NIGERIA GOVERNORS' FORUM
HelpDesk

TAXPAYER COMPLIANCE MANAGEMENT

Resource Guide for State Internal Revenue Services

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Foreword

The Nigeria Governors' Forum (NGF) has continued to play an active role in strengthening institutional and governance systems at the subnational level. This support has been through the provision of evidence to influence policy formulation and implementation, the development of knowledge resources to strengthen the implementation of reforms and the delivery of platforms for peer learning in areas such as economic development, public financial management, health, human resource management, and citizens engagement amongst others.

To strengthen the reform environment and fast track full domestication of commendable practices across the 36 States, the NGF Secretariat regularly develops guides for implementing State-level reforms based on extensive experience in peer reviewing the 36 States since 2009. This has significantly improved the way State Governments are run and the governance climate in the country.

We encourage States to adapt the approaches documented in this guide given that they have worked in many States. The guide is used by the NGF Secretariat to build the capacity of State governments in strengthening domestic revenue mobilization. It has served as a functional tool at different administrative levels, in the design, implementation and monitoring of sub-national tax reforms.

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Prelude and Acknowledgement

The HelpDesk is a technical support programme instituted by the Nigeria Governors' Forum (NGF) to support States in Improving their development performance by providing demand-based technical assistance in the areas of public financial management (PFM) and domestic financing (Internally Generated Revenue).
This publication is a guide for State Internal Revenue Services (SIRSs) on taxpayer compliance management. It highlights proactive taxpayer management approaches including risk profiling protocols and mitigation actions for motivating compliance and demotivating non-compliance attitudes by taxpayers.

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Acronyms and Abbreviations

BVN	Bank Verification Number
CAC	Corporate Affairs Commission
FCT	Federal Capital Territory
FIRS	Federal Inland Revenue Services
GDP	Gross Domestic Product
HNWI	High Net Worth Individual
IT	Information Technology
JTB	Joint Tax Board
LFN	Laws of The Federal Republic of Nigeria
MDAs	Ministries, Departments & Agencies
NESG	Nigerian Economic Summit Group
NGF	Nigeria Governors' Forum
NGN	Nigerian Naira
NGO	Non-Governmental Organizations
NIMS	Nigeria Identity Management System
NIN	National Identification Number
OECD	Organization for Economic Cooperation and Development
PAYE	Pay As You Earn
PFM	Public Financial Management
PIT	Personal Income Tax
PITA	Personal Income Tax Act
SIRS	State Internal Revenue Service
TCC	Tax Clearance Certificate
TV	Television
TIN	Tax Identification Number
UK	United Kingdom
WHT	Withholding Tax
VAIDS	Voluntary Assets and Income Declaration Scheme

1.0 Background

Ideally, the goal of every tax system should be to see that every taxpayer pays his or her tax correctly, on time and voluntarily to the government. This utopian state which implies 100 percent collection of taxes due is generally referred to as full voluntary compliance. While this would be the most ideal situation, it is not the case with tax systems around the world. By the non-compliant actions of taxpayers, whether due to ignorance, a deliberate act of avoidance or evasion, or weaknesses in tax administration, failure to comply with the tax law is inevitable. Therefore, there is usually a gap between what is collected and what is collectable; this is the tax gap.

An internationally accepted index of measuring the tax gap is the 'tax-to-GDP ratio'. A higher tax-to-GDP ratio reflects a narrower tax gap and a higher level of compliance. Tax authorities pursue a tax regime of steady and sustained improvement in tax performance to achieve a target level of tax-to-GDP ratio considered optimal in the context of the operating environment. To achieve this optimal level of tax compliance, both the taxpayer and the tax authority have roles to play in the tax compliance process, right from tax registration, tax returns filing and declaration to tax payment.

At less than 6%, Nigeria's tax-to-GDP ratio is very low compared to other West African countries and amongst developing countries. This indicates a low compliance level in the country and a high potential to raise tax revenues by implementing measures that will improve compliance. A well-articulated and structured compliance programme that promotes best use of available resources to focus on the most significant risks in the system should be embarked upon by all tax authorities in the country especially at the State-level, where tax compliance is low. The compliance management programme implemented should ensure that both the taxpayer and the tax authority play their respective roles in the entire tax compliance process. While the taxpayer is obliged to provide accurate information for registration, file tax returns and promptly pay the appropriate tax amount, the tax authority should put in place appropriate and cost-effective measures and strategies to ensure that taxpayers comply.

2.0 Objective of Taxpayer Compliance Management

The objective of taxpayer compliance management is to identify and respond to compliance risks in the tax system. This involves instituting appropriate measures and strategies along the compliance process, to motivate taxpayer compliance and maximize tax revenue collection for the government.

3.0 Tax Compliance Process (Registration, Filing, Declaration and Payment)

TAX COMPLIANCE PROCESS

1. Registration	2. Filing	3. Declaration	4. Payment
It is the obligation of a taxpayer to register with a tax office and obtain a tax identification number (TIN)	A taxpayer is expected to fill a tax return, which shows the computation of the tax payable for the tax period.	A taxpayer is expected to fully disclose all financial transactions and the final tax liability in the tax returns filed	A taxpayer must pay the total liable tax amount to be considered compliant.

The tax compliance process covers the stages that taxpayers go through to meet their tax obligations within a legally defined timeframe. These stages include registration, filing of tax returns, the declaration of the appropriate tax and the payment of a final tax liability. The taxpayer has an obligation to first register with the appropriate tax authority, file tax returns at the time required by law, disclose fully the tax liabilities due and finally, pay the taxes due. However, there are compliance risks associated with each of these stages which should be mitigated.

a. **Registration:** The first obligation of a taxpayer is to register with a tax office and obtain a tax identification number (TIN). This number is a unique identifier used in all correspondences between the tax office and the taxpayer. In a bid to improve taxpayers' compliance with their registration obligation, TIN is now a requirement for bank account opening especially for companies and businesses. Similarly, ministries, departments, and agencies (MDAs) of government now insist on the provision of TIN as a prerequisite for the establishment of any business relationship with any company or individual.

   Although company taxes are within the Federal Government jurisdiction, the enlistment of these companies within the Federal Inland Revenue Service (FIRS) database provides a platform that the SIRSs can leverage on to collect Personal Income Tax (PIT) (PAYE and direct assessment) and other eligible State taxes from companies. Some SIRSs still employ manual registration of taxpayers, but many have transited to electronic registration as part of the process of improving the ease of doing business and efficiency in tax administration. It is best practice for a taxpayer to register once and for the singular registration to suffice as registration for all other tax types the taxpayer is eligible for. This should be cross referenced with national databases such as the National Identity Number (NIN) database, Bank Verification Number (BVN) database and Nigeria Immigration Service (NIMS) database for data validity. The taxpayer's data should also be re-validated at regular intervals to maintain data integrity.

b. **Filing of Tax Returns:** A tax return is a statement prepared by the taxpayer showing the computation of the tax payable for a given tax period. There are two types of tax returns filed under the Personal Income Tax Act Cap P8 LFN 2004 (as amended 2011) (PITA), namely:

   i. **Direct Assessment Returns:** This is filed by individuals who are self-employed and liable to the PIT. As the name implies, they are directly assessed to tax on their income.

   ii. **Pay As You Earn (PAYE) Returns:** This is filed by the employer on behalf of an employee for taxes deducted at source from the emolument paid by the employer to the employee.

   A tax return is considered filed when the taxpayer submits their personal income tax return to the tax office within the time frame stipulated in the tax law. The relevant provisions of PITA relating to tax returns are summarized in Appendix 1. In the case of employers, a return is considered filed if it is returned by 31st January of the year following the year of employment. There is also the monthly requirement to submit the schedule of employees for each month and their returns (and payment made) submitted by the 10^{th} of the following month. Other timelines as stipulated in various State legislations may apply for other taxes such as consumption, property, and MDA charges.

c. **Disclosure:** It is not only desirable that a taxpayer should register for tax and file tax returns, but more important is that the tax returns filed disclose fully the underlying financial transactions and resultant tax liability. To do this, the taxpayer must keep proper books of accounts. There should be no hidden or unreported transactions or understated income or overstated expense transactions.

d. **Payment:** This is the final stage of a tax compliance process. The taxpayer is expected to pay the appropriate tax due or final tax liability in the case where an objection was raised to an assessment issued by the tax office. The taxpayer is not deemed compliant until taxes due are paid.

4.0 Legal Frameworks For Taxpayer Compliance

The laws governing taxes administered by the State Internal Revenue Services in Nigeria are:

I. **Constitution of the Federal Republic of Nigeria 1999 as amended.**

Section 24(f) of the Constitution clearly provides that "it shall be the duty of every citizen to declare his income honestly to appropriate and lawful agencies and pay his tax promptly."

II. **Personal Income Tax Act, Cap P8 LFN 2004 (as amended 2011)**

This Act imposes income tax on individuals and provides for the administration of the tax. The Personal Income Tax Act (PITA) governs the Pay-As-You-Earn (PAYE) system which empowers employers to deduct taxes at source from salaries, wages, and other remuneration of employees. The law also regulates the payment of taxes by self-employed individuals (direct/self-assessment) as well as the withholding tax system through which taxes are deducted from payments made to individuals or partnerships and remitted to the relevant State Internal Revenue Service in respect of contracts for service e.g. supplies, management fees, commission, technical services, royalty, dividends, director's fees, etc.

