

The impact of VAT compliance on business

Introduction

Value Added Tax (VAT) is now the most common form of consumption tax system used around the world. This analysis covers VAT¹ and equivalent sales tax systems implemented in 145 different countries.

Although the principles of the tax are broadly the same everywhere, the rules can be enacted and implemented differently in different countries so that the compliance burden on business varies considerably.

This study has been undertaken to look at the differences in the time required for VAT compliance in different countries, and to demonstrate how the way in which taxes are implemented using different administrative practices can have a significant impact on the compliance cost for business.

This study uses data collected by the World Bank Group on the ease of paying taxes in different economies around the world as part of the Paying Taxes 2010 project². It also uses supplementary data collected by PricewaterhouseCoopers LLP (PwC) specifically for this study from a representative sample of the countries which have a VAT system.

The purpose of the Paying Taxes study is to provide data to help inform tax policy and tax reform. The Paying Taxes study results enable governments to compare their tax systems on a like-for-like basis against relevant peer groups. The wealth of data available on VAT in the study enables a comparison on how this tax is implemented and administered.

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¹ In this report "VAT" is used to refer to Value Added Tax, Goods and Services Tax, and equivalent Sales tax systems.

² Paying Taxes 2010- the global picture is a joint publication from the World Bank Group/ International Finance Corporation and PricewaterhouseCoopers LLP – see <http://www.pwc.com/gx/en/paying-taxes>

Results in summary

VAT is the predominant form of consumption tax system used around the world.

On average it takes the case study company longer to comply with VAT around the world, than to comply with corporate income tax.

The time needed to comply with VAT varies considerably around the world and even between neighbouring countries.

It generally takes less time to comply with VAT in the developed world than in developing countries.

VAT compliance tends to be more time-consuming in countries where indirect taxes are not administered by the same tax authority that deals with corporate income tax.

Administrative procedures vary from country to country and these have a significant impact on how long it takes to comply with VAT.

It takes less time to comply, on average, in countries where business uses online filing and payment for VAT.

The frequency with which VAT returns are required (monthly/quarterly), and the amount of information requested has a significant impact on the time it takes to comply.

Compliance takes longer where extra documentation has to be submitted with the return.

There is a correlation between the VAT compliance burden and the time delay in receiving a VAT refund. Typically, where it takes longer to receive a refund, it takes longer to comply.

Methodology

Paying Taxes 2010 – the global picture

This study uses data collected by the World Bank Group from contributors around the world for the Paying Taxes 2010 project.

Paying Taxes 2010 measures the ease of paying taxes in calendar year 2008 across 183 economies. It uses three indicators which cover both the cost of taxes (the Total Tax Rate) and the compliance burden (the time needed to comply and the number of tax payments). The data collected for the Paying Taxes project is extensive, and includes the time required for VAT compliance activities.

The case study company

The Paying Taxes project uses a case study company with a standard fact pattern. The case study company is a limited liability company engaged in a taxable activity for VAT. VAT is not therefore a significant cost to the company, but is a compliance burden. The company is domestic and does not participate in any foreign trade (no imports or exports). A high level description of the case study company is provided in [Figure 1](#).

The use of a case study company with a standard fact pattern does of course bring limitations. For example, the size of the company (60 employees) may be considered large in some countries, modest in others. However, it does enable the collection and comparison of data from a large number of countries on a like-for-like basis, and the potential identification of best practices.

Figure 1

The Paying Taxes case study company

- A limited liability taxable company
- Operates in the country's most populous city
- Is 100% domestically-owned and has 5 owners
- Is in its second year of operation
- Purchased all the assets shown in its balance sheet and hired all its workers 2 years ago.
- Has 60 employees – 4 managers, 8 assistants and 48 workers, all nationals
- Produces flower pots and sells them at retail
- Does not participate in any foreign trade (no imports or exports)
- Has a turnover of 1,050 times income per capita

List shows a high level summary of facts and assumptions for the Paying Taxes case study company.

See Paying Taxes 2010 for a complete set.

Source: Paying Taxes 2010

What compliance activities are measured?

In the Paying Taxes project, expert local contributors in each country are asked to estimate the time that will be needed by the case study company to prepare, file, and pay its VAT, based on a defined list of compliance activities, as set out in Figure 2.

Inevitably, as this is an estimate, there is a degree of judgement involved. However considerable effort by the World Bank Group goes into checking and confirming that the methods used are consistent, including verification by several contributors in an economy.

