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How much do tax authorities cost us?

The authorities responsible for collecting tax and customs revenues in Croatia spend an extra 2.2 lipas per kuna of collected revenues. That is the conclusion of research conducted by the Institute of Public Finance.

As we know, all work involves cost. Consequently, the collection of tax and customs revenues involves costs, too. In Croatia, this task is performed by Tax and Customs Administrations¹. For many years now, the Institute of Public Finance has carried out an analysis of the revenue collection costs borne by these departments². These costs are known as *costs of tax authorities* or *administrative costs of taxation and customs clearance*³. The costs of tax and customs authorities are largely financed from the State Budget and, to a smaller extent, from the authorities' own funds.

According to the budgetary classification, costs of tax authorities comprise operating costs (costs of employees, inventory spent, energy, DP equipment etc.), financial and other costs, as well as capital assets procurement costs.

The purpose of the research carried out by the Institute of Public Finance was to quantify the total costs of tax authorities in Croatia in the period 1997-2001, to determine the main characteristics of these costs and to provide recommendations for tax policy. What are the results of the research?

Table 1 Costs of tax authorities as shares of Budget revenue and GDP (in million kuna)

| | 1997. | 1998. | 1999. | 2000. | 2001. |
|--|---------|---------|---------|---------|---------|
| Budget revenue | 33.846 | 43.808 | 46.357 | 44.636 | 53.504 |
| GDP at current prices | 123.812 | 137.604 | 142.700 | 157.511 | 169.800 |
| Tax revenues (excluding contributions) | 33.846 | 33.846 | 33.846 | 33.846 | 33.846 |
| Total costs of tax authorities | 33.846 | 33.846 | 33.846 | 33.846 | 33.846 |
| Costs of tax authorities as a share of | | | | | |
| Budget revenue | 2,0 | 1,8 | 2,0 | 1,9 | 1,5 |
| GDP | 0,5 | 0,6 | 0,7 | 0,6 | 0,5 |
| Tax revenues | 2,15 | 1,96 | 2,46 | 2,16 | 2,05 |

Source: *Monthly Statistical Review of the Ministry of Finance* 76/02.

Taken from Bratić i Pitarević (2002).

¹ Tax and customs revenues were also collected by the Financial Police (FP) until its abolishment in May 2001.

² See e.g. *Financijska teorija i praksa* 24 (2), 2000, pp 169-188 and 28 (3), 2004, pp 271-399; available at: www.ijf.hr/financijska_praksa/2000/2.htm and www.ijf.hr/financijska_praksa/2004/3.htm.

³ Besides the costs of tax authorities, there are also costs born by taxpayers. They are further discussed in other publications of the Institute for Public Finance.

By the estimate of the Institute of Public Finance, the costs of tax authorities in Croatia in the period 1997-2001 averaged 0.6% of GDP. The share of these costs in tax revenues⁴, which was an indicator of the tax administration efficiency, was about 2.2%. What did this actually show? It showed that the authorities responsible for tax and customs revenue collection, i.e. Tax Administration and Customs Administration spent an extra 2.2 lipas per kuna of collected revenues.

The research also demonstrated that all major determinants of the costs of tax authorities (their total level, share in GDP and in Budget revenue) decreased during the last three observed years (1999-2001). The share of the costs of tax authorities in total Budget revenue, which was 1.6% on average, fell from 2% in 1997 to 1.5% in 2001.

(CA) with around 38% and Financial Police (FP) with around 11%.

The total number of employees in tax and customs authorities increased in the period 1999-2001. Employment in these authorities averaged 7,400 during the observed period. The largest number of employees in tax and customs authorities (7,700) was recorded in 2000. The largest department was the Tax Administration with an average number of 3,700 employees. The second largest was the Customs Administration (2,800 employees on average) while the smallest department, until its abolition, was the Financial Police with 660 employees.

We can conclude that there is no good tax or customs policy without efficient tax and customs administrations. The costs of tax authorities are directly influenced by professional skills, motivation, diligence and possible corruption of the Tax and Cu-

Table 2 Total costs of tax authorities (in million kuna and in %)

| | 1997. | % | 1998. | % | 1999. | % | 2000. | % | 2001. | % |
|---------------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| Tax Administration | 390,8 | 55,0 | 467,6 | 57,5 | 517,9 | 54,9 | 498,3 | 57,7 | 430,7 | 52,6 |
| Financial Police* | 77,7 | 11,1 | 92,6 | 11,4 | 120,8 | 12,8 | 88,8 | 10,3 | 79,9 | 9,8 |
| Administration | 240,8 | 33,9 | 253,6 | 31,1 | 304,3 | 32,3 | 276,8 | 32,0 | 308,2 | 37,6 |
| Total | 709,3 | 100,0 | 813,8 | 100,0 | 943,0 | 100,0 | 863,9 | 100,0 | 818,8 | 100,0 |

* For Financial Police, the costs covered by own funds throughout the observed period are not shown.

As shown in Table 2, the total absolute costs of tax authorities rose in the first part of the observed period and boomed during 1999. After that, they decreased over the three observed years from HRK 943 million in 1999 to HRK 820 million in 2001.

In the total costs of tax authorities, Tax Administration (TA) participated with the largest share, 51%. It was followed by Customs Administration

stoms Administrations. The assessment of these departments' efficiency should be based on the costs incurred by them in the course of revenue collection. The results obtained are significant (the costs account for 0.6% of GDP, 2.2% of tax revenues and 1.6% of total Budget revenues). However, in order to see how realistic these indicators are and whether they imply high or low values, a comparison should

Table 3 Number of employees in tax and customs authorities

| Number of employees | 1997. | % | 1998. | % | 1999. | % | 2000. | % | 2001. | % |
|---------------------|-------|-------|-------|-------|-------|-------|-------|-------|--------|-------|
| TA | 3.285 | 48,5 | 3.679 | 50,3 | 3.915 | 51,4 | 3.956 | 51,3 | 3.814 | 51,7 |
| FP | 820 | 12,1 | 846 | 11,5 | 873 | 11,0 | 872 | 11,3 | 700* | 9,5 |
| CA | 2 670 | 39,4 | 2 795 | 38,2 | 2 861 | 37,6 | 2 885 | 37,4 | 2859 | 38,8 |
| Total | 6.775 | 100,0 | 7.320 | 100,0 | 7.613 | 100,0 | 7.713 | 100,0 | 7.373* | 100,0 |

* As the data on the number of employees in FP during 2001 did not exist, we used the data from Vjesnik of 25 May 2001.

⁴ Excluding social security contributions

be made with the research results in similar countries, which is currently impossible.

It needs emphasising that in the last three observed years all major determinants of the costs of tax authorities (the share in GDP and the shares in Budget and tax revenues) decreased. These trends are favourable, but both Tax and Customs Administrations should continue to re-duce their costs and increase efficiency in the next period. In order to increase their efficiency, the Tax and Customs Administrations must do the following:

- Improve communication with tax and customs payers;
- Establish special departments for developing closer relationships with taxpayers (particularly big taxpayers);
- Increase the level of staff specialisation;
- Provide incentives for employees by offering them performance-related pay, further education and professional advancement opportunities; avoid employment discrimination.