

# Legal Aspects of Tax Administration Electronisation

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## Abstract

Nowadays, information and communication technologies are used in all areas of human activity. Naturally, tax administration is not an exception. There is no dispute that the introduction of such technologies has a positive performance impact in many areas. However, does the introduction of such technologies have some legal consequences as well? The aim of the paper is to identify the legal aspects arising from the usage of such technologies in tax administration.

## Keywords

tax administration; electronisation; law and technologies

## 1 Introduction

Nowadays, tax administration is more and more influenced by information and communication technologies.<sup>2</sup> The influence on tax administration does not lie only in a simple replacement of paper media with electronic media. With these new technologies, new legal problems arise, some of them not imaginable before, such as data mining. Data mining is a technique of information handling, which uses a systematic analysis of a huge amount of data to discover hidden relations in the data and new information, which could be even unknown to a person to whom the data are

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<sup>2</sup> The information and communication technologies are commonly abbreviated as “ICT”.

pertinent. As a result, data mining represents an intrusion to the privacy of the data object and, therefore, violates the protection of their privacy and personal data, which is a constitutionally protected right.

The aim of this paper is to identify various legal aspects of the tax administration electrification.

## 2 Tax Administration Electrification

As one can surmise directly from the term “tax administration electrification”, it is a term related to the administration of taxes. Standard English dictionaries<sup>3</sup> do not list the word “electrification”. However, it could be inferred, that it is a word derived from the word “electronic” meaning “using a computer”. Electrification could mean either a process of change or a result of such change. Therefore, first, it is necessary to define the meaning of the word for the purposes of this paper. This paper does not deal with the legal aspects of the introduction of information and communication technologies into tax administration. It does not focus on the analysis of the necessary changes of law, which must be done to electrify tax administration. Thus, in this paper, electrification does not mean a process of change. Instead, the focus is on the legal aspects of tax administration which heavily uses information and communication technologies, i.e. the legal aspects of the result of the introduction of these technologies.

Moreover, the paper does not handle legal aspects of electronic phenomena in tax law, which are not tightly connected to tax administration, such as taxation of virtual currencies (Kohajda and Moravec, 2016: 36–46), execution upon virtual currencies or taxation of shared economy services (Tuláček, 2017a; Hrdlička, 2017; Klamo, 2017).

In this paper, the Tax Procedure Code (Act No. 280/2009 Sb.) is taken as a frame of reference for the examination of the tax administration electrification. This act deals exhaustively with tax administration. Generally, the common tasks of tax administration, where information and communication technologies are useful, are communication (deliveries, filings, information publication and information exchange), and information handling (records keeping and information protection). The general provisions are accompanied by enforcement provisions. A fine can be imposed if a taxpayer files a submission in a non-electronic way.

Moreover, the Tax Procedure Code contains provisions on electronic auctions. In this paper, electronic auctions will not be studied in detail. However, it is necessary to mention the provision as an example of a bad approach to “electrify” a legal institute. The Tax Procedure Code contains detailed arrangements on a non-electronic auction. However, the electronic one is stipulated only in one section, which states that provisions on non-electronic auctions should be reasonably used on electronic auctions, as well (Secs. 194, 194a and 195–202 of the Tax Procedure Code). Nevertheless, it is

<sup>3</sup> For instance, Hornby and Turnbull, 2010.

completely unclear, which provisions can be used and which are unacceptable (Tuláček, 2017c: 33–40).

### 3 Electronic Communication and Tax Administration

One of the most important preconditions of tax administration electronisation is an electronic communication between a taxpayer and a tax administrator. This precondition is so important that it can be considered a precondition *sine qua non*. Otherwise, it would not be possible to effectively keep files in an electronic form due to a constant need to convert them from the electronic to non-electronic form and *vice-versa*. Therefore, the law must recognise ways of electronic communication and allow both deliveries of documents from a tax administrator to a taxpayer and submissions from a taxpayer to a tax administrator.

In the private sector, e-mail is used as a general means of electronic communication. However, this does not generally apply in case of communication in tax administration since it does not hold the basic requirements of communication means usable during official delivery. E-mail is an open message readable on all relay servers, which breaks tax secrecy. Moreover, there is no built-in technology, which could provide a proof of delivery. It is not possible to just assume, that all messages sent are messages received as well.<sup>4</sup> Finally, there is no built-in technology, which could link an email address holder to a particular taxpayer. Therefore, e-mail in its common implementation cannot be used for official delivery and is not included in the list of delivery methods in the Tax Procedure Code (Sec. 42 of the Tax Procedure Code). However, all of these problems can be resolved. An e-mail message can be encrypted using the asymmetric cryptography algorithms such as RSA (Brookshear et al., 2013). Encryption solves two of the mentioned problems. First, it changes the character of the message from an open one to a closed one. Second, it ensures that only a valid recipient can read the message. Still, a tax administrator must somehow determine the taxpayer's email address. This problem could be solved in two ways, a mandatory registration process or mailbox provided by the government. Finally, the delivery proof problem could be solved in two ways, as well. First, the message could be perceived as delivered only after its recipient confirms the delivery with a separate message. However, this opens the possibility to avoid a delivery of an official document simply by not sending the confirmation message. Second, the state could provide a mailbox and track the delivery of such a message itself. For instance, Estonia provides e-mail mailboxes to their citizens.<sup>5</sup> To conclude, nowadays, it is not possible to use e-mail as a means of delivery in tax administration. Moreover, to enable this means, it would be necessary to eliminate the problems

