-populated return information.

4 In Estonia, information used for pre-populating returns is made available to taxpayers for their review via e-Tax Board (an internet application) well ahead of the mandatory date for issuing pre-populated returns (which is by the law February 15). Information on payments made to natural persons and income tax withheld is available monthly immediately after the payer has submitted a withholding tax return to the revenue body. Information on deductions is available for reviewing at the beginning of February immediately after deduction-granting institutions have submitted deduction-related information declarations. The purpose of this review period is to give taxpayers the option of informing payers or deduction-granting institutions of mistakes and omissions ahead of the mandatory date for sending pre-populated returns.

Issue of pre-populated returns (Step 5 - Figure 1)

- All surveyed countries target salary and wage earners in their pre-populated return systems. In the case of Denmark, Estonia and Sweden the arrangements are broader and cover virtually all personal taxpayers.

- With the exception of Chile and Estonia, all countries produce hard copy pre-populated returns that are sent to taxpayers, although most of these countries also have an electronic version that can be accessed via the Internet. Chile and Estonia require their taxpayers to access an electronic version of the pre-populated return although, in the case of Estonia, a paper version can be obtained on request at regional tax offices.

- Typically, each pre-populated return details all reported sources and amounts of income, rebates/credits, deductions, etc. and tax withheld at source, computes an overall tax liability on the basis of the information available, and arrives at any further amounts payable or refundable. In addition, they typically show all relevant client identification information, including relevant bank account details. A conceptual outline of Sweden's pre-populated return is shown at Annex 2.

Processing of pre-populated tax returns by taxpayers (Step 6 - Figure 1)

- With the exception of Denmark, the initial practice with pre-populated returns in each country was to require all taxpayers to respond, either by confirming that the return gave a complete and accurate picture of his/her tax affairs or by advising further adjusting information in order to arrive at a correct outcome. In more recent years, a number of countries have moved to a system of 'deemed acceptance' where no response is required after a prescribed period, and the return is deemed to have been accepted as complete and accurate by the taxpayer. Denmark has used the system of 'deemed acceptance' since the first year pre-populated returns were introduced (i.e., 1988).

- Taxpayers are given relatively short periods to respond to their pre-populated return, ranging from 2-6 weeks.

- With the exception of Finland,[5] all countries permit taxpayers to confirm their pre-populated returns or advise adjustments electronically (via SMS, phone, and/or the Internet). Estonia and Chile reported the highest rate of electronic confirmation/adjustment at 76 percent and 77% respectively, in both cases with responses made exclusively via the Internet.

Processing of pre-populated tax returns by revenue body (Steps 7 to 9 - Figure 1)

- Pre-populated returns in paper form with adjustments are examined manually (in some cases using rule-based systems to detect cases warranting examination) while the approach for electronically-advised adjustments appears more selective. In Denmark, for example, adjustments to fields in a pre-populated return are only examined, and this applies to adjustments that are reported electronically by taxpayers,

5 Finland has advised that it intends to provide this functionality in 2006.

if they are not supported by corresponding additional information supplied by third party reporting bodies.

- The rate of adjustment required to pre-populated returns varies substantially from country to country and obviously is influenced by the target group initially chosen to receive pre-populated returns, the comprehensiveness of the third-party reporting arrangements in place, and the complexity of the underlying legislation for each country. Across the Nordic countries, the incidence of returns not requiring any adjustments by taxpayers generally ranges from around 50 to 75 percent. (NB: Iceland reported that it has an abnormally high rate of adjustment owing to its inability to receive third-party reports of interest income, a weakness it is aiming to remove from its arrangements.) Denmark, the originator of the pre-populated returns concept, not surprisingly reported the highest rate of non-adjustment at around 78%.

- Chile reported a rate of non-adjustment of 57% for its latest fiscal year. Spain reported that only 40% of the pre-populated returns sent to taxpayers are actually "filed" by them, with a 78% non-adjustment rate for these returns.

- Reported reasons for adjustments tend to be deduction-related (e.g. travel and child care), and in the income arena for non-employee taxpayers (e.g., rents, capital gains). Chile reported its primary reason as discrepancies between third party reports and taxpayers' own records.

