INTERNATIONAL

The Occasional Failure in VAT Implementation: Lessons for the Pacific*

Christophe Grandcolas

Fiji, Samoa, Vanuatu and Cook Islands have already implemented a single-rate VAT (10% to 12.5%). These countries have also adopted a threshold to limit the number of taxpayers to a size that is compatible with their administrative capacity, although this was not the case in every country at the date of implementation (e.g. Samoa). Most other PICs (i.e. Kiribati, Tonga, Tuvalu, the Federated States of Micronesia, Republic of Marshall Islands and Niue) have already requested additional information on the functioning of the VAT system.

Table 1 shows that VAT is a major source of revenue wherever it has been adopted. The share of VAT in total tax revenue ranges from 19% in PNG to 49% in the Cook Islands. Indeed, the average for the five PICs (i.e. 32%) is higher than the world average of 27% and also higher than that for small islands (i.e. less than 1 million of people; 29%). The VAT collected compared to the GDP, which is the efficiency ratio,4 ranges from 4.5% in PNG to 13% in the Cook Islands and averages at 7.9%. The thresholds (minimum of annual turnover to be VAT registered taxpayer) vary from USD 8,000 in Fiji to USD 65,000 in Vanuatu.

1. INTRODUCTION

In many developing countries, the adoption of value added tax (VAT) has been bolstered as trade tax revenues have come under pressure from increasing trade liberalization commitments. In the Pacific, tariff reductions are driven by two agreements, i.e. the Pacific Islands Countries Trade Agreement (PICTA) and the Pacific Agreement on Closer Economic Relations (PACER).2 Although some preliminary studies have predicted that the effect on tax revenue will be manageable, it is possible that the small islands states will nevertheless have to adopt substantial structural adjustments by designing and implementing the tax reforms necessary to reduce reliance on tariffs in order to maintain government revenue as a percentage of the gross domestic product (GDP). Consequently, more than seven Pacific Island Countries (PICs) are considering implementing a VAT or a similar broad-based consumption tax while phasing out their customs duties.

I previously documented how five PICs had successfully implemented a VAT3 regime. Papua New Guinea (PNG),

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1. PFTAC, which is based in Fiji, provides technical advice and training in public financial management, tax administration and policy, banking regulation and supervision, and macroeconomic and financial statistics to its 15 member countries. The member countries are the Cook Islands, Federated States of Micronesia, Fiji, Kiribati, Marshall Islands, Nauru, Niue, Palau, Papua New Guinea, Samoa, Solomon Islands, Tokelau, Tonga, Tuvalu and Vanuatu.
2. PICTA is a free trade agreement among all PICs, excluding Australia and New Zealand, and only covers trade in goods between members (services are excluded). Under PICTA, exports from member countries will not be subject to any form of trade barrier when imported into other member countries. PICTA became effective on 14 April 2003, and by 2012, the tariffs should be reduced to zero for all PICs and “negative list” (protection) tariffs reduced to zero by 2016. PACER is an economic cooperation agreement for all forum members including Australia and New Zealand. The key elements in achieving this trade integration are trade liberalization and trade facilitation.
4. The efficiency ratio is defined as the ratio of the share of VAT revenues in GDP to the standard rate. Average 35 implies that a 1-point increase in the standard rate is associated with an increase in the share of VAT revenues in GDP of about 0.35 percentage points.
three main criticisms were raised:

- political commitment (i.e. politicians had promised to repeal the VAT if elected);
- poor performance due to poor planning prior to its introduction; and
- an inadequate definition of registration threshold, which resulted in an excessive number of taxpayers to be administered.

This article, after briefly reviewing three cases of failures (i.e. Malta, Grenada and Ghana) in 2., goes on to discuss two successful cases (i.e. Gabon and Mauritius) in 3., and in 4., lessons are drawn on the prerequisites for successful VAT implementation in the PICs.