III. **Capital Gains Tax Act Cap C1 LFN 2004**

This law imposes taxes on gains made by individuals or corporate organizations from the disposal of their chargeable assets. The tax is payable to the State Internal Revenue Service if the disposal is by individuals or group of individuals and to the Federal Inland Revenue Service (FIRS) if the disposal is made by corporate bodies. The tax rate is 10% of the capital gain.

IV. **Stamp Duties Act Cap S.8 LFN, 2004**

This Act imposes tax on instruments, agreements or written documents executed between two or more parties. Where one or more of the executing parties is a company, the stamp duty is payable to the FIRS. However, where the parties are individuals or group of individuals, the duty is payable to the State Internal Revenue Service. Stamp duty may be chargeable at a fixed rate or at variable rate (i.e. *ad valorem*), depending on the type of instrument under consideration as provided for in the schedule to the Stamp Duties Act. Under the Stamp Duties Act LFN 2004 (as amended by Finance Act 2019) and the Federal Government Financial Regulations 2009, deposit money banks are mandated to charge stamp duty on their customers on eligible transactions above NGN 10,000 at the rate of N50 per transaction. The regulation presents an updated stamp duty rate and conditions for liability and exemption. There are exemptions for transactions between accounts held by the same bank customer and for salary accounts.

V. **Taxes and Levies (Approved List for Collection) Act Cap T2 LFN 2004 and the Amendment order 2015**

This law was introduced through Decree No. 21 of 1998 to specify the taxes and levies that are collectible by the Federal Government, State Government, and the Local Government. The essence of the law is to curtail the problems associated with multiplicity of taxes, a situation where government at different levels collects the same tax from the same taxpayer. The law limited the Federal Government to eight (8) taxes, the State Government to eleven (11) taxes and the Local Government to twelve (20).

The Minister of Finance on the advice of the Joint Tax Board and exercising the power to amend the schedule of the decree, executed and published the Taxes and Levies (Approved List for Collection) Order, 2015 to the schedule of taxes collected by the 3 tiers of government. Consequently, the taxes and levies collectible by the Federal Government increased from 8 to 9, those by the State Government increased from 11 to 25 while those by Local Governments increased from 20 to 21. The order also introduced a list of 6 levies that are to be harmonized between the State and Local Governments.

On 8th May, 2020, the Federal High Court ("FHC" or "the Court"), sitting in Lagos, declared the Taxes and Levies (Approved List for Collection) Act (Amendment) Order, 2015 ("Amendment Order") null and void. This decision was reached in the case of the *Registered Trustees of Hotel Owners and Managers Association of Lagos ("HOMAL") v. Attorney-General of the Federation & Anor.*

In law this means that all the levies and taxes added in 2015 are not collectable. Therefore, taxpayers can refuse to pay any of these taxes and levies unless a State has passed an explicit law for such a collection. An example is a State legislation on Hotel Occupancy. Consequently, the basis of collection will no longer be Taxes and Levies Act but the State law.

European Commission. 2010. Compliance Risk Management Guide for Tax Administration. [ONLINE] Available at: https://ec.europa.eu/taxation_customs/sites/taxation/files/resources/documents/common/publications/info_docs/taxation/risk_managt_guide_en.pdf . [Accessed 14 May 2019].

5.0 Compliance Risk Management

Compliance risk management is a systematic process by which tax authorities proactively deal with inherent risks identified across tax types, tax groups and the tax compliance process. It informs deliberate actions on which methods, strategies and mitigation actions are best fit to effectively promote compliance and prevent non-compliance, based on taxpayers' behaviours. Inherent risks to compliance include failure of taxpayers to register for tax, file tax returns, make necessary disclosure of income and pay appropriate taxes as at when due.

More specifically, compliance risk management helps the tax authority to achieve the following:

- Respond quickly to changing circumstances.
- Weigh the possibilities that a compliant taxpayer could become non- compliant.
- Ensure that mitigation strategies are applied to activities of the highest priority, and that those strategies have a high probability of success.
- Focus the burden of audit to non-compliant taxpayers.
- Make best use of the available human, financial and technical resources.
- Increase the level of voluntary compliance of taxpayers.

5.1 Limitations to Compliance Risk Management

The success of a compliance risk management strategy will depend on several factors including financial resources, data, technology, economy, enabling legislation, staff capacity and culture. Understanding these factors and their status will go a long way in influencing the design of a risk mitigation management matrix.

- **Financial Resources:** It is important that the tax authority is adequately funded. This is to ensure it can operate effectively and efficiently. Designing and implementing compliance programmes can be expensive, as it requires skilled personnel, innovative technology, and publicity to create awareness on incentives for compliance. Poor funding of any input will impact on the success of the compliance programme.

- **Access to Data and Availability of a Robust Information Management System:** The importance of having credible data on taxpayer background, tax history and associated behavioural patterns cannot be overemphasized. The tax authority will require this information to make informed decisions about mitigating compliance risks. To facilitate real-time data mining of information, the tax authority will require a robust information management system designed to provide quick analytical outputs for the purpose of sorting taxpayer information and identifying risk patterns. The robustness and credibility of data available to the tax authority will determine the extent of success it can record in managing compliance risk.

- **Economic Condition:** The prevailing economic conditions within a jurisdiction can impact tax compliance levels. During recessions or economic downturns, which are usually periods of economic hardship, taxpayers may perceive taxes as burdensome on their already dwindling incomes and may seek ways to evade taxes.

- **Legislation**: It is important that tax laws are not ambiguous. The laws should explicitly state the formal powers, jurisdiction and obligations of the tax authority. The effectiveness of any tax authority strongly depends on the extent of complexity and stability of the tax structure it is expected to administer vis-à-vis its capacity. A good tax law should be appropriate to the environment and enforceable; good enforcement requires a good tax law.

  Also, tax authorities through the Joint Tax Board (JTB) should work more closely to ensure loopholes between the tax legislations/policies of individual States are not exploited by taxpayers desirous of evading taxes. Since **Personal Income Tax is chargeable based on the place of residence,** a taxpayer may exploit the residence rule to avoid or even evade tax. This is usually the case where the tax policy in a neighbouring State is more favourable than the State where the taxpayer is resident. The taxpayer in this case can choose to migrate from the less favourable jurisdiction to avoid paying higher tax rates.

Staff Capacity: Low staff capacity to deal with emerging compliance risks can limit the ability of the tax authority to promote voluntary compliance amongst taxpayers. Key staff skills needed to develop and implement compliance strategies and programmes include interpersonal relationship, data analytics, research, and audit, among others.

- **Public Perception:** The perception of the public especially taxpayers about the quality of governance and service delivery goes a long way in informing their attitude towards taxation. Attitudes shape intentions and intentions affect behaviour. Negative perceptions about the tax authority and government can promote evasion. It is important tax authorities build up taxpayer trust and literacy. It is also important that governments maintain a strong social contract with their citizens. This will build the confidence of the taxpayer in the tax system.

Although there are other factors not mentioned above, those discussed potentially shape the compliance risks that tax authorities face and should be considered in designing a compliance risk management programme.

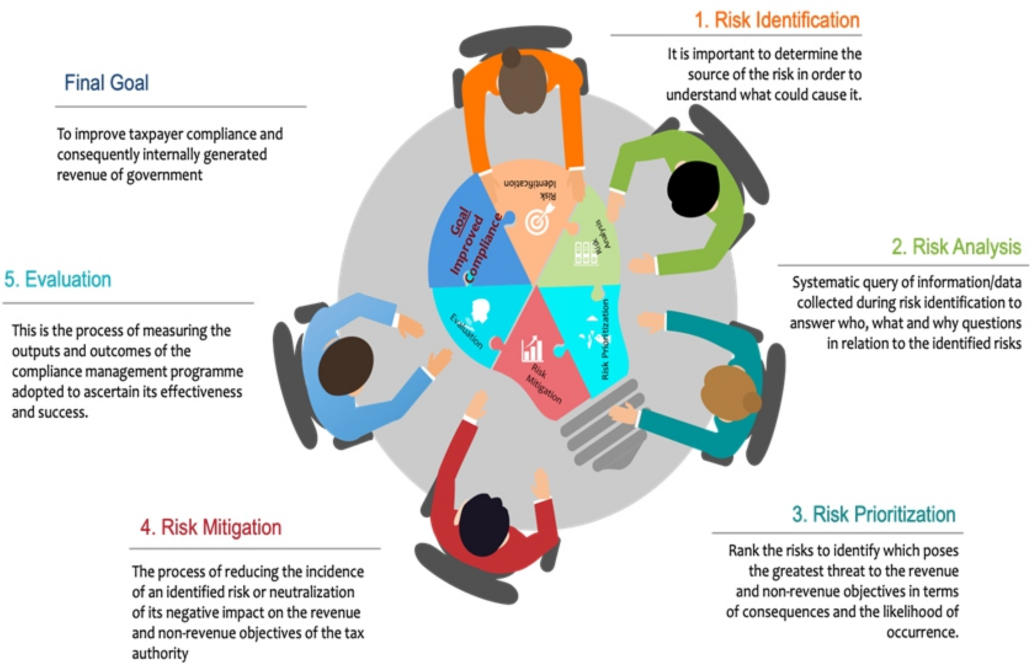
5.2 Compliance Risk Management Cycle

According to the European Commission Compliance Risk Management Guide for Tax Administration, a risk management cycle may be divided into seven (7) consecutive stages. The first three stages relate to risk identification, analysis of risks and the behaviour of taxpayers that cause the risks. The next two relate to mitigation planning i.e. making choices – about (groups of) taxpayers, risks, and options for mitigation as well as the implementation of mitigation actions. The final stages relate to measurement, evaluation, and learning. All 7 stages revolve around the goals offset by the tax authority such as higher compliance or higher taxpayer satisfaction.

