



Dialogue on
SME Development in South Asia
How Conducive are the Tax Policies?

Tax Policy and Enterprise Development in South Asia
Regional Meta Analysis

Organised by
Centre for Policy Dialogue (CPD)
in collaboration with
Governance Institutes Network International (GINI)

Dhaka: 23 April 2015



BUDGET 2012-13

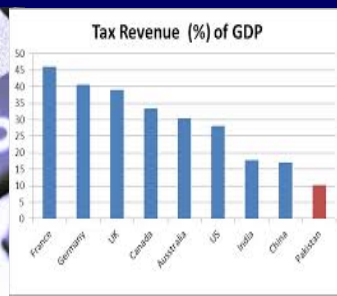
TAX LIABILITY

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Sl. No.	When the taxable income exceeds	Rate of tax
1.	Where the taxable income does not exceed Rs. 400,000	0%
2.	Where the taxable income exceeds Rs. 400,000 but does not exceed Rs. 1,500,000	10% of the amount exceeding Rs. 400,000
3.	Where the taxable income exceeds Rs. 1,500,000 but does not exceed Rs. 2,500,000	Rs. 25,000 + 10% of the amount exceeding Rs. 1,500,000
4.	Where the taxable income exceeds Rs. 2,500,000 but does not exceed Rs. 5,000,000	Rs. 147,500 + 20% of the amount exceeding Rs. 2,500,000
5.	Where the taxable income exceeds Rs. 5,000,000	Rs. 347,500 + 25% of the amount exceeding Rs. 5,000,000

New shades of income tax for salaried class

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2.	Where the taxable income exceeds Rs. 400,000 but does not exceed Rs. 1,500,000	10% of the amount exceeding Rs. 400,000
3.	Where the taxable income exceeds Rs. 1,500,000 but does not exceed Rs. 2,500,000	Rs. 17,500 + 10% of the amount exceeding Rs. 1,500,000
4.	Where the taxable income exceeds Rs. 2,500,000 but does not exceed Rs. 5,000,000	Rs. 87,500 + 10% of the amount exceeding Rs. 2,500,000
5.	Where the taxable income exceeds Rs. 5,000,000	Rs. 347,500 + 25% of the amount exceeding Rs. 5,000,000



Research Objectives

To advance technical knowledge on the relationship between tax policies, development of small enterprises, and inclusive growth in South Asia through collaborative time-bound research in South Asia.

Specific Objectives:

- To develop country study reports that focus on the impacts of tax exemptions and concessions, value-added-tax (VAT) reforms, and property tax (respectively) on the development of small enterprises in South Asia, with particular emphasis on those operating outside the tax net in the undocumented economy, as well as those owned/managed by women.
- To organize a Policy Engagement Workshop in each South Asian country to disseminate the findings of the research and advocate for policy recommendations emanating from this research among key government officials responsible for formulating and implementing policies on taxation and enterprise development.

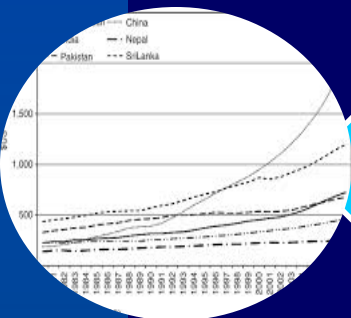
Framework for Meta Analysis



Meta Analysis Overview



Tax Revenue, Political Will and Tax Reforms - Regional Comparison



Key Regional Survey Findings -Theme 1, 2 and 3



Conclusion and Policy Recommendations

Meta Analysis Overview

■ Aim:

Meta-analysis is aimed at highlighting the similarities, differences, learning outcomes, and cross-cutting recommendations at the regional level.

■ Data Collection:

- Literature Review for independent variables and historical and current tax governance systems
- Purposive Survey of around 1000 SMEs in South Asia
- Focus Group Discussions with SMEs owners/managers, tax administration, civil society etc.
- Key Informant Interviews with tax officials and tax service providers
- Case Studies with women entrepreneurs

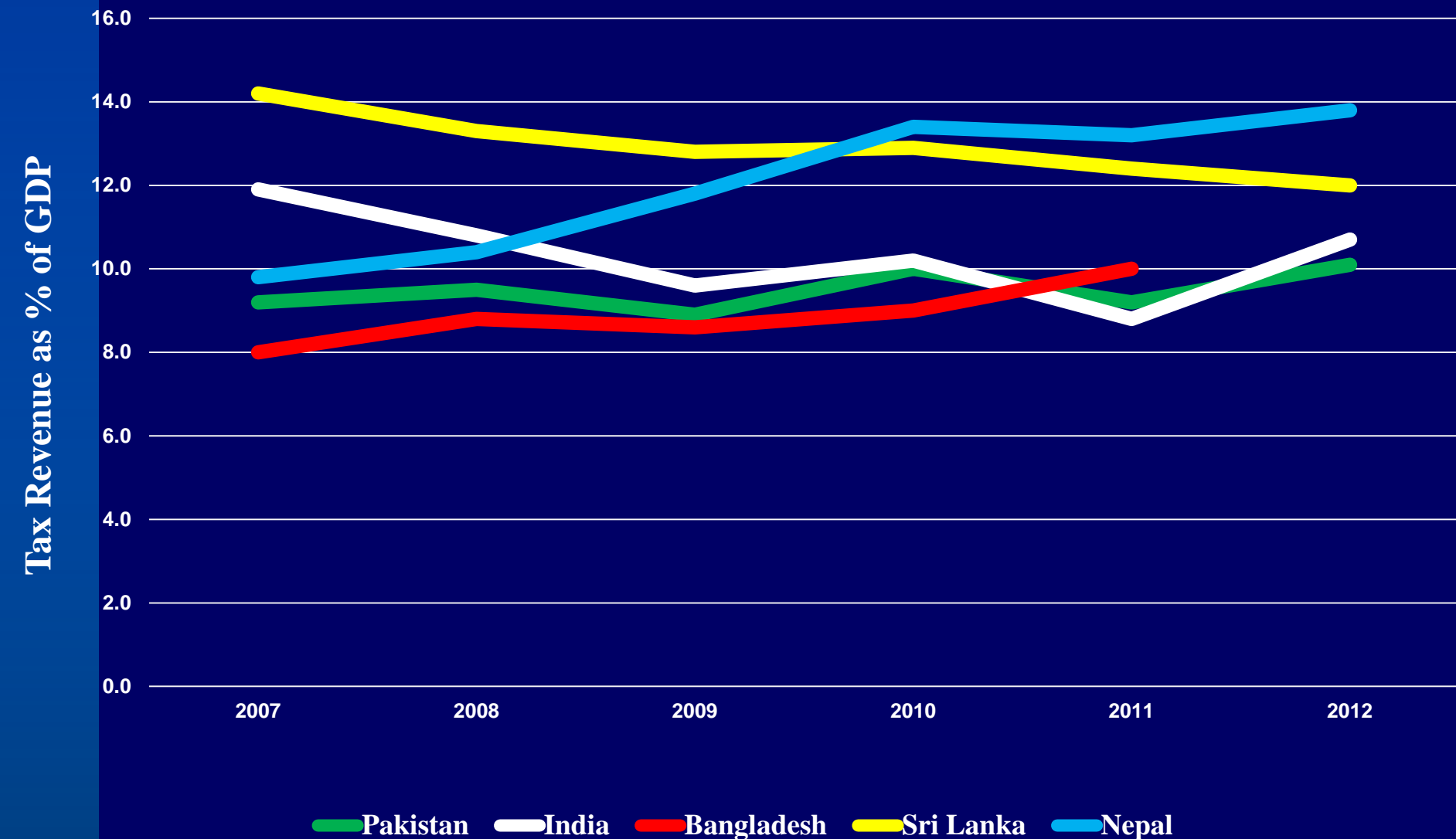
■ Data Analysis:

- Regional Descriptive Statistics
- Triangulation to:
 - Draw learning outcomes
 - Propose cross cutting recommendations





South Asian Tax to GDP Ratio Comparison : FY 2007-2012



Political Parties' Election Manifesto on Tax Reforms – Regional Comparison

● India – Ruling Alliance/Party

- Provide a non adversarial and conducive tax environment.
- Rationalize and simplify the tax regime.
- Overhaul the dispute resolution mechanisms.
- Bring on board all State governments in adopting GST, addressing all their concerns.
- Provide tax incentives for investments in research and development, geared towards indigenization of technology and innovation.
- BJP is committed to protecting the interest of small and medium retailers, SMEs and those employed by them. The FIPBs (Foreign Investment Promotion Board) functioning shall be made more efficient and investor- friendly



Pakistan – Ruling Alliance/Party

- **Decreasing tax rates.**
- **Improve the process of self-assessment and audit compliance.**
- **All exports will be sales tax free.**
- **Through reforms in FBR and the tax system, we will target to improve the tax to GDP ratio to 15% by 2018.**
- **Informal economy will be brought into tax net through improved documentation process and rationalize the tax base to broaden the tax system.**
- **Reduce Tax evasion by facilitating tax payers' compliance, and where possible, rationalizing tax rates**
- **Provincial governments will be asked to increase their own tax revenues to increase their contribution in overall taxation.**
- **Sales tax to be rationalized by ensuring standard rate for all items and broadening the scope of sales tax. Simplify the administration of taxes and compliance especially for small businesses**
- **No increase in the tax rates. Once the tax system becomes fully operational, tax rates will be reduced over a period of time to ensure regional equity and to encourage foreign investment.**
- **Improve the process of self-assessment and audit compliance.**



Nepal – Ruling Alliance/Party

- **The tax collection system will be expanded and will be made more simple, efficient and transparent.**
- **The system of VAT will be free from duality, bureaucratic and administrative hassles.**
- **The government will effectively control unnecessary and unproductive public expenditures.**