- Taxpayers typically receive refunds of any overpaid tax some months after filing/accepting the pre-populated return. There are exceptions to this rule. In Denmark and Estonia, taxpayers responding electronically to their pre-populated returns, can receive a refund within in 2-3 and 5 working days respectively.[6]

6 In the case of Estonia, the 5 day rule also applies to returns, other than pre-populated ones, that are filed electronically.

POTENTIAL BENEFITS, COSTS & CRITICAL SUCCESS FACTORS

17. As currently practiced, the use of pre-populated returns appears to provide a range of benefits to taxpayers and revenue bodies, although there are additional costs and some major challenges to successfully implementing such arrangements. From the information provided by surveyed countries, it is also possible to point to a number of 'critical success factors' that underpin an effective and efficient system of pre-populated tax returns.

Benefits

18. In terms of benefits from the use of pre-populated returns, these potentially include: 1) a substantially reduced compliance burden for taxpayers; 2) greater certainty for taxpayers that they have fully reported their income and properly claimed their deduction entitlements; 3) an improved image of revenue body, resulting from the more personalised service being given to taxpayers; 4) faster processing of taxpayers' tax return information; 5) quicker refunds of overpaid tax to taxpayers; and 6) within the revenue body, the elimination of much of the work associated with raising amended assessments that result from unintended taxpayers' errors and/or traditional post-assessment verification programs.

19. These benefits are likely to be relatively significant in the countries concerned, given the requirement for all taxpayers to file returns, but are difficult to quantify without considerable research. The data in Table 1 gives some insights as to the coverage of the systems in place, the rate of adjustment in practice, and the media used for the pre-populated returns systems, all factors that have a bearing on the benefits arising from the use of pre-populated returns.

Table 1: Coverage and use of pre-populated tax returns

Country	No. receiving pre-populated return /1 (mln)	Proportion of all personal taxpayers (%)	Media used for personalised returns /2	Must taxpayers respond?	Adjustment rate for returns (%)	Media available for advising adjustments /2
Denmark	4.5	100	P,I	No	22	P, I, Ph
Estonia	0.638	100	I	Yes	35	I
Finland	3.1	66	P	Yes	30	P
Iceland	0.235	100	P,I	Yes	Very high /3	P, I
Norway	3.4	93	P,I	Yes	50	P,I
Sweden	7.1	100	P,I	Yes	50	P,I
Chile	1.65	100	I	Yes	43	I
Spain	7.54	49	P,I	Yes	22 /4	P, I, Ph

***Source**: Country survey responses*

/1. Also includes taxpayers who receive partial information by way of a letter or statement with personal information.
/2. Legend: P- Paper; I- Internet; and Ph- Phone.
/3. High rate of adjustments results from inability to obtain reports of interest income.
/4. Spain reported that 40% of taxpayers use the pre-populated return received by them; 78% of these returns are accepted without change.

Costs

20. In relation to additional costs arising from use of pre-populated returns, there appear to be two potentially significant items.[7]

21. The first relates to the system of personalized withholding rates that is a feature of the tax system in most Nordic countries. In practice, this requires the tax body to track the employment location of all employee taxpayers and to advise individual taxpayers and/or their employers each year of the rate of withholding that should be applied to payments of wages, etc; taxpayers are also given the opportunity to vary these rates (which are initially based on historical data) where their circumstances have changed. Administering such arrangements presents additional costs for the revenue body, and potentially employers that are generally not incurred under traditional approaches. The extent of these additional costs will depend on a range of factors (e.g. workforce stability, the extent of automation in place, etc).

22. A second area of potential additional cost involves the need to process taxpayers' adjustments to the pre-populated returns received by them. As noted earlier in the report, the rate of adjustment across surveyed countries in Nordic countries and Chile varies from around 25 to 50 percent. The magnitude of the effort required by the revenue body in this area will be influenced by the extent it is prepared to accept taxpayers' advice in the first instance (e.g., by applying self-assessment principles), and the degree of automation in place to receive and process taxpayers' adjustments. As noted earlier in this report, one country8 appears to have made considerable progress in this area, although it needs to be acknowledged that the volumes involved are very small. Other surveyed countries reported further enhancements in the medium term that will reduce the costs of processing adjusted returns, as well as the proportion of returns that require adjustment.