Compliance Risk Management Cycle

Source: Organisation for Economic Co-operation and Development. 2004. Compliance Risk Management Guide for Tax Administration. [ONLINE] Available at: http://www.oecd.org/tax/administration/33818656.pdf. [Accessed 14 May 2019].

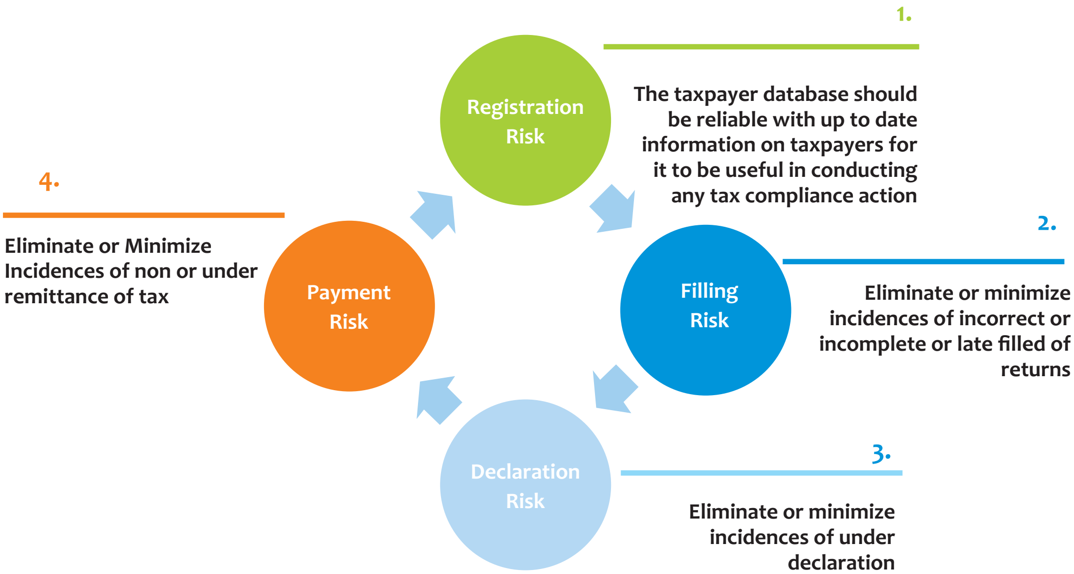
This guide simplifies and consolidates these 7 stages into 5 stages namely, risk identification, risk analysis, risk prioritization, risk mitigation and evaluation. The first 4 stages are the input stages while the evaluation stage is the output – outcome stage.



5.2.1 Risk Identification

This is the first stage in compliance risk management which provides the background to the problem statement. It is important to determine the source of an identified risk to understand what could cause it.

At the risk identification and analysis stage, the tax authority reviewing its engagement with taxpayers based on available compliance data must identify challenging compliance points for individual taxpayers, taxpayer groups and tax types. The earlier these compliance points are identified, the earlier the tax authority will be able to identify and put the perceived risks in context for them to be treated. A



shorter period between detection and action reduces the risk of non-payment and increases the overall compliance outcome. Broadly speaking, compliance risks may be categorized under registration, filing, declaration and payment of taxes.

5.2.1.1 Risk Genres

The first step in effectively tackling compliance risks is to identify the type and nature of risk in question. This is because the type of risk identified will determine the way it should be managed. The type and nature of risk associated with each phase of the compliance process are highlighted below:

I. **Registration Risk:** Registration is the first step in the tax compliance process. At the point of registration, data such as the name of the taxpayer, year of registration or incorporation, business address, residential address of individuals, nature of business or source of income, bank verification number/international passport number/national identity number/voters card number etc. are captured. The taxpayer is then assigned a TIN and subsequent information about the taxpayer is fed into the taxpayers' database of the tax authority, building background and historical information for the purpose of meeting the taxpayer's needs.

    The taxpayer database should be reliable for it to be useful in conducting any tax compliance action. It should be accurate and up to date. One of the risks associated with data integrity is the error of entering incorrect taxpayer information. Where a taxpayer can register with inaccurate data/information suggests data integrity issues for the tax authority taxpayers' database. There is also the risk of including a taxpayer on a list of taxpayers entitled to a particular tax incentive by act of error or omission when that taxpayer does not qualify or no longer qualifies to be on the list. An example is the risk of treating a taxpayer as small taxpayer when the taxpayer has since grown to qualify as a large taxpayer. Other risk areas are risk of data duplication, use of wrong or inaccurate data, etc.

    Beyond taxpayer-specific data, industry, economic and demographic data are also maintained by the tax authority for planning purposes. It is important that a process is in place to ensure that the data collected are reliable in terms of accuracy, timeliness and relevance such as verifying information provided with national or third party databases such as BVN, NIN, Immigration, CAC, trade association, property mart, hotel.ng etc.

    In order to prepare for expected risks, attention should be paid to the source of data; there should be a process of verifying data sources and ensuring that there is no human error in inputting the data into the database of the tax authority. A process of updating the database to take account of changes should also be in place.

As usual with every growth process, capacity, human and technological issues may impede the ability of the tax authority to sufficiently cover all taxpayers and maintain an accurate and reliable database. For this reason, it is considered expedient that periodic database audits are conducted as a key component of the data verification process. Management should take serious interest in the database audit as a poor database presents an opportunity for delinquent or fraudulent taxpayers and officials to abuse the tax system.

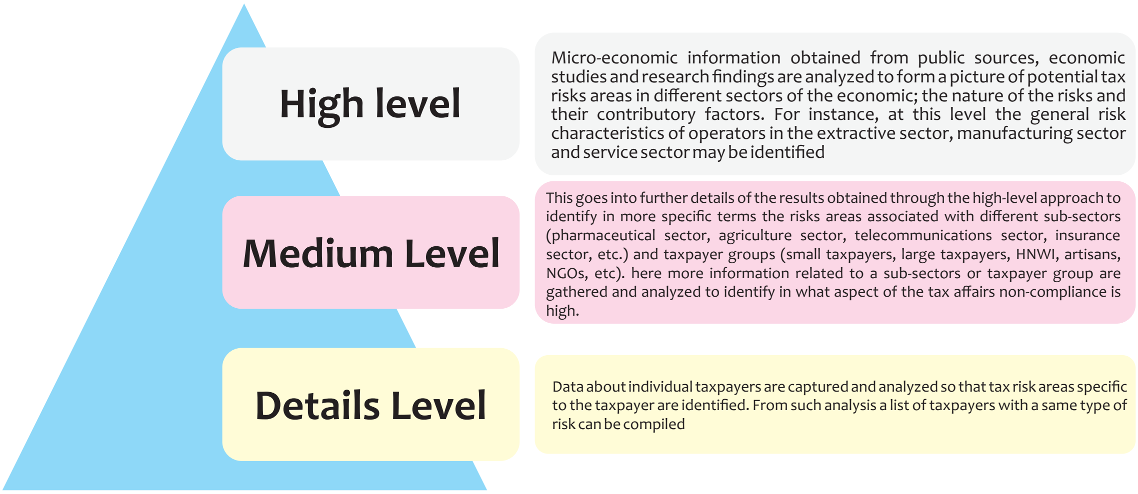
II. **Filing Risk:** Where taxpayers file their returns later than the due date, it reduces the tax yield for the year in which the returns are due. There are also those who fail to file their returns. Such cases require the tax authority to put in place countermeasures to mitigate such cases. Preventive measures will include a widely communicated tax calendar, pre-filling returns on behalf of taxpayers, dissemination of nudge messages to taxpayers especially delinquent ones, increasing engagement with taxpayer representatives/associations where the pattern of risk relates to specific tax groups or tax types, etc. Nudge reminders in widely circulated newspapers, announcements on television and radio may help mitigate filing risks. Corrective measures on the other hand include audits, investigation and sanctions as may be considered appropriate depending on the motive of the taxpayer.

III. **Declaration Risk:** Sometimes taxpayers by error or deliberate act under declare their tax obligations in their tax returns. This is usually the focus of many tax authorities, as they periodically sort out cases for audit and investigation. The tax authority should take proactive steps to quickly flag suspected or incorrect declarations. Where such declarations were unwittingly made, the taxpayer should be immediately informed and permitted to make necessary revisions. However, if the taxpayer's action was ascertained to be deliberate or attempted fraud, an audit or investigation may be carried out, with the application of deterrent penalties and interests including the issuance of a warning letter. Tax authorities may also carry out preventive /measures to encourage taxpayers to get their declaration right from the start. Such measures include the provision of assisted service in tax offices, guides for tax calculation/deduction and the simplifications of tax declaration forms.

IV. **Payment Risk:** A taxpayer is not considered fully compliant until the tax due has been paid. It happens sometimes, that taxpayers comply up to the point of declaration, but fail to pay the right tax stated on their tax return or do not pay the declared tax at all. Dealing with this type of risk requires the use of both subtle and stringent collection and enforcement tactics depending on the tax compliance behaviour of the taxpayer under consideration. For a willing taxpayer who is constrained by financial difficulties duly confirmed, payment by instalments on liberal terms may be given to such a taxpayer. However, for a financially capable but unwilling taxpayer, tough enforcement actions such as imposition penalty and interest, distraint of property, account freezing, substitution order and prosecution.

Linking potential non-compliant taxpayers to any of the risk types discussed above puts the tax authority in a stronger position to mitigate actual non- compliance.