2. COUNTRY EXPERIENCE: FAILED VATs

2.1. Malta

Malta introduced a VAT in January 1995 and the initial performance was strong. The VAT revenue raised was about 6.8% of GDP, with a C-efficiency ratio of around 73%.

In December 1996, a new government, which was committed to repealing the VAT, came to power. As noted in the White Paper For a Better Tax System (January 1997), three main criticisms were raised:

- “The reality of VAT in a state like Malta is that much of it is disguised customs duty.” It was argued that a return to explicit tariffs would be superior recognizing that “… in the particular geographic and economic situation of Malta, customs duties need not be replaced by VAT to ensure a non-discriminatory system”;
- compliance costs were perceived to be high, especially for medium-sized enterprises; and
- the quite extensive zero rating of domestic consumption, including food other than catering, introduced is of considerable complexity.

With regard to the first criticism above, Malta is indeed one of the few countries where imports exceed consumption, so there is some merit to the argument. However, it is always possible to generate at least as much revenue from a consumption tax as from a tariff. Setting the consumption tax at a rate equal to that of the initial tariff ensures that consumption is unaffected by the switch but revenue is now collected not only on imports but on all consumption, a base that will be wider to the extent that there is any domestic production. Besides it is always better to raise revenue by taxing consumption properly than by distorting trade. A properly structured VAT would be less distorting than a broad-based tariff or other forms of sales tax. Furthermore, as an economy develops, the merit of the VAT in preserving the chain of taxation will grow in importance.

As to the second criticism, an unusual feature of the Maltese system was that the initial VAT threshold was set at zero. Most VAT is paid by a relatively small number of taxpayers. Monitoring numerous small taxpayers who collectively pay little tax utilizes administrative resources that would be better devoted to ensuring compliance by larger taxpayers. Reducing the number of taxpayers could be achieved by introducing a minimum turnover before taxpayers are required to register. In most modern tax administrations, special organizational units and systems are set up to monitor and control the large VAT taxpayers.

The widespread zero rating on domestic transactions, which was the third criticism, is not inherent only in small countries. Zero-rated basic goods (e.g. books, clothes) or basic services (essentially electricity) distort the entire concept of zero rating, which is meant only for products that are not consumed locally (i.e. exports) with lower administrative consequences.

In 1997, Malta replaced its VAT with a single-stage sales tax (i.e. the excise tax on products (ETP)) and with selective excises on services. The ETP included crediting and other arrangements to avoid cascading. These replacements were introduced sequentially during the year, thereby complicating the evaluation of the revenue effects
of the reform. There seems, however, to have been a noticeable fall in revenue by about 1.5% of GDP. This system was very complex to administer. Moreover, the introduction of a credit mechanism made the tax closer to a VAT.

Following a further change of government, the VAT was successfully reintroduced in January 1999. The main structural difference from the initial VAT was an increase in the threshold from zero to about MLT 15,000 for goods. Currently, VAT is imposed at a standard rate of 18% and a reduced rate of 5% for specified items, and the revenue raised is more than 5% of the GDP.

2.2. Grenada

Grenada introduced a VAT in 1986 as one element of a more comprehensive tax reform programme. However, the new VAT was unsuccessful and within months of its introduction, it began to see frequent amendment and was finally replaced in 1995 by a “general consumption tax”.

The VAT system was originally intended as a broad-based tax at a 10% rate, on all production and distribution including retail sales. The introduction of VAT in Grenada suffered from severe design and administration weaknesses. On the design side, there were two important issues that contributed to its failure:

- In order to preserve the benefits of tax exemptions granted previously, many domestic goods and services were zero-rated. As a result, the 1986 VAT did not become a broad-based tax on value added at the manufacturing level, but instead left a substantial portion of domestic manufacturing untaxed. This not only reduced the potential tax base but also discriminated against imports. Moreover, the number of tax refund requests overwhelmed the tax administration. Consequently, Grenada did not benefit from the fundamental advantage of a VAT system, with the systematic credit mechanism treating all taxpayers equally, because it maintained a cumbersome case-by-case system of exemptions essentially driven by protectionism.

