

Administrative and Compliance Costs of Taxation in Croatia

SUMMARY

The goal of the project is to calculate the administrative and compliance costs of taxation in Croatia for the period of 2001/2002, establish their characteristics and give some policy recommendations. This is one of the first measurements of these costs in one of the countries in transition.

The institution that has led the project is the Institute of Public Finance, Zagreb, Croatia. The project proposal was started by Katarina Ott (Institute of Public Finance, Zagreb) and Helena Blažić (Faculty of Economics, Rijeka) on the basis of the previous research done by Katarina Ott and Anto Bajo. The two leaders of the project were later joined by Danijela Kuliš, Mihaela Pitarević and Vjekoslav Bratić (Institute of Public Finance) and Mira Dimitrić (Faculty of Economics, Rijeka). The Institute of Public Finance also hired the survey agency PULS (Zagreb) to run surveys throughout Croatia. The Tax Administration of Croatia (and especially their data processing department) prepared different data for the project and the representatives of the Chambers of Trades, accounting unions and different accounting firms (offices) were consulted.

The administrative costs survey was done using official data from the Tax and Customs administrations. The tax compliance costs survey was divided into the following parts (covered by different questionnaires): individuals (personal income tax), business units that pay personal income tax (all taxes except customs and excise duties), business units that pay profit tax (all taxes except customs and excise duties), customs (separately for business units that pay personal income tax and business units that pay profit tax) and excise duties (the non-profit and state sector were excluded, as is common for this type of research). The part of the survey that encompasses the different taxes of business units was, because of its complexity and enormous amount of data, later further divided into two parts: “core” compliance costs measurement and the “qualitative” part of research. The entire tax compliance costs survey was done mostly by different face-to-face interviews – a postal survey was rejected because of the very low response rate and the relatively high postal costs in Croatia. Only a part of excise duties survey was done as a postal survey. The Tax Administration and their data processing department were engaged not only to provide us with relevant data, but to create some additional data for the purposes of our research.

The interview process was attended with a number of difficulties. The responding taxpayers complained that it was very hard for them to assess the time spent on tax matters, they were suspicious concerning the promised anonymity, complained that it took too long. The biggest problem for the interviewers, in the cases where we needed more than one interviewee (for instance the owner and the bookkeeping office, importer and customs clearing agent), was to convince both sides to cooperate. So, the interview process lasted much longer than we had expected and in the end we did not succeed in gathering as many responses as we had wanted.

On the other hand, the Tax Administration was overwhelmed with other duties and unable to support us with all the data we wanted.

Nevertheless, we did succeed in fulfilling the main objectives of the project.

Aggregate operating (administrative and compliance) costs of taxation amount to 3.13% of GDP. As expected, compliance costs are higher than administrative costs, the latter amounting only to 0.47% of GDP (and 1.76% of tax revenues (excluding social security contributions)). Among compliance costs of taxation (2.66% of GDP) the highest are, as expected, compliance costs of VAT (0.81% of GDP), compliance costs of customs (0.6% of GDP) and compliance costs of wage taxes (part of personal income tax, including local surtax)

together with social security contributions (0.48%) of GDP. The share of compliance costs of personal income tax of businesses that pay personal income tax is 0.25% of GDP – almost the same as of compliance costs of profit tax – 0.23. The reason lies in the number of businesses paying personal income tax being 50% higher than number of business units paying profit tax. The share of compliance costs of excise duties as well as compliance costs of individuals filing personal income tax returns are almost negligible, being 0.03 and 0.02% respectively. The relatively low percentage of the latter is the result of the fact that the bulk of income taxes is collected by withholding, which is considered as final, and that the average time spent on income tax returns is only 1.7 hours.