Sri Lanka – Ruling Alliance/Party

- **A reform to the tax system to facilitate capital accumulation, investment, entrepreneurship, employment, growth and international competitiveness.**
- **The promulgation of strong anti-Trust legislation to prevent monopolies in the private or public sectors and the strengthening of a Monopolies commission dedicated to ensuring competitive conditions with regard to all goods and services for the benefit of the public.**

VAT Rates Comparison- South Asia

VAT Rates in South Asian Countries

Pakistan	Bangladesh	Sri Lanka	India	Nepal
GST 17%	VAT 15%	VAT 12%	VAT 12.5%	VAT 13%

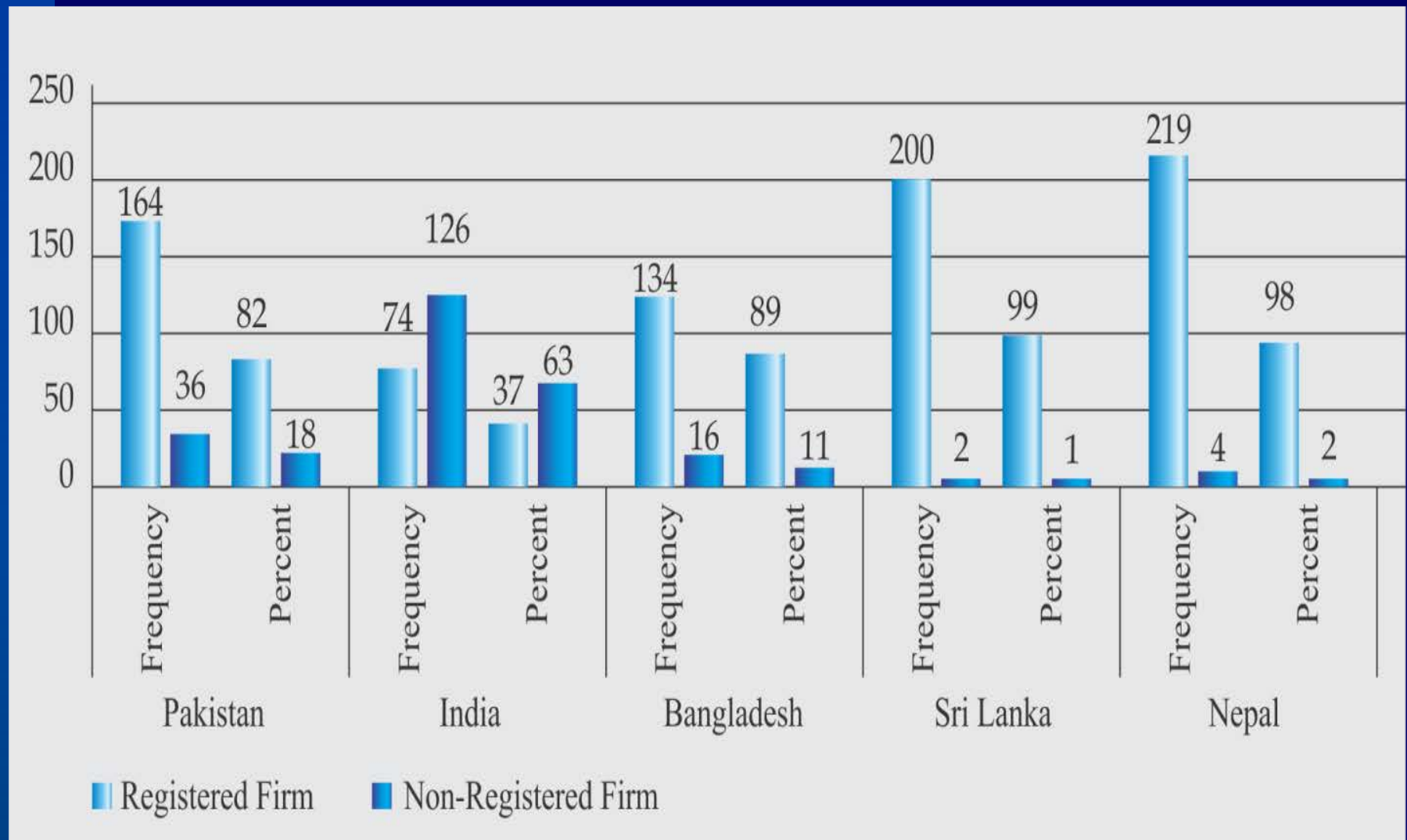
Key Regional Survey Findings: Theme 1, 2 and 3

Owners/Managers Characteristics

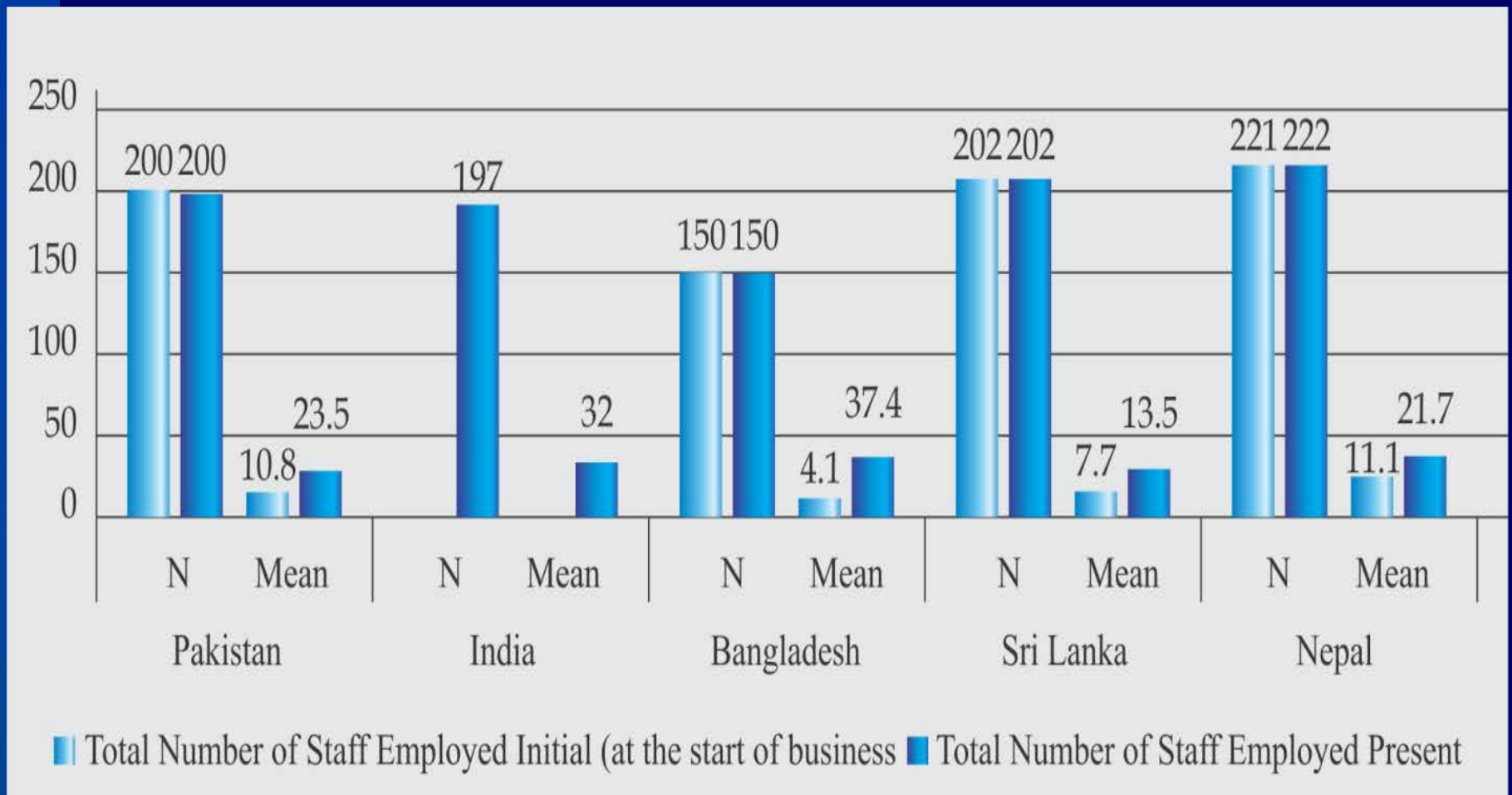
- **Ownership Pattern:** The owner ownership pattern of majority of sample SMEs across targeted countries is sole proprietorship. Second most common is limited company except in Bangladesh where partnerships have larger chunk than limited company.
- **Age:** most of the owners/managers fall in the middle age group i.e. above 45 years in Pakistan, India and Nepal. However, in Bangladesh and Sri Lanka this trend is 36-45 years of age.
- **Experience:** Most of the firms owners/managers reported their experience less than 10 years across the region except India where majority of sample entrepreneurs have 11-20 years of experience
- **Education:** Majority of sample entrepreneurs had acquired secondary education however, in India 50% of the sample respondents were graduates