23. Also relevant in terms of potential costs is whether there is a risk associated with revealing to taxpayers all known information, which may encourage some taxpayers to take a risk and not disclose other income not revealed in the pre-populated return. None of the countries surveyed reported this as a significant issue to them with the arrangements currently in place. [9] [10]

---

7 As traditional post-assessment matching programs generally entail substantial programs of reporting and matching with tax records, the costs of these arrangements in countries using pre-populated returns are not deemed as "additional" costs.

8 Estonia reported that returns for which adjustments are advised electronically can generally be finalized within five working days.

9 **Denmark** reported that….. "it does not find that there is a risk associated with disclosing third party reports. On the contrary, the Danish experience is that control of the reported information before printing ensures a far more correct assessment, and thereby reduces the need for manual modifications. The relieved resources can be used for control. It should be noticed that nearly all income is reported. The taxpayer need for supplementary information is mostly related to deductions. The fact that the taxpayer receives a pre-filled income tax return does not release him/her from the obligation to submit missing information. The penalty for non-compliance is the same whether the taxpayer actively gives false information or omits to correct the tax return. Deemed acceptance of an incorrect tax return is considered positive tax fraud. The penalty is a fine or up to two years imprisonment if fraud is identified."

Norway reported that a study made in 2000 showed that the potential loss from this risk was much smaller than the benefits from pre-population with respect to increased formal data quality and the fact that taxpayers very seldom take the risk to make corrections to pre-populated data items that are correct. Earlier, Norway often found that taxpayers' data did not match the correct data items from third parties.

Sweden reported that from its experience in many cases people found to have omitted income from their return claimed they believed everything was covered by the pre-populated return. In order to decrease this problem information on the pre-populated return and in associated materials has been improved in recent years. In practice, taxpayers are obliged to report income not shown in the pre-populated return, or face a potential tax surcharge of up to 40 percent if the omission is detected.

10 Estonia reported that ……. "information on all tax matters of a person is freely available to the same person. Thus anyone can request his or her information (including what the tax administration, so to say, "has on me") at any point in time. This information can also be accessed via Internet. So bringing this act of disclosure to a single moment in time does not change the fact that the information has been available all the time. In fact, there are many

Critical success factors

24. As will be evident from the experience of surveyed countries, establishing an effective and efficient system of pre-populated returns requires a number of precise and time critical processes to be executed smoothly so that the majority of taxpayers are provided with complete and timely pre-populated returns for their examination. In particular:

- ***Accurate withholdings at source***: To minimise the incidence of large refunds of tax, and thus the desire of taxpayers to file their tax returns shortly after the end of the fiscal year, withholdings at source (where they are a feature of the tax system in place) are typically calibrated so as to ensure that aggregate withholdings over the course of a fiscal year more or less approximate to taxpayers' annual liabilities. To achieve this objective, most of the revenue bodies surveyed issue a tax card (or notification of a rate to be applied) to taxpayers and/or their employers just prior to the beginning of each new fiscal year that provides personal information that can be used to establish individual amounts of withholdings. This information is derived from historical tax assessment data.

- ***High integrity taxpayer identifiers***: Given the need to match large volumes of third party reports accurately and quickly with tax records, it is essential that all the third party reports received by the revenue body contain a high integrity taxpayer identifier. This is achieved by requiring those bodies with reporting obligations to capture each taxpayer's citizen identification number which in all surveyed countries is used as the primary identifier for tax purposes.

- ***Comprehensive systems of third party reporting to the revenue body***: The comprehensiveness of the information that can be presented in each pre-populated return depends directly on the nature and scope of information that must be reported to the revenue body by third parties. All of the countries surveyed have substantial systems of third party reporting covering the major types of income (i.e., wages, pensions, government benefits, interest, and dividends), important deduction items (e.g., home mortgage interest, union subscriptions, childcare, pension contributions), and other information relevant to determining tax liabilities (e.g., purchases and sales of assets to compute capital gains).