<sup>4</sup> In fact, such an assumption would be unconstitutional. See the decision of the Constitutional Court, ref. no. Pl. ÚS 32/15.

<sup>5</sup> Using@eesti.ee address, cf. Eesti.ee, 2017.

mentioned above. Otherwise, this means of delivery could not be used as a standard, primary way of delivery in a low-compliance environment, where taxpayers and tax administrators do not cooperate.

Nevertheless, there is an e-mail alternative recognised by the Czech law, and that is data boxes (Act No. 300/2008 Sb.). The above-mentioned problems of e-mails do not apply to data boxes. Data boxes are accessible only to the officially identified subjects, the messages are not transferred in an open environment and the data boxes information system has a built-in functionality of proof of delivery. As a result, data boxes are the only means of an electronic delivery, which is nowadays allowed to be used in tax administration (Sec. 42 of the Tax Procedure Code).

The conclusions valid for the official delivery using e-mail do not necessarily apply to taxpayer filings. It is up to the taxpayer, whether they will use an encryption or not.<sup>6</sup> Moreover, there is no problem with the proof of delivery. However, there is still the identification problem, since it is usually not possible to identify the sender of an e-mail message. Though, this problem can be resolved by using an electronic signature or by confirming the filing using a different means of communication. Both approaches are used in the tax administration (par. 71(1)(a) subsec. 71(3) of the Tax Procedure Code). Therefore, it can be concluded, that e-mail is an acceptable means of communication in tax administration. However, the Financial Administration of the Czech Republic, which is a main tax administration body in the Czech Republic, refuses to accept e-mail filings, since it has not published an e-mail address of its electronic registration office. Instead, a web page address of its web filing system is published as an address of the electronic registration office.<sup>7</sup> Since the Tax Procedure Code does not prescribe what kind of electronic registration office should be used (par. 56(1)(b) of the Tax Procedure Code), it is not *per se* contrary to the law. However, I consider such an arrangement contradictory to the purpose of the Tax Procedure Code provision on electronic registration office, since it eliminates the usage of the most common means of electronic communication. Moreover, there is no need to exclude e-mail because e-mail messages can be processed automatically in the same way they are processed in the web filing system.

Additionally, electronic means of communication can be effectively used in mass communication, as well. By default, the Tax Procedure Code states that all information published on an official notice board should be published on the Internet, as well.<sup>8</sup> However, there are several kinds of information, which are currently published only on the Internet, but should be stipulated in a legal regulation instead, such as specifications of data format and structure of electronic filings.<sup>9</sup> Notwithstanding, this is not applicable to the publishing of form filings, distinctively a tax return. There are opinions,

<sup>6</sup> Under an assumption, that they file a filing which contains information only on themselves.

<sup>7</sup> ePodatelna, 2013–2018.

<sup>8</sup> Subsec. 56(2) of the Tax Procedure Code.

<sup>9</sup> See also Tuláček, 2018a: 359, 360.

that form filings must be published in a legal regulation, as well.<sup>10</sup> However, since there is a clear specification of a tax return content, there is no need to publish these forms in a legal regulation (Tuláček, 2018b). Moreover, bodies of the Financial Administration of the Czech Republic publish some information in an official instruction, which is contrary to the law (Tuláček, 2018b). To conclude, the legislation on communication means used for mass communication could be considered as going in the right direction. However, they are currently unsatisfactory and need further improvement.

#### **4 Handling of Information and Privacy Intrusion**

As identified before, the second area of legal aspects of tax administration electronisation is information handling and related privacy intrusion. In this context, it is necessary to state that legal entities and non-subjects, who are taxpayers, are entitled to privacy protection, as well. Tax administrators must overcome the information asymmetry during tax administration. Therefore, privacy intrusion is inevitable during tax administration (Tuláček, 2016: 70–71).

Since privacy intrusion is inevitable, the information must be protected accordingly during tax administration. Therefore, the Tax Procedure Code stipulates the duty of tax secrecy (sec. 52 of the Tax Procedure Code). Naturally, this duty must be held in the electronic environment, as well. This leads to a duty to secure the information and communication technologies used by tax administrators. However, it leads to an important issue of technical staff and their access rights to the tax administrators' data. In the light of this issue, there arises another issue whether the information and communication technologies administration can be outsourced or not.