VAT administration

This study also uses data on tax administration which is collected as part of the Paying Taxes project. This is not used in calculations for the ease of paying taxes indicators, but is used to provide insight to the results. In addition, PwC has collected supplementary data, specifically for this study, from a sample group of countries³ around the world who have a VAT.

This group of 30 countries are a 20 percent sample of those included in Paying Taxes 2010 who have a VAT, and have been selected to be representative across the range of results for the time required for VAT compliance activities.

Figure 2

VAT compliance activities measured in Paying Taxes

Preparation activities

- Data gathering from internal sources
- Additional analysis of accounting information
- Calculation of tax liability including data inputting
- Preparation and maintenance of mandatory tax records if required
- Complying with changes in tax rates and rules (if relevant in the year)

Filing activities

- Completion of tax return forms, including any additional documentation required
- Submission of forms to tax authority, which may include time for electronic filing, waiting time at the tax authority office, etc.

Payment activities

- Calculations of tax payments required including extraction of data from accounting records, and maintenance of accounting systems
- Analysis of forecast data and associated calculations if advance payments are required
- Making tax payments, whether online or at the tax authority office, which may include time for waiting in line and travel

Table shows the compliance activities for VAT measured in the Paying Taxes project.

Source: Paying Taxes 2010

³ These countries are: Australia, Bolivia, Chile, China, Colombia, Cote d'Ivoire, Czech Republic, El Salvador, Ghana, India, Indonesia, Ireland, Jamaica, Kazakhstan, Kenya, Latvia, Luxembourg, Mauritius, Mexico, Namibia, Peru, Philippines, Romania, Singapore, South Africa, Tanzania, Thailand, Trinidad and Tobago, the United Kingdom and Zambia.

VAT is the predominant form of consumption tax around the world

In 2008, 145 of the 183 economies measured in *Paying Taxes 2010* used a VAT system representing nearly 80 percent of the population. Twenty of the 183 economies used a different consumption tax system in 2008, and 18 economies had no consumption tax which applied to the case study company.

Figure 3 shows the countries with a VAT, by regional or economic grouping. All 26 EU countries included in *Paying Taxes* (Malta is not included) have VAT, and of the OECD countries, only the US has a different type of sales tax.

VAT is also used in the developing world. Around 80 percent or more of the economies in Africa and Latin American and the Caribbean that were included in *Paying Taxes* have a VAT.

In the Middle East, only six of the 15 economies in *Paying Taxes* had a VAT system in 2008. One had another form of consumption tax and eight had no consumption tax systems relevant to the case study company.