- The low threshold of XCD 12,000 per annum brought many small businesses under the ambit of the VAT regime, even though these businesses could not meet the requirements for record keeping. This eroded taxpayers’ compliance, creating widespread discontent and increasing political pressure to amend the law.

With regard to the administration, neither the government, nor the business community were adequately prepared for the operation of a VAT:

- There was no overall framework to address the necessary changes in administration to implement a VAT including staffing, training and procedures (including improved cooperation between different administrative agencies). One example of the unprepared approach, was the switch of responsibility for VAT collection from the customs department to the inland revenue department just a few weeks before the introduction of VAT.

- A taxpayer education programme to provide comprehensive information and convince the public of the advantages of the VAT had not been implemented. Moreover, there was a lack of taxpayer training, which would have been critical for smaller businesses with limited administrative capacities.

Grenada is now considering implementing a new VAT system in 2008.

2.3. Ghana

Prior to the introduction of the VAT in March 1995, taxes on domestic consumption in Ghana were generally imposed at the importation and manufacturing stage of production (not extended through the retail stage). The sales tax was levied on goods albeit with numerous exemptions by the customs administration. The Inland Revenue Services collected other domestic indirect taxes, which were imposed on a narrow range of services. The government recognized that the main defects of the regime were its relatively narrow domestic coverage and weak administration. Moreover, the tax system had a cascading effect resulting in severe economic distortions.

As a consequence, the government undertook two years of planning and preparation to introduce a VAT. The Parliament passed the VAT Act in November 1994, and the VAT Regulations were subsequently passed in February 1995. Although the VAT became effective in January 1995, actual collection of the tax commenced in March 1995 and initial returns were to be filed in April 1995.

The government repealed VAT in June 1995 in response to civil unrest⁸ and concerns about the tax’s impact on inflation. Upon repeal of the VAT law, the previous sale and service taxes were revived along with their respective administrative systems and procedures.

Based on the study by Seth Terkper,⁹ there are four general reasons why the implementation of VAT failed in Ghana. First, delays in adopting the VAT legislation and regulations adversely affected the preparation for the introduction of the VAT. As Terkper noted:

After the draft act was tabled, Parliament set the bill aside and requested that the VAT management team engage in a national education campaign to sensitize the population to the objective of the tax. Needless to say that the education that took place between May and November 1994 was virtually ineffective because it lacked precision and the legal backing to prompt any serious interest among the general public. The rate was not clearly announced until after the beginning of 1995, which allowed little time for businesses to assess the impact of the VAT on the prices of their goods and services. The 1995 budget increased the standard rate of sales tax from 15 to 17.5% for January and February 1995. Therefore the decision to fix the single VAT rate had an adverse effect on the VAT implementation and strongly suggested that the VAT rate would at worst not exceed the standard rate of sales tax, which in 1994 was 15%. The inability of the Ministry of Finance to stick to the anticipated coverage for goods and services may also have con-
tributed to the decision to increase the rate of tax from 15 to 17.5%.

Second, the threshold for small traders to register for VAT was set at a very low level of GHC 25 million (approximately USD 14,000). This low threshold resulted in too many taxpayers (i.e. over 10,000) being registered for the VAT, and the VAT administration did not have the capacity to deal with so many taxpayers. “The appropriate level of the registration threshold was never completely settled until the repeal of the VAT law in June 1995” (Terkper, S.).

Third, none of the branches of tax administration (i.e. VAT, Inland Revenue Services, and Customs and Excise Services) were adequately prepared to implement the VAT. Terker found that:

One issue that raised the most resentment among the revenue institution was the creation of the VAT Service as a third revenue institution. The creation of the VAT was meant to consolidate the administration of all domestic indirect taxes, including the excise duty on local output. Indeed, the rivalry between Customs Services and the new VAT Services adversely affected the successful implementation of the VAT. It became increasingly difficult in some instance to separate the resentment against the new VAT Service from the rancor against the tax itself.