- ***Compatible legislative framework***: Ideally, a high proportion of taxpayers' returns will be fully populated with information captured by the revenue body so that relatively few returns require adjustment by the taxpayers receiving them. In addition to comprehensive information reporting, this requires that the tax law provides relatively limited scope for tax deductions, rebates, credits, and discretions that cannot be predicted by the revenue body using third party reports or some other approach (e.g., statutory limit or formula).[11] While a number of surveyed

---

taxpayers who study their pre-filled return every year (either via Internet or obtaining it from a local service bureau) and never file it. The only objective of such behaviour is to make sure that the tax administration has correct information on taxpayer's income."

11 Surveyed countries commented variously that their tax regimes had a broad or limited range of tax deductions. In addition, most reported some form of standard deduction that limits the aggregate deduction a taxpayer can receive for a range of deduction items. Further research would be needed to ascertain how readily comparable the deduction provisions of surveyed countries are to other countries that may be contemplating the use of pre-populated returns.

countries reported that their systems provided a 'broad range of deductions', the range of deduction items identified by them appeared relatively limited vis-à-vis the situation known to exist in some other countries. With the exception of Denmark,[12] none of the surveyed countries identified any particular issue arising with employment-related work expenses, suggesting that these are relatively insignificant from a tax deduction and pre-populated return viewpoint. Also relevant here is the use of a standard deduction in some countries which caps the maximum deduction that is permissible for a range of items.

Clearly, pre-populated return systems work best where the range of deduction items is fairly limited and they are verifiable, in a relatively efficient manner, using third party sources.

- ***High degree of automation among information suppliers***: Processing of third party reports is greatly facilitated by extensive use of information technology systems by third-party reporting bodies and the automated reporting of third party information reports to the revenue body.

- ***Large scale information processing***: Revenue bodies typically have around 6-10 weeks to complete the processing of third party reports required to generate pre-populated returns. To meet these deadlines, substantial information processing systems are required to capture, validate, and prepare relevant data for the generation of pre-populated returns.

- ***Automated and minimal interactions with taxpayers***: To avoid large scale clerical (and thus costly) vetting of completed pre-populated returns returned by taxpayers to the tax body, a variety of mechanisms have been devised to ascertain taxpayers' acceptance or otherwise of the pre-populated returns sent to them. These include 1) provision for deemed acceptance, if no response is received; 2) automated acceptance, using SMS, phone, or Internet communications; and 3) provision for the communication of adjustments by the Internet.[13]

25. Significantly, all of the abovementioned factors are critical to the success of pre-populated return systems—a major weakness in any of the abovementioned areas is likely to significantly reduce the potential benefits that can be achieved in practice from the use of pre-populated returns.

[12] To reduce the level of adjustments concerning travelling expenses, Denmark will include field on estimated travel expenditure in future pre-populated returns.

13 Estonia reported that entering the unique ID code of each pre-populated return (generated for that particular return at the time it is prepared) results in the automatic transmission of data contained in the pre-populated return into their return processing system. This enables rapid processing of pre-populated returns without adjustments.

CONCLUSIONS

26. Based on the information gathered to date, countries in the Nordic region have made considerable progress in establishing comprehensive and efficient systems of pre-populated returns and appear to be deriving many benefits from their operation. These benefits include reductions in taxpayers' compliance burden, improved overall compliance in liability reporting, and reductions in administration costs from the more efficient processing of taxpayers' data, reduced volumes of taxpayers' unintended errors, and a significantly scaled down back-end verification program. More investigation would be required to quantify the extent of these benefits but on the surface, they appear substantial. An additional benefit is the improved image of the tax body that arises from a shift in emphasis from 'enforcement' to 'service' that is inherent in widely applying the concept of pre-populated returns.

27. Noting these positive developments and their potential to improve tax administration, other countries have implemented similar arrangements over the last 3-5 years, while a number of others are understood to contemplating moves in this direction.