Firm Characteristics

Registration of Firm with Legal Authority



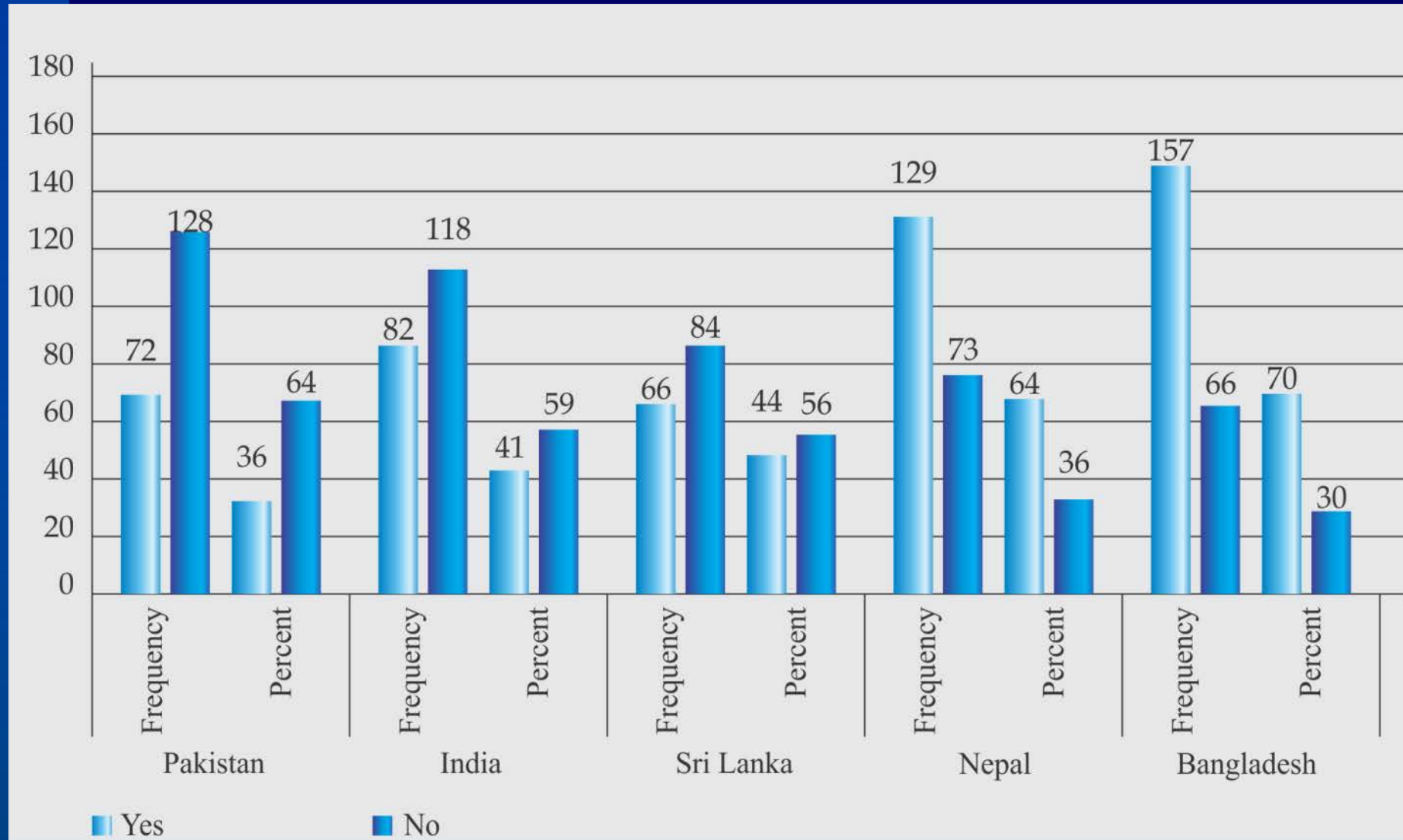
Total Number of Staff Employed



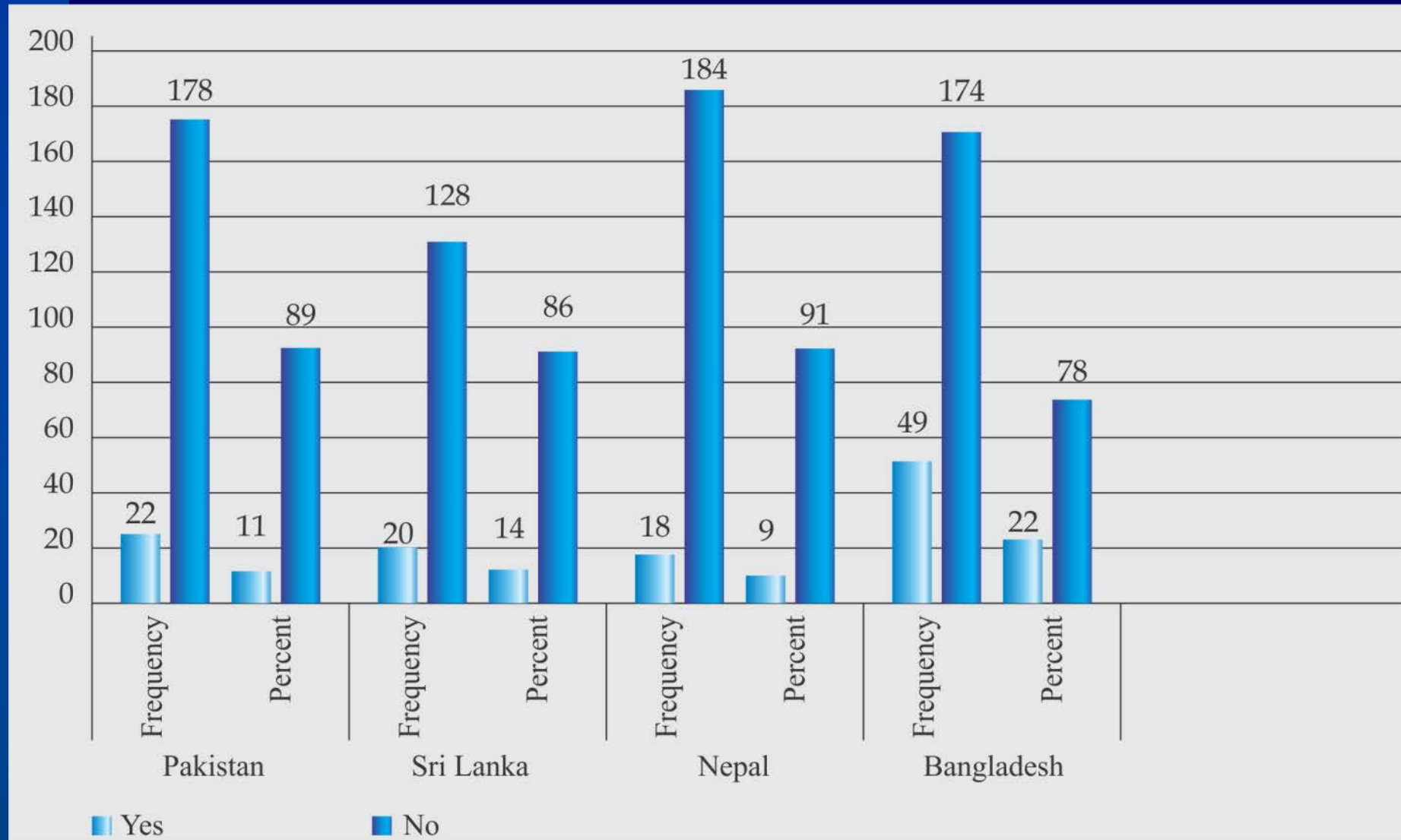
*N = Number of Respondents

Access to Credit

Loans Taken During Last 5 years



Application for Loan in Last Fiscal Year

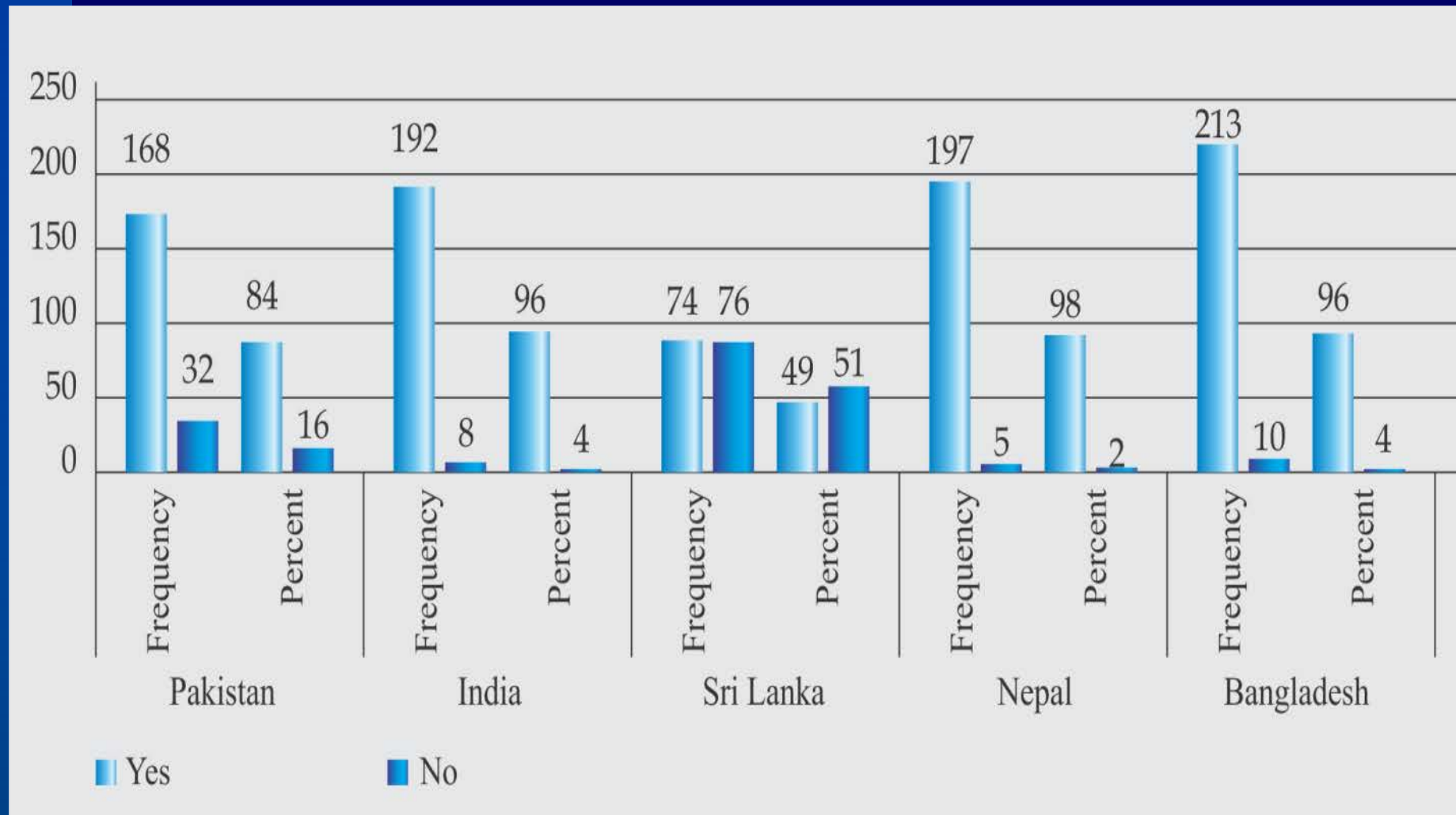


Main Reasons for not Applying for Loan?

