Paying Taxes 2012

Keeping the fiscal agenda in focus as Nigeria turns 52

By Taiwo Oyedele

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Paying tax is important. Taxes provide government revenues and those who pay them have a stake in the system and in how government spends the money. Taxes are a life blood of a stable and prosperous society. In the words of Oliver Wendell Holmes, US Supreme Court of Justice, in 1904, "Taxes are the price you pay for civilisation". Franklin D. Roosevelt, former president of the United States once said also that, "Taxes, after all, are the dues that we pay for the privileges of membership in an organised society."

Taxes are essential to economic and social development and there is no doubt about the need for and benefits of taxation. But how economies approach taxation varies substantially. Paying Taxes is a joint annual publication by PwC and the World Bank which examines the impact of tax systems on business using a case study company in 183 economies. The study, which looks beyond corporate income tax to all of the taxes and contributions mandated by government, enables an assessment of tax systems around the world from the point of view of business to determine the full impact of taxation in terms of cost and compliance burden.

Based on the recently released 2012 Paying Taxes Study, Nigeria now ranks 138 out of 183 economies on the ease of paying taxes compared to a ranking of 134 in the previous year. Put differently, this means that in Nigeria, a medium size company on average pays nearly one third of its commercial profit in taxes, spends over 23 weeks in a year dealing with its tax affairs and makes a tax payment every 10 days. With this, Nigeria is far behind many of the leading investment destinations in Africa including Mauritius which ranks 9, South Africa 36 and Ghana 87.

The Paying Taxes results enable governments to benchmark their tax system with others on a like-for-like basis and to identify best practices. The study measures three separate aspects of paying taxes. Two of these relate to the tax compliance burden and one to the tax cost. All three are equally weighted to arrive at an overall ranking. The three indicators are – (1) number of tax payments, (2) total tax rate as a percentage of commercial profit and (3) time required to comply with tax requirements. On these sub-indicators for 2012, a medium size company in Nigeria makes 35 tax payments annually, pays 32.7% of its commercial profit in taxes, and spends 938 hours to comply. As a result, Nigeria ranks 123 on number of tax payments, 56 on total tax rate and 180 on time required to comply out of 183 economies covered by the survey.

Clearly the worst sub-indicator for Nigeria, which has been dragging the overall ranking down, is the amount of time required to comply with tax obligations. This covers the time required to comply with major taxes (hours per year) including collection of information, computation of tax payable, completing tax return forms, filing with relevant tax authorities, arranging payment or withholding and preparing tax accounting records and supporting documentation. Going by this indicator, Nigeria ranks lowest in Africa and only ahead of three countries in the world; Vietnam (181), Bolivia (182) and Brazil (183). The enormous time required for tax compliance in Nigeria is a reflection of the bureaucratic, complex and cumbersome tax administration system in the country. By comparison to the 938 hours for Nigeria, the average tax compliance time for Sub-Saharan Africa is 318 hours while for OECD countries it is 186 hours.

Nigeria has been slipping consistently on the ease of Paying Taxes index because of slow and uncoordinated approach to tax reform while many countries have improved their tax systems significantly and continue to do so. Tax reform is very high on government agendas around the world.

During 2010/2011 covered by the 2012 study, 33 economies made it easier to pay taxes or reduced tax rates. Introducing electronic systems to make compliance easier was the most common feature of tax reform during the period.

Reducing rates of profit tax is also a popular reform, but easing the compliance burden is equally important for business. Certain practices have been effective in improving the ease of paying taxes. These include simplifying tax compliance by reducing the frequency of filing or allowing joint payment and filing of several taxes, tax systems which have effective electronic filing and payment (over 60 economies currently do), those which have one tax per base (over 50 economies have one tax per base rather than multiple taxes), and those which use a filing system based on self-assessment (74% of economies allow companies to calculate their own tax liabilities). Good tax administration is extremely important. The approach of the tax authorities especially dealing with tax audits and disputes are the aspects of the tax system that businesses around the world most want governments to improve.

To a very large extent, the study shows that there is a correlation between the ease of paying taxes and economic development as paying taxes is easiest for businesses in high-income economies. These countries have the lowest tax cost and the lowest administrative burden. In addition, they tend to have more mature tax systems, a lighter administrative touch and greater use of electronic interface with tax authorities.

Governments in economies of all sizes and at all stages of development are struggling with the tax policy choices available to them. While taxes are essential for economic and social development, it is important that the taxes levied do not hinder the ability of companies to generate a sufficient and consistent return so that they can reinvest and grow their business. But while the perspective of business and government on what the optimum amount of taxes to levy may differ, there should be a common agenda regarding the administration of tax systems and the need to ensure that it is simple and efficient.

Tax revenue depends on governments' administrative capacity to collect taxes and firms' willingness to comply. Compliance with tax laws is important to keep the system working for all and to support the programmes and services that improve lives. Keeping rules as simple and clear as possible is undoubtedly helpful to taxpayers.

Overly complicated tax systems risk high evasion where the majority of firms perceive taxes as not 'worth paying' because of low-quality public goods and poor infrastructure. High tax compliance costs are associated with larger informal sectors, more corruption and less investment. Economies with well-designed tax systems are able to help the growth of businesses and, ultimately, of overall investment and employment.

The impact that tax systems have on companies is important and governments should continue to develop tax systems which foster business investment and economic growth. When considering how the tax system impacts business, and what companies contribute to public finances it is important to look at all of the taxes that companies pay and not just corporate income tax.

Businesses have a key role to play in economic development and taxation is a major consideration in the equation. Reducing tax rates, broadening the base and making it easy to pay, can be important in encouraging local business to register and pay tax. It is therefore important for government, investors and civil society to foster a new collaborative approach to meet the common aims of a fair, stable and sustainable tax system.

Taiwo Oyedele is a Partner and Head of Tax and Corporate Advisory at PwC Nigeria. He is a regular writer and speaker on professional accounting and tax matters.

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