28. The survey has also revealed that a considerable administrative effort is required over a fair period of time to fully obtain the benefits now being realised. For many countries, an incremental or "opportunistic" approach has been adopted as various obstacles have been removed. Based on the survey findings, of particular importance have been:

    - The need to have a comprehensive base of third party information, covering both income and deduction items, that must be routinely reported to the revenue body;
    - A capacity for this information to be accurately and rapidly reported to revenue bodies and matched, using a system of high integrity taxpayer identifiers, with taxpayers' records;
    - A capability to quickly deal with taxpayers' adjustments arising with personalized returns. Optimal use of technology by information providers, the revenue authority, and taxpayers is also central to having highly efficient and effective arrangements in place; and
    - A relatively simple legislative framework in place, thus limiting the amount of "adjustment" action required by taxpayers.

29. Revenue bodies contemplating the possible use of pre-populated return arrangements are likely to benefit greatly from a close examination of the experiences of Nordic region countries.

Annex 1
Information from Country Survey on Use of Pre-populated Returns

Features of System	COUNTRIES SURVEYED							
	Denmark	**Estonia**	**Finland**	**Norway**	**Sweden**	**Iceland**	**Chile**	**Spain**
1) Scope and nature of tax withholding arrangements								
Is tax withheld from salary income?	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Is tax withheld from interest?	No	Yes (where taxable)	Yes (& final)	No	Yes (& creditable)	Yes	No	Yes
Is tax withheld from dividends?	Some	Paid (not withheld) by company	Yes	No (imputation applies)	Yes	Yes	No	Yes
Are wage withholdings computed on a cumulative or non-cumulative basis?	Non-cumulative	Flat rate withholdings /1	Both /1.	Non-cumulative.	Non-cumulative	Cumulative	Non-cumulative? (NB: Almost 70% of labour force is exempt from personal income tax) /7	Non-cumulative
How are employees' withholdings aligned with tax liability	Use of tax card with historical tax rate and any further advice from taxpayer	Flat rate computation	Use of tax card with historical tax rate. See /1	Use of tax card with historical tax rate	Based on estimated tax rate for year of income, which can be varied.	Use of tax card that records income and tax withheld on cumulative basis	Monthly withholding (reflecting progressive rate scale)	Based on historical data with option for taxpayers to vary.
Revenue body requirements for tax cards or similar information	Tax card sent to employer & employee just prior to new fiscal year	Nil. Withholding made based on flat rates applicable	Tax card sent to taxpayer and employer just prior to new fiscal year	Tax card sent to employer & employee just prior to new fiscal year	Revenue body advises employer electronically of requirements just prior to new year	Tax card	No	No
2) Use of taxpayer identifiers								
What taxpayer identifier is used?	Citizen ID number							
Use of taxpayer identifier by third parties is obligatory?	Yes- all for all information suppliers							

