Paying taxes

Jean-Baptiste Colbert, French philosopher and minister of finance to King Louis XIV, once remarked that “the art of taxation consists in so plucking the goose as to obtain the largest possible amount of feathers with the smallest possible amount of hissing.” How taxes are collected and paid has changed a great deal since then. But governments still face the challenge of maximizing revenue collection while minimizing distortions.

Doing Business records the taxes and mandatory contributions that a medium-size company must pay in a given year and also measures the administrative burden of paying taxes and contributions. It does this with 3 indicators: number of payments, time and total tax rate for the *Doing Business* case study firm. The number of payments indicates the frequency with which the company has to file and pay different types of taxes and contributions, adjusted for the way in which those filings and payments are made.[1] The time indicator captures the number of hours it takes to prepare, file and pay 3 major types of taxes: profit taxes, consumption taxes, and labor taxes and mandatory contributions. The total tax rate measures the tax cost (as a percentage of profit) borne by the standard firm. The indicators do not measure the fiscal health of economies, the macroeconomic conditions under which governments collect revenue or the provision of public services supported by taxation. The ranking on the ease of paying taxes is the simple average of the percentile rankings on its component indicators, with a threshold applied to the total tax rate (table 15.1).[2]

WHO REFORMED IN PAYING TAXES IN 2011/12?

From June 2011 to June 2012 *Doing Business* recorded 31 reforms making it easier or less costly for firms to pay taxes (table 15.2). Sixteen economies mandated or enhanced electronic filing, eliminating the need for 196 separate tax payments and reducing compliance time by 134 days (1,070 hours) in total. In Uruguay small and medium-size companies can now file and pay corporate income tax, value added tax and capital tax online. This option was available only for large taxpayers until 2011. Seven other economies implemented electronic filing for the first time, raising the number offering this option from 67 in 2010 to 74 in 2011.[3] Thanks to improvements in electronic systems for filing and paying social security contributions, Saudi Arabia

TABLE 15.1 Where is paying taxes easiest—and where most difficult?

Easiest	RANK	Most difficult	RANK
United Arab Emirates	1	Cameroon	176
Qatar	2	Mauritania	177
Saudi Arabia	3	Senegal	178
Hong Kong SAR, China	4	Gambia, The	179
Singapore	5	Bolivia	180
Ireland	6	Central African Republic	181
Bahrain	7	Congo, Rep.	182
Canada	8	Guinea	183
Kiribati	9	Chad	184
Oman	10	Venezuela, RB	185

Note: Rankings are the average of the economy’s rankings on the number of payments, time and total tax rate, with a threshold imposed on the total tax rate. See the data notes for details.

Source: Doing Business database.

- **Firms in the United Arab Emirates face the lightest administrative burden in paying taxes. They must make only 4 payments a year and spend 12 hours doing so.**
- **From June 2011 to June 2012 *Doing Business* recorded 31 reforms making it easier and less costly for companies to comply with taxes.**
- **Liberia made the biggest improvement in the ease of paying taxes in the past year.**
- **Belarus has advanced the most toward the frontier in regulatory practice in paying taxes since 2004.**
- **The most common feature of tax reforms in the past 8 years was to reduce profit tax rates, often in the context of parallel efforts to improve tax compliance. But in the past 2 years more economies focused on introducing electronic systems.**
- **Among regions, Eastern Europe and Central Asia had the biggest improvement in the ease of paying taxes in the past 8 years.**

For more information on good practices and research related to paying taxes, visit http://www.doingbusiness.org/data/exploretopics/paying-taxes. For more on the methodology, see the section on paying taxes in the data notes.

TABLE 15.2 Who made paying taxes easier and lowered the tax burden in 2011/12—and what did they do?

