Paying Taxes 2017

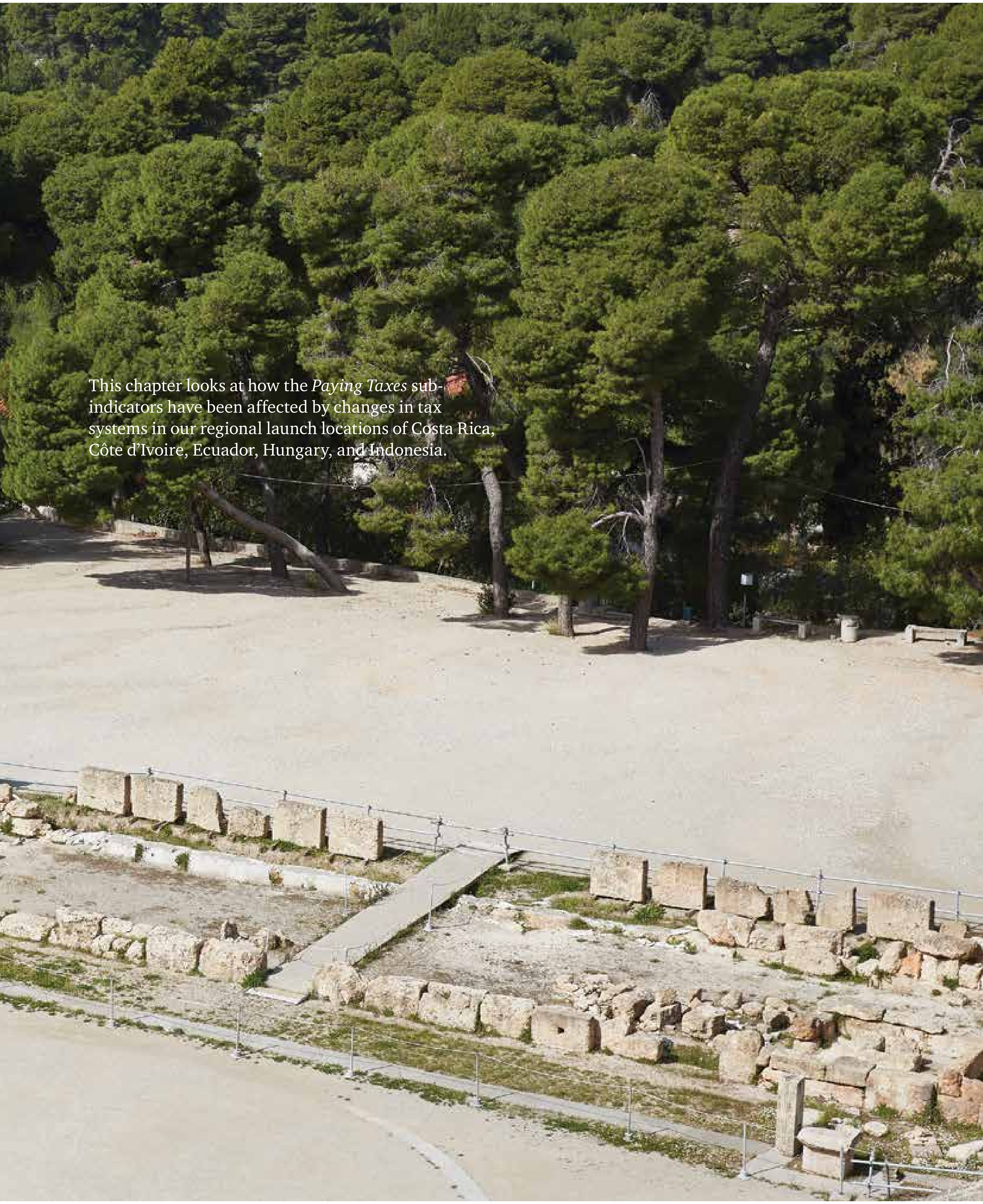
+1

Now including a new measure: the post-filing index.

www.pwc.com/payingtaxes

Contents

Chapter 3 – Country articles



This chapter looks at how the *Paying Taxes* sub-indicators have been affected by changes in tax systems in our regional launch locations of Costa Rica, Côte d'Ivoire, Ecuador, Hungary, and Indonesia.

Costa Rica

Digital innovation to increase voluntary compliance

Luis Diego Barahona, PwC Costa Rica

From 2003, the Costa Rican tax administration has made increasing use of electronic systems to facilitate voluntary tax compliance by taxpayers. This has helped to achieve greater efficiency and effectiveness in the collection of taxes which is reflected in the *Paying Taxes* sub-indicators from 2007 onwards. Standardising, simplifying and accelerating certain processes such as filing returns and electronic payments of taxes have all played a part in significantly reducing the time to comply and the number of payments.