	Pakistan		India		Sri Lanka		Nepal		Bangladesh	
	Frequency	Percent	Frequency	Percent	Frequency	Percent	Frequency	Percent	Frequency	Percent
No need for a loan - enterprise had sufficient capital	150	135	80	134	50	111	164	173	82	47
Application procedures were complex	12	11	9	15	28	62	18	19	64	37
Interest rates were not favorable	40	36	26	44	7	16	3	3	25	15
Collateral requirements were too high	9	8	3	5	2	4	3	3	39	23
Size of loan and maturity were insufficient	7	6	1	2			2	2	29	17
Did not think it would be approved	4	4			3	7			22	13

General Tax Behavior

Tax Compliance- Do You pay Taxes?



Tax Multiplicity: Too many Types of Taxes

	Pakistan		Sri Lanka		Nepal		Bangladesh	
	Frequency	Percent	Frequency	Percent	Frequency	Percent	Frequency	Percent
Strongly Agree	83	49	57	38	21	11	102	46
Agree	81	48	87	58	128	63	72	32
Disagree	3	2	3	2	32	16	31	14
Strongly Disagree	1	1	1	1	5	2	4	2
Neither Agree nor Disagree			1	1	16	8	13	6

Tax Laws and Procedures are too Complicated

	Pakistan		India		Sri Lanka		Nepal		Bangladesh	
	Frequency	Percent	Frequency	Percent	Frequency	Percent	Frequency	Percent	Frequency	Percent
Strongly Agree	79	47	82	41	48	32	18	9	110	50
Agree	79	47	85	42	96	64	106	52	73	33
Disagree	9	5	17	9	4	3	52	26	22	10
Strongly Disagree	1	1	4	2		0	4	2	4	2
Neither Agree nor Disagree			12	6	2	1	22	11	13	6

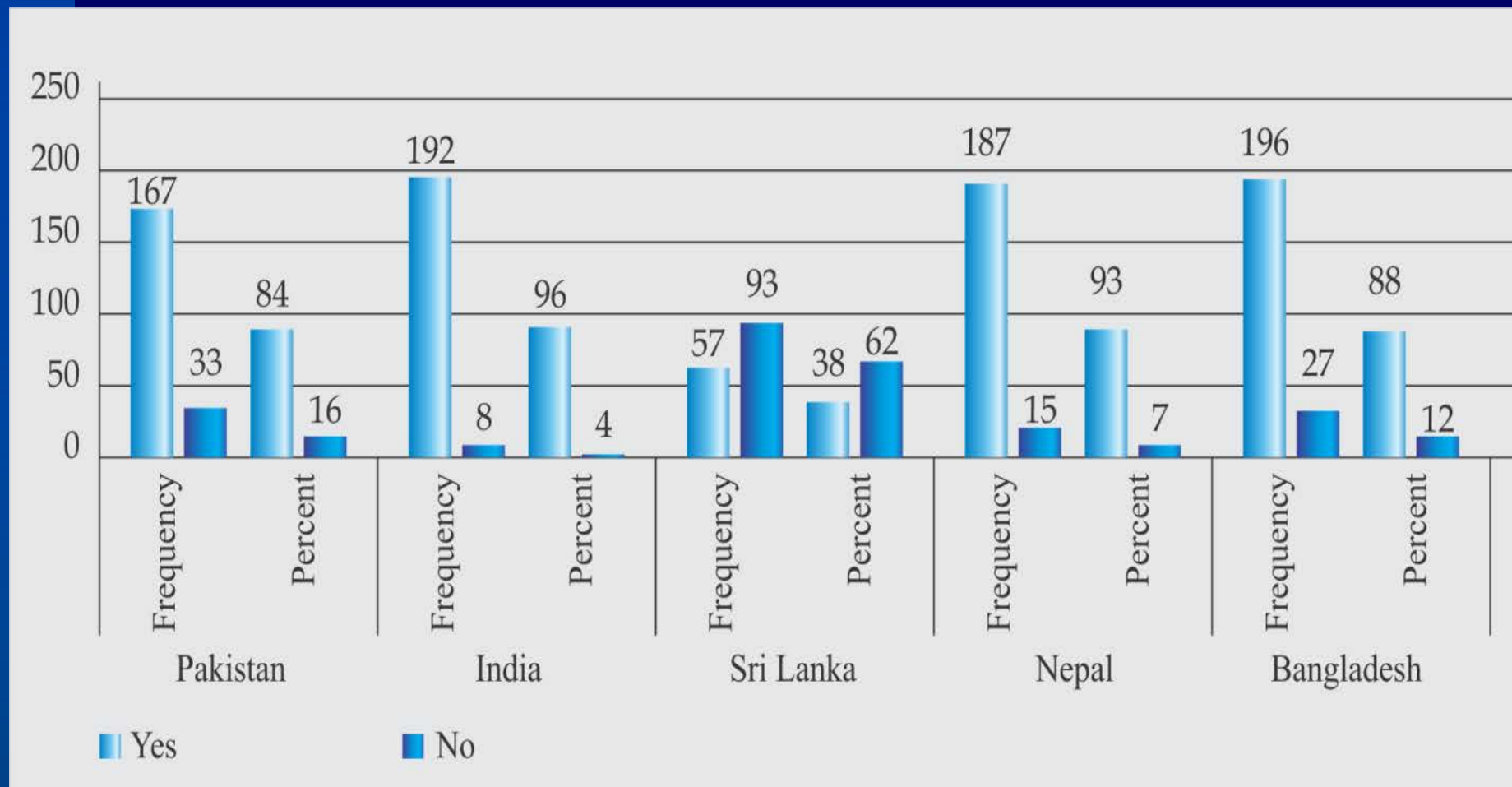
Competent Tax Officials and Convenient Location of Tax Office

	Pakistan		India		Sri Lanka		Nepal		Bangladesh	
	Frequency	Percent	Frequency	Percent	Frequency	Percent	Frequency	Percent	Frequency	Percent
Strongly Agree	12	7	9	4	6	4	11	5	39	18
Agree	28	17	104	52	85	57	127	63	99	44
Disagree	69	41			2	1	34	17	51	23
Strongly Disagree	54	32	58	29		0	10	5	12	5
Neither Agree nor Disagree	5	3	29	15	57	38	20	10	22	10

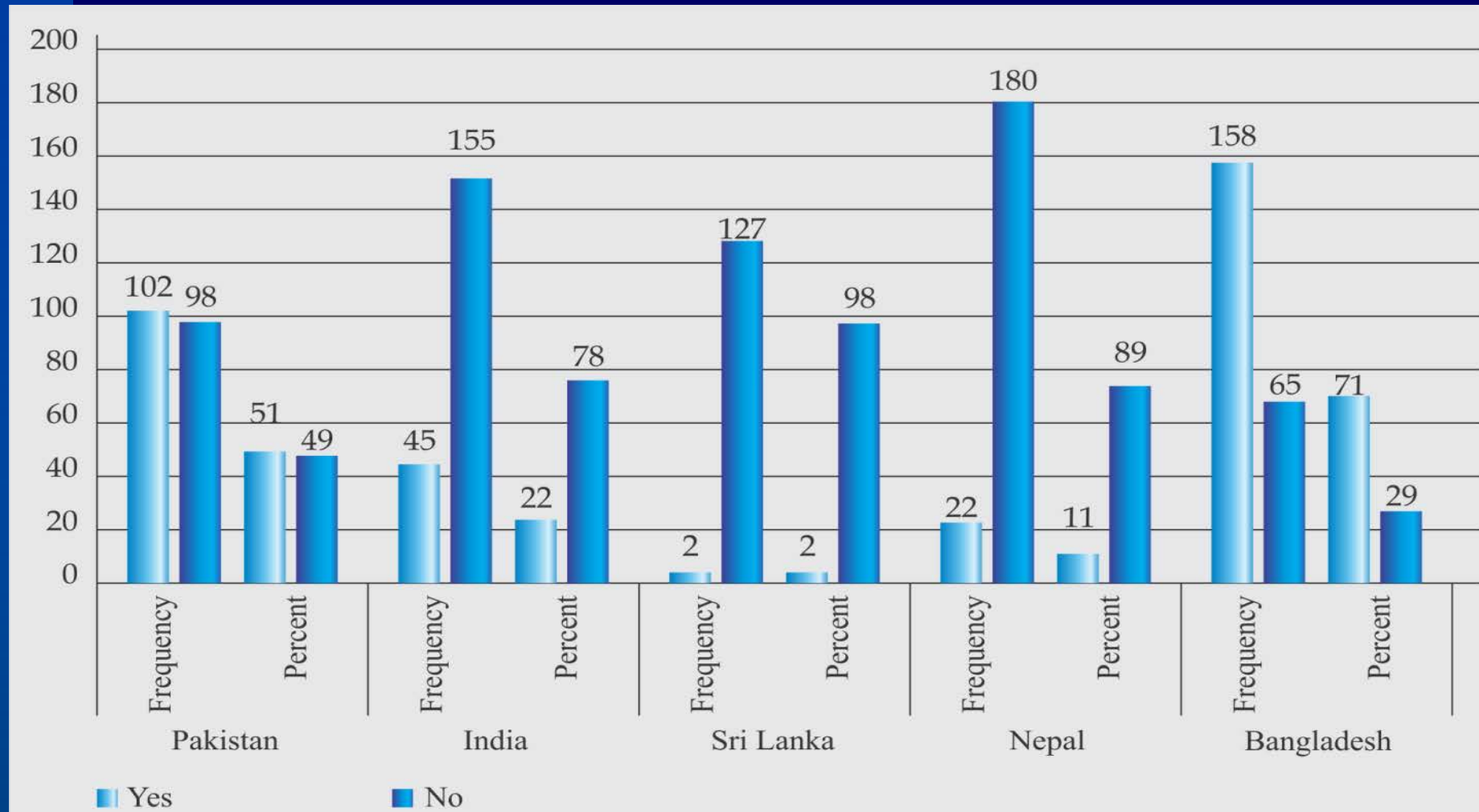
Fairness and Respectfulness of Tax Staff