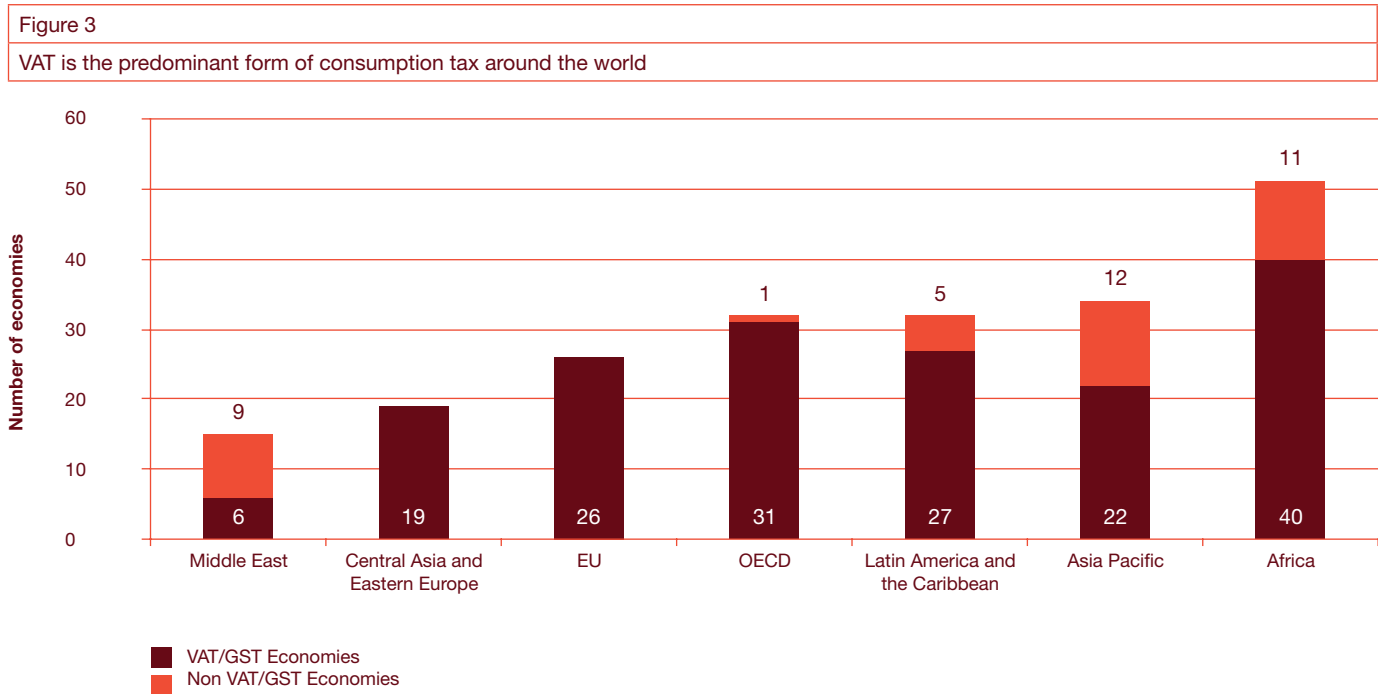


Chart shows the number of economies with/without a VAT system using selected regional and economic groupings.
Source: *Paying Taxes 2010*, PwC analysis

On average, it takes longer to comply with VAT than it takes to comply with corporate income tax.

On average, in the 145 countries included in this study, it takes the case study company 125 hours to comply with VAT. Two thirds of this time (82 hours) relates to preparation activities, 19 percent of the time (24 hours) is spent carrying out filing activities, and the remaining 15 percent (19 hours) on payment activities.

Figure 4 compares the time needed for compliance activities on corporate income tax and VAT. The average time taken for the same case study company to comply with corporate income tax, as measured across all 183 economies in Paying Taxes 2010, is just 74 hours, which is 40 percent less time than needed for VAT.

These are average results for all of the countries covered. The amount of time taken to comply with VAT varies greatly between the different countries.

Figure 4
On average, it takes the company longer to comply with VAT than with corporate income tax

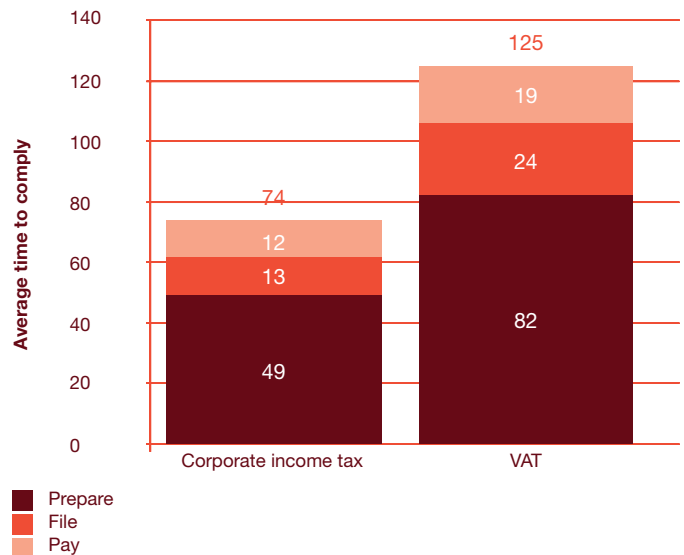


Chart shows the global average time taken to comply with CIT and VAT as measured in Paying Taxes 2010.

Source: Paying Taxes 2010, PwC analysis

The time needed to comply with VAT varies considerably around the world and even between neighbouring countries

The time needed to comply with VAT varies significantly around the world (see Figure 5). It ranges from eight hours in Switzerland and 22 hours in Finland to 480 in Bolivia and 1,374 in Brazil. The majority of countries fall within a range of 25 to 200 hours. However, in seven countries it takes less than 25 hours and in a further seven, over 300 hours.