Features of System	COUNTRIES SURVEYED							
	Denmark	**Estonia**	**Finland**	**Norway**	**Sweden**	**Iceland**	**Chile**	**Spain**
3) Available tax deductions								
Briefly outline provisions of tax code on deductions, especially for employees work expenses	Fairly broad range incl. travel expenses, trade union fees, child allowance and child care, unemployment insurance, interest on home mortgages and student loans, repaid social benefit, gifts, and retirement plans Personal relief allowance for all.	Fairly limited range, incl. home loan interest, self-education expenses, gifts, union fees, and alimony (with overall limit), and insurance premiums, pension fund etc., subject to limits.	Fairly limited deductions, incl. standard expense deduction for employee work expenses, trade union fees, & social security premiums	Fairly broad range, incl. employment, child care, alimony, mortgage interest, pension plans. Standard deduction of 24% covering specific items.	Fairly limited deductions, incl. work expenses, pension plans, interest payments. Some deductions have base limit. Standard deduction for all.	Relatively few with the main ones being car expenses and per diem travel, pension savings, and high medical costs.	Fairly limited (including home mortgage interest, voluntary social security savings) but no work related expenses	Fairly broad range (incl. regional variations) covering personal/ family allowances, social contributions, union fees, pension plans, child care, and main residence costs, etc.
4) Third party reporting obligations								
When are end-year reports due?	By 20 January- within 3 weeks	By 10 January for employers and government bodies; by 1 February for other reporters	By 31 January- within 1 month /2	By 20 January- within 3 weeks	By 31 January- within 1 month	By 14 February- within 6 weeks	Progressively after end-year up to end- March	By end-January
What types of income-related transactions are reported?	Wages, bonuses, severance payments, employee benefits, pensions, welfare benefits, interest, dividends, and financial instruments /3	Wages, pensions, interest, welfare benefits, rent, insurance payments and sickness benefits.	Wages, benefits, pension plan premiums, interest, insurance payouts, loans, purchase/ sale of securities etc., and union fees.	Wages, benefits, pensions, interest, dividends, welfare benefits and financial instruments /3	Wages, benefits, pensions, welfare payments, interest, dividends, and sales and end year balances of financial instruments	Salaries, benefits, pensions, student loans, dividends unemployment benefits (but **not** interest)	Wages, pensions, interest, dividends, payments to independent contractors, asset purchases and sales	Wages, pensions, certain rents, interest, dividends, asset purchases and sales
What types of deduction-related information is	Unemployment insurance, trade union fees, retirement plans,	Child care expenses, union fees, gifts	Pension savings, union fees, interest on home and study loans	Interest paid, child care expenses	Interest paid, union fees and payments to unemployment	Information about car loans and some housing loans	Home mortgage interest, voluntary social security savings	Pension plan contributions, home loan interest, and

Features of System	COUNTRIES SURVEYED							
	Denmark	Estonia	Finland	Norway	Sweden	Iceland	Chile	Spain
reported?	interest on home mortgage & student loan, and repaid social benefit				funds			some donations
How many reports are received?	90 million	/4	Around 30 million	Around 40 million	Around 80 million	2 million	28 million	424 million
Is electronic reporting mandated?	No	Employers: Yes- for state bodies with capacity; no- for others. Deductions: Yes for returns with > 10 records	Yes. For employers with 40+ employees	Yes	No. Free software provided	No	Yes (from 2004)	Yes (where volume exceeds prescribed limit)
What proportion of reports is made electronically?	99.7%	Varies for different categories; up to 90% from employers	Around 80% (incl. diskettes). Balance of reports is keyed. /6	Virtually all	99.5%	Around 90% is reported electronically	100%	Around 97%
5) Preparation of pre-populated returns / tax proposals								
Fiscal year when pre-populated returns first available to taxpayers (excludes test periods.)	1988	2001	1995 (initially with a fairly small group of taxpayers)	1998	1994 (To all personal taxpayers from 2002.) /7	2000	2001 fiscal year	2002 fiscal year
What period is required to complete all necessary data processing?	Around 4 weeks	Around 5-6 weeks	Around 9-12 weeks	10 weeks	Around 7 weeks (starting mid-January)	Around 6 weeks (starting from mid-January)	Up to 10 weeks	Around 7 weeks
What data items are supplied on the pre-populated returns?	1) Taxpayer identifying information; 2) For all income items- gross income, payer details, tax withheld; 3) Specific data for certain deduction items (e.g. trade union fees) where available; 4) Sales and purchase information for capital assets (limited for some countries; and 5) Calculations of tax assessed, credits, tax payable/refundable.							