	Pakistan		India		Sri Lanka		Nepal		Bangladesh	
	Frequency	Percent	Frequency	Percent	Frequency	Percent	Frequency	Percent	Frequency	Percent
Strongly Agree	12	7					15	7	17	8
Agree	19	11	85	43	37	24	107	53	16	34
Disagree	75	45	115	57	1	1	50	25	90	40
Strongly Disagree	57	34				0	7	4	16	7
Neither Agree nor Disagree	5	3			112	75	23	11	24	11

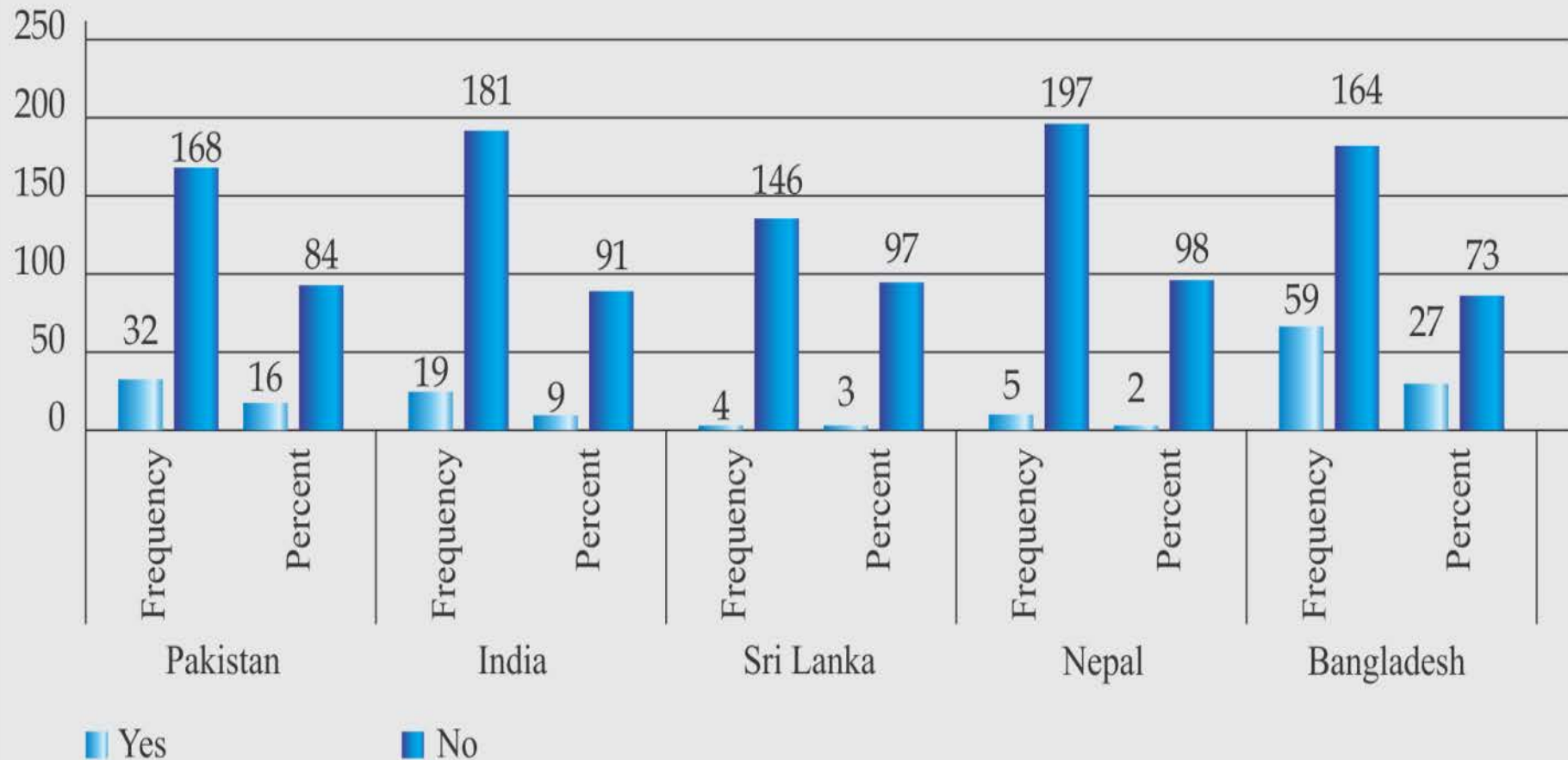
Registered with any Tax Authority



Not Interested in Tax Benefits to Avoid Hassles Associated with Compliance Requirements



Impact of Exemptions and Concessions: Receiving Tax Exemptions



Firm Sales, Productivity and Competitiveness

Increase in Sales								
	Pakistan		India		Nepal		Bangladesh	
	Frequency	Percent	Frequency	Percent	Frequency	Percent	Frequency	Percent
High	13	41	3	16	2	40	27	48
Medium	8	25	11	58	2	40	19	34
Low	6	18	3	16	1	20	8	14
No effect	5	16	2	11			1	2
Don't know							1	2
Total SMEs	32		19		5		61	
Increase in Productivity								
High	9	28	2	11	2	40	29	52
Medium	14	44	12	63	2	40	18	32
Low	5	16	1	5	1	20	6	11
No effect	4	12	4	21			2	4
Don't know							1	2
Total SMEs	32		19		5			
Increase in Competitiveness								
High	5	16	1	5	1	20	27	48
Medium	12	37	8	42	2	40	24	43
Low	5	16	1	5	1	20	4	7
No effect	10	31	9	48	1	20	1	2
Total SMEs	32		19		5			

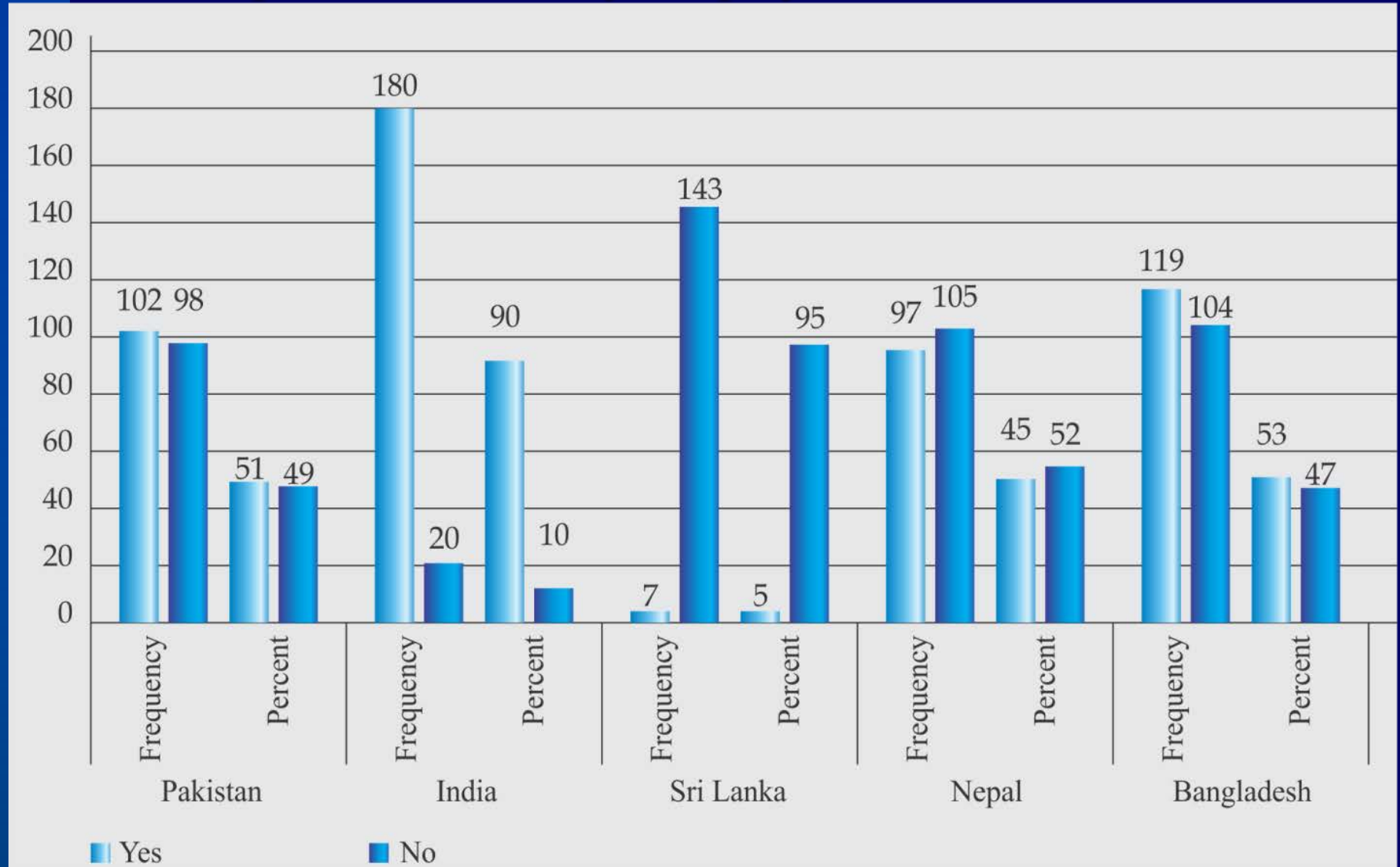
* The four Sri Lankan respondents who get exemptions did not provided any further information

Tax Related Govt. Assistances Needed for Business Expansion: What they want?