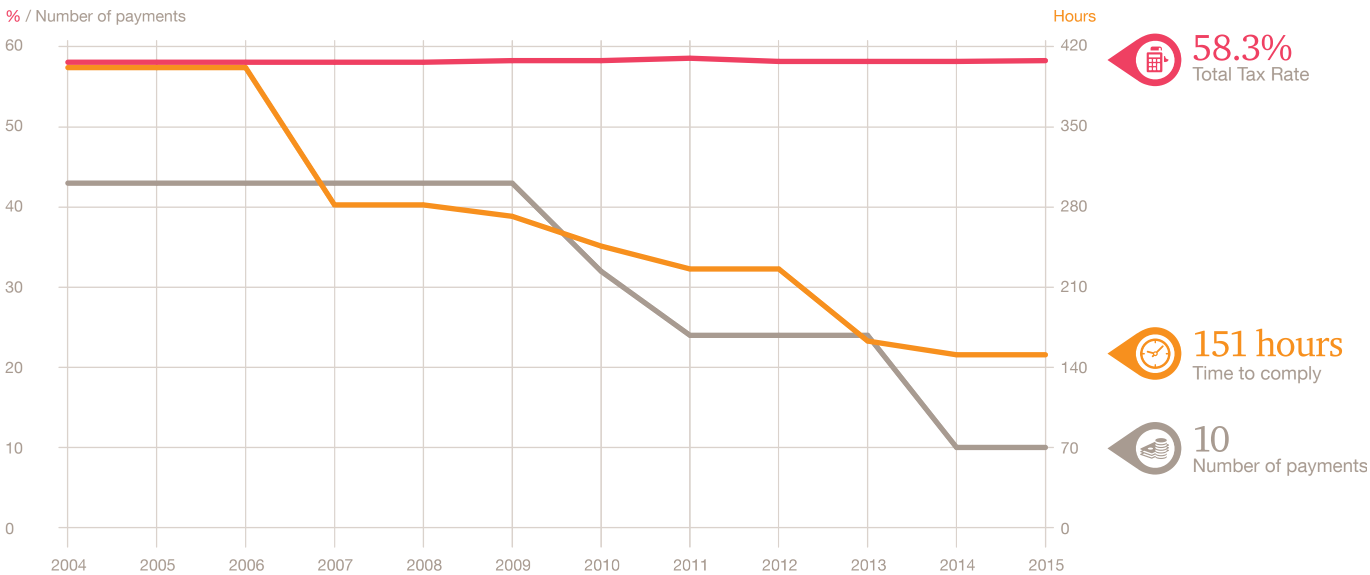
Digital tax management has been gradually developed and implemented in Costa Rica in phases, depending on the capacity of the tax administration. The first phase, between 2002 and 2003, was the introduction of mandatory electronic filing and payment for large taxpayers. As the system was optimised by being used by this small group of taxpayers, and the tax administration gained experience and skills, the system was rolled out to cover other taxpayers.

33

Average number of payments sub-indicator decreased from 43 to 10 between 2004 and 2015.

Figure 48

Trend in the *Paying Taxes* sub-indicators for Costa Rica since 2004



In 2006, a new law dealing with digital signatures and electronic documents further facilitated the direct delivery of services by the tax authorities allowing them to receive and process documents signed electronically by the taxpayer's representatives. This encouraged the use of digital systems within all public agencies. In 2008, the Costa Rican tax administration introduced standardised tax returns, which were made available to taxpayers through the Digital Taxation website. Paying taxes was made easier in 2013 by the implementation of electronic tax payments, though the National System of Electronic Payments (Sinpe).

In 2015, the tax administration developed a new advanced technology platform, which offered taxpayers electronic services via the Virtual Tax Administration website. A number of electronic services, which allow taxpayers to comply with their tax obligations, are available on the site. The creation of the platform and website was driven by the tax administration's desire to maximise voluntary tax compliance from those responsible for declaring and paying tax.

The benefits of this digital innovation are apparent from the movements in the time to comply and number of payments sub-indicators. Between 2004 and 2015, the average time to comply with tax obligation has fallen significantly from 402 to 151 hours and the average number of payments decreased from 43 to 10 payments.

The enhancement of electronic systems has made paying and filing taxes less time consuming and less involved. Under the previous old fashioned, paper-based system, tax returns had to be printed and signed, and payments had to be made during business hours at a specific bank, using only cheques for that bank. Now there is an online system for preparing and filing tax returns and, with the assistance of several banks, for making payments.

Companies in Costa Rica have also benefitted from a very stable tax system. Whenever tax legislation changes, taxpayers have to spend time understanding the new rules. A stable tax system also provides companies with more certainty, which is good for business more generally as it is easier for companies to make investment decisions. In Costa Rica the corporate income tax rate has been 30% since 2003 while over the same period social security contributions have stood at 26.17% with an increase to 26.33% from January 2015.

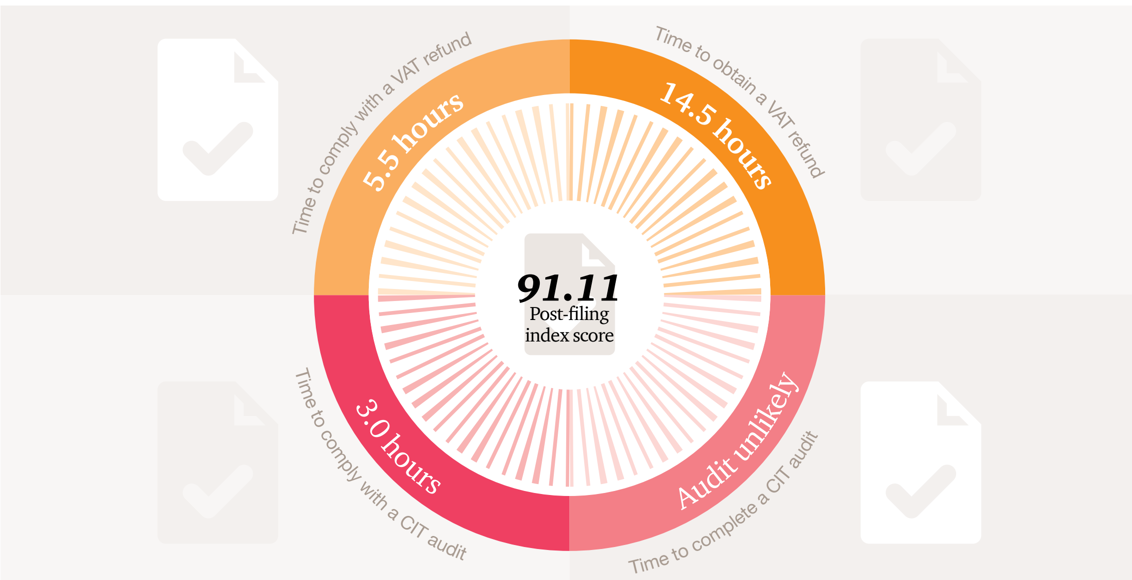
Costa Rica also scores well on the new post-filing index, suggesting that not only is it relatively easy to pay and file taxes in Costa Rica, but getting a refund and agreeing tax liabilities is also reasonably straight forward. Our case study company would need to spend less than six hours requesting a VAT refund, wait less than 15 weeks to receive the refund, and the refund request would be unlikely to trigger an audit. The company would need only three hours to correct an inadvertent error in a corporate income tax return and similar to the VAT refund, it would be unlikely to trigger an audit. On both of these post-filing processes therefore Costa Rica scores not only better than the global average, but better than the average for EU & EFTA which is the best performing region for post-filing processes.