Features of System	**COUNTRIES SURVEYED**							
	Denmark	**Estonia**	**Finland**	**Norway**	**Sweden**	**Iceland**	**Chile**	**Spain**
Which taxpayers receive pre-populated returns?	All taxpayers—around 90% get a fully pre-populated return, around 10% get a service letter pre-populated with the taxpayer data available	All taxpayers have access to electronic or paper return	Generally personal taxpayers except self-employed and larger income investors.	Virtually all wage earners and pensioners	All personal taxpayers	All personal taxpayers	Largely wage earners and pensioners	Largely wage earners and investors
When are returns sent to taxpayers?	Normally, from 15 March to 14 April. (For 2006, planning to give Internet access to taxpayers to their pre-populated return data from 1 February.)	Returns are not sent in paper form. By law, taxpayers can access electronic version via Internet or paper version at tax office after 15 February	During May. Issued on a staggered basis	Early April	From 15 March-15 April	From 1 March (in one bulk process)	From 1 April (only via Internet)	Over 8 weeks (from 20 March to 15 May)
Are returns sent only on paper?	No. Internet version also available	No paper returns sent. Electronic version only available	Yes	No. Internet version also available	No. Internet version also available	No. Internet version is available	Returns are available only on Internet	No. Internet version is accessible also.
6) Taxpayers' use of pre-populated returns/ tax proposals								
Are taxpayers required to confirm acceptance of information in pre-populated return?	No. Any refund and notice is automatic from 1 May	Yes	No.	Yes	Yes	Yes	Yes (but not obligated to use pre-populated return)	Yes. But taxpayers are not obligated to use pre-populated return
Can taxpayers respond electronically?	Yes.	Yes, both without and with adjustments	No	Yes. By SMS, phone, & Internet	Yes. By SMS, phone, and Internet (with and without adjustments)	Yes (over Internet)	Yes (via Internet or mobile phone)	Yes
How many taxpayers accept returns without adjustments?	3.0 million (78% of those receiving a pre-populated return)	Around 65%	Around 70% of those receiving a tax proposal	1.9 million (50%)	Around 50%	Small proportion in the absence of information from banks	57%	Around 28% (40% use the pre-populated return; 78% of these are

Features of System	COUNTRIES SURVEYED							
	Denmark	**Estonia**	**Finland**	**Norway**	**Sweden**	**Iceland**	**Chile**	**Spain**
								accepted without adjustments).
What are the main causes of adjustments?	Travel expenses and gifts	To include missing income data (e.g. rents, royalties, gains from property	Travel expenses, other work expenses, capital gains, rents	Expenses for travel, child care, medical	Travel, other employment expenses, capital gains, business income	Missing bank interest income and some employment income	Third party data does not match taxpayers' own records	Principal residence investments and earnings related to real estate
What other steps are taken?	Taxpayers can advise missing data electron-ically or on paper. Taxpayers responding elect-ronically can access notice of assessment on-line (real time). Tax refunds are credited direct to bank accounts.	Paper returns with adjustments are processed manually, with refunds generally issued by 1 July; returns submitted electronically are processed within 5 days if closer scrutiny not needed	Returns with adjustments are processed; some are selected for closer check. Refunds sent in December	Between 85-90% receive final tax notice and small refund in June	Information processed with refunds issued in June for taxpayers responding electronically, and in August for those responding on paper	Processing of returns done with rule based system that checks integrity of return. Final assessment at end July, which can be retrieved electronically from web page	Responses evaluated and, if necessary, refund sent to taxpayer. Amounts due have to be paid when return is "filed".	?
Any further developments planned?	Yes. Automatic calculation of mileage allowances on returns and reporting of gifts	Yes. Some plans to obtain data on securities etc for pre-filled returns	System's scope to be extended in 2006 to all taxpayers; usage of Internet for adjustments /7	In 2005, scope expanded & enhancements made to enable adjustments over the web.	Ongoing refinements	Obtaining information from banks	Ongoing enhancements (incl. electronic invoices and exploring their use to prepare VAT proposals)	Focus on reduction on need for adjustments
7) Metrics								
Number of personal taxpayers	4.5 million	0.638 million	4.7 million	3.65 million	7.1 million	0.235million	1.65 million /9	15.4 million (for fiscal year 2004)
Average number of third party reports/ personal taxpayer	20	Not available /8	7	11	12	9	5 (using labour force as base /9	29
Number (and %) of personal taxpayers receiving or	4.5 million (100%)	All (100%)	3.1 million (66%)/6	3.4 million (93%)	7.1 million (100%)	All	In 2005, 1.2 million had access over Internet to a	7.54 million (49%)

Features of System	COUNTRIES SURVEYED							
	Denmark	Estonia	Finland	Norway	Sweden	Iceland	Chile	Spain
having access to pre-populated returns							complete pre-populated return, while 0.5 million had a partially completed return	
Number (and %) who respond electronically	0.9 million (68% of those who respond to the pre-populated return)	0.354 million (76%)	Nil	1.8 million (55%)	2.1 million (30%)	88%	96.3% of total tax returns received over the Internet	?