The shares of different tax compliance costs (gross) in relevant tax revenues (“efficiency”) reveal a different picture:

- VAT – 6% (with a considerably larger share for businesses paying personal income tax and a lower share for businesses paying profit tax)
- Customs – 26%
- Wage taxes and social security contributions – 4%
- Profit tax – 12 %
- Personal income tax – businesses - 96%
- Personal income tax – individuals (tax returns) – 0.9%
- Excise duties – 0.3% (most excise duties have a percentage below 0.5, the only exception being non-alcoholic beverages – 1.6, coffee – 2.9 and luxury products – 3.5)

It must be borne in mind that the stated percentages are the result not only of high compliance costs, but also of high tax revenues. So, for instance, the high percentage of VAT compliance costs relevant to GDP (and the high total amount of VAT revenues respectively) still does not make this tax remarkably inefficient concerning compliance costs expressed as a percentage of tax revenues. The same holds for wage taxes and social security contributions. The opposite holds for personal income tax for businesses.

The research also proved the regressivity of tax compliance costs, as expected, even comparing the smallest businesses.

The business community seems to be unsatisfied with the complexity of the tax system, especially the frequent changes (but mostly satisfied with the Tax Administration). Only excise duties tax compliance and filing a personal income tax return does not seem to present much problem.

Policy recommendations to reduce compliance and administrative costs of taxation:

- Self-assessment of personal income tax for businesses (small businesses) should be replaced by a lump sum tax (estimated tax)
- The VAT threshold should be increased
- VAT compliance for business units that pay personal income tax should be eased
- The deadline for the calculation and payment of VAT should be longer
- Partial acknowledgement of some expenses (for instance entertainments, car expenses) for VAT, income tax and profit tax purposes should be abolished
- The customs house should calculate VAT on import and not the taxpayer itself, which is the case in some import services (for example the tourist industry)
- Parallel records (for accounting purposes and tax purposes – for instance for VAT) should be abolished, especially for business units that pay personal income tax
- Tax supervision because of the refunding of overpaid VAT should be abolished
- Calculation of income tax should be better adjusted with the cash-flow principle

- New tax reliefs make income tax returns more complicated, but a lot of taxpayers can not use them entirely (because of the low income) – in order that benefit from the new reliefs outweighs the higher compliance costs reliefs should be made non-wastable
- The calculation of profit tax should be better adjusted with the accounting system
- Spillage and wastage on products for which tax has already been paid should be acknowledged
- The tax system should be more stable, without frequent changes
- Forms should be simplified and the number of forms should be reduced, particularly in the taxation of wages, where considerable overlapping occurs
- The number of paying-in accounts should be reduced (in the meantime this is already achieved)
- Better connections between the Tax Administration, the Croatian Statistics Bureau and the pension system should be established, so that the taxpayers not have to give each one of them the same data
- Some order should be brought into the changes of the rates for social security contributions, taxes and surtaxes – so that they are allowed to be changed only at the beginning of the year, for example, and not at just any time
- The provisions of the tax law should be clear and precise so there should not be any unnecessary alternative interpretations in their implementation
- Closer cooperation between taxpayers and customs and tax officials is required
- Along with standardized, simplified customs procedures, the maximum use of information technology is essential (customs information system compatible with similar systems in the countries of EU, from the points of view of hardware, software and telecommunications; the basis for such an information system should be the Automatic System for Customs Data (ASYCUDA) developed by UNCTAD, broadly accepted worldwide) as is the ongoing development and perfection of customs control (greater selectivity of control)
- Agents/forwarders should be informed at once and in detail about every, even the smallest, change in the customs regulations and not just have it revealed to them at the customs house
- As many narrowly specialized and highly qualified customs officers and agents as possible
- More customs houses should have inspection departments (phyto, veterinary, market and so on) so as to speed up the customs procedure
- The actions for tax collection, especially concerning customs, should be improved by introducing a systematic monitoring of the state of claims concerning customs and the prompt actions for their collection (by the organizational linkage of people who would oversee the promptness of procedures undertaken and take care of the quality of guarantees received)
- The efficiency of the tax and custom administrations should be improved (a greater orientation to the payers of taxes and customs duties – the founding of separate departments for relations with payers, special departments for major taxpayers, specialization of officers, an increasing degree of independence, incentives to officials via raises, greater salaries, advanced training, promotions and lack of bias during hiring, bonuses and so on, in every territorial TA the number of officials according to the norms of the jobs and the level of expertise with respect to the demands of the given jobs should be reconsidered, the speed of transmission of data along the communications channel should be stepped up, the proportion of people with secondary education only should be reduced in favor of those with higher qualifications, especially in the determination of taxes).