Despite the improvements so far to the Costa Rican tax system, there is scope for further efficiencies. This would help the tax administration to reduce the amount of tax that is not paid and also to bring into full compliance those companies that participate in the informal economy. This, in turn, would give those companies better access to the national banking system.

The enhancement of electronic systems has made paying and filing taxes less time consuming and less involved.

Figure 49

Post-filing index and components for Costa Rica for 2015



Côte d'Ivoire

Achieving tax reform and broadening the taxable base

Dominique Taty, PwC Côte D'Ivoire

The *Paying Taxes 2017* launch in Côte d'Ivoire comes at a time when the country is increasingly recognised as an economic force in West Africa. Since 2012, Côte d'Ivoire has had an average GDP growth rate of 8%, and against this backdrop the ability for the country to raise tax revenues, but in an efficient and effective way, has become an important priority for government in pursuing its ambitions for future growth.

Although it has significantly expanded its tax system during the past twenty years, the country has not been able to demonstrate that it has an attractive tax system through competitiveness indicators which are often reviewed by foreign investors.

Since 2004, the three original *Paying Taxes* sub-indicators assessed by the World Bank have remained almost constant, suggesting a lack of substantial reform of the tax system and a poor result when compared with other economies.

After more than a decade, the Total Tax Rate has only reduced by a little over two percentage points from 53.4% (in 2004) to 51.3% (in 2015).

The government significantly reduced the corporate income tax (CIT) rate from 35% to 25% between 2006 and 2008. However, the impact of this reduction was largely neutralised by increases in social security contributions paid by companies. The case study company in Côte d'Ivoire has 11 taxes that contribute to its Total Tax Rate.

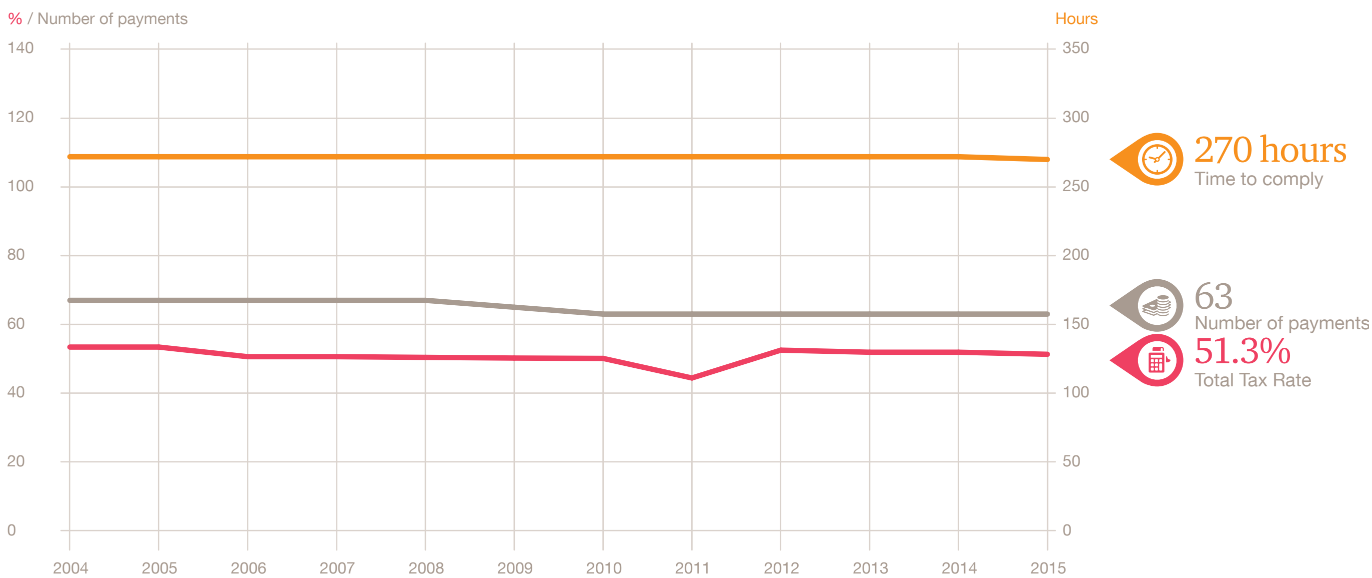
Moreover, it is important to note that during the socio-political crisis from 1999 to 2011, there was a lack of financial support from donor countries, and foreign investment fell. Collection of tax revenues became an increasing challenge for public funding, so that the number of taxes was maintained along with high tax rates.

11

The case study company in Côte d'Ivoire has 11 taxes that contribute to its Total Tax Rate.

Figure 50

Trend in the *Paying Taxes* sub-indicators for Côte d'Ivoire since 2004



The time to comply sub-indicator had been 272 hours since the start of the study, but has fallen slightly to 270 hours this year. With a view to addressing the issues that lie behind this number of hours, which has remained consistently above the global average, in December 2015 the tax administration implemented a single tax return form, the Formulaire Unique. This represents a first step towards simplifying the compliance obligations and it is intended that this will be followed by the implementation of an online filing (e-filing) facility. In practice this form has not yet provided all the benefits that were expected. Its introduction in December 2015 means that it could not impact the results now being released in this publication. While the form may have some benefits for taxpayers in future years, currently it remains a paper declaration which covers most of the main taxes and so it will not significantly reduce the burden without further enhancements.

The number of payment sub-indicator (63) measures the number of taxes, the frequency of filings and payments made in relation to those taxes and the method of payment. The single tax return has attempted to provide a solution for multiple payments by consolidating certain taxes, but the implementation of electronic filing and payment systems will be needed to help lower the frequency of interactions with the tax authority and ease the compliance burden on taxpayers.

As regards the new post-filing index, results are mixed. For CIT post-filing, the compliance time is lower than the world average and the fact that an audit is not likely to happen in connection with a CIT correction benefits the result. For VAT, the lack of a refund being available for our case study company (as refunds are only available for international traders) results in a poor score. Reforms have however been introduced in recent years regarding VAT refunds for exporters and international traders and these have been welcomed. Since 2006, a state financial body has been established which is responsible for VAT refunds for companies involved in such trade so that VAT credit management is more efficiently handled than in the past.