5.2.1.2 *Levels of Risk Identification*



The identification of a taxpayer's compliance risk can be done using a top-bottom approach or the bottom-top approach.

Under the top-bottom approach, the risk identification process starts with a general review of the national or sub-national or regional macroeconomic data to give a general insight into the areas of tax risks in the economy. This is then drilled down to identify areas of tax risks in the sub-sectors or taxpayer groups and further drilled down to individual taxpayers' identity and their specific tax risks.

The bottom-top approach is the reverse of the top-down approach as it starts with risk identification at individual taxpayer level through to risk identification at taxpayer group level and ultimately scaled up to identification of risks associated with the different sectors of the economy as well as the general taxpayer population.

Simply put, these two approaches identify three levels of risk identification namely – High Level, Medium Level, and Details Level.

The High Level of Risk Identification makes use of macro-economic information in the identification. In other words, macro-economic information obtained from public sources, economic studies and research findings are analysed to form a picture of potential tax risks areas in different sectors of the economy, the nature of the risks and their contributory factors. For instance, at this level the general risk characteristics of operators in the extractive sector, manufacturing sector and service sector may be identified. A more specific example is a situation where a key taxpayer engaged in the business of retailing cement files its tax returns showing a low turnover whereas national economic data is showing a huge increase in infrastructure and construction projects. The surge in projects consequently suggests an increase in cement factory output and demand during the period. Such a scenario is therefore an indication of the risk of turnover suppression. For SIRSs, the focus will be PAYE and WHT, which will likely be higher because of increased operations. A lot of the factory workers for firms such as cement companies are on contract and are engaged based on the level of operation envisaged. So where huge demand and profit on turnover is expected, such firms engage more factory staff. To ascertain correctly, changes in their employment profile, a tax audit may be required, examining their financial records more closely. This can also be conducted by way of a joint audit with the FIRS.

The Medium Level of Risk Identification goes into further details of the results obtained through the high level approach to identify in more specific terms the risks areas associated with different sub-sectors (drug sector, agriculture sector, telecommunications sector, insurance sector, etc.) and taxpayer groups (small taxpayers, large taxpayers, HNWI, artisans, NGOs, etc.). Here more information related to a sub-sector or taxpayer group is gathered and analysed to identify in what aspect of the tax affairs is non-compliance high. For example, tax compliance of a sub-sector or taxpayer group can be observed over a period to ascertain which risk genre is particular to them. A medium level analysis may throw up under declaration of income or over claim of relief and allowances as the risk area in a particular taxpayer group. Information from tax audit and tax investigation are very useful in carrying out analysis at this level.

At the Details Level, data about individual taxpayer are captured and analysed so that tax risk areas specific to the taxpayer is identified. From such analysis a list of taxpayers with a particular type of risk can be compiled. The taxpayer database provides detailed taxpayers' compliance information with which the tax authority can draw inference regarding the potential risk nature of each taxpayer.

For example, taxpayer XY from ZQZ local government failed to register until he was caught up in a tax drive. He has persistently filed his returns late and pays only when threatened with court action. The risks therefore are non-registration, non-payment of tax due, etc. And the counter measures to address the risk are enhanced tax drive; routine and closer monitoring as well as legal action to send the right signal to the taxpayer community that non-compliance will not be tolerated.

In conclusion, an effective tax risk identification strategy should entail a general review of a taxpayer's or group of taxpayers' behaviour and attitude with regard to their tax obligation in the areas of tax registration, returns filing, disclosure and payment of tax.

Such a review may be carried out based on taxpayer segmentation using size (a large, medium, small and micro taxpayers), sectors (extractive, manufacturing and services) or industry (such as MDA, Telecommunications, Oil and Gas, Trading, Shipping and Transportation, etc.). This way, the compliance risks peculiar to each individual taxpayer, taxpayer group, taxpayer segment, sectors or industry are identified and strategies for dealing with such risks are formulated.

5.2.1.3 Data Types and Sources of Information for Risk identification

Risk identification involves the analysis of data from sources available to a tax authority. Information specific to individual taxpayers, taxpayer group, trade group, industry or sector is required for proper identification of potential risks that a taxpayer or group of taxpayers poses to the realization of revenue objectives of a tax authority.

In broad terms the information that a tax authority needs to create a database for risk identification purposes may be obtained internally i.e. from its own self-generated information or from external sources such as government agencies, other tax authorities, statistical bulletins, trade associations, trade journals, etc. Other sources of external data include third party circularization, bank information, Pensions office, incorporation documentation with the Corporate Affairs Commission, customs and excise declarations, immigration declarations, internet information (company publications, news alerts), Community or "whistle blower" tip offs. In many cases, the whistle blower provides very concrete evidence to corroborate non-compliance such as duplicate accounts, hidden transaction, computer data and secret bank accounts.

Sources of internal data include tax returns filed with the tax authority alongside accompanying financial statements and employer payroll records (PAYE returns). Others include internal research reports, tax survey, registration drive report, tax audit and 6investigation report.

5.2.1.4 Approaches for Sourcing Information for Risk Identification

As aforementioned, there are several sources from which information for risk identification may be obtained. None of them is sufficient to give good result. The best practice is to combine them to achieve an optimal risk identification outcome. The following approaches can be explored:

Horizon Scanning

This is an organized formal process of monitoring external developments through the gathering, analysing and dissemination of value-added information obtained from external sources to support decision making of a tax authority. It involves cooperation with other tax authorities, MDAs, and law enforcement agencies on exchange of information. In this regard, relevant data; case specific, industry and economic data is collected and continually accumulated over time. The data collected is progressively processed, analysed, and transformed into knowledge and intelligence for the formulation and implementation of a well-informed compliance risk management strategy. A major outcome of such a process is the identification of strategic risks, whether operational or case-based risks. For instance, sectors that are booming may be identified and appropriate measures taken to take advantage of the emerging opportunities for tax revenue.

Legislation, Policies, Regulations

Periodically, the government in a bid to stabilize and stimulate growth in the economy passes legislations, reviews monetary and fiscal policies by issuing regulations bound on all MDAs operations including the tax authority. These sometimes can be counterproductive to the objective of the tax authority to raise tax revenue through increased coverage and effective collection. These legislations, regulations and policies can sometimes have inherent incentives that present opportunities for avoidance hence should be proactively studied to device strategies for managing these risks. The tax authority also needs to step into the shoes of the taxpayer to identify elements of the existing, prospective, and new legislations that offers opportunities for non-compliance with certain tax obligations.

Societal Support

The support of the citizens and interest groups such as the association of tax consultants, accountants, lawyers, etc. should be harnessed to provide information that could aid a tax authority in identifying prevailing tax risks in the society. It happens often that both the tax authorities and these bodies have common interests and so their cooperation and collaboration is easy to foster in achieving a win-win situation.

Engagement with Trade Associations

Every industry or economic sector or trade group has its own peculiarities in terms of culture, trade practices, operational and economic activities. It is therefore desirable for a tax authority to gather data on a particular trade through its trade association. Such data can also be transformed into knowledge and intelligence to aid an understanding of the compliance issues connected with that sector or group. Members of the association can be engaged directly in forums for the purpose of tax education or tax awareness or discussing matters relating to tax compliance in the sector. Establishing relationship with taxpayer groups and their representative associations or union has proven useful in managing non-compliance. The tax authority can get membership information to reduce the incidences of registration, assessment or filling errors, improving the integrity of its database. Informally also, the associations and unions are able to guide the tax authority to the operational complexity, potential areas of tax avoidance and evasion common to the individual professions as well as members under them alongside suggestions on how best to manage them. For example, the association can advise the tax authority on rates for presumptive tax that would yield voluntary compliance.

Engaging other Tax Authorities

It is a common practice globally for tax authorities to cooperate and collaborate in a variety of areas that are of mutual interest including exchange of information, joint audit and investigation, joint training, etc. Such interactions between tax authorities provide a veritable source of data for compliance risk management purposes. The Joint tax Board (JTB) provides a veritable platform for this collaboration and harmonization of interests for the purpose of ensuring effective tax administration and increased revenue mobilization.

Compliance Monitoring Exercise

Monitoring is necessary to assess the workability or efficacy of an existing compliance programme or the emergence of new compliance challenges. Some of these challenges may arise out of an intentional desire of a taxpayer to evade tax or unintentionally arising from a plethora of factors such as new tax legislation, regulations, advances in technology, human and financial resources deficiencies, etc. Information obtained from this exercise may be used in horizon scanning as it may provide a context for identifying a particular type of risk. Similarly, the front-line staff of the service should be encouraged to observe and report emerging avoidance tactics or new risk particular to tax groups for the purpose of improving compliance mitigation strategies.

Random Audits/Investigation

This may also be used to monitor compliance where there is huge doubt that compliance strategy employed is effective and therefore loss of tax revenue is envisaged. Third party information including whistle blowers' testimony can also provoke an audits or investigation. Again, information obtained may be useful in horizon scanning.

5.2.2 Risk Analysis

The task in risk analysis is to systematically process and query information/data collected during risk identification to obtain knowledge and intelligence to answer the following questions - *who, what and why* in relation to the identified risks:

- Who are the risky taxpayers?
- Why do identified risky taxpayers behave the way they do? What are the reasons for the risky behaviour of the taxpayers?
- What are the characteristics of the identified risky taxpayers?
- What is the likelihood and frequency of the risk reoccurring?
- What are the indicators of the identified risks?