At the time of the introduction of the VAT, the administration did not have a sufficient number of well-trained personnel to administer the VAT. The delay in passing the VAT law resulted in an inadequate number of trained staff at the time of introduction. Additionally, the lack of collaboration between the three branches of the tax administration hindered the implementation because proper administration and enforcement of a VAT requires the sharing of import and export information between all three branches.

Finally, taxpayers and consumers claimed that they were not fully informed of the impact of the VAT on their business or consumption decisions. While information material was prepared on various aspects of the VAT, several businesses demonstrated that they did not understand the workings of the tax and its impact on their pricing and purchasing decisions. Activities such as advertising, seminars, workshops, consultations, book-keeping reviews and advisory visits to businesses were not adequately undertaken in the lead up to the implementation of the VAT. The small number of skilled staff at their post at the time of the introduction led to a lack of advisory visits to new VAT taxpayers. As a consequence, several businesses simply increased their prices by the amount of tax on sales, not taking into account credit for tax paid on inputs and the removal of the previous sales and services taxes. This was exacerbated by inflationary pressures present in the economy at the time of the introduction of the VAT, as noted by Terker:

The 1995 budget has increased the excise duty on fuel products. The economy was experiencing poor food harvest during this period because the lack of rainfall in most parts of the country. The fast depreciation of the local currency against major convertible currencies meant an upward pressure on the cost of imported goods and services.

Ghana successfully reintroduced the VAT in 1999 with a new threshold of USD 75,000.

3. COUNTRY EXPERIENCE: SUCCESSFUL VATs

3.1. Gabon

Tax policy

The VAT system that was introduced in Gabon in April 1995 (same date as Ghana) had a broad coverage, a single rate, few exemptions, a high threshold and special procedures to expedite VAT refunds to exporters through the tax department.

Tax administration

The Gabonese authorities made a strong commitment to implement VAT, two years before its introduction. As a result, they managed to benefit from two years of technical assistance from France and the IMF. Before the introduction of VAT, the authorities gradually implemented a strategy that included (i) a reliable Taxpayer Identification Number (TIN) system, (ii) a pilot large taxpayers unit to monitor registration, collection, audit, and enforcement and (iii) a basic computerized tax system to detect, control and enforce late filers and “stop filers” (i.e. taxpayers who had stopped filing VAT returns).

Results

As a result of the policy and administration measures taken, Gabon found that:

- compliance was high: 800 VAT taxpayers have been registered using a registration threshold of USD 1 million or more. Since the implementation of VAT, all receipts and notices have been issued electronically, and 80% of returns are filed on time and 87% upon receipt of the first reminder;
- VAT was a revenue generator: During the first year of implementation (i.e. April 1995 to March 1996), VAT revenue had been 45% greater than the revenue from the taxes it had replaced. In 1995, for the first six months of its implementation, VAT accounted for about 32% of the total non-oil revenue and 5.5% of the non-oil GDP; and
- tax reform and statistics: In Gabon, most of the fiscal data is now available from computer analyses provided by the tax, customs and treasury departments on a regular and reliable basis.

3.2. Mauritius

Tax policy

The introduction of VAT in Mauritius became effective in September 1998. The level of VAT was fixed at a single rate of 10%, a compromise that was approved by the National Assembly instead of an originally proposed 12%, which was considered to be revenue neutral. In line with standard VAT practice, exports were zero rated. The annual threshold for compulsory registration for VAT was fixed at MUR 3 million (equivalent to USD 100,000). The sales tax was abolished at the time VAT became effective and the hotel and restaurant tax was phased out over a period of three years. The rate of VAT was increased to
12% with effect from 1 July 2001 and 15% with effect from 1 July 2002.