Generally speaking, the *Paying Taxes* results for Côte d' Ivoire do not currently match the country's ambitions. In the Government National Development Plan (PND) for the coming years, the improvement of the business climate is a key priority.

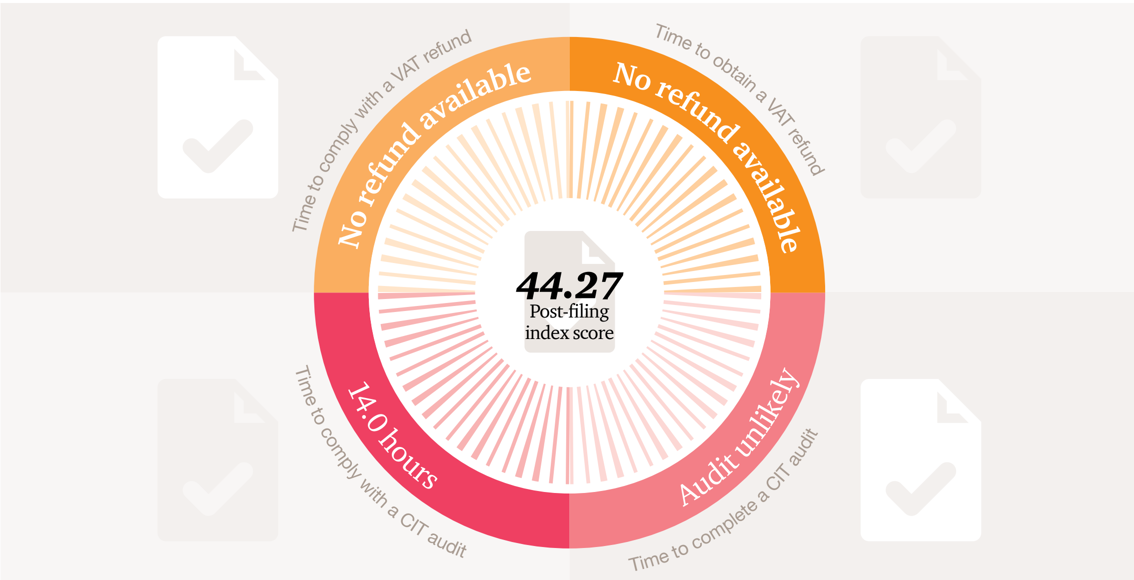
On 5 September 2014, the Prime Minister set up a tax reform commission bringing together stakeholders from the public and private sectors. They were asked to review the Ivorian tax system with the objective of aligning it with the country's overall development objectives.

The Prime Minister has also created a working group which is responsible for improving Côte d' Ivoire's position in the World Bank Doing Business ranking, with reform to the tax system being an important element. It is clear that the government and the private sector have an appetite and high ambition to improve the Ivorian tax system. We would encourage the government to continue its reflection on the mechanisms to reduce tax rates and to examine certain taxes which may be considered unattractive for investment. The ultimate aim is to make Côte d'Ivoire more attractive for investors, to increase investment and to improve taxes revenues by broadening the taxable base.

Generally speaking, the Paying Taxes results for Côte d' Ivoire do not currently match the country's ambitions.

Figure 51

Post-filing index and components for Côte d'Ivoire for 2015



Ecuador

Pressures on government finances leading to increased tax regulation

Pablo Aguirre, PwC Ecuador

With a time to comply of 664 hours, but a number of payments sub-indicator of just 8, the Paying Taxes results for Ecuador continue to reflect a tax system that is difficult to comply with, despite the availability of electronic systems for filing and paying taxes. The current economic backdrop may however present barriers to improving the system.

Ecuador's fiscal revenue depends greatly on its oil exports which have been significantly affected by the global oil price crisis that hit at the end of 2015. The drop in oil prices directly impacted the country's trade balance as well as the capacity of the Government to sustain and finance its infrastructure and socio-economic agenda. In addition, a sizeable earthquake seriously affected the coast of Ecuador.

With GDP growth of less than 1% for 2015, and negative growth projected for 2016, the Ecuadorean Government has sought, in part, to compensate the loss of its oil revenues and the impact of the earthquake with increased tax collection activities through the implementation of tax reforms including temporarily increasing the VAT rate from 12% to 14%, raising taxes to support people and areas affected by the earthquake, providing incentives to attract foreign and local investment and enacting several clarifying regulations. This has created the current environment of increased regulation for taxpayers and foreign investors.

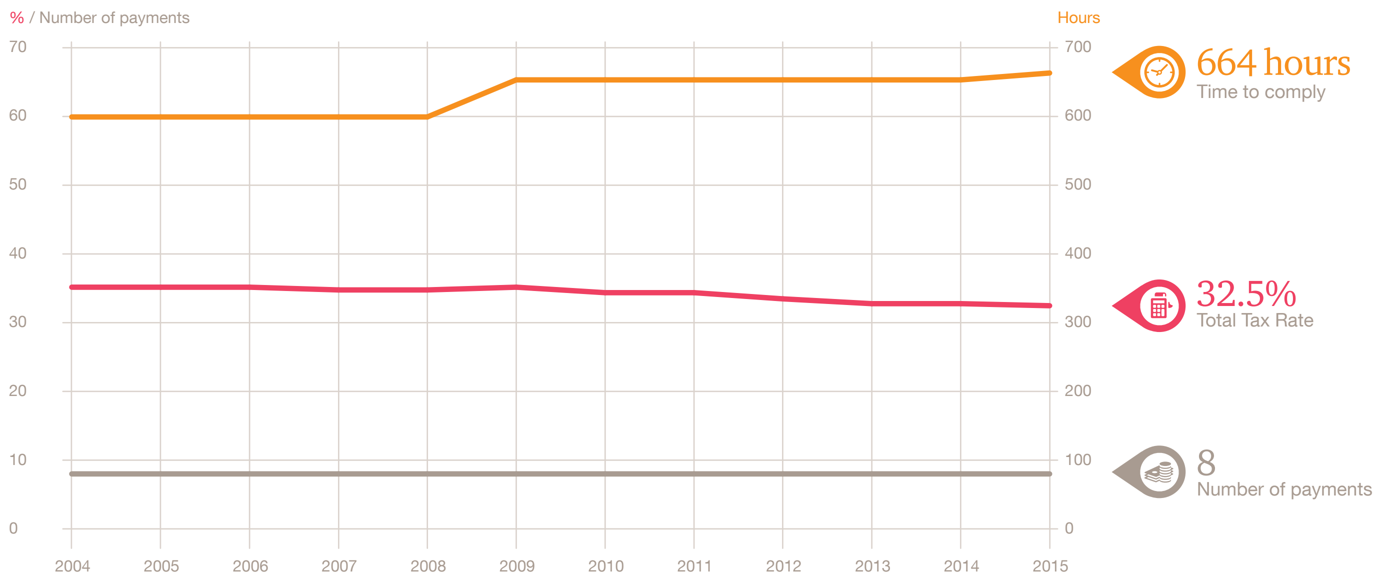
Whilst the increased regulatory activity in Ecuador is partly driven by the economic situation of the country, it is also a consequence of the Tax Authority's overall strategy to align itself with global tax positions relating to anti-avoidance provisions, interest deductibility changes, transfer pricing, transparency and double non-taxation together with the promotion of long term and transparent foreign investment.