- What is the trend of the risk - is it growing or declining?
- What are the possible mitigation measures or options to deal with these risks?
- What is the average cost of a mitigation action?
- What are the consequences or effects or impact of these risks on tax revenue objectives -low, medium, or high?

The essence of risk analysis is to establish risk profiles for various taxpayer groups, understanding the behavioural trends for tax compliance, casual factors, and likelihood of reoccurrence of non-compliance. Due to the large volume of data and trend analysis to be computed and compared, risk analysis is easier done using computer systems that support data analysis.

Pre-registration information is compared with residential addresses, database of government MDAs and third-party organizations including associations and societies. Post-registration profiling is done upon receipts of tax returns or based on periodic reviews pooling several taxpayers together or incidental due to an event warranting the review of a number of taxpayers or taxpayer groups.

Exercise One: Based on your key function or department, list the risks to taxpayer compliance that you may face. Use the who, what, and why questions

(45 Minutes)

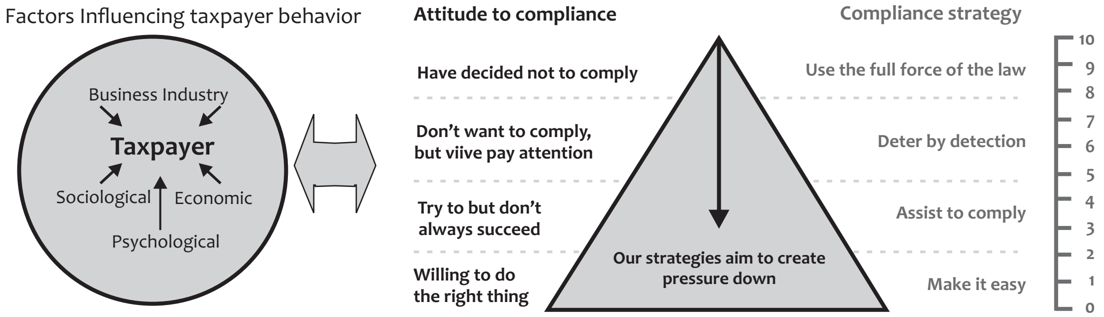
- Who are the risky taxpayers?
- Why do identified risky taxpayers behave the way they do? What are the reasons for the risky behaviour of the taxpayers?
- What are the characteristics of the identified risky taxpayers?
- What is the likelihood and frequency of the risk reoccurring?
- What are the indicators of the identified risks?
- What is the trend of the risk - is it growing or declining?
- What are the possible mitigation measures or options to deal with these risks?
- What is the average cost of mitigation action?
- What are the consequences or effects or impact of these risks on tax revenue objectives -low, medium, or high?

5.2.2.1 Risk-Based Taxpayer Profiling Process

A tax office administers taxes on different categories of taxpayers. There will always be some element of risk associated with every taxpayer either based on individual own characteristics and peculiarities or as a member of a sector or an industry. It is therefore important that taxpayers are profiled in their individual capacities or as a group or a combination of both. The profiling will enable a tax authority to properly manage its taxpayers by classifying them according to their compliance risk level- high risk, medium risk, or low risk. Such risk classifications serve as a guide to determining which compliance mitigation strategy to employ. Profiling should cover the entire cycle of the tax administration process namely - tax registration, returns filing, tax information disclosure or payment of tax.

5.2.2.2 Identifying Causal Factors

Recognizing a Spectrum of Compliance Behaviour



Source: OECD: Managing and Improving Tax Compliance (2004)

A tax authority should have as standard a level of tax compliance that it would consider as optimal. A deviation or variance from the standard constitutes non-compliance. A significant variation is a cause for concern. The goal of a tax authority is to keep the deviation to a level as a low as possible. To achieve this, it must identify the causal factors i.e. factors that caused the deviation. The Figure above shows that the compliance behaviour of taxpayers can be influenced by a combination of factor(s) emerging from their association with a type of business, industry, sociological, economic, and psychological traits. These factors can be internal or external to the tax authority. It is internal when non-compliance is attributable to wrong actions or failure on the part of the tax authority to follow due process or institute a tax administrative system that encourages voluntary tax compliance for businesses, industries or taxpayer groups or demographic. For example where corruption is vibrant in the tax authority, the taxpayers are left with the believe/assumption that the tax system does not work and that they can pay to cheat the system either by getting tax official to permit a wrong assessments or accept underpayments as if they are correct. External factors on the other hand are outside of the tax authority's control such as sociological issues like poverty and poor education, psychological issues like greed and poor values, business/industry changes like technological revolution and introduction of new national guidelines for private operators and lastly, economic events like inflation, recession, government policies, interest rates, etc.

To understand these factors more closely, the tax authority will need to consistently engage with relevant stakeholders including associations/industry players/society to identify economic, social and technological patterns that might directly or indirectly cause non-compliance/poor compliance within a period. Similarly, delinquent taxpayers caught by the tax authority should not just be penalized or prosecuted in the case of deliberate evasion but be interviewed to understand factors that might have triggered the non-compliance act. For example, a sudden surge in unemployment for a sector due to technological evolution can cause many taxpayers to begin to hide income to avoid/evade taxes because they do not want further expense pressures on their income at the time. Same act can be triggered by a recession or economic crisis during which businesses and their owners/shareholders might explore concealing income ordinarily subject to taxes. On another hand, deliberate evasion can be common with persons in places of authority or affiliated with Government and with believe that they can be exempted from penalties/prosecution even when they deliberately renege on their tax obligations.

Also, the inefficiencies in the tax system such as poor database integration and collaboration among tax authorities presents non-compliant minded taxpayers with the confidence that they can effectively avoid/evade taxes by exploiting the residency rule. This has been a common dispute between States like Ogun and Lagos State, Abuja, and Nasarawa State, etc. Taxpayers sometimes migrate between States based on their perception of how convenient the tax policy and rates in a State are. This is because without cooperation and data integration among the tax authorities, it is difficult for a State Internal Revenue Service to easily confirm a taxpayer registration status with another State Internal Revenue and the validity of Tax Clearance Certificate (TCC) where the taxpayer claims to have registered and paid taxes there. The JTB TIN project when fully implemented will assist in addressing this problem as one TIN will apply to a taxpayer in all its dealing with any tax authority in Nigeria at both Federal and State levels.

Overall, the tax authority must not just identify risk but also understand why certain taxpayers employ certain avoidance/evasion tactics at certain periods. The periods within which these activities happen or surge the most should be closely studied, as the associated risk with the particular taxpayer/group may just be seasonal.

5.2.3 Risk Prioritization

This is the third stage in the compliance risk management cycle. After risks are identified and analyzed, the tax authority will need to rank the risks to identify those requiring immediate mitigation. This is because it may not be feasible to address all risks for a variety of reasons including costs implication, the magnitude of its effect on tax revenue, etc. A tax authority must therefore devise a means to choose which risk poses the greatest danger to its revenue mobilization objectives in terms of consequences and the likelihood of its occurrence. Risk prioritization should be a continuous process due to the dynamic nature of the business environment and the compliance behaviour of taxpayers.

Factors to be considered in doing this include:

- The source of the risk identified.
- An assessment of its potential consequences for the tax authority.
- The likelihood that the consequences will occur (in the absence of any specific mitigation).
- The amount of tax directly or indirectly involved. This amount would have been determined in the risk analysis phase.
- The available mitigation routes: Risk transfer (passing the risk to other parties), risk reduction (minimizing the frequency and/or the extent of the risk in a coming period) and risk covering (carrying out activities to neutralize the impact of the risk).
- The resources available for risk mitigation (for instance, staff time in hours and competence to handle the risk in question).
- The social and political effects. In deciding what risk to select or not to select, tax authority should consider the deterrent effect, social acceptability, and effect on compliance levels of taxpayers. For instance, treating some risks can have a positive deterrent effect on the society and the taxpayer, while addressing others may have a negative deterrent effect. Those risks that when tackled will resonate positively with members of the society or incentivize an improvement in the compliance levels of taxpayers, should be given priority.
- The need for randomness in the choice of which risk to treat to have some element of unpredictability in the process.

The process of risk prioritization involves the following steps:

First, risk levels should be defined and assigned weights to express their severity. See below an example of risk definition and application to a SIRS context

Risk Level	Risk Weight
Extreme	5
Very High	4
High	3
Medium	2
Low	1

Consequence Rating					
Risk Criteria/ corporate Objective	1 Low	2 Medium	3 High	4 Very High	5 Extreme
Revenue Risk **Deliver to Government**	Objective achieved...				
	Variation of from revenue target of NGN2 billion monthly				

Consequence Rating					
Non- Revenue Risk	Less than NGN 100 Million	Between NGN101 Million and NGN500 Million	Between NGN501 million and NGN700 Million	Between NGN701 Million and NGN1 Billion	More than NGN1 Billion
Objective achieved...					
Maintain taxpayer confidence	Criticisms which ...				
	Is justified but minor and likely to last less than a week	Is justified but minor and if left untreated could cause loss of support	Results in moderate loss of support and small amount of adverse media coverage	Results in large amount of adverse media coverage and causes major damage to the authority's reputation	Results in large volume of adverse media coverage, attracts government scrutiny and causes extensive wide ranging and long-term damage to reputation
Minimize Compliance Costs	We achieve... from baseline				
	No change =0	Minor increase (<5%)	Serious increase (5% - 19%)	Major Increase (20% – 39%)	Huge increase (=/>40%)
Reduce assessment related complaints	We achieve... from baseline				
	No change =0	Minor increase (<5%)	Serious increase (5% - 19%)	Major Increase (20% – 39%)	Huge increase (=/>40%)
Increase number of taxpayers in taxpayer database (Active)	We achieve... from baseline				
	No change =0	Minor increase (<5%)	Serious increase (5% - 19%)	Major Increase (20% – 39%)	Huge increase (=/>40%)
Improve voluntary compliance by taxpayers (Direct Assessment)	We achieve... from baseline				
	No change =0	Minor increase (<5%)	Serious increase (5% - 19%)	Major Increase (20% – 39%)	Huge increase (=/>40%)
Improve voluntary compliance by taxpayers (informal sector)	We achieve... from baseline				
	No change =0	Minor increase (<5%)	Serious increase (5% - 19%)	Major Increase (20% – 39%)	Huge increase (=/>40%)

- **Low (1) – Medium (2) = Little or no negative impact requiring no strong/ immediate action**
- **High (3) – Extreme (2) = Negative impact warranting strong/immediate action**

Beyond assigning levels to risks, they should be categorized by likelihood of occurrence.