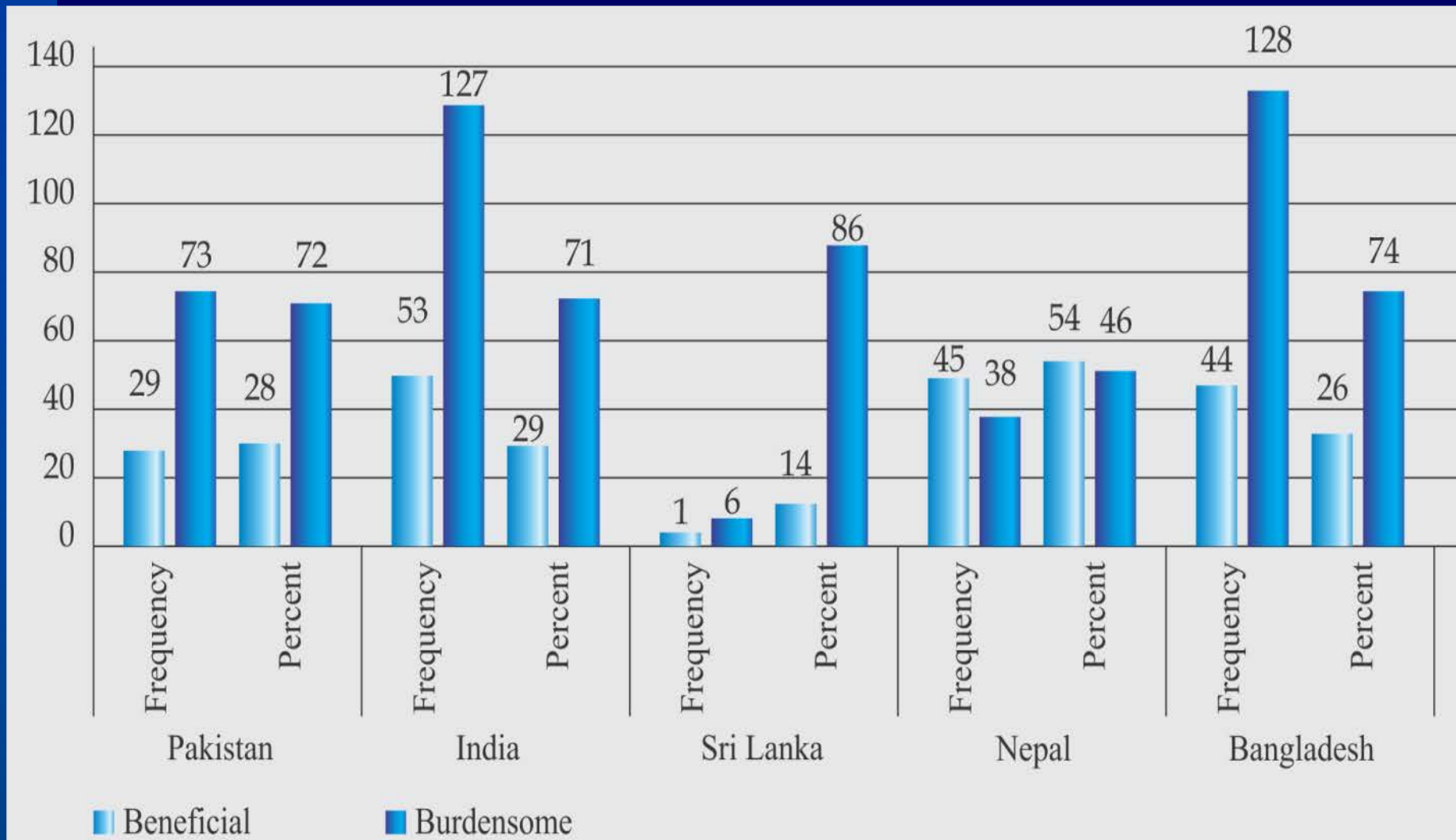
	Pakistan		India		Sri Lanka		Nepal		Bangladesh	
	Frequency	Percent	Frequency	Percent	Frequency	Percent	Frequency	Percent	Frequency	Percent
Reducing tax rates.	145	64	171	87	144	56	142	70	117	53
Granting tax exemptions	105	44	79	40	127	49	25	12	74	33
Granting tax holidays.	106	45	88	45	125	48	106	53	84	38
Strengthen the services of tax authorities towards SMEs.	119	50	21	11	121	47	73	36	67	30

Impact of Value Added Tax

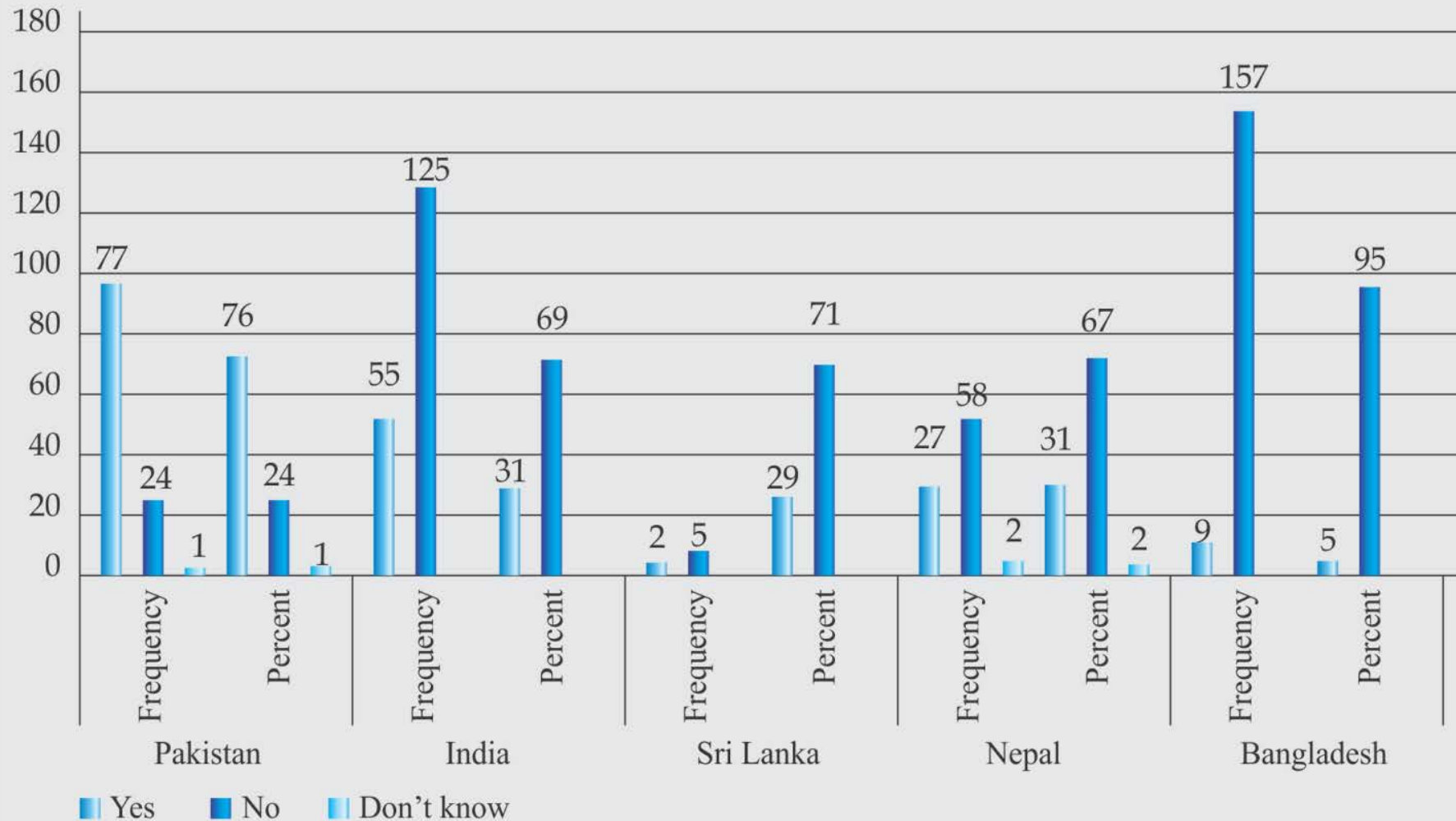
VAT Compliance – Do you pay VAT?



Is VAT Compliance Beneficial or Burdensome for Business Development?



Has this Enterprise faced Difficulties in Obtaining VAT Refunds?



Reasons behind SMEs/MSMEs not being VAT Compliant?