664 hours

Ecuador has a time to comply of 664 hours, but a number of payments sub-indicator of just 8.

Figure 52

Trend in the *Paying Taxes* sub-indicators for Ecuador since 2004



Tax compliance: More than just an administrative function

This year's study showed a slight increase of 10 hours in the time to comply from 654 in 2014 to 664 for 2015 as taxpayers spend more time computing their corporate income tax liability because of the new regulations. This change is particularly important in that it is a quantitative reflection of the impact on the taxpayer's administrative burden of the tax laws that came into effect in 2015. This increase has occurred even though most taxes are filed electronically. New laws and compliance obligations have also been enacted in 2016 which may affect the Paying Taxes sub-indicators in future years.

These changes in tax regulation mean that companies need to adjust their view of their tax compliance activities from simply completing and filing tax returns to being able to thoroughly substantiate the economic essence of their operations and provide adequate documentary support to the Tax Authority when required. Other obligations include statutory filings, such as the Shareholders Annex, which requires local taxpayers to disclose detailed information regarding their shareholders (local and foreign), corporate structure, and inter-company relationships.

The integration of the tax function into a company's overall business strategy is likely to require a shift in the mindset of many taxpayers – an approach that, whilst intuitive to taxpayers in more sophisticated tax jurisdictions, is likely to prove challenging within Ecuadorean business culture.

Anti-avoidance rules: increasing the Total Tax Rate?

With new limits on tax deductions for certain costs of transactions with related parties for fiscal year 2015 on, as well as the enforcement of limitations on the automatic application of benefits under double taxation treaties, the corporate income tax cost for multinational and local enterprises operating in Ecuador will be impacted significantly as taxpayers register increased levels of non-deductible expenses arising from their intra-group operations. This is likely to result in higher Total Tax Rates for many companies in Ecuador that conduct cross-border trade. These changes however will not be reflected in Paying Taxes which considers only domestic transactions.

The Ecuadorean Tax Authorities have however sought to offset the increase in the corporate tax burden by introducing benefits and incentives to benefit new investment, foreign financing and companies commencing economic activities in Ecuador.

A new measure for post-filing

With regard to the new post-filing index, Ecuador has a mixed performance. In common with the rest of South America, a VAT refund would not be available to the case study company as VAT refunds are available only to exporters and certain other types of company. On the corporate income tax correction and underpayment, however, Ecuador performs very well as it would take three hours to correct the tax return and make the additional payment and it would be unlikely to give rise to an audit.

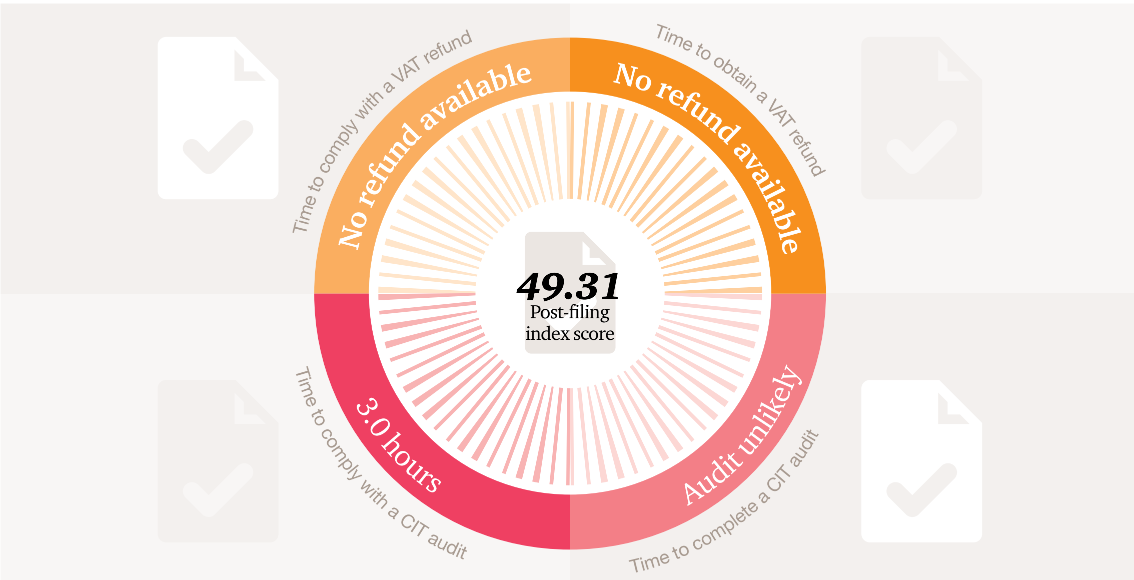
Looking forward

The on-going challenge for the Tax Authority will be to find a balance between continuing to enact its strategy (increase and improve revenue collection) and stabilising and reducing tax costs and administrative burdens for taxpayers.

This shift in the taxpayer's mindset reflects the integration of the tax function into a company's overall business strategy.