Figure 5
The time needed to comply varies considerably around the world

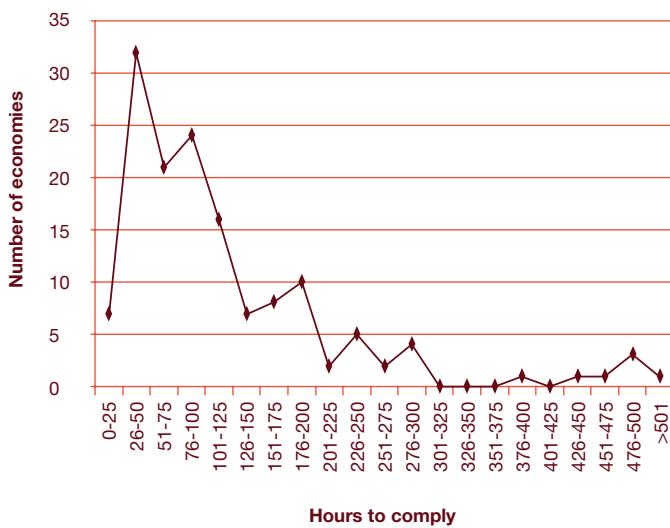


Chart shows the distribution of results for time taken to comply with VAT in Paying Taxes 2010.
Source: Paying Taxes 2010, PwC analysis

VAT systems are used in countries across all levels of development. However, in high income countries, the time taken to comply with VAT tends to be lower. This suggests that the more developed countries may have more streamlined VAT procedures. Figure 6 shows that 63 percent of countries taking 25 hours or less, and 56 percent of those

taking 50 hours or less, are high income countries. In contrast, 65 percent of countries taking more than 150 hours, and 72 percent of countries taking over 300 hours are either lower middle or low income countries⁴.

Figure 6
In high income economies it tends to take less time to comply

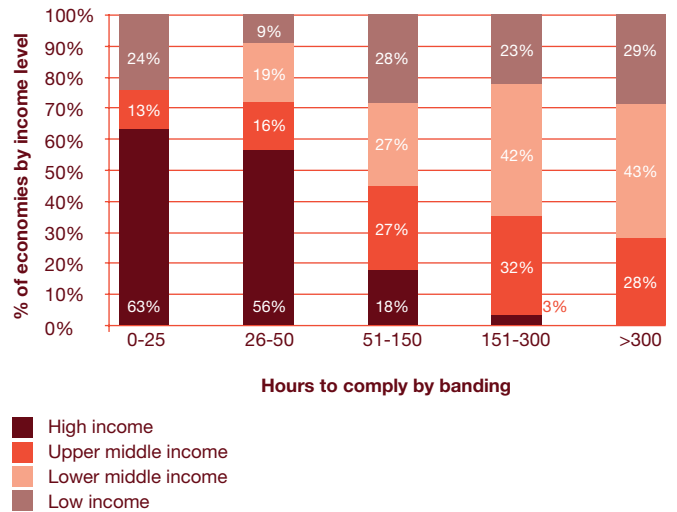


Chart shows time needed to comply with VAT by banding across the income level from the World Bank Doing Business project.
Source: Doing Business 2010, Paying Taxes 2010, PwC analysis

The time taken to comply varies considerably by geographic region. It takes the least time on average (73 hours) in the EU countries and the most time in Latin America and the Caribbean (192 hours) – see Figure 7.

⁴ Income levels from the World Bank/IFC Doing Business Project.

Figure 7
The time needed varies by region

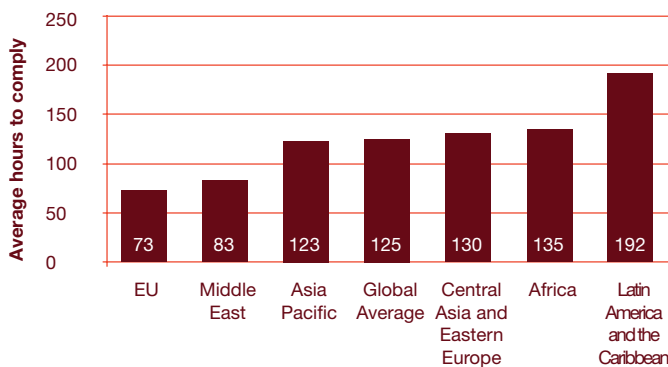


Chart shows the average time needed to comply with VAT for economies in each economic/geographic region and the world average for all economies with a VAT.

Source: *Paying Taxes 2010, PwC analysis*

The time needed can also vary between geographic neighbours. An interesting example of this is the European Union (*Figure 8*), particularly given that there is a common legal framework for VAT systems. However, there is still a wide range of results from 22 hours in Finland to 288 in Bulgaria, reflecting different administrative practices.