Compliance Risk Likelihood Matrix[3]

Rating	Likelihood Description	Illustrative definitions to help determine the likelihood rating	
		Subjective definitions	Objective definitions
1	Rare	May occur only in exceptional circumstances	Likely to occur once in 3 years
2	Unlikely	Could occur at some time	Likely to occur once in 2 years
3	Possible	Might occur at some time	Likely to occur once this year
4	Very Likely	Will probably occur in most circumstances	Likely to occur twice this year
5	Almost certain	It expected to occur in most circumstances	Likely to occur more than twice this year and at frequent intervals

N.B: Likelihood description and definitions can be domesticated as appropriate.

Matching the likelihood of risks with the level of their intended consequence allows the SIRS assign risk ratings – low, moderate, significant, high, and severe as shown in the compliance risk-rating matrix below.

Compliance Risk-Rating Matrix[4]

Consequence						
	Extreme	High	High	Severe	Severe	Severe
	Very High	High	High	High	Severe	Severe
	High	Significant	High	High	High	High
	Medium	Moderate	Moderate	Significant	Significant	Significant
	Low	Low	Low	Moderate	Moderate	Moderate
		Rare	Unlikely	Possible	Very Likely	Almost Certain
				Likelihood		

The compliance risk-rating matrix informs responsibility assignment within the SIRS as shown in the responsibility table.

Responsibility Table

Risk Rating	Management
Severe	Executive management and State Government
High	Executive management
Significant	Senior management
Moderate	Middle management
Low	Adhoc Staff with middle level management

[3]Source: OECD: Managing and Improving Tax Compliance (2004) https://www.oecd.org/tax/administration/33818656.pdf

[4]Source:http://ec.europa.eu/taxation_customs/resources/documents//taxation/tax_cooperation/gen_overview/Risk_ Management_Guide_for_tax_administrations_en.pdf

For example: The risk of failure to pay tax by a major taxpayer who is known to be contributing on the average about 10% of the total tax revenue in a year will be adjudged HIGH even if it is UNLIKELY that the taxpayer will fail to pay tax to the revenue authority in a particular year. This is simply because if the taxpayer does fail to pay in a particular year, the CONSEQUENCE on tax revenue will be high. What is done here is to simply match "unlikely" in the Likelihood horizontal row with "high" on the Consequence vertical row.

Exercise Two:
Following the earlier exercise, prioritise the risks you identified using the matrix below.

- Assign an impact level and likelihood of occurrence.
- Assign management responsibility based on results.

S/N	Risk	Impact					Likelihood					Compliance Risk Rating	Responsibility
		1	2	3	4	5	6	7	8	9	10		
		Low	Medi-um	High	Very High	Extreme	Rare	Unlik-ely	Possi-ble	Very Likely	Almost Certain	(Impact x Likelihood)	
1													
2													
3													
4													
5													

S/N	Compliance Risk Rating (Impact x Likelihood)		Responsibility
1	Severe	36 to 50	Executive Management and State Government
2	High	21 to 35	Executive Management and State Government
3	Significant	16 to 18	Senior Management
4	Moderate	8 to 14	Middle Management
5	Low	7 and less	Ad-hoc Staff with Middle Management

5.2.4 Risk Mitigation

After the identification and analysis of the risk, a judgment is made as to consequences if not addressed. If the risk is considered significant enough to warrant action, an appropriate action is planned and implemented. The process of reducing the incidence of an identified risk or neutralization of its negative impact on the revenue objectives of the tax authority is regarded as risk mitigation. This should be executed in the most cost effective and timely manner possible. Hence, the tax authority reviews the risk mitigation plan to identify the most appropriate, effective, and efficient mitigation actions to address an identified risk given the prevailing circumstances established under risk assessment for prioritization. It is analogous to medical mitigation interventions that follows a diagnosis of a chronic and possibly avoidable ailment.

Broadly, risk mitigations are categorized under the following:

i. Risk Transfer
ii. Risk Reduction
iii. Risk Covering

5.2.4.1 Risk Transfer

Risk transfer is a means by which the tax authority shifts compliance risk to another organization/entity. An example of this is the appointment of banks as collection agents, hence, holding the bank responsible for ensuring that amount enough to cover concluded assessed liabilities is held on the account of a taxpayer. Similarly, the tax authority can contract out some of its collections, agreeing to a fixed tax remittance sum by the collecting agent to it periodically. In both cases, the payment risk has been transferred to the bank and a collection agent who is now responsible for payment recovery from the taxpayer.

One legal way of mitigating the payment of tax is by using Withholding Taxes (WHT). WHT is an advanced payment of income tax recognized by the tax law. The legal provision for WHT[5] mandates for an amount (See appendix one for WHT schedule of applicable rates) to be withheld from payment for a contracted service and remitted to the relevant tax authority with which the service provider is registered for tax purposes. The withheld amount remitted to the tax authority serves as an advance payment and is set off the final tax liability of the service provider. WHT from transaction with individuals is paid to the SIRS (FCT IRS in the case of residents in the FCT) while that from transaction with companies and non-resident individuals is remitted to the FIRS.

By this singular action, the tax authority has transferred part of the payment risk to the paying organization; making it accountable for a percentage of the taxpayers actual tax liability incurred on the income earned from providing service to the organization. Under WHT, if the deduction is made, then the SIRS can hold the payer to account for the unremitted tax. But there must be evidence that the payee received the payment net of the WHT. If the payee was paid the gross amount, then the SIRS will not give a credit for the WHT until evidence is provided for the deduction**Case Study**

Ogun State risk transfer strategy

The Ogun State IRS in conjunction with key stakeholders such as the Motor Parks & Garage Unions, Local Governments, Ministry of Environment and Commercial Motorcyclist Unions introduced a harmonized charge of NGN 300 per day by way of ticketing. A percentage of which is retained by the OGIRS while other stakeholders share the balance on each charge. The risk transfer strategy adopted for the collection

[5] The applicable laws on withholding tax in Nigeria are of the Personal Income Tax Act (PITA), Sections 69 – 72

process was the OGIRS selling the ticket booklets to the associations at a subsidized rate that ensures the service gets its share accruing to the government upfront while the difference between the wholesale price and the retail price of NGN300 accrues to the association as cost of collection.Other risk transfer mitigation actions include contracting collection to trade/market association in the case of informal sector taxpayers and the adoption of bulk ticket sales in the case of road taxes.

Case Study

Ogun State risk transfer strategy

The Ogun State IRS in conjunction with key stakeholders such as the Motor Parks & Garage Unions, Local Governments, Ministry of Environment and Commercial Motorcyclist Unions introduced a harmonized charge of NGN 300 per day by way of ticketing. A percentage of which is retained by the OGIRS while other stakeholders share the balance on each charge. The risk transfer strategy adopted for the collection process was the OGIRS selling the ticket booklets to the associations at a subsidized rate that ensures the service gets its share accruing to the government upfront while the difference between the wholesale price and the retail price of NGN300 accrues to the association as cost of collection.

5.2.4.2 Risk Reduction

This refers to methods employed to mitigate the frequency of risks occurring in the future. Mitigating actions to reduce risks can be categorized under the following approaches:

a. Limiting opportunities for the risks to occur.
b. Reducing unintentional errors.
c. Reducing intentional errors.

a. Limiting Opportunities for the Risks to Occur

This involves taking actions that continually reduce opportunities for errors, deliberate or accidental, to happen. The goal of this approach is to ensure that there is no occurrence or reoccurrence of treated errors.

Some measures used by tax authorities to limit opportunities for risk to occur include:

Legislative and Policy Actions: This is done through initiatives such as new or amended legislation to address existing loopholes, ambiguities or grey areas in tax administration exploited by taxpayers for the purposes of tax avoidance/evasion.

- Introduction of thresholds in tax legislation so that attention and focus is directed better at risks of high tax significance. By this, less significant risks are eliminated. For instance, a tax legislation could provide that persons with annual income of less than N1, 000, 000 should pay a flat rate of N10, 000 per annum. Threshold for sales tax registration may also be introduced based on turnover so that only those who meet a certain turnover threshold may register for and collect sales tax.

- Introduction of new provisions within the guiding legal framework to limit authorization and approval of delicate tax administration assignments, duties, or tasks to skilled and experienced cadres within the tax authority. For instance, only experienced and skilled staff within the tax authority should be authorized to approve certain tax incentives/waivers/exemptions. This limits the risk of granting exemptions/waivers and incentives to deliberately delinquent or undeserving taxpayers by inexperienced tax officers within the service.