Feature	Economies	Some highlights
Introduced or enhanced electronic systems	Albania; Belarus; Bosnia and Herzegovina; Costa Rica; Czech Republic; Georgia; Germany; Kenya; Panama; Russian Federation; Saudi Arabia; Slovak Republic; Slovenia; Ukraine; United Arab Emirates; Uruguay	Ukraine introduced an online filing and payment system and made its use mandatory for medium-size and large enterprises.
Reduced profit tax rate by 2 percentage points or more	Belarus; Brunei Darussalam; Fiji; Japan; Republic of Korea; Lao PDR; Liberia; Mali; Puerto Rico (U.S.); Slovenia; Thailand; United Kingdom	The United Kingdom reduced 2 corporate income tax rates: the main rate from 28% to 26% and the small-company rate from 21% to 20%.
Merged or eliminated taxes other than profit tax	Albania; Hungary; Liberia	Liberia abolished the turnover tax.
Simplified tax compliance process	Jamaica; Mali; Panama; Poland	Jamaica introduced joint filing and payment of all 5 types of social security contributions that firms must make.
Reduced labor taxes and mandatory contributions	Croatia	Croatia made paying taxes less costly by reducing health insurance contributions.
Introduced change in cascading sales tax	Swaziland	Swaziland introduced value added tax to replace its cascading sales tax.

Source: Doing Business database.

this year ranks among the 10 economies with the fewest payments and lowest tax compliance time (table 15.3).

Electronic systems for filing and paying taxes eliminate excessive paperwork and interaction with tax officers. They can reduce the time businesses spend on complying with tax laws, increase tax compliance and reduce the cost of revenue administration.[4] But achieving these results requires effective implementation and high-quality security systems.

Twelve economies reduced profit tax rates in 2011/12: 6 high-income economies (Brunei Darussalam, Japan, Korea, Puerto Rico [territory of the United States], Slovenia and the United Kingdom), 4 middle-income ones (Belarus, Fiji, Lao PDR and Thailand) and 2 low-income ones (Liberia and Mali). Reductions in profit tax rates are often combined with efforts to widen the tax base by removing exemptions and with increases in the rates of other taxes, such as value added tax (VAT). Liberia improved the most in the ease of paying taxes. It reduced the corporate income tax rate from 35% to 25% and abolished the turnover tax. The total tax rate fell from 43.7% of profit to 27.4%.

Eleven economies introduced new taxes (Cambodia, Costa Rica, Cyprus, El Salvador, Ethiopia, Japan, Malawi, Maldives, Mali, Nigeria and República Bolivariana de Venezuela). Others increased profit or income tax rates (Botswana, the Dominican Republic and Moldova)[5] or social security contributions (Hungary and Poland).

WHAT HAVE WE LEARNED FROM 8 YEARS OF DATA?

Since 2005 *Doing Business* has recorded 296 tax reforms in 142 economies (figure 15.1). Some of these reforms introduced online filing, added in 29 economies in the past 8 years. These and other improvements to simplify tax compliance reduced the time required to comply with the 3 major taxes measured (profit, labor and consumption taxes) by 54 hours on average, and the number of payments by 7. Eastern Europe and Central Asia had the biggest improvement, with the time reduced by 181 hours and the number of payments by 24 (figure 15.2). Upper-middle-income economies have advanced the most toward the frontier in regulatory practice in paying taxes, followed by lower-middle-income economies (figure 15.3).

TABLE 15.3 Who makes paying taxes easy and who does not—and where is the total tax rate highest?

Payments (number per year)

Fewest		Most	
Hong Kong SAR, China	3	Antigua and Barbuda	57
Saudi Arabia	3	Guinea	58
Norway	4	Senegal	59
Qatar	4	Panama	60
Sweden	4	Congo, Rep.	61
United Arab Emirates	4	Sri Lanka	61
Georgia	5	Côte d'Ivoire	62
Singapore	5	Serbia	66
Chile	6	Tajikistan	69
Malta	6	Venezuela, RB	71

Time (hours per year)

Fastest		Slowest	
United Arab Emirates	12	Cameroon	654
Bahrain	36	Ecuador	654
Qatar	48	Senegal	666
Bahamas, The	58	Mauritania	696
Luxembourg	59	Chad	732
Oman	62	Venezuela, RB	792
Switzerland	63	Vietnam	872
Saudi Arabia	72	Nigeria	956
Seychelles	76	Bolivia	1,025
Hong Kong SAR, China	78	Brazil	2,600

Total tax rate (% of profit)