Figure 8
The time taken can also vary between geographic neighbours

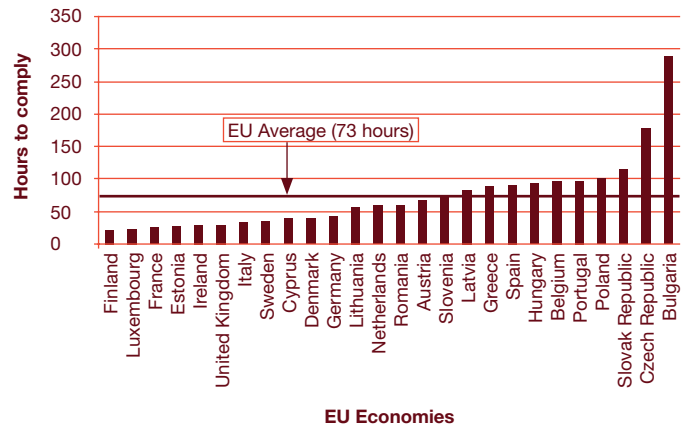


Chart shows the time to comply with VAT for economies in the EU. Note: Malta is not included in the *Paying Taxes* project.

Source: *Paying Taxes 2010, PwC analysis*

Administrative procedures vary and can significantly impact the compliance burden

It takes less time on average when indirect taxes are administered by the same tax authority

The Paying Taxes project shows that, on average, it takes less time to comply in countries where VAT is administered by the same tax authority as corporate income tax. Figure 9 shows that the average time taken to comply is 12 percent (16 hours) lower where the same tax authority administers both indirect taxes and corporate income taxes.

Figure 9
It takes less time to comply on average when indirect taxes are administered by the same tax authority as corporate income tax

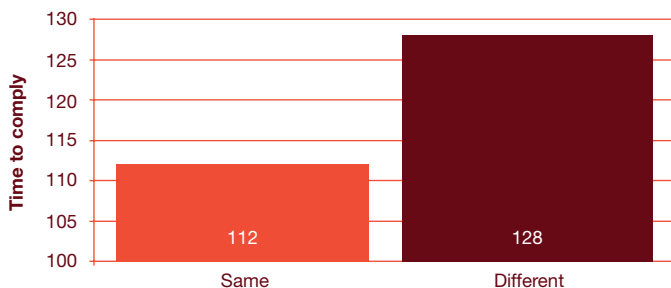


Chart compares the average time to comply with all consumption taxes for all economies in Paying Taxes 2010 where these are administered by the same or separate tax authorities.

Source: Paying Taxes 2010, PwC analysis of non indicator data

It takes less time on average in countries where business uses online filing and payment

In countries where electronic filing and payment is available and is used, the average time taken to comply with VAT is significantly lower. From our additional analysis of a sample of 30 countries, the average time taken to comply with VAT is 41 hours lower where online filing and payment is used (see Figure 10).

Figure 10
It takes less time on average in countries where business uses online filing and payment

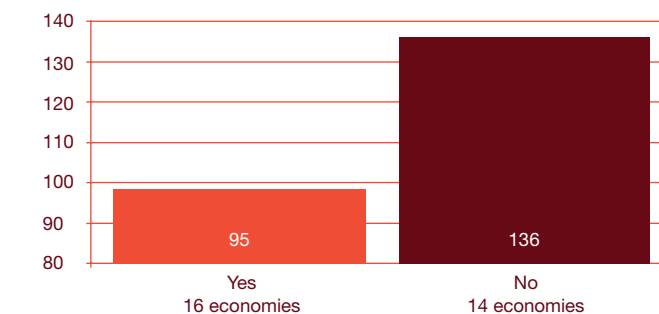


Chart compares the average time to comply with VAT for economies in the sample group where business of the size and nature of the case study company file and pay VAT online.

Source: Paying Taxes 2010, PwC analysis

The frequency at which VAT returns are required impacts the time to comply

As might be expected, the number and frequency of returns also impacts on the time taken to comply. In countries where monthly VAT returns are required, the time taken to comply is higher (on average 125 hours) compared with countries where returns are required to be made bi-monthly or quarterly (on average 81 hours) (see Figure 11).

The more information is required in the VAT return, the more time is needed

For the 30 economies in the sample, the average time needed to comply with VAT, per return, is 12 hours. However, this also varies by country. For example, it takes five hours per return in Ireland; 18 in China; and 25 in Kenya.

Clearly, the more extensive the tax return, the longer it takes to comply. An analysis of the sample group shows that in countries where the tax return has more than 20 boxes to be

completed, the average compliance time per return is over twice as much as in countries where the return has less than 20 boxes (see Figure 12).

