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Efficiency of Croatian Tax Authorities

Croatian tax authorities are becoming more successful and efficient in collecting tax: in the period 1997–2006 they spent increasingly less money per kuna of collected revenues. The ever better indicators are even more evident if we analyse the periods 1997–2001 and 2002–2006 separately: in the first period 2.18 and in the second 1.90 lipa per kuna of collected tax revenues were spent on average.¹

Due to increasing financial needs and less funds flowing into the state treasury, tax authorities have to be disciplined and as efficient as possible in implementing tax and customs laws and regulations. Naturally, tax authorities have to continue doing their job ethically and transparently in conformity with the rules of profession and good business practice, but their more intensive work will certainly have to be noticed in stricter tax controls, too, and consequently, in better tax collection. While doing so it is important how much tax authorities really cost us – the taxpayers, i.e. how efficient they are in tax collection. What is meant by greater or higher efficiency is as high amount of collected tax revenues as possible at the lowest possible cost. The costs of tax collection are known as *costs of tax authorities* or *administrative costs of taxation and customs clearance*.

The administrative costs of taxation (the costs of tax authorities) are public sector costs which emerge when implementing current taxation laws including the proposals for their change (Sandford, Godwin and Hardwick, 1989). The compliance costs of taxation are all the costs made by the taxpayers while meeting the requirements of tax legislation and tax authorities together with the amount of actually paid tax as well as all other costs caused by the economic distortions resulting from the very nature of tax (Sandford, 1995:1). The sum of the administrative and compliance costs of taxation make total taxation costs. This paper analyses the administrative costs of taxation only.

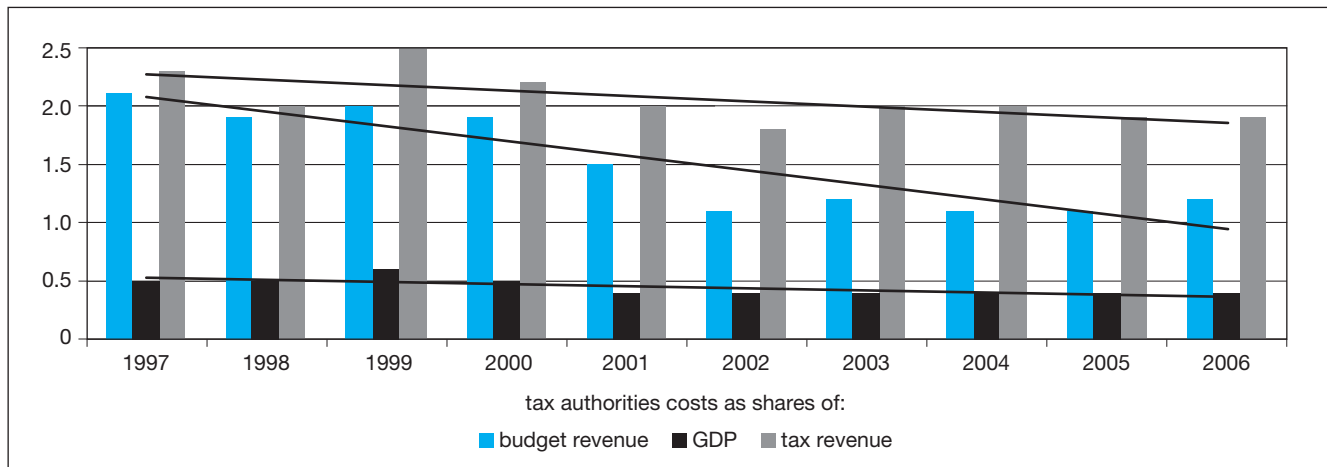
The Tax and Customs Administration as well as the Financial Police are responsible for collection of all tax and customs duties in Croatia. The Tax and Customs Administration are financed from the State Budget and, to a smaller extent, from the authorities' own sources, whereas the Financial Police is financed only from the State Budget ever since 2006 when it was re-established after it had been abolished in 2001. Graph 1 shows the efficiency of the above authorities in public revenue collection.