Figure 53

Post-filing index and components for Ecuador for 2015



Hungary

Slow but steady improvements to the tax system

Dora Mathe, PwC Hungary

Between 2004 and 2015, the *Paying Taxes* sub-indicators for Hungary have shown slow but steady improvement. As a result of the Hungarian government's efforts to make the tax system more competitive and efficient, Hungary is moving closer to the EU & EFTA average for Total Tax Rate, time to comply and number of payments sub-indicators.

Hungary's Total Tax Rate decreased from 56.6% in 2004 to 46.5% in 2015; above the average of 40.3% for the EU & EFTA region. In the last six years, the stated goal of the government has been to shift the focus of taxation from income tax to consumption taxes.

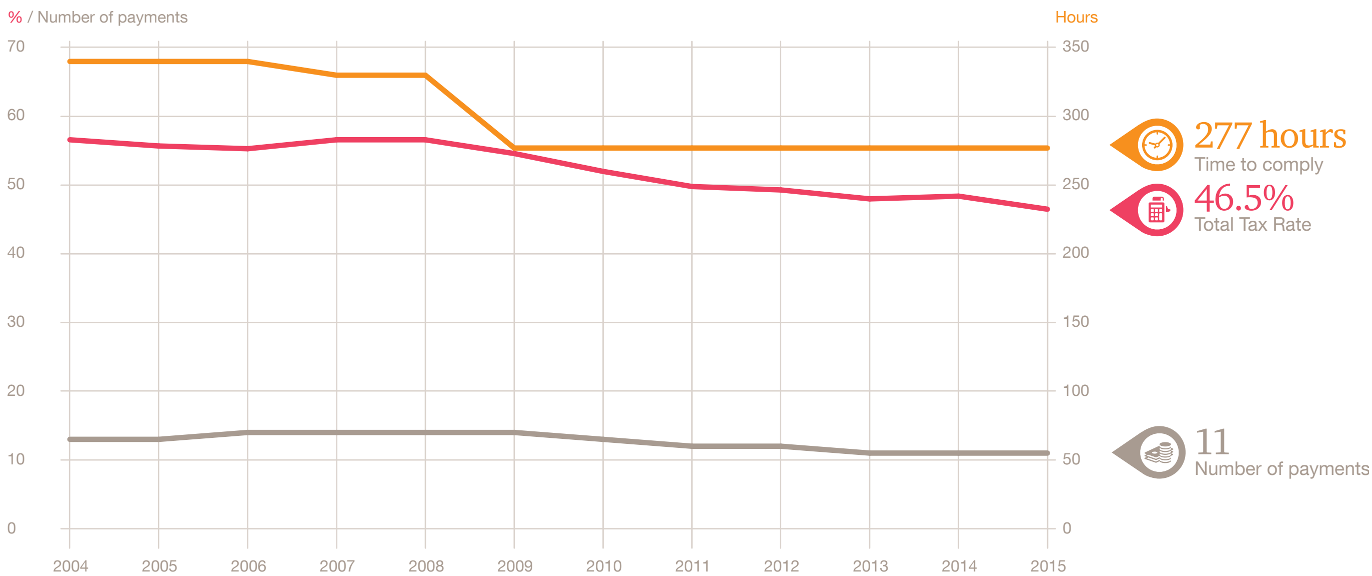
For corporate income tax, the first HUF 500 million is now taxed at 10% (raised from HUF 50 million) while the general VAT rate has been increased from 25% to 27% in 2012. The direction of the shift in the tax burden is not expected to change in the near future, but ultimately the government's goal is to decrease both the number and the rates of taxes.

The Government is also using the tax system to tackle several demographic challenges which are outside the scope of our case study. Tax incentives have been introduced for families with children to help combat issues presented by an aging population and to acknowledge the importance of families.

2004
56.6%
2015
46.5%
Decrease in the Total Tax Rate.

Figure 54

Trend in the *Paying Taxes* sub-indicators for Hungary since 2004



Other recent tax related measures seek to address the lack of skilled workers in certain sectors and regions including permitting tax deductions for investments in employee accommodation and new cafeterias and subsidising employees' mortgage costs.

Hungary's time to comply has fallen by 19% since the start of the study, largely due to the introduction and enhancement of an electronic tax compliance portal. At 277 hours it does, however, remain more than 100 hours above the EU & EFTA average of 164 hours.

At 11, the number of payments sub-indicator is slightly below the EU & EFTA average of 11.8.

Sector specific 'austerity taxes' have, however, been introduced in recent years, for banks, insurance companies, energy companies, retailers and telecommunications companies. These new taxes are not reflected in the study as they do not apply to the case study company. The government has announced its intention to reduce the number of taxes levied in Hungary.

Post-filing index

Overall, Hungary's post-filing index of 75.79 is better than the world average, but worse than the regional (EU & EFTA) average. EU & EFTA is however the best performing region for the post-filing index and so sets a high benchmark.

The VAT refund process is likely to trigger an audit in Hungary. This may account for the time to comply with a VAT refund being longer than the world average and almost twice the regional average. On average though it takes less time to obtain the VAT refund than in other economies globally or in EU & EFTA. Our experience is that an audit would, in many cases, not extend the time a company has to wait for a VAT refund in Hungary.

Correcting a CIT return, as per the case study scenario, is thought likely to trigger an audit in Hungary. Despite this, the time to comply with a CIT audit is lower than the world average. It is higher than the EU & EFTA average, but this is not surprising as in many economies in the EU & EFTA the correction does not trigger an audit. The resultant audit would on average be quicker in Hungary than in other economies globally or in the EU & EFTA.

While the *Paying Taxes* data shows improvements in recent years and the new post-filing index is relatively good, there is room for further improvement and the government is making efforts to speed up tax administration processes and audits. From 2016, the National Tax and Customs Authority is able to classify taxpayers as "reliable" or "risky" and the two categories have different legal consequences. "Reliable" taxpayers may benefit from less detailed and shorter audits. Taxpayers that are not assigned to either category will continue to be subject to the general rules.