Figure 11

The frequency at which VAT returns are required impacts the time to comply

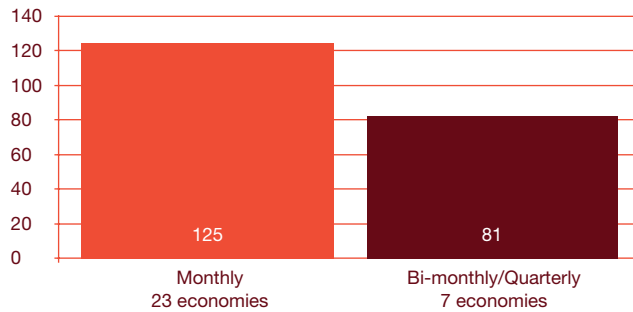


Chart shows the average time needed to comply in economies in the sample group depending on whether VAT returns are required to be made monthly, bi-monthly or quarterly.

Source: *Paying Taxes 2010*, PwC analysis

Figure 12

The more extensive/long the tax returns, the more time is needed

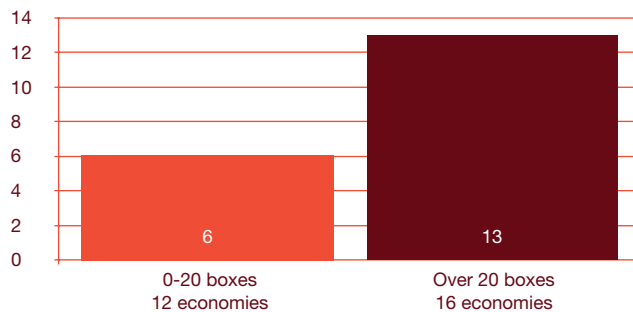


Chart shows the average time to comply per return for economies in the sample, depending on the number of boxes in the return which need to be completed.

Source: *Paying Taxes 2010*, PwC analysis

Two countries in the EU provide a good example of the impact of the length and frequency of returns on the compliance burden. Figure 13 compares the time taken to comply in the Czech Republic and Ireland. In Ireland, six returns are required each year, and each return has four boxes to be completed. In the Czech Republic, monthly returns are required and each has 67 boxes to be completed. The time to comply per return is three times longer in the Czech Republic than in Ireland.

Figure 13

Comparison of hours to comply with VAT in the Czech Republic and Ireland

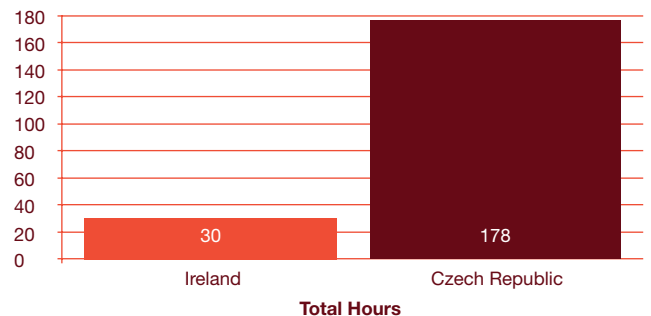


Chart shows the hours to comply with VAT in Czech Republic and Ireland.

Source: *Paying Taxes 2010*

The requirement to submit invoices or other documents with the return adds to compliance time.

Just under half of the countries in the sample group require businesses to submit invoices or additional documentation with the VAT return. The average time taken to comply for these countries is double that of countries where there is no requirement (158 hours compared with 76 hours) (see Figure 14).

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Figure 14

The requirement to submit invoices or other documentation with the return adds to compliance time

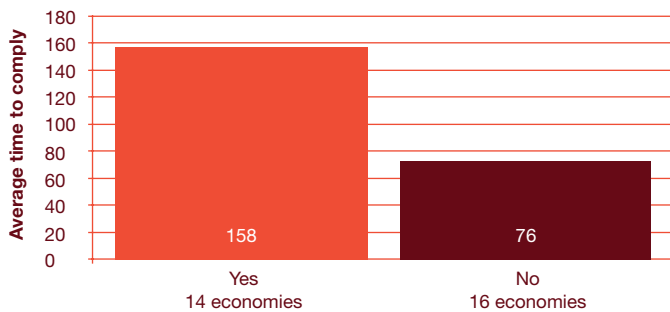


Chart compares the average time to comply for economies in the sample group where there is/is not a requirement to submit invoices or other documentation with the VAT return.