**Tax administration**

As VAT was considered a catalyst to modernize the entire tax administration, the following steps were taken: (i) a new VAT Department was created to monitor registration, collection, and enforcement, (ii) a basic computerized tax system was implemented to help detect, control, and enforce payment by late filers and "stop filers", (iii) VAT registration forms and TIN certificates were designed and printed, (iv) VAT payment forms were designed, (v) a tax school was set up to train the staff selected to monitor and audit VAT, (vi) free seminars, workshops, and conferences for enterprises and accountants were held, (vii) a publicity campaign and a VAT registration programme were designed and launched, and (viii) a Revenue Authority was set up by merging progressively the Income Tax Department, the Registrar Department, and the VAT Department.

**Results**

In his Budget speech for 1999-2000, delivered on 14 June 1999 to Parliament, the Minister of Finance emphasized that “... the coming into operation of this new taxation has been smooth and efficient. I am pleased to report to the House that the rate of return compliance is over 95%. This speaks clearly of the effectiveness of the deterrents in-built in the legislation”. The introduction of VAT in Mauritius saw:

– outstanding levels of compliance: At the end of May 1999 (nine months after its introduction), the level of voluntary compliance was close to 99.5%. At the end of May 1999, only 38 monthly returns were missing (0.48%) compared with 7,825 VAT monthly returns receivable since October 1998; and

– high levels of revenue collected: For the first fiscal year after its introduction, the VAT collected was 53% higher than the amount collected from the sales tax and hotel tax during the same period for the previous year. For fiscal year 1999-2000, the VAT collected was estimated at 5.6% of the GDP.

### Table 2: Prerequisites for a successful VAT implementation. Situation in the PICs at the date of implementation

<table>
<thead>
<tr>
<th>Prerequisites</th>
<th>Cook Islands</th>
<th>Fiji</th>
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<th>Samoa</th>
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<th>Tonga (2005)</th>
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<tbody>
<tr>
<td>1. Steering committee and project team</td>
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<td>Y</td>
<td>N</td>
<td>Y</td>
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<td>2. VAT law with:</td>
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<td>– broad base</td>
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<td>– single rate</td>
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<td>– few exemptions</td>
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<tr>
<td>– high threshold</td>
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<td>N</td>
<td>Y</td>
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<tr>
<td>– self-assessment</td>
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<td>N</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
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<tr>
<td>– effective refunds system</td>
<td>Y</td>
<td>N</td>
<td>N</td>
<td>N</td>
<td>Y</td>
<td>N/A</td>
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<tr>
<td>– sound penalty system</td>
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<td>N</td>
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<tr>
<td>4. Correct planning of implementation (over 18 months)</td>
<td>Y</td>
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<td>5. Cooperation within the revenue services and TIN</td>
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<td>6. Public education campaign</td>
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<td>Y</td>
<td>N</td>
<td>NYA</td>
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<tr>
<td>7. Effective audit programme</td>
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<td>Y</td>
<td>Y</td>
<td>NYA</td>
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<tr>
<td>8. Technical assistance</td>
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<td>Y</td>
<td>N</td>
<td>Y</td>
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<td>N/A</td>
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<td>2. VAT law with:</td>
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<td>– broad base</td>
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<td>– high threshold</td>
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<td>N</td>
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<td>– self-assessment</td>
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<td>N</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
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<td>Y</td>
<td>N</td>
<td>Y</td>
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<td>Y</td>
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<tr>
<td>5. Cooperation within the revenue services and TIN</td>
<td>Y</td>
<td>N</td>
<td>N</td>
<td>N</td>
<td>N</td>
<td>NYA</td>
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<td>N</td>
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<td>Y</td>
<td>N</td>
<td>Y</td>
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<tr>
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<td>Y</td>
<td>N</td>
<td>Y</td>
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<td>N/A</td>
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11. Based on statements and organization in place at the time of the implementation.
In a modern tax administration system, there should be no formal assessment (before or after payment) and the returns should be accepted as determined and reported by the taxpayers. Heavy sanctions should be imposed on taxpayers to discourage underpayment.