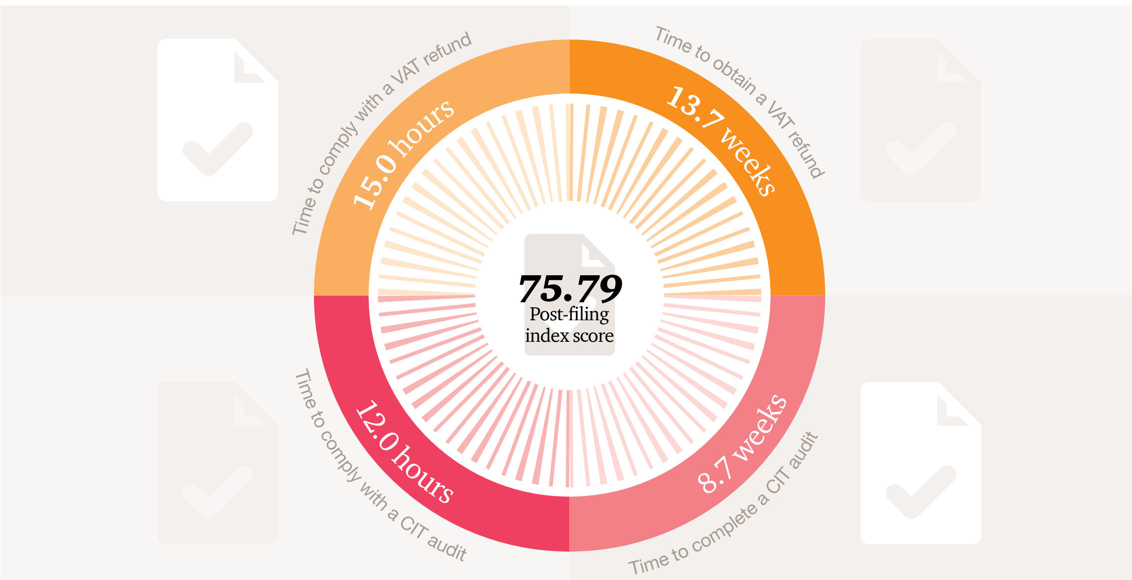
We are expecting further improvements to electronic systems, as the tax authority is requesting more and more online information from taxpayers. Electronic tills and invoicing software will soon have to be connected to the tax authorities' system in real time. More transactional information is collected via the VAT return process, which can be used for automatic cross checks.

75.79

Hungary's post-filing index of 75.79 is better than the world average.

Figure 55

Post-filing index and components for Hungary for 2015



Indonesia

Improvements realised and more to come

Ay Tjhing Phan, PwC Indonesia

Indonesia has been stepping up its tax reform drive. Tax reforms resulted in the country moving up the *Paying Taxes* ranking by 11 places when looking at the reforms introduced in 2015, but an improvement of over 40 places when compared with the published position last year in view of the implementation of the new post-filing index and the recognition of efficient post-filing processes.

In 2015, Indonesia's number of payments and time to comply sub-indicators improved to 43 payments and 221 hours respectively, thanks to the use of electronic social security systems. Indonesia's Total Tax Rate marginally increased from 29.7% to 30.6% due to the addition of a new pension contribution with 2% paid by employers.

As for the new post-filing index, Indonesia has a favourable score of 76.49, which is above the average for the Asia Pacific region of 58.53.

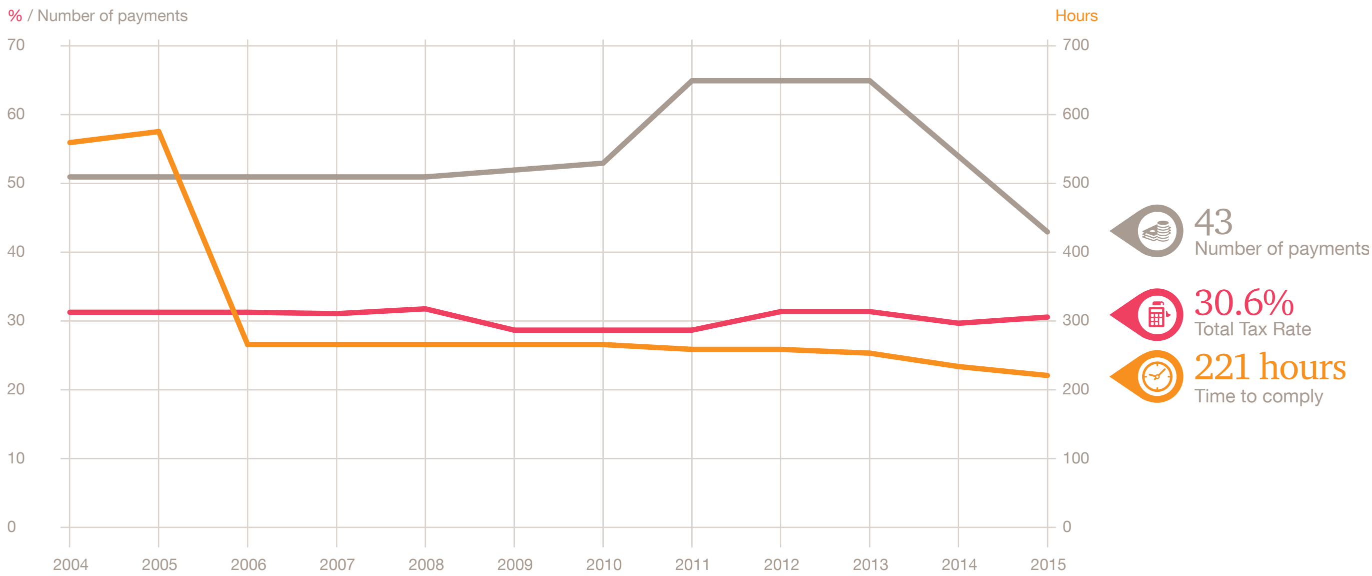
Indonesia operates a self-assessment system. The tax office generally relies on clarifications from taxpayers and tax audits to assess the quality of tax compliance, though tax audits are not applied in all scenarios. For instance, the correction of an error in a company's corporate income tax return, which had led to a tax underpayment (as is included in the corporate income tax components of the post-filing index) would not generally be expected to trigger an automatic tax audit.

Indonesia
76.49
Asia Pacific
58.83

Indonesia has a favourable post-filing index score of 76.49, which is above the average for Asia Pacific.