Source: *Paying Taxes 2010*, PwC analysis

In Kenya, supporting information must be submitted along with the monthly return including an analysis of all purchase invoices (invoice dates, invoice numbers, supplier names and registration numbers and the corresponding VAT amounts), plus details of any zero-rated supplies (invoice dates, numbers, and the value of the supplies) and where VAT is withheld (analysis of and including withholding tax certificates). While filing must be online in Kenya, which can save time, inputting data into Taxpayer Software (TSW) can still be time-consuming. For our case study company, it takes a total of 300 hours to comply with VAT in Kenya (or 25 per return), which is significantly longer than in other East African Community countries.

In China the control of VAT invoices is an important aspect of VAT compliance. VAT invoices on purchases have to be authenticated by the Tax Authority before they can be used to claim input VAT. And the case study company has to export data on all the VAT invoices issued in the month from its invoicing system and visit the tax office to input this into the Tax Authority system to ensure consistency of information. The time needed to comply in China is 216 hours, or 18 hours per return.

Changes to the rules and regulations can increase compliance time

Several countries in the sample group reported that extra hours were needed in 2008 to implement changes to the VAT rules and regulations. For example, in the United Kingdom, an extra five hours (or 17%) were needed to implement the temporary VAT reduction which became effective on 1 December 2008 as part of the government's fiscal stimulus in response to the recession. A similar amount of extra time was also needed when the temporary rate came to an end on 31 December 2009. In view of the latest changes announced in the new coalition's budget in June 2010, it is expected that additional hours will again be needed when the VAT rate increases in January 2011.

In some countries business has to comply with more than one consumption tax

In some countries, business has to comply with more than one consumption tax, which of course adds to the compliance burden. In 10 of the economies covered in *Paying Taxes 2010*, contributors reported that the case study company has to comply with more than one consumption tax. As *Figure 15* shows, the time to comply is considerably higher on average in those economies.

As an example, in India there are three different consumption taxes – Central sales tax and State VAT, administered by the State Revenue Department; and CENVAT, by the Federal Revenue.

Brazil is the country where it takes the longest time to comply. It takes our case study company 1,374 hours (or one person full time for two thirds of the year) to comply with the three consumption taxes relevant to it – which are PIS/COFINS and IPI (Federal taxes) and ICMS (State tax) – see *Figure 16*. The State tax system (ICMS) is very complex and involves compliance obligations in all of the 26 Brazilian states into which sales are made.

Figure 15

In some countries business has to comply with more than one consumption tax

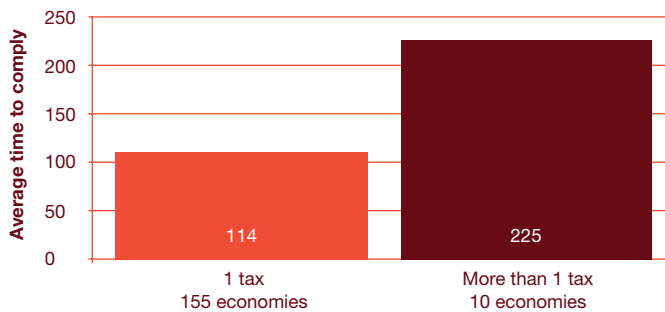


Chart shows the average time to comply with consumption taxes for the 165 economies in Paying Taxes 2010 with a consumption tax comparing countries with one or more than one consumption tax.

Source: Paying Taxes 2010, PwC analysis

There is a correlation between the VAT compliance burden and the time delay in receiving a tax refund

How long it takes for a taxpayer to receive a refund could be seen as a useful test of the efficiency of tax authorities. This is also important for business in view of the impact on corporate liquidity and the time value of money on delayed refund processing. In Paying Taxes 2010, contributors in all 183 economies were asked the question “In a typical situation, how long is it likely to take, in practice, for a company to receive a VAT or withholding tax refund in your country (time from claiming a refund to receiving the cash)?” Figure 17 compares the responses overall to this question with the responses for selected regional and economic groupings.

In some regional groupings, the typical time was notably quicker, in others slower. Sixty five percent of respondents in the OECD, and 63 percent in the EU, said the typical time taken is less than three months. In the African Union countries however, 19 percent reported a typical time of less than three months, and 30 percent indicated more than a year. In Latin America and the Caribbean, the figures were 19 percent for less than three months and 32 percent for more than a year.

Figure 16

Hours to comply with consumption taxes in Brazil

	Hours per year
Preparation	
Data gathering	247
Additional analysis	330
Calculation of tax liability	165
Mandatory tax records/ keeping up to date	82
	824
Filing	
Completion of tax returns	330
Submission to tax authorities	82
	412
Payment	
Calculation of tax payments	14
Analysis of forecasts for advance payments	14
Making tax payments	110
	138
Total	1,374

Source: Paying Taxes 2010

There is a correlation between the time to receive a refund and the time to comply. On average it takes twice as long, or more, to comply in Africa and in Latin America and the Caribbean, where refunds are slower, than in the OECD and EU countries (see Figure 18).