4.2. Inadequacies of the penalty system and failure to take appropriate action against defaulters

Compliance covers three aspects of VAT collection ensuring that (i) the VAT return is submitted promptly, (ii) the tax is paid on time and (iii) the correct net tax is declared on the returns.

Obviously, failure to take action to enforce submission of returns and payment of tax undermine the credibility of the tax. This, in turn, could result in increased non-compliance. A “gentle enforcement approach” in the early stage of the tax should be avoided. Indeed, non-filers need to be dealt with firmly and immediately. The main objective of a tax administration, when self-assessed procedures are the rule, is not to collect the maximum amount of tax, but firstly to improve the level of voluntary compliance.

The maintenance of proper records is vital for the effective administration of VAT. Consequently, substantial penalties should be imposed on a taxpayer who fails to comply with this obligation. The maximum penalty depends on the degree of culpability of the taxpayer in relation to the particular failure. Further, a taxpayer who fails to maintain proper records but wishes to challenge a taxation assessment may not be able to satisfy the burden of proving that the assessment is excessive.

In Fiji, for example, the taxpayer files a return and pays at the same time. However, the tax office issues and sends a post-assessment payment notice to the taxpayer who reconciles the declaration and the payment. Although the system works, the human resources deployed to this task are very important. These time-consuming and burdensome procedures can have a negative impact on an administration’s “effectiveness”, as tax officers will need to deal with substantial paper work every month. To deal with this paper work, ambitious computerization efforts to speed up the processing of returns and issuance of assessments have been developed. But there is a question as to whether this is an effective use of computer resources, especially as at times, a more experienced staff official carries out a second check. Extensive duplication of work can be observed all along the cashier/data entry/assessing/dispatching/audit chain. This duplication happens further in the computerized system as the system is able to compute all the calculations and to flag the errors.

The issuance of assessments by the administration also discourages the application of a strong penalty system in case of discrepancies discovered later by a tax audit in the field. The taxpayer can always argue that his declaration has already been scrutinized by the tax administration and has passed inspection without any errors. The auditors are thus partly judging the effectiveness of their own assessors.

### Prerequisites

<table>
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<th>Vanuatu</th>
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<tbody>
<tr>
<td>9. Efficient computer system</td>
<td>Y</td>
<td>N</td>
<td>Y</td>
<td>Y</td>
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<tr>
<td>10. Appropriate offices</td>
<td>Y</td>
<td>Y</td>
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However, we must recognize that there are some issues in the PICs that can critically undermine the successful implementation of a VAT. These include:

- the absence of self-assessment procedures;
- inadequate structure of the penalty system and failure to immediately take the right actions against non-compliers;
- failure to refund exporters and investor on time; and
- failure to perform effective audits.

### 4.1. The absence of self-assessment procedures

As mentioned by Ebrill et al., “With few exceptions, modern tax administrations require taxpayers to self-assess their tax liabilities. They do not examine the details of tax returns when filed but use special selection techniques to identify appropriate cases for audit (including desk audits and field audits) at a later time. Such a system, based on voluntary compliance provides a more effective allocation of the scarce resources of a tax department for audit and enforcement work”.

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The issuance of assessments by the administration also discourages the application of a strong penalty system in case of discrepancies discovered later by a tax audit in the field. The taxpayer can always argue that his declaration has already been scrutinized by the tax administration and has passed inspection without any errors. The auditors are thus partly judging the effectiveness of their own assessors.
for the level of compliance and also because the trader is an intermediary for the collection of the tax”.13

Computer systems often are not helpful in dealing with non-filers. Such systems should be designed to be able to identify a non-filer within a few hours of the filing deadline and to print overnight, not only the list of non-filers but also the reminder notices. These actions should be done automatically without the need for any specific request by a tax official. The tax office’s manager should only have to sign the reminder notices and to send them, by fax if possible, to the taxpayer. Reactivity is the key answer against non-filers. Computer systems should be programmed to follow up on the reminder notice and assist with default assessment, temporary closure of business and with management reporting.