Highest	
Colombia	74.8
Palau	75.7
Bolivia	83.4
Tajikistan	84.5
Eritrea	84.5
Uzbekistan	98.5
Argentina	108.3[a]
Comoros	217.9[a]
Gambia, The	283.5[a]
Congo, Dem. Rep.	339.7[a]

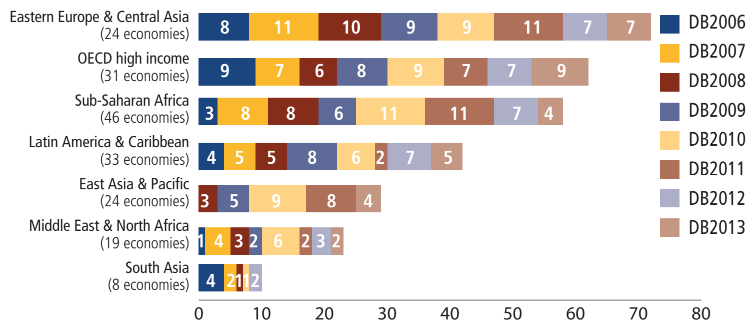
Note: The indicator on payments is adjusted for the possibility of electronic or joint filing and payment when used by the majority of firms in an economy. See the data notes for more details.

a. As a result of assumptions about the profit margin used to standardize the financial statements of the case study company, in 4 economies the amount of taxes due would exceed the profit of the company. To be able to comply with its tax obligations in these economies, the company would therefore have to charge more for its products and generate a higher profit. The methodology does not allow for price adjustments and assumes a standard cost markup of 120%. See the data notes for more details.

Source: Doing Business database.

FIGURE 15.1 Tax reforms implemented by more than 75% of economies in the past 8 years

Number of *Doing Business* reforms making it easier to pay taxes by *Doing Business* report year



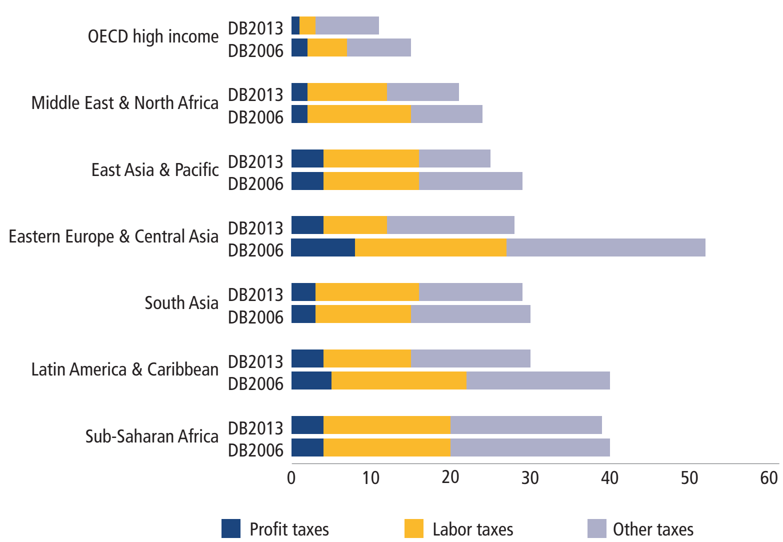
Note: An economy can be considered to have only 1 *Doing Business* reform per topic and year. The data sample for DB2006 (2004) includes 174 economies. The sample for DB2013 (2011) also includes The Bahamas, Bahrain, Barbados, Brunei Darussalam, Cyprus, Kosovo, Liberia, Luxembourg, Malta, Montenegro and Qatar, for a total of 185 economies.

Source: Doing Business database.

Besides lessening the administrative burden of taxes, many economies also reduced tax rates, often from relatively high levels and with complementary efforts to improve tax compliance. Sub-Saharan Africa had the largest reduction in the total tax rate, 13.3 percentage points on average since 2005. Some of this reduction came from the introduction of VAT, which replaced the cascading sales tax.[6] Burundi, Djibouti, Mozambique, Sierra Leone and Swaziland all introduced VAT systems. In Sierra Leone tax revenue remained relatively stable as a percentage of GDP, rising only from 10.8% in 2005 to 11% in 2009. But the share of revenue coming from taxes on goods and services increased from 11.9% to 24.6%.[7]