Introduction of New Legislation or the Repeal/amendment of limiting Legislation: A tax authority cannot operate outside the provisions of the tax laws. Hence, it is imperative that where there are provisions within the existing legislation limiting the tax authority to effectively function, the tax authority pursues a repeal/an amendment. Considering the tax environment is dynamic, new legislations are sometimes required to address new areas or technicalities that cannot be captured through an amendment of the existing legislation.
It is therefore necessary to conduct a periodic review of the enabling tax laws guiding tax administration. Common issues observed from past reviews include low penalty regimes that do not deter offenders, complex and ambiguous provisions, complex wording and little or no autonomy for the tax authority to function effectively. Explanatory circulars, practice direction and regulations that will improve tax compliance should also be made a feature of the tax authority's compliance programme.

Introduction of Strategic Tax Schemes: An example could be keying into the FIRS platform for collection of WHT due on payments made to companies. A software can also be deployed by SIRSs to directly collect and remit WHT due on individual transactions as this is within their jurisdiction to collect. Also, a version of the Federal Governments' Voluntary Assets and Income Declaration Scheme (VAIDS) can be adopted at State level to improve tax compliance and boost tax revenue.

Technological Solution: The use of information technology in tax administration can eliminate risks arising from human errors. For example, errors that may arise from manual transfer of tax data from paper to a digital format is eliminated using a taxpayer information management database programme. In the same vein, human errors associated with manually carrying out validity checks on the tax returns are eliminated with integration of the taxpayer database with key identity verification platforms e.g. BVN, NIN, NIMS, etc. Also, electronic copies of prefilled tax returns can be sent to taxpayers to limit filling errors.

Collaborations: An integrated and collaborative approach to tax administration is a recognized best practice across tax administrations. Tax authorities must see collaboration with relevant government and non-governmental organization as *sine qua non* in improving taxpayer compliance. These collaborations are entered into by way of agreements, MoUs and informal alliances. From experience, collaborations work better and are sustained when they deliver a win-win outcome- meaning that all parties benefit from the relationship.

b. Reducing Unintentional Errors

This mode of risk mitigation recognizes the fact that not all errors made by taxpayers are intentional or deliberate and therefore aims at reducing those errors that are unintentional. The forms of risk mitigation that may be used to reduce such errors include:

- Simplification of tax legislation to make compliance easy
- Consistency in the interpretation and application of tax legislation and regulations
- Tax registration process should be simple and information to be supplied by the taxpayer at this level of the compliance should be limited to only those that are essential for taxpayer identification- contacts and nature of business. Online self-registration platforms should be considered, as it may be more convenient for some taxpayers.
- Tax returns filing should also be made easy for taxpayers. Complicated forms and voluminous annexures should be replaced with simplified versions that capture only the essential information required for a correct determination of the tax payable.
- Pre-filling of tax returns and tax forms by the tax authority using taxpayer historic data. Amendments can however be made at the behest of the taxpayer where the taxpayer has information that is different from those used by the tax authority. However, the tax authority should have embedded in this process a system of checks and balances.
- Developing guidance notes such as explanatory notes accompanying tax returns, public notices, tax leaflets, tax bulletins, etc. easily accessible to taxpayers and tax consultants. The language used in writing them should be simple, clear, and easy to understand.
- For the micro and small taxpayers, the road to optimal tax disclosure starts with the bookkeeping practices. A lot of these taxpayers do not have the human and financial capability to meet this need. Therefore, assistance by way of workshops and training sessions, distribution of bookkeeping information pamphlets, help desks, etc. may be provided to these categories of taxpayers.
- Use of mass media – press, radio, television, and the internet to

disseminate information to reach a huge population of taxpayers.
- Setting up dedicated enquiry toll free telephone lines, contact us form and possibly a chat plugin on the website of the tax authority.

c. Reducing Intentional Errors

Intentional errors are infractions by taxpayers considered to be tax evasion or tax fraud. These types of error are committed by taxpayers who intentionally take steps to commit them regardless of whether the tax system creates opportunity for it. The following mitigation measures can be adopted.

- **Increasing Perceived Probability of Detection**

When a taxpayer is under a high and increasing perception that there is high likelihood that any infraction of the tax law will be detected and addressed, they are likely to conduct themselves in a more compliant manner. It is however the duty of the tax authority to create such an environment through its actions. The publicity of deterrent and enforcement actions taken by the tax authority against taxpayers found to be non-compliant especially those guilty of evasion and tax fraud triggers a positive reaction towards tax compliance amongst other taxpayers. Getting the right impact from this approach requires employing the right enforcement communication strategy focused on discouraging tax evasion and tax fraud. The strategy can be to use a combination of publications, recent audits and investigations, press releases on distraints and enforcement actions executed or even warning notices.

Meanwhile, care must be taken to ensure that all efforts aimed at creating an atmosphere where taxpayers increasingly perceive high probability of detection of intentional errors are characterized by transparency, openness, certainty, accessibility, and an accommodating attitude. To do otherwise, may create uncertainty, which will be counterproductive.

- **Enroll the Participation of the Public in the Process**

Generally, it is a bilateral relationship that exists between the taxpayer and the tax authority. The goal here is to expand it into a tripartite relationship by enlisting the public as an interested third party and thus provoking their interest in ensuring that every citizen is tax compliant. This can be done in several ways including:

- Asking citizens to demand invoices and receipts for all purchases and payments.
- The use of a well-crafted emotional campaign such as "the less others pay, the more you pay".
- Encouraging whistle blowing.

5.2.4.3 Risk Covering

Risk covering is the risk mitigation approach used to manage high-risk taxpayers whose non-compliant behaviour is rooted in a deliberate and conscious effort to cheat the tax system. The method subjects them to repressive control measures and actions. It should be noted that the sooner the risks are analysed and detected, the sooner they can be addressed. The following approaches below are considered under risk covering:

Request to the Taxpayer

This involves sending written letters, emails and even placing a call through to a taxpayer persuading he/she to voluntarily declare truthfully. The taxpayer may also be asked to provide documents and explanation on specific grey areas regarding his/her tax compliance. Contacting the taxpayer could also be to communicate an invitation for voluntary disclosure in return for less punitive sanctions. An invitation for voluntary disclosure may be addressed to a group of taxpayers, for instance, taxpayers who are known or suspected to operate undisclosed foreign accounts or own offshore investments that have not been disclosed to the tax authority. Interaction and communication via channels under this type of risk covering should be guided by a questionnaire to uphold a certain standard desired by the tax authority.

Desk Inspection

This form of risk covering involves an inspection of the tax returns upon submission by the taxpayer to the tax authority. The inspection is conducted in the tax authority's office and may be restricted to a part of the tax return or the whole of the tax return. During the inspection, the taxpayer may be contacted to send in additional documents for the purpose of the inspection.

Field Audit

This involves on site visit to the taxpayer's premises during business hours with the aim of examining the books and records of the taxpayer and collecting information to aid the tax authority in addressing the risks posed by the taxpayer. The advantage of the field audit over the desk inspection is the opportunity to observe how things are done, obtain direct information about the taxpayer's business including the level of its activity. In the case of SIRS jurisdiction, the tax authority can examine liabilities for WHT and PAYE from these records, as it will likely indicate the number of staff on payroll and contracted services for which WHT is liable.

While an audit should be communicated to the taxpayer upon commencement, a visit to his/her premises may be unannounced especially where the taxpayer in question is high risk and might likely destroy relevant records and documents. An important point to note in constituting an audit team is to have people with the right skills, knowledge, and experience for the concerned audit. So, an audit team may comprise of persons other than a tax inspector like IT specialists, accountants, lawyers, engineers occasioned by type of income source/taxpayer whose risk coverage is the object of the audit.

Tax Enforcement

The goal of every tax authority is to see that all taxpayers voluntarily comply with their tax obligation in all phases of the tax compliance process from tax registration to the payment of tax due. While this expectation may be utopian, some degree of voluntariness is expected from every taxpayer. Every tax authority should be able to define the acceptable level of compliance beyond which some degree of force may be deployed to bring the taxpayer into compliance. Tax enforcement should be an integral part of the tax compliance process. Tax enforcement measures available to a tax authority include search and seizure, distraint, substitution[6], account freezing order, etc.

Criminal Investigation/Prosecution

Where a taxpayer's risky behaviour is criminal nature, the taxpayer automatically becomes a suspect for which a criminal investigation is initiated. This is a more intensive risk cover treatment. The aim of the investigation is to collect evidence for criminal prosecution in court. Because of the need to comply with the rules of evidence and other legal issues at stake, it is strongly advised that specialists and experts handle the investigation process. Above all, a criminal investigation should be sparingly used and any decision to use it must be well considered in the light of the effect it may have on the entire tax environment. While a successful criminal prosecution will have a positive effect where the risk bothers on gross abuse of the tax system, it could be counterproductive in a situation where a less adversarial approach is most appropriate. It could also be very expensive and time consuming.

5.2.5 Evaluation

Evaluation is essentially the process of measuring the outputs and outcomes of the compliance risk management programme especially checking how effective and successful risk mitigation measures adopted by the tax authority have been.

Output refers to what is produced (e.g. number and quality of audits performed, or the amount of tax collected) while outcome refers to the impact or effect (e.g. change in compliance level). Therefore, the evaluation stage is concerned with answering three critical questions:

1. What are the outputs and outcomes of the compliance programme?
2. Does the outputs and outcomes meet expectation? In other words, did the compliance programme work?
3. How and why did it work or not work?