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Figure 17

How long is it likely to take in practice for a company to receive a VAT refund?

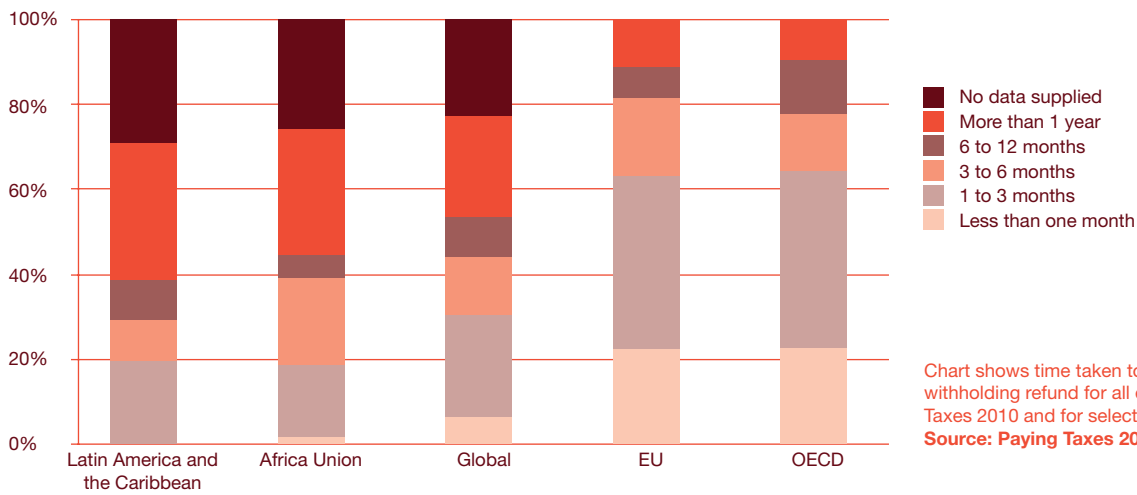
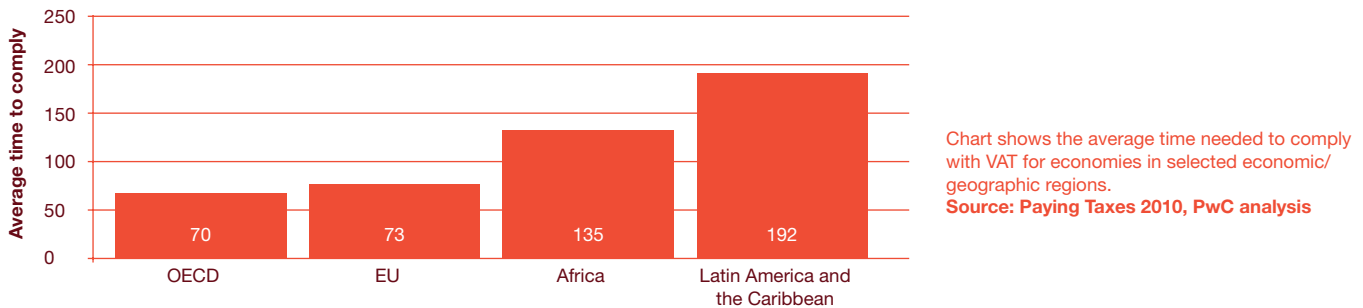


Figure 18

Where it takes longer to get a refund it tends to take more time to comply



Summary

VAT is the most common form of consumption tax system used around the world.

Although the principles of the tax are broadly the same everywhere, the compliance burden on business varies considerably.

Our study suggests that different administrative practices and the way in which VAT has been implemented are key reasons for the range in hours that it takes our case study company to comply with VAT requirements.

- More time is spent on compliance activities where VAT is administered by a separate Tax Authority.
- More time is spent where tax administration is weaker (as measured by the time it is likely to take to obtain a refund).
- The frequency of returns and the amount of data which has to be submitted have an impact on how long it takes to comply.
- Less time is spent where business uses online filing and payment.

The compliance burden tends to be lower in the developed world and higher in lower income countries.

Streamlining the compliance burden and reducing the time needed by business is important for the efficient working of VAT systems.

PricewaterhouseCoopers LLP
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