FIGURE 15.2 Tax compliance simplified the most in Eastern Europe and Central Asia

Average payments (number per year)

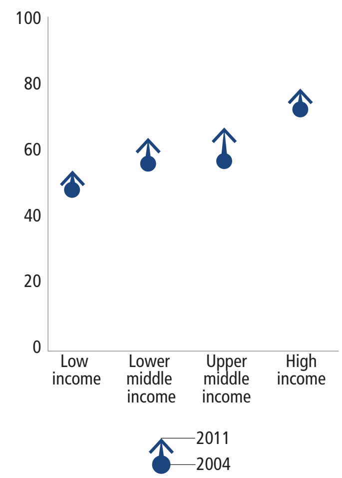


Note: To ensure an accurate comparison, the figure shows data for the same sample of 174 economies for both DB2006 (2004) and DB2013 (2011) and uses the regional classifications that apply in 2012. The economies added to the *Doing Business* sample after 2004 and therefore excluded here are The Bahamas, Bahrain, Barbados, Brunei Darussalam, Cyprus, Kosovo, Liberia, Luxembourg, Malta, Montenegro and Qatar. DB2006 data are adjusted for any data revisions and changes in methodology.

Source: Doing Business database.

FIGURE 15.3 Middle-income economies have advanced the most toward the frontier in paying taxes

Average distance to frontier (percentage points)



Note: The distance to frontier measure shows how far on average an economy is from the best performance achieved by any economy on each *Doing Business* indicator—in this case for the paying taxes indicators since 2004. The measure is normalized to range between 0 and 100, with 100 representing the best performance (the frontier). The data refer to the 174 economies included in *Doing Business 2006* (2004). Eleven economies were added in subsequent years. The figure shows data for the financial years 2004 (measured by the paying taxes indicators in *Doing Business 2006*) and 2011 (measured in *Doing Business 2013*).

Source: Doing Business database.

Many African economies also reduced profit tax rates in the past 8 years, reducing the share of profit taxes in the total tax rate by 0.9 percentage point on average in the region. But the biggest reduction in this share occurred in OECD high-income economies, where it fell by 4.1 percentage points on average. Over the same period tax revenue increased slightly as a percentage of GDP in Sub-Saharan Africa and remained relatively stable in OECD high-income economies.[8]

Such reforms have had positive effects. Matching the data available since 2005 on total tax rates with investment data indicates that a reduction of 1 percentage point in the total tax rate is linked to an increase in investment equivalent to 1% of GDP.[9]

Belarus has advanced the furthest toward the frontier in regulatory practice in paying taxes since 2004 (table 15.4). Embarking on an ambitious tax reform in

TABLE 15.4 Who has narrowed the distance to frontier in paying taxes the most since 2004?

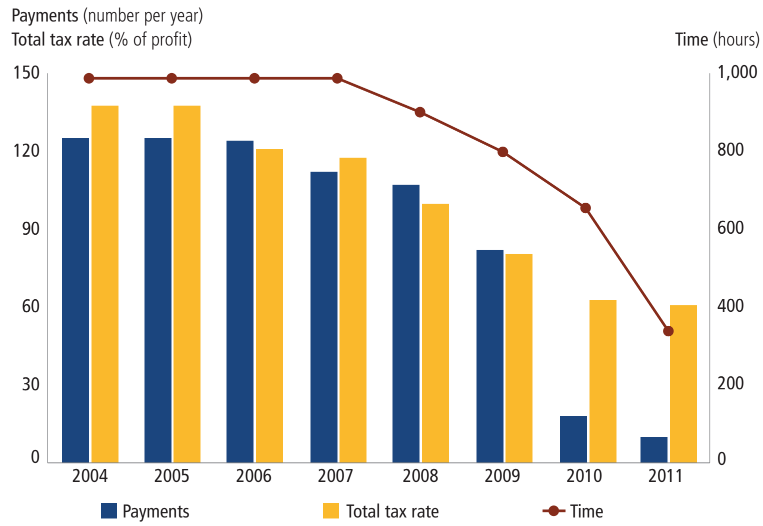
Most improved	Improvement in distance to frontier (percentage points)
Belarus	61 (0→61)
Colombia	47 (13→60)
Georgia	47 (39→86)
China	42 (19→61)
Azerbaijan	37 (38→75)
Ukraine	31 (16→47)
Argentina	30 (14→44)
Sierra Leone	30 (34→64)
Uruguay	30 (31→61)
Yemen, Rep.	30 (33→63)