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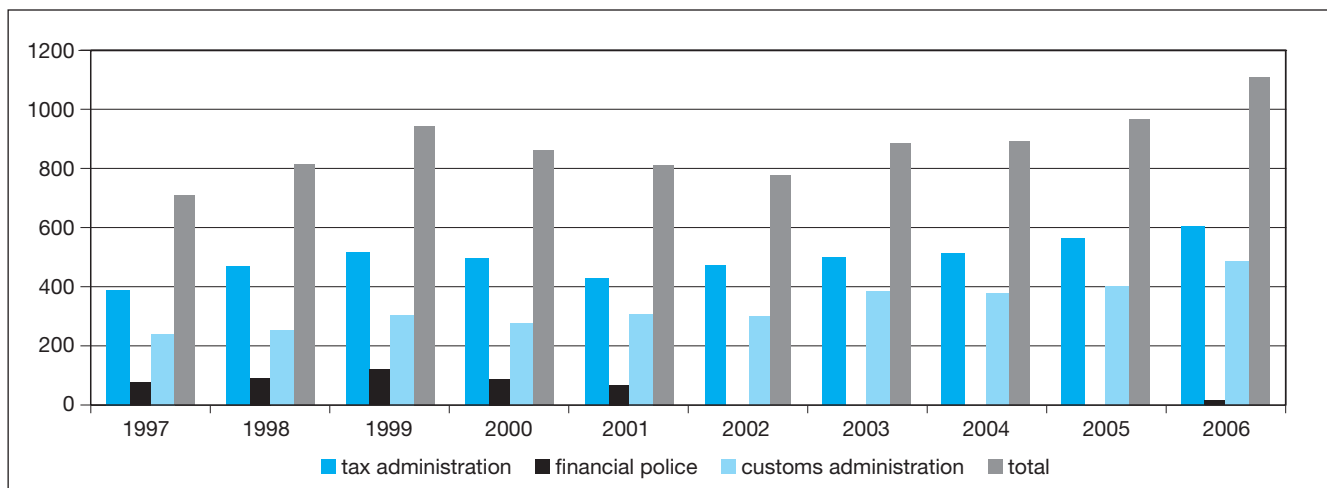
¹ For more on efficiency in the first period see Bratić (2005). But in the meantime, the classification and scope of the State Budget had been changed, as well as the structure and scope of GDP, which to some degree affected the analysed shares (of tax authorities' costs in total Budget revenue and GDP). To be specific, since 1 January 2001 State Budget revenue included welfare (social) contributions, i.e. revenues of the Croatian Pension Insurance Institute, and since 1 January 2002 it included both revenues of the Croatian Institute for Health Insurance and the Croatian Employment Institute, whereas the Child Benefit Fund ceased existing. Similarly, GDP was revised due to the adjustment to the European System of Accounts (ESA 95) but mostly due to the inclusion of underground economy (more at www.dzs.hr). We tried to adjust the calculation methodology to the whole period and use the latest adjusted data.

The Institute of Public Finance deals with economic research and analysis related to various forms of public finances such as the budget, taxation and customs duties. Its orientation is thus to the various economic, legal and institutional topics that are important for the sound long-term economic development of the Republic of Croatia. So that the public should be able to have a better insight into certain issues, the Institute of Public Finance is launching its Newsletter, in which it will from time to time publish informed and independent analysis of economic questions. The views expressed in the articles published in the Newsletter will reflect the opinions of the authors, which do not necessarily coincide with those of the Institute as institution. Full text of Newsletter is also available on Institute's Web site: <http://www.ijf.hr/newsletter>.

Graph 1 Indicators of tax authorities' efficiency, 1997–2006 (%)



Graph 2 Total costs of the tax authorities, 1997–2006 (in million HRK)