In providing answers to these questions, the following steps should be taken:

1. What was the baseline compliance outputs and outcomes?

[6]Substitution is the act of appointing an agent as a tax agent for the purpose of tax liability recovery from the taxpayer. This is supported by Section 50 PITA 1993.

2. Set targets and timeframe for the outputs and outcomes desired from the new programme. For example, target for output could be say 20% annual increase in audits completed within the next 5 years while target for outcome could be a 3% annual increase in tax/GDP ratio within next 5 years.
3. Adopt objective and scientific (as much as possible) data collection methods (e.g. in-house tax data, web survey forms, paper questionnaires, telephone calls, etc.).
4. Analyse the outputs and outcomes achieved during the period of implementing the new compliance programme e.g. during the five-year period as indicated in step 2 above.
5. Compare outputs and outcomes achieved with targets, highlighting variances.
6. Analyse the variances to explain the cause and necessary remedial action and mitigation measure.

The above steps depend heavily on a having a robust database and a strong skilled monitoring & evaluation team. There should be an efficient and effective data gathering process that produces data of high quality and integrity. Also, the evaluation process should consider external factors such as changes in the economic environment and changes in legislation.

5.2.5.1 Case Studies

Two evaluation case studies are presented below:

Case Study 1[7]

Evaluating compliance campaigns to change the tax compliance attitudes of a specific segment of the community by the Swedish Tax Agency

The Swedish Tax Agency undertook extensive surveys to assess the attitudes of people in the community towards tax issues. The surveys revealed that young people had a more positive attitude towards tax evasion than the total population. One item in the survey was: 'I think it is okay to evade tax if I have the opportunity'. 12% of the age group 18-24 agreed compared to 7% of the total population.

The agency decided to run a campaign with the objective of influencing attitudes of young people towards less acceptance of tax evasion. The campaign was designed to run for three years. It started in 2002 with TV-advertising (a short film about how the society would look like if they didn't pay tax), distributed information in schools about how the taxes are spent and the Director General sent a letter to the target group with some information about taxes. A website was developed for general tax information. During the second year, the campaign continued with additional TV-advertising showing the connection between taxes and benefits like healthcare, libraries,

[7]European Union. 2010. compliance risk management guide for tax administrations. [ONLINE] Available at: https://ec.europa.eu/taxation_customs/sites/taxation/files/resources/documents/common/publications/info_docs/taxation/risk_managt_guide_en.pdf . [Accessed 14 May 2019].

infrastructure etc. The municipalities also put up small posters (stickers) with the message 'Paid for by you' on park benches, waste bins, schools, and similar objects.

The surveys as at 2004, showed that the campaign was working and that the attitudes of young people have changed. Attitudes became comparable to those of the total population with only 7% in the age group 18-24 agreeing with survey question: 'I think it is okay to evade tax if I have the opportunity'.

Note: Even though the above scenario came from a study done in Europe where tax compliance is higher compared to Sub-Saharan Africa, if a survey with the same question is conducted in Nigeria, it is very likely that a far higher percentage of the sample will support tax evasion. According to a Nigeria Economic Summit Group (NESG) report that surveyed 10,000 households and 5000 small firms (<50 employees) in 2019, more than 50 percent of the population believes that although government has a right to tax them, not paying tax is justified. Also, the survey showed that only 12% of Nigerians have received any kind of communication from the Government about the taxes that they should pay in the last year. This indicates that more sensitization and tax education need to be conducted by the tax authorities. This includes making available to the public necessary educational and guidance materials on how to be tax compliant.

Case Study 2[2]

The use of letters designed to influence the compliance behaviour of a specific group: The UK Experiment

In the United Kingdom, self-assessing self-employed businesses with a turnover under £15K are not required to provide analysis of expenditure in their Income tax returns. Routine monitoring and statistical analysis of the returns for businesses in this category for both 1999 and 2000 indicated that many people appeared to be suppressing turnover so that they would fall below the £15K threshold — thus only need to submit a simplified account.

As audits tend not to be cost-effective for this group, the UK Inland Revenue decided to conduct a letter campaign. This provided the opportunity to test, which, if any, messages would influence people in this group to increase declared turnover over the threshold. To allow proper statistical analysis of results, an experiment was designed with five groups, each receiving a different treatment and one group no treatment to act as a control.

Thus, each of the five groups was sent one of the following letters:

1. 'We can provide you with advice and support'.
2. 'Paying the right tax increases public spending on hospitals, schools etc.'

Center for Tax Policy and Administration. 2004. Compliance Risk Management: Managing and Improving Tax Compliance. [ONLINE] Available at: https://www.oecd.org/tax/administration/33818656.pdf. [Accessed 14 May 2019].

3. A warning: 'We are increasing enquiries — your return may be chosen'.

4. As in letter 3 – but adding that 'we charge financial penalties'.

5. 'Your 2001 Return has already been selected for audit'.

As indicated, a further group received no letter and acted as a control for evaluation purposes.

Letters of type 3, 4 and 5 produced significant increases in self-reported turnover and net profit on the next return, by comparison with the group who did not receive any letter. To check the accuracy of the self-reporting by recipients of letters 3 and 4, audits were carried out on 10% of their next returns. The initial assessment showed that both letters were far more effective in achieving improved compliance than an enquiry unsupported by any previous warning. The next return of all letter 5 recipients was audited. The self-reported profits of this group, with the addition of yield from the audit, should provide the most accurate measure of actual turnover.

The project successfully achieved its aim of testing which messages were most effective in improving the compliance of this risk group. Although letter 5 resulted in higher self-reported income, the most cost-effective effective intervention (with a cost/yield ratio of 1:3) was letter 4, because the improved accuracy of self-reporting by this group was achieved without the costs of carrying out an audit in every case.

APPENDICES

Appendix One: Legal Provisions on Time Frame for Filling Returns (PITA)

a. Direct Assessment

In respect of Direct Assessment Returns, Section 41 of PITA provides as follows:

i. A taxable person shall, for every year of assessment, without notice or demand file a return of income in a prescribed form with the Tax Authority.

ii. The return should disclose the amount of income from every source in the preceding year.

iii. The return should contain such particulars on the income, allowance, relief, deduction, and other information as may be required by the tax authority in accordance with the tax law or related regulations.

iv. The return shall be filed within 90 days from the commencement of every year of assessment.

Section 43 provides that a person whose only source of income in any year of assessment is employment and earns N30,000 or less from that source shall not file tax returns.

b. PAYE Returns

In respect of PAYE Returns, Section 81(2) provides that every employer shall file a return with the relevant tax authority of all emoluments paid to its employees, not later than 31st January of every year in respect of all employees in its employment in the preceding year.

Highlights of Legal Allowances/Reliefs/Deductibles under PITA

I. **Direct Assessment and PAYE**

Pursuant to section 37 of the Personal Income Tax Act Cap. P8 LFN 2004 (as amended) and as contained in its Sixth Schedule, the following are the legal allowances, reliefs, and deductibles under the Act.

(1) A consolidated relief allowance shall be granted on income at a flat rate of ₦200,000 Plus 20 *per cent* of gross income.

(2) Tax Exempt: The following deductions are tax exempt-

(a) National Housing Fund Contribution

(b) National Health Insurance Scheme

(c) Life Assurance Premium

(d) National Pension Scheme

(e) Gratuities

(3) After the relief allowance and exemptions had been granted in accordance with paragraphs 1 and 2 of this Schedule, the balance of income shall be taxed as specified in the tax table below:

1. First ₦300,000 @ 7 *per cent*
2. Next ₦300,000 @ 11 *per cent*
3. Next ₦500,000 @15 *per cent*
4. Next ₦500,000 @ 19 *per cent*
5. Next ₦1,600,000 @ 21 *per cent*
6. Above ₦3,200,000 @ 24 *per cent*

c. Withholding Tax Return

The use of withholding tax is a powerful compliance tool in tax administration. Through the withholding tax system, the tax law provides that when payment is due to a supplier of goods or services, the contracting party is required to deduct tax at a statutorily prescribed rate on the supplier's invoice fee/cost. The tax deducted is paid over to the relevant tax authority the supplier or service provider is registered with for tax purposes. By so doing, the supplier/service provider is made to pay tax upfront on his/her income. The contracting party i.e. the organization that made the deductions is required to remit the taxes deducted to the tax authority monthly and the remittance should be accompanied by a schedule showing:

- The gross amount of the invoice or payment.
- The names and addresses of the suppliers or recipient of incomes; and
- The amount of tax deducted.

Sections 69-74 of PITA are the relevant provisions on the application of withholding tax regime in Nigeria. The current rates of withholding tax under PITA are as follows:

Types of Payment	**WHT for companies (%)**	**WHT for individuals (%)**
Dividends, interest, and rents	10	10
Directors fees	N/A	10
Hire of equipment	10	10
Royalties	10	5
Commission, consultancy, technical, service fees	10	5
Management fees	10	5
Construction/building (excluding survey, design, and deliveries)	5	5
Contracts other than sales in the ordinary course of business	5	5

The period for filing WHT is 21 days after the duty to deduct arose for deductions from companies. The penalty for failure to deduct or remit tax is 10% of the amount not deducted/remitted.

Note that companies are required to submit, in electronic form, a schedule of all their suppliers for the month showing the Tax Identification Number (TIN), address of the suppliers, the nature of the transaction, WHT deducted, and invoice number[9].

[9] PWC. 2019. Nigeria Corporate Withholding Taxes. [ONLINE] Available at: http://taxsummaries.pwc.com/ID/Nigeria-Corporate-Withholding-taxes . [Accessed 16 April 2019].

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