4.3. Failure to refund exporters and investors on time

The processing of refunds in relation to exports is one of the most problematic features of VAT in developing countries because the magnitude of the refunds can be substantial (more than 25% of the VAT collected) and fraud (e.g. overstatement of exports, falsification of invoices, production and purchase records, and underreporting of sales) is at times used to support claims of excess discretionary credit to be refund. Also, the fact that the administration has the power to issue refunds, can open up opportunities for corrupt practices (e.g. favouritism, prejudices and overprovision of refunds) and for governments to be tempted to delay the payment of refunds as temporary source of funds for their budgets.

Without an effective treatment of excess credits, VAT can introduce significant distortions. To quicken the refund process, the law should provide for interest on the amount of VAT not refunded within a reasonable period of time. This acts as a self-disciplinary tool for the administration. Unfortunately, where this provision exists, it is often not implemented. A number of reasons are given for this situation, a favourite being the claim that the credit were the subject of an audit and hence no interest is payable.

In some countries, refunds of taxes are paid from a specific account, which is limited by an approved allocation specified in the budget or an account that has insufficient funds to cover all the legitimate refunds. As a result, claimants may have to wait many months to receive tax refunds. These procedures are inappropriate. Refunds are not expenditure and are a normal part of tax administration. This is particularly true in a VAT where tax credits and resulting refunds are a vital element of the tax. It would be inappropriate to restrict payment of VAT refunds from a budget account limited by an annual appropriation. Ideally, refunds should be paid directly from a subaccount of the main account to which VAT revenues are deposited. To limit risks, it is advisable to set off excess credits against VAT and other tax arrears, require excess credits (other than for exporters) to be carried forward for some specified time (e.g. three to six months) and pay refunds only if they cannot be set off.14

4.4. Failure to perform effective audits

Effective audits are another key element of a successful VAT implementation. “The consequences of a weak audit program may not be immediately perceptible. While the lack of effective collection enforcement systems, especially those needed to deal promptly with non-filers and non-payers has an immediate impact on revenue, the lack of effective audits to detect underreporting of gross receipts and/or over reporting of credits may affect tax compliance only in the medium term. There have been some cases in which insufficient attention has been paid to the development of an audit function when the VAT was implemented. The development of an effective VAT audit program significantly helps improve income tax compliance. The experience of countries with successful audit programs also shows that a VAT audit plan should be primarily based on short, issue-oriented audits covering a limited tax period.”15

The need for more qualified, highly skilled auditors must be addressed in all PICs. An important lesson from a number of countries is that in the interval leading up to implementation of VAT, it may be necessary to develop a plan to recruit (or identify internally) a number of people with accounting backgrounds, and train them in the skills of auditing.

5. CONCLUSIONS

In administrative terms, VAT systems can work well in PICs if certain requirements are satisfied. Firstly, there must be a strong and explicit political commitment from the highest authority. Secondly, a detailed implementation plan with realistic dates for the main milestones must be prepared, and lastly, the necessary resources for implementation must be provided and this should be clearly identified in an implementation budget. For all the PICs, international help in terms of technical support will help to bring the experience of other countries in implementing VAT.

However, it is also important to pay attention to all the other aspects discussed in this paper that have helped other countries implement successful VATs.

These are the vital considerations in the process of planning, executing and following up on the implementation of a VAT-type tax. Following these considerations closely will, with no doubt, ensure a smooth transition to an efficient and effective VAT.

REFERENCES


13. Chengapen, E., note 7 above.
14. Ebrill et al., note 6 above, Chap. 15.
15. Ebrill et al., note 6 above, Chap. 14.