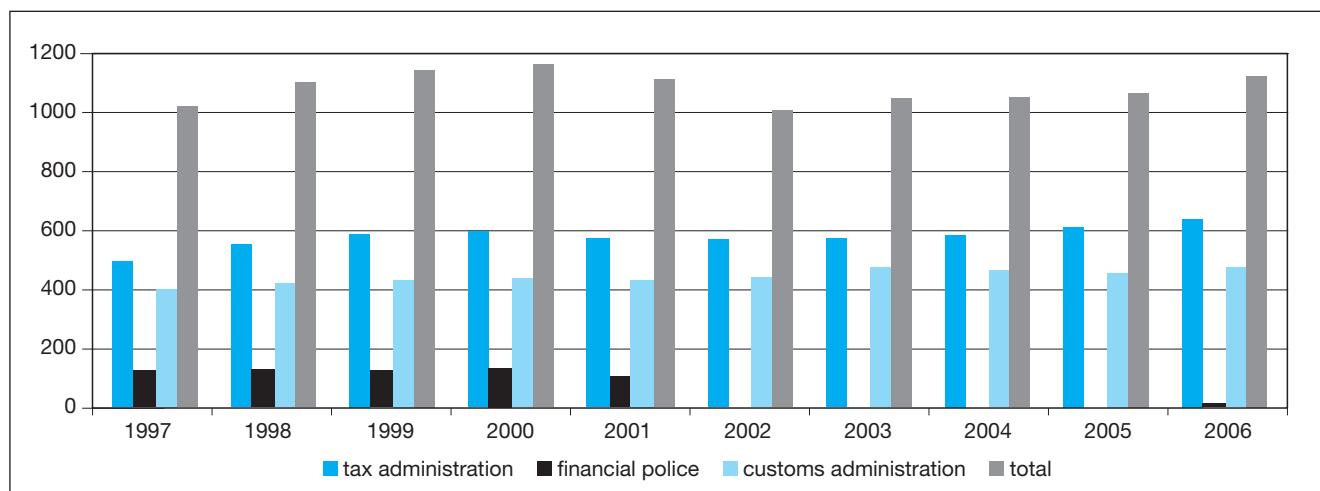
In the period 1997–2006 the costs of tax authorities as shares of all observed categories – GDP, budget and tax revenue – decreased. Higher efficiency of Croatian tax authorities in collecting public revenue is supported by the downward trend on graph 1, but caution is needed before drawing any valid conclusions. In other words, the trend could have been affected by many factors. For example, total State Budget revenue was affected by the inclusion of contributions in the Budget since 2002 and improved privatization revenues during some years, whereas the tax revenue could have been affected by the growth of industrial production and increase in corporate revenue especially in the period after 2001. The trends shown in Graphs 2 and 3, which evidently show

both, growth in total nominal costs of tax authorities and the increase in the number of their employees, call for utmost caution when drawing conclusions.

Total costs of the tax authorities grew continually and decreased only in the period 2000–2002. In the total costs, the Tax Administration participated with the largest share and the Customs Administration the lowest.² Over the last few years the costs of the Customs Administration grew stronger. We assume that what we have here is increased investment due to the adjustment to the requirements of the European Union. Graph 3 shows whether the total number of employees in the tax authorities was, to some extent, behind the growth in total costs.

² Unfortunately, we do not have the data on costs financed from the own funds of the Customs Administration and the Financial Police prior to 2001, therefore we have no information on their actual total costs. We managed to obtain the data on the total costs of the Customs Administration (own funds and revenues from the State Budget) in the period 2002–2006, but since 2006 the Financial Police is financed only from the State Budget and does not have any own funds as in the past. Actual Tax Administration costs are shown during the whole period, that is, including the costs financed from the State Budget and from its own funds.

Graph 3 Number of employees in the tax and customs authorities, 1997–2006 (in million HRK)



The total number of employees increased about 10% in the period observed. The increase in the total number of employees would have been even larger if the Financial Police had not been abolished in 2001 when the total number of employees was decreased significantly, but by 2006 the number of employees grew again and reached the similar level as in the year before its abolishment. Although the Customs Administration had the biggest increase in costs over the last years, the graph shows that the increase was not caused by the number of employees, for in the period 1997–2001 the Customs Administration had smaller increase in the number of employees than, for example, the Tax Administration.