	Pakistan		Sri Lanka		Nepal		Bangladesh	
	Frequency	Percent	Frequency	Percent	Frequency	Percent	Frequency	Percent
Lack of Awareness	105	48	21	23	93	55	78	45
No Benefits	138	63	129	132	77	46	51	30
Procedural Complexity	88	40	20	20	91	54	130	75
Problematic Behavior of VAT Administration	42	19	11	11	24	14	12	7
Possibility of Future Harassment	65	30	14	14	52	31	33	19
Others	1	0	1	1	1	1	10	6

Perception about VAT Administration

Perception towards performance of VAT officials is:

	Pakistan		India		Sri Lanka		Nepal		Bangladesh	
	Frequency	Percent	Frequency	Percent	Frequency	Percent	Frequency	Percent	Frequency	Percent
Very Low	39	20	5	3	1	1	8	8	5	2
Low	110	55	49	25	4	3	51	53	33	15
Indifferent	24	12	85	43	125	95	29	30	108	48
High	27	13	55	28	1	1	9	9	68	31
Very High			2	1					9	4

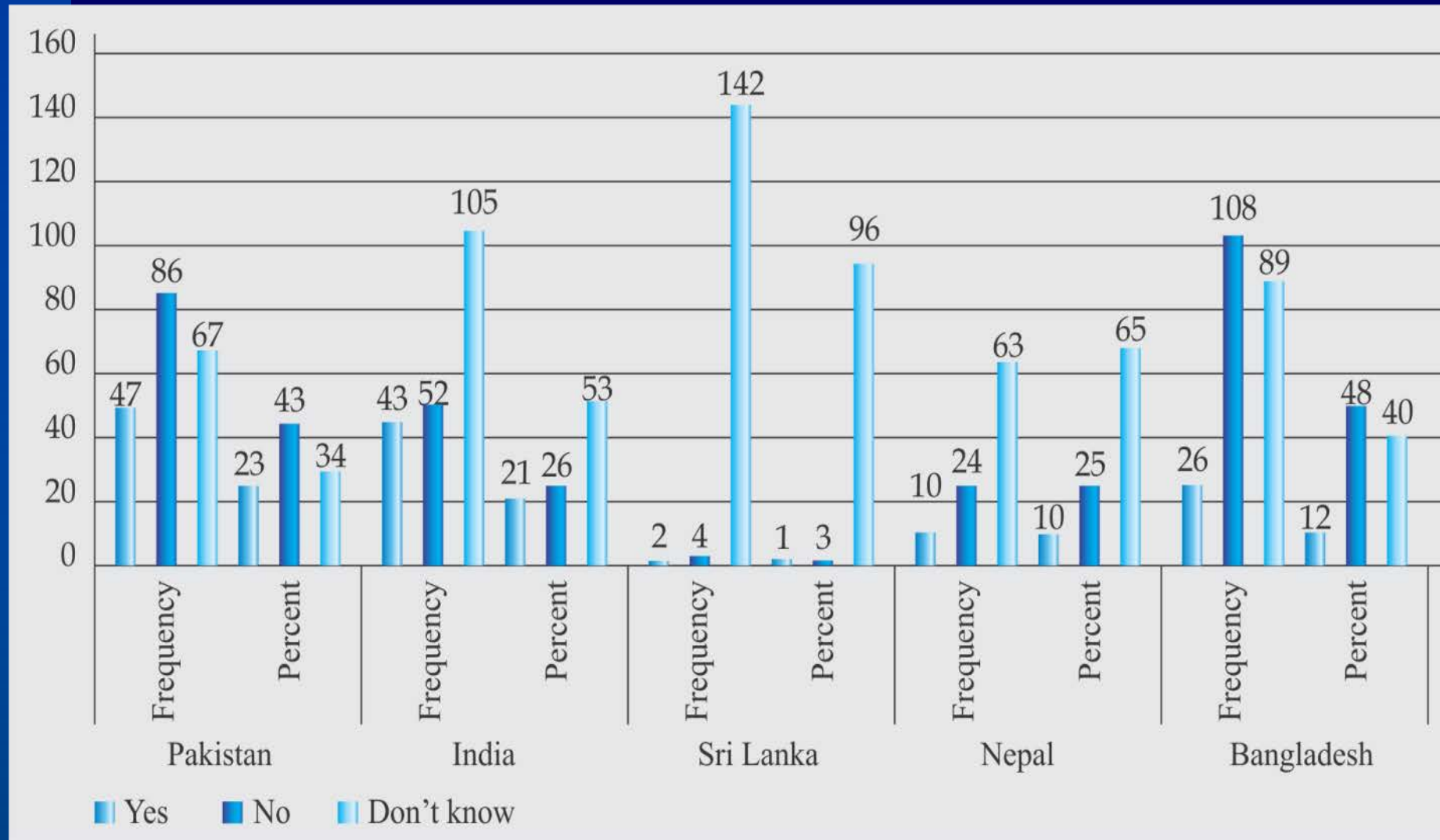
Perception towards the Friendliness of VAT Regulations towards SME/MSME Development:

Very Low	67	34	7	4	1	1	5	5	20	9
Low	91	46	66	34	3	2	50	52	72	32
Indifferent	26	12	86	44	128	96	34	35	77	35
High	16	8	36	18	1	1	8	8	50	22
Very High			1	1					4	2

Frequency of Visits the Tax officials perform:

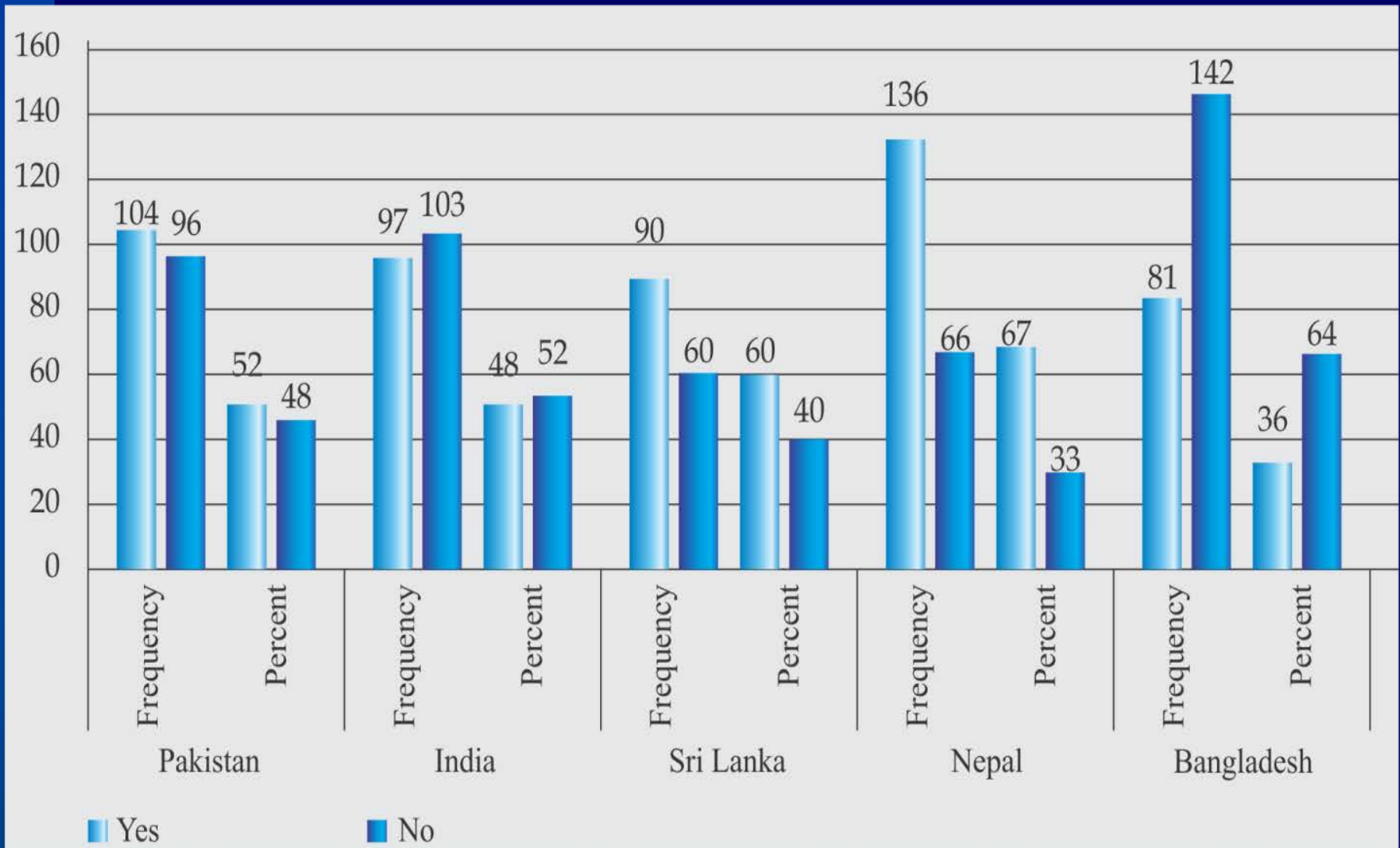
Monthly	12	6	10	5.1	1	1	3	3	5	2
Quarterly	82	41	24	12.2	1	1	7	7	48	22
Biannually	26	13	19	9.6	2	1	24	25	57	26
Annually	80	40	69	35	3	2	63	65	79	35
Never			75	38.1	142	95			34	15

Are VAT Regulatory Authorities less Administrative Friendly towards Women Entrepreneurs?