Note: The distance to frontier measure shows how far on average an economy is from the best performance achieved by any economy on each *Doing Business* indicator—in this case for the paying taxes indicators since 2004. The measure is normalized to range between 0 and 100, with 100 representing the best performance (the frontier). The data refer to the 174 economies included in *Doing Business 2006* (2004). Eleven economies were added in subsequent years. The first column lists the top 10 most improved economies in order; the second shows the absolute improvement in the distance to frontier between financial years 2004 and 2011.

Source: Doing Business database.

2005, Belarus abolished several taxes, reduced tax rates, broadened the tax base, simplified filing forms and the tax law and invested in electronic systems that make it easier to file and pay taxes. These changes reduced the number of annual payments from 125 to 10, the time from 987 hours a year to 338 and the total tax rate from 137.5% of profit to 60.7% (figure 15.4). The efforts to make tax compliance easier and less costly are paying off. While 1,681 new limited liability corporations registered for the first time in 2005 in Belarus, 6,142 did so in 2011. Indeed, the total number registered in this period increased by 68.9% (from 27,619 to 46,653).[10]

FIGURE 15.4 Broad tax reform in Belarus reduces payments, time and total tax rate



Source: Doing Business database.

NOTES

This topic note was written by Nan Jiang, Pawel Kopko, Nina Paustian, Momodou Salifu Sey and Tea Trumbic.

1. Companies sometimes prefer more frequent payments, to smooth cash flow, and less frequent filing.
2. The threshold is set at the 15th percentile of the total tax rate distribution, and this year is 25.7%. All economies with a total tax rate below this level receive the same percentile ranking on this component. The threshold is not based on any economic theory of an "optimal tax rate" that minimizes distortions or maximizes efficiency in the tax system of an economy overall. Instead, it is mainly empirical in nature, set at the lower end of the distribution of tax rates levied on medium-size enterprises in the manufacturing sector as observed through the paying taxes indicators. This reduces the bias in the indicators toward economies that do not need to levy significant taxes on companies like the *Doing Business* standardized case study company because they raise public revenue in other ways—for example, through taxes on foreign companies, through taxes on sectors other than manufacturing or from natural resources (all of which are outside the scope of the methodology).
3. One of the economies added to the sample in this year's report, Malta, has offered electronic filing for several years and so is included in the count for 2010.
4. Mexico, for example, has relied heavily on technology and the use of electronic systems to lessen the administrative burden for taxpayers. These efforts simplified requirements for firms, reducing the number of annual tax payments recorded by *Doing Business* from 27 in 2007 to 6 in 2011 and the time to comply with major taxes from 549 hours to 337.
5. At the same time Moldova reduced the withholding tax for dividends from 15% to 6% and lowered the withholding tax for payments other than dividends from 15% to 12%. In addition, it introduced a new tax regime for small and medium-size enterprises under which small companies pay a single tax of 3% of revenues from operational activities.
6. VAT is collected by the firm and its cost is fully passed on to the consumer. Because the firm has to make the payments and spend time filling out the returns, VAT is included in the indicators on payments and time. But the amount of VAT paid is not included in the total tax rate. Cascading sales tax, which is paid at every point of the supply chain, is included in the total tax rate, because the firm cannot deduct the sales tax it pays on its supplies from the amount it owes on its sales. Economies introducing VAT regimes to replace the sales tax regime have therefore seen a reduction in their total tax rate.
7. World Bank, World Development Indicators database, http://data.worldbank.org/.
8. World Bank, World Development Indicators database, http://data.worldbank.org/.

9. Following Eifert (2009) and Djankov, McLiesh and Ramalho (2006), the analysis controls for government consumption, institutional quality and corruption perception. It also controls for total trade openness and rents from natural resources.
10. World Bank Group Entrepreneurship Snapshots. The full data set is available on the *Doing Business* website (http://www.doingbusiness.org).