The tax administration electronisation brings new approaches to data collection. Traditionally, tax administrators collected information either by collecting tax returns or by an investigation. In clearly specified cases, they could impose a record-keeping duty, as well. However, nowadays, it is possible to massively collect data on taxpayers and their economic activities. For instance, recapitulative statements (sec. 102 of the Act No. 235/2004 Sb.) and control statements (secs. 101c to 101k of the Act No. 235/2004 Sb.) allow tax administrators to collect information on all taxpayers at once and to model transactions between them. Moreover, the registration of sales (Act No. 112/2016 Sb.) allows collecting data on cash transactions in real time. As a result, tax administrators store a large quantity of data on taxpayers, which can be examined in deep detail and new information can be data-mined from the data. This new information could even be unknown to the respective taxpayers themselves (Tuláček, 2017b: 12; Gaudamuz and Cabell, 2013: 3). Therefore, a combination of the massive collection of data and usage of the data mining techniques represents a completely new way of privacy intrusion, which was unimaginable before the introduction of information and communication

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<sup>10</sup> For instance, see Motion, 2017.

technologies to tax administration. Additionally, the data-mined information can be used to profile taxpayers, i.e. to classify them and based on this classification automatically decide on important issues related to them.

Once a tax administrator collects data, they can exchange them with other tax administrators, be it domestic or foreign. Traditionally, the information can be exchanged on request or spontaneously without any previous request (secs. 9 to 15 of the Act No. 164/2013 Sb.). The easement of handling data in electronic forms allows exchanging the information on an automatic basis. The range of automatically exchanged data gradually widens.<sup>11</sup> The above-mentioned issue of tax secrecy keeping arises in this context as well, especially in relation to the international information exchange.

## 5 Promoting and Enforcing Tax Administration

Generally, tax administration electronisation leads to a more effective performance of tax administration tasks. However, it is necessary to ensure that both tax administrators and taxpayers are able to communicate electronically to enjoy the advantages of the electronisation. This goal can be achieved in two ways. First, the electronisation can be promoted by a tax administrator. In this case, taxpayers should use the electronisation voluntarily, to get access to related advantages. Second, the electronisation can be enforced either by closing the non-electronic ways of communication or by punishing their usage.

Nowadays, enforcement by punishment is in force (subsec. 247a(2) of the Tax Procedure Code). However, in some other countries, the promotion way is the more common one. For instance, electronic filings could be handled preferentially, which could lead to faster returning of overpaid money.

The question, whether to use promotion or enforcement to achieve the desired outcome is more likely an economic, philosophical or sociological issue. However, it is an important legal question, whether the preferential treatment of compliant taxpayers is an allowed form of discrimination or not.

## 6 Conclusion

In this article, the legal aspects of the tax administration electronisation are examined. Tax administration electronisation is considered to be the result of introducing information and communication technologies into tax administration. In this context, there are two main groups of legal aspects, one related to communication and the other related to information handling and privacy intrusion. Moreover, there is an issue

<sup>11</sup> See amendments of the Council Directive 2011/16/EU of 15 February 2011 on administrative cooperation in the field of taxation and repealing Directive 77/799/EEC.

regarding the possibility of a positive discrimination of taxpayers, who voluntarily cooperate on the usage of electronic means of communication with a tax administrator.

As presented, communication has a different constraint dependent on the direction of the communication. There are other requirements for the official delivery of a document and for the filing performed by a taxpayer. Nowadays, it is not possible to use e-mail for official delivery and is *de facto* not possible to use for filing to bodies of the Financial Administration of the Czech Republic. I consider this state faulty since e-mail is the most used means of electronic communication today. Therefore, it should be possible to use it at least for the electronic filing.

There are legal issues related to mass communication, as well. Currently, the most important issue connected to mass communication is the method of publishing of the form filings and data formats and structures for electronic filings.

The issues related to the handling of information and privacy intrusion do not affect only natural persons, but all taxpayers. The introduction of information and communication technologies into tax administration brought a new way to privacy intrusion having severe legal consequences. For instance, a massive collection of information combined with data mining techniques allow tax administrators to find data, which are even unknown to the respective taxpayer. Moreover, tax administrators could use this new information to profile the taxpayers. Therefore, it is necessary to pay greater attention to the respective legal regulations. Finally, new challenges for tax secrecy keeping arise from the automatic exchange of information, where large amounts of information on taxpayers are exchanged internationally.

To conclude, increased attention must be paid to issues related to the introduction of information and communication technologies into tax administration. It is not possible to ignore them, as well as it is not possible to simply state, that a particular institute should be reasonably used in an electronic environment without further specifications or at least some idea surrounding the real implementation.

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