It can be assumed that the increase in the total costs of tax authorities was to some degree affected by the total number of employees. However, when observing the last years in the two analysed periods (2001 and 2006), the question why the tax authorities had almost the same number of employees during those years but the total costs increased 300 million HRK remains open. In order to answer this and other questions on the work performed by the Croatian tax authorities, which is exactly what could and should be the subject of future research, a more detailed analysis of their work and expenditure structure is required. In the meantime, tax authorities will have to continue insisting on as efficient revenue collection as possible, but also on further total costs reduction, especially in times of growing financial needs and employment restrictions in the public sector. Since the total costs of tax authorities are directly influenced by high quality infrastructure and professional skills, motivation, diligence and possible corruption of their employees, further investment in the infrastructure, specialist training and providing incentives for employees is imperative, as it can be assumed that, among other things, the above mentioned factors influ-

enced the established ever higher average efficiency of Croatian tax and customs authorities.

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Table 1 Indicators of tax authorities' efficiency, 1997–2006

	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	Average
A– Total State Budget revenues (million HRK)	33,846	43,808	46,357	44,636	53,504	69,651	74,677	80,464	85,653	95,236	
B– GDP, in current prices (million HRK)	145,394	160,603	164,054	176,690	190,796	208,223	227,012	245,550	264,367	286,341	
C– Tax revenues of State Budget (million HRK)	31,338	40,327	38,318	39,939	39,999	42,810	45,281	47,150	50,688	58,469	
D – Total costs of tax authorities (million HRK)*	709	814	943	864	809	777	888	890	966	1.106	
Costs of tax authorities as a share of:											
– State Budget revenues (D/A)	2.1	1.9	2.0	1.9	1.5	1.1	1.2	1.1	1.1	1.2	1.49
– GDP (D/B)	0.5	0.5	0.6	0.5	0.4	0.4	0.4	0.4	0.4	0.4	0.45
– Tax revenues (D/C)	2.3	2.0	2.5	2.2	2.0	1.8	2.0	2.0	1.9	1.9	2.04

* Internal data of the Central Tax and Customs Administration.

Table 2 Total costs of tax authorities, 1997–2006, in million HRK and %

in million HRK	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	Average*
Tax Administration	390,8	467,6	517,9	498,3	430,7	474,6	502,8	512,5	565,1	605,0	496,5
Financial Police	77,7	92,6	120,8	88,8	70,1	–	–	–	–	15,7	77,6
Customs Administration	240,8	253,6	304,3	276,8	308,2	302,2	384,7	377,7	400,8	485,4	333,5
Total	709,3	813,8	943,0	863,9	809,0	776,8	887,5	890,2	965,9	1.106,1	–
in %											
Tax Administration	55,0	57,5	54,9	57,7	53,2	61,1	56,7	57,6	58,5	54,7	56,7
Financial Police	11,1	11,4	12,8	10,3	8,7	–	–	–	–	1,4	9,3
Customs Administration	33,9	31,1	32,3	32,0	38,1	38,9	43,3	42,4	41,5	43,9	37,7
Total	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0	–

*Average indicators for the Financial Police were calculated based on six years of its activity, whereas for the Tax and Customs Administration for the whole analysed period.

Source: Ministry of Finance (2001, 2002, 2004, 2005 and 2006), Central Bureau of Statistics; internal data of the Tax and Customs Administration's Central office; author's calculation.

Table 3 Number of employees in the tax and customs authorities, 1997–2006

	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	Average*
Tax Administration	3285	3679	3915	3956	3814	3781	3799	3896	4064	4242	3843
Financial Police	820	846	837	872	approx. 700**	–	–	–	–	88	577
Customs Administration	2670	2795	2861	2912	2882	2919	3162	3090	3028	3151	2947
Total	6775	7320	7613	7740	7396*	6700	6961	6986	7092	7481	–
in %											
Tax Administration	48.5	50.3	51.4	51.1	51.6	56.4	54.6	55.8	57.3	56.7	53.4
Financial Police	12.1	11.5	11.0	11.3	9.4	0.0	0.0	0.0	0.0	1.2	9.4
Customs Administration	39.4	38.2	37.6	37.6	39.0	43.6	45.4	44.2	42.7	42.1	41.0
Total	100.0	100.0	100.0	100.0	100.0	86.6	100.0	100.0	100.0	100.0	–

* Average indicators for the Financial Police were calculated based on six years of its activity, whereas for the Tax and Customs Administration for the whole analysed period.

** Kapetanić, 2001.

Source: internal data of the Tax and Customs Administration's Central office; author's calculation.

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