Sources: Individual survey responses from countries involved

/1. ***Estonia***—The income tax-system in Estonia is proportional. Employment income is subject to a withholding tax at the general rate of 24 percent, starting from 1 January 2005 (and it will further drop by 1% annually until it is equal to 20%). The withholding tax rate on royalties, payments to non-residents for services provided in Estonia, and on payments to non-resident artistes and sportsmen is 15 percent. The withholding tax rate for certain pensions is 10%. The withholding agent (enterprise or employer) has the obligation to remit the relevant amounts to the tax authority monthly. Since the system is proportional, there is no need to implement a cumulative approach.
Finland—The *employee* can choose between a cumulative or a non-cumulative approach. The *employee's* withholding allowance certificate i.e. the tax card for 2005 has two new major features. Wage earners now have the right to choose a withholding scheme either based on the pay period or on a certain amount of annual gross income. The latter scheme, including a certain income limit, is intended for those who only work a few months of the year or for those who have varying amounts of income every month. The opportunity to select between two withholding schemes does not affect the applicable rates of withholding tax. It has been estimated that the new features of the tax card will reduce the processing work at our withholding adjustment service by 500,000 requests per year. If the *employee* chooses a withholding scheme based on pay period the *employer* can chooses between a cumulative or a non-cumulative approach. He/she can either choose to take into consideration only the specific pay period (at each time) or to take into consideration previous pay periods too.

/2. A later date (i.e. 28 February) applies to selected reports (i.e. shareholder borrowings, days unemployed, and trade union fees).

/3. Includes details of sales and purchases of shares and financial instruments, including end of year balances.

/4. Over 2,300 reports received on deductions (covering multiple taxpayers) and 0.925 million reports received from employers covering all employees (monthly reporting requirement.)

/5. Optical reading/ data capture from 2006.

/6. In addition, around 1.6 million received pre-completed returns in 2005 which contain basic identity information, bank account information and details of dependants. In 2006, the tax proposal procedure will cover all individuals who declared their income and wealth for 2005; a facility enabling taxpayers to advise adjustments via the Internet is planned for the future.

/7. From 1987, the Swedish Tax Agency sent out a summary of income statements received from third parties after they had filed their returns. Taxpayers were asked to check this information and advise if it was accurate and complete.

/8. Comparable data not available as employers report monthly. As a result, for most employees there are at least 12 reports per year.

/9. The labour force in the country has about 5.28 million workers. About one million are subject to personal income tax (PIT), given their level of income. The rest have a level of salary under the exempt limit. However, 1.65 million (31% of labour force) presented an annual tax return in 2004, because they are subject to withholding for some of their sources of income.

Annex 2
CONCEPTUAL REPRESENTATION OF PRE-POPULATED INCOME TAX RETURN
(based on the Swedish model)

Key elements	Description of data displayed (all computer-generated)
Personal identification information	Name Address Personal identification number
Summary tax return information	***Aggregate data:*** All income categories All deduction categories All capital income Wealth items Foreign life assurance Real property
Detailed tax return information	***Individual reported items***: Wage income & payers Pension income & payers Interest & payers Dividends & payers Capital income & source Tax withheld at source for each item Pension contributions Other deductions (***)

*** Under Swedish law, the costs of travel to and from work are deductible (where they exceed a threshold of SEK 7,000). Other deductions are also subject to a minimum threshold (SEK 1.000).

Preliminary calculation of liability and final amount payable/ refundable	***Calculations:*** Total income Total deductions Net taxable income Gross tax payable Tax credits Net amount payable/refundable

Additional information (provided by taxpayer, as necessary)

Taxpayer's explanations of any adjustments to items (e.g. income, deductions, taxes withheld at source) in return.