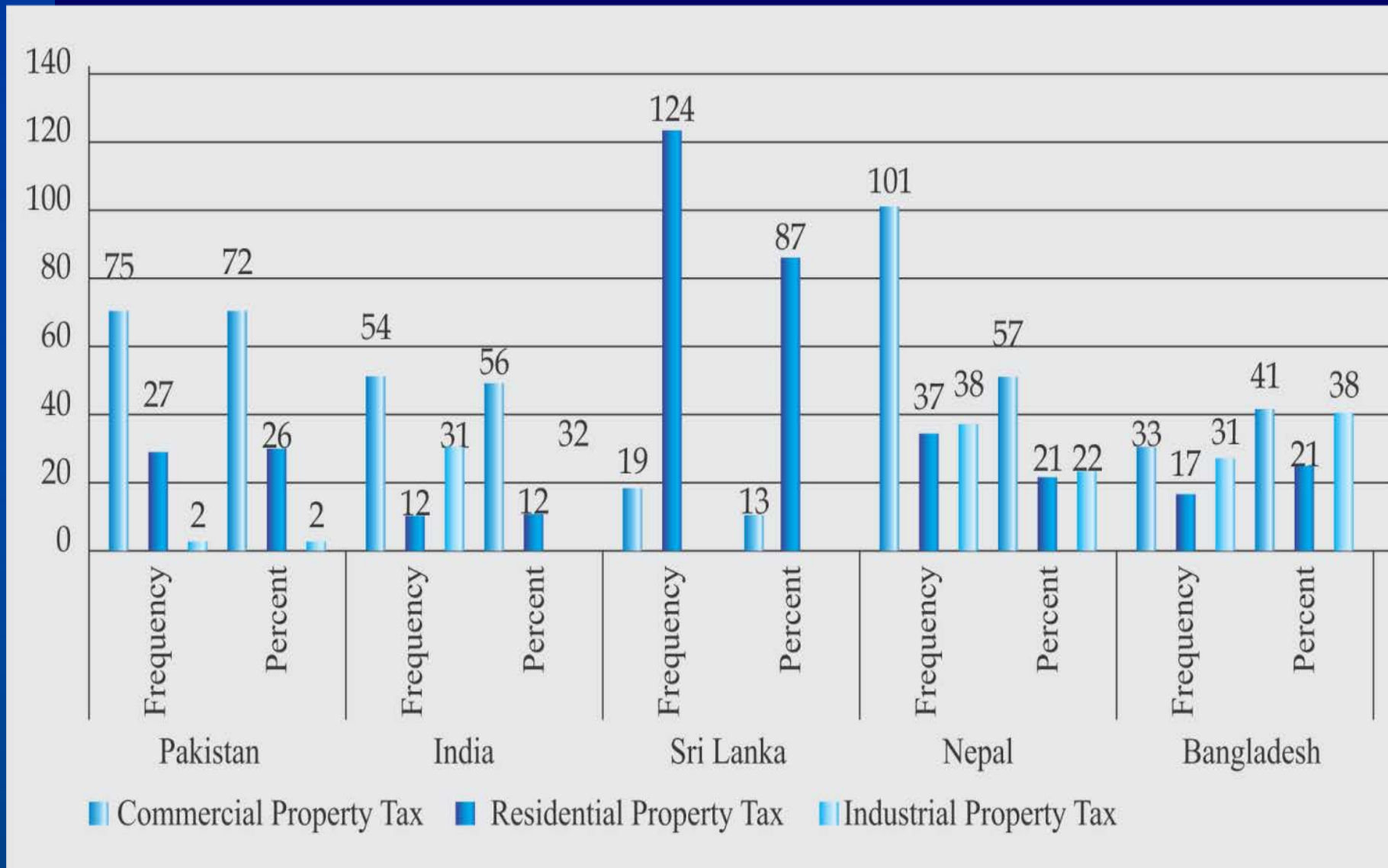


Impact of Property Tax

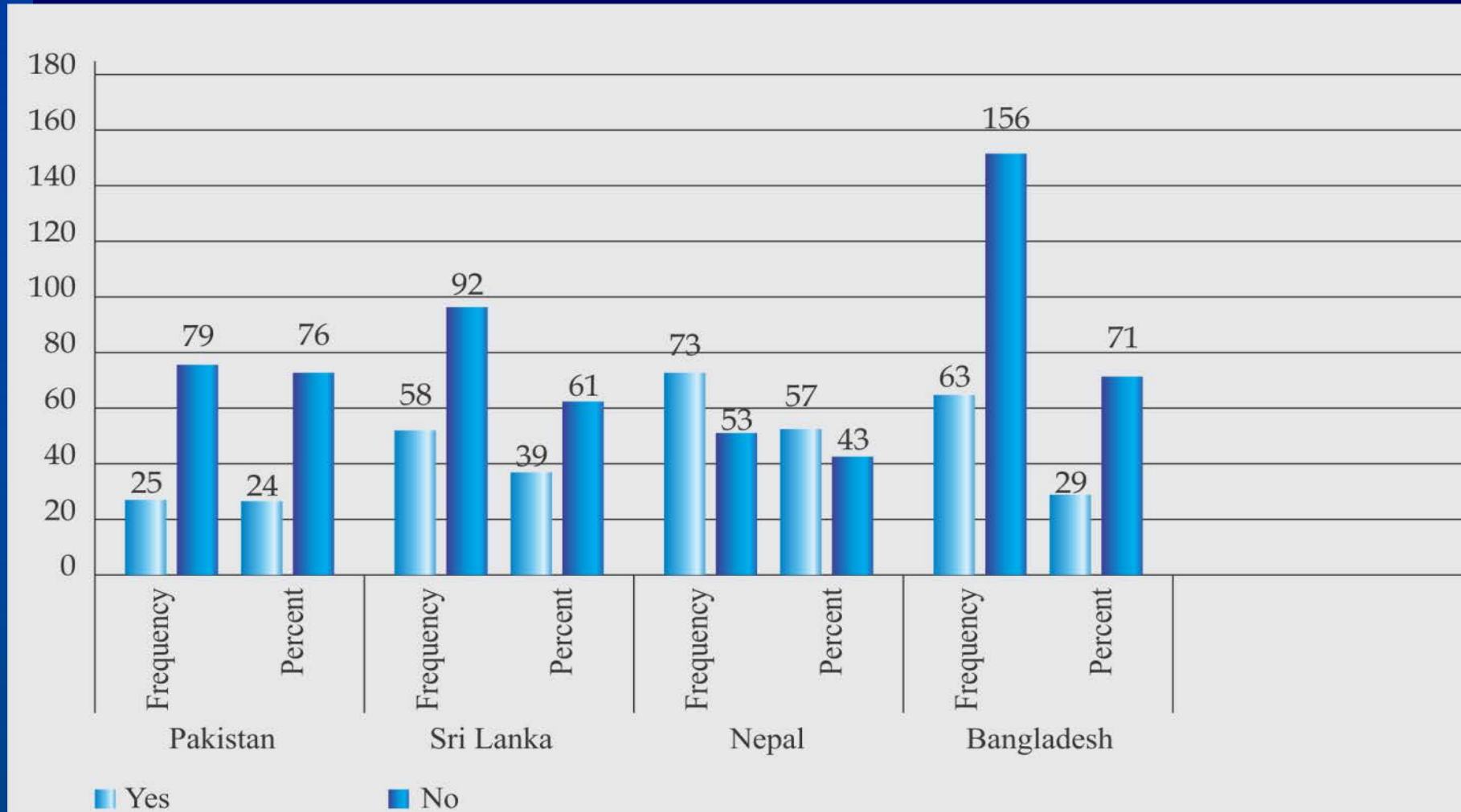
Does your Enterprise pay Tax on its Property?



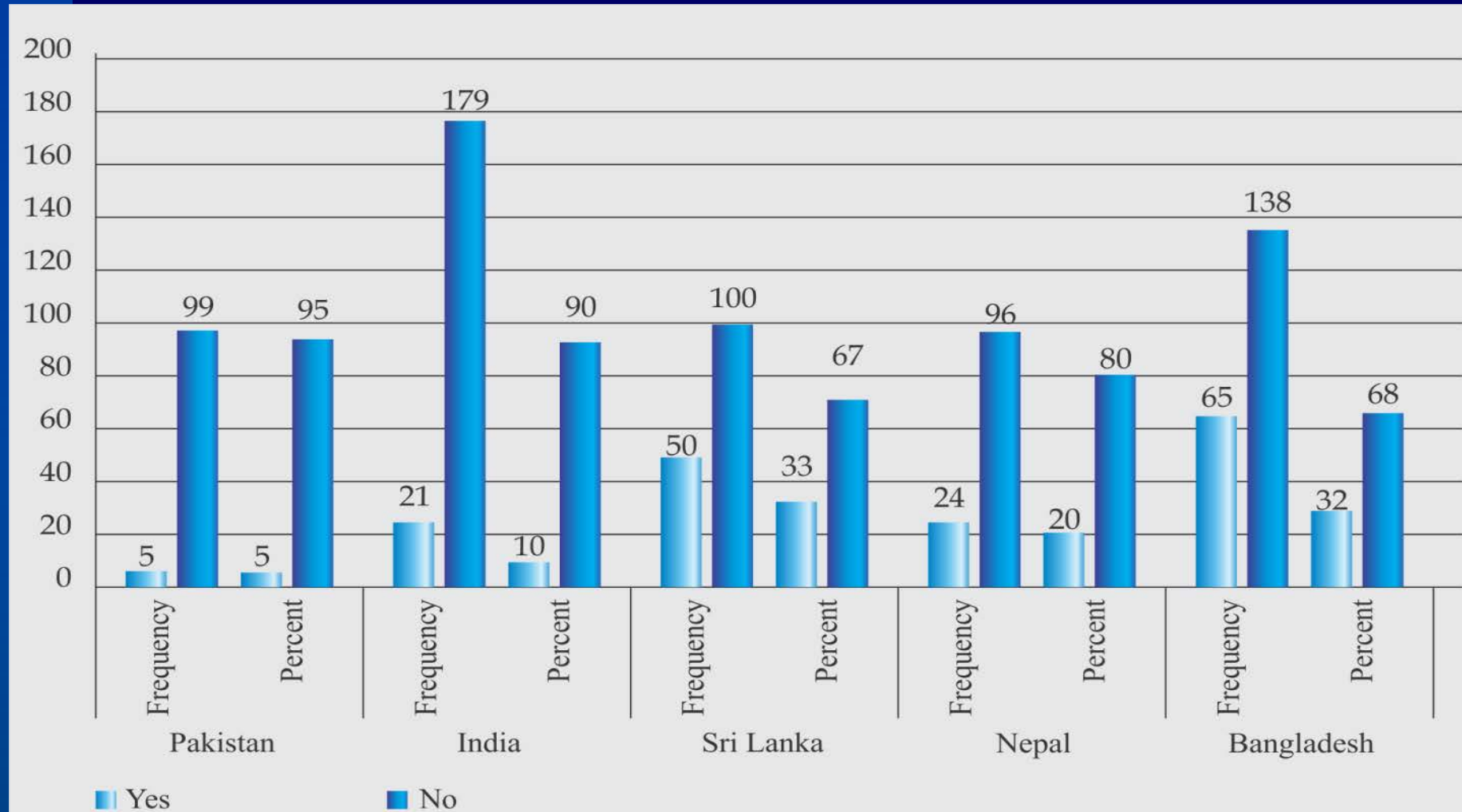
Which type of Property Tax do you pay?



Does Property Tax Payment Play an Important Role in Selecting Location for your Business?