Figure 56

Trend in the *Paying Taxes* sub-indicators for Indonesia since 2004



Efforts to streamline the ease of paying taxes are not new. There has however been a renewed focus since President Joko Widodo took office in 2014. Given the ongoing efforts, the impact of reforms in 2016 and later, such as compulsory e-payment for tax liabilities, are not yet included in the current year's *Paying Taxes* data which relates to the calendar year ending on 31 December 2015. The effect of these recent reforms may however be seen in future years.

The impact of other key reforms, while far reaching, are not reflected in the study as they do not apply to the case study company. For example, regulations were introduced in 2013 for very small taxpayers (below the case study threshold) with qualifying turnover of below IDR 4.8 billion (about USD 370 thousand) to apply a 1% final tax to turnover. Targeted measures like this reduce the burden for corporate income tax calculations and minimise future disputes for small taxpayers.

In July 2016, Indonesia launched its highly anticipated Tax Amnesty Program. Over IDR 3,793 trillion (about USD 291.8 billion) of assets previously undeclared was reported in the first trimester of a nine month long program – approximately 95% of an IDR 4,000 trillion target. More than 392,000 taxpayers participated in the same period. This provides a substantial one-off redemption receipt for the government. It also drastically improves tax literacy among taxpayers and widens the tax base of declared assets to improve the quality and coverage of future tax compliance.

The success of the Tax Amnesty Program reflects the growing trust of taxpayers in the current Indonesian government. Credit must also be given to comprehensive communication campaigns nationwide. To date, Indonesia's tax-to-GDP ratio remains low (averaging 11%-12%) relative to the target of 16% by year 2019. To achieve this goal, Indonesia has to widen and stabilise its tax net through reform and public education to encourage more and better tax compliance.

Changes to Indonesia's tax system should take into account the complexities and wide range of taxpayers in its dynamic economy. Continuing regular engagement with business communities and practitioners to receive industry feedback is therefore key.

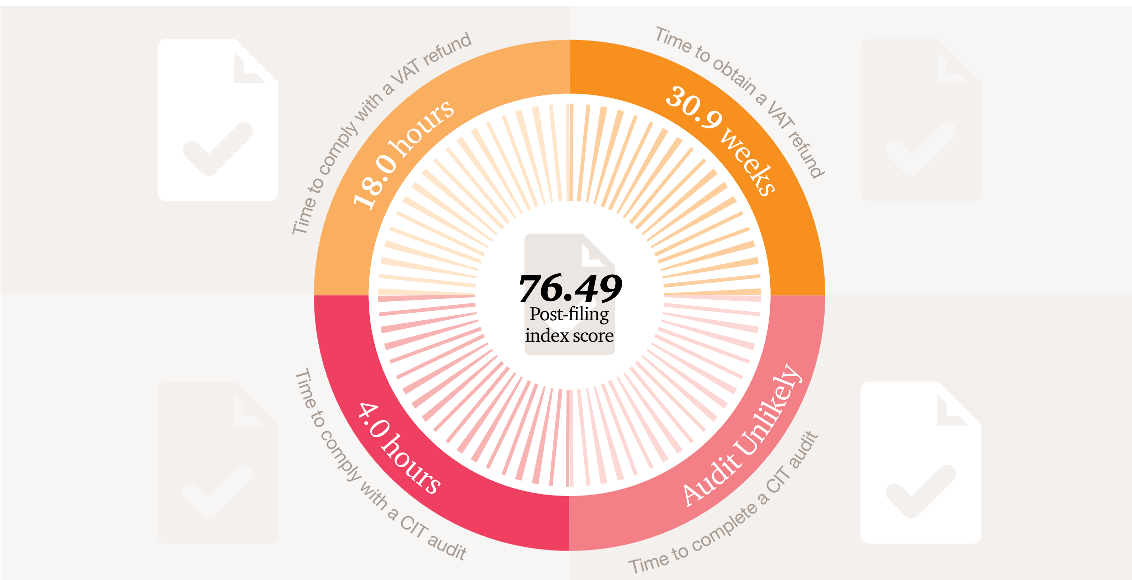
Reforms to the general tax administration law, income tax law and VAT law (among others) are expected to be debated in the coming months. On-going professionalism of tax authority staff has been helpful in improving and increasing their knowledge of commercial trends and international tax practices. Additional data collection and improved processing for more targeted tax enforcement is another priority area. Further measures, if adopted, such as the mandatory use of electronic tax filing could also further ease the administrative burden of complying with tax obligations.

We remain encouraged that the government will be able to build on momentum from the Tax Amnesty Program and maintain their focus on the ease of paying taxes to further improve tax compliance in Indonesia.

The success of the Tax Amnesty Program reflects the growing trust of taxpayers in the current Indonesian government.

Figure 57

Post-filing index and components for Indonesia for 2015



World Bank Group Paying Taxes team

Rita Ramalho
Joanna Nasr
Nadia Novik
Emily Jane Bourke
Rodrigo A. Sarmento de Beires
Edgar Chavez

PwC Paying Taxes team

Neville Howlett
Tom Dane
Gwendolin Chau
Sopheaktra Meas

The Total Tax Rate included in the survey by the World Bank Group has been calculated using the broad principles of the PwC methodology. The application of these principles by the World Bank Group has not been verified, validated or audited by PwC, and therefore, PwC cannot make any representations or warranties with regard to the accuracy of the information generated by the World Bank Group's models. In addition, the World Bank Group has not verified, validated or audited any information collected by PwC beyond the scope of *Doing Business Paying Taxes* data, and therefore, the World Bank Group cannot make any representations or warranties with regard to the accuracy of the information generated by PwC's own research.

The World Bank Group's *Doing Business* tax ranking indicator includes three components in addition to the Total Tax Rate. These estimate compliance costs by looking at hours spent on tax work, the number of tax payments made in a tax year, and evaluate and score certain post-filing compliance processes. These calculations do not follow any PwC methodology but do attempt to provide data which is consistent with the tax compliance cost aspect of the PwC Total Tax Contribution framework.

At PwC, our purpose is to build trust in society and solve important problems. We're a network of firms in 157 countries with more than 223,000 people who are committed to delivering quality in assurance, advisory and tax services. Find out more and tell us what matters to you by visiting us at www.pwc.com.

11/16. Design Services 30038.

www.pwc.com/payingtaxes
www.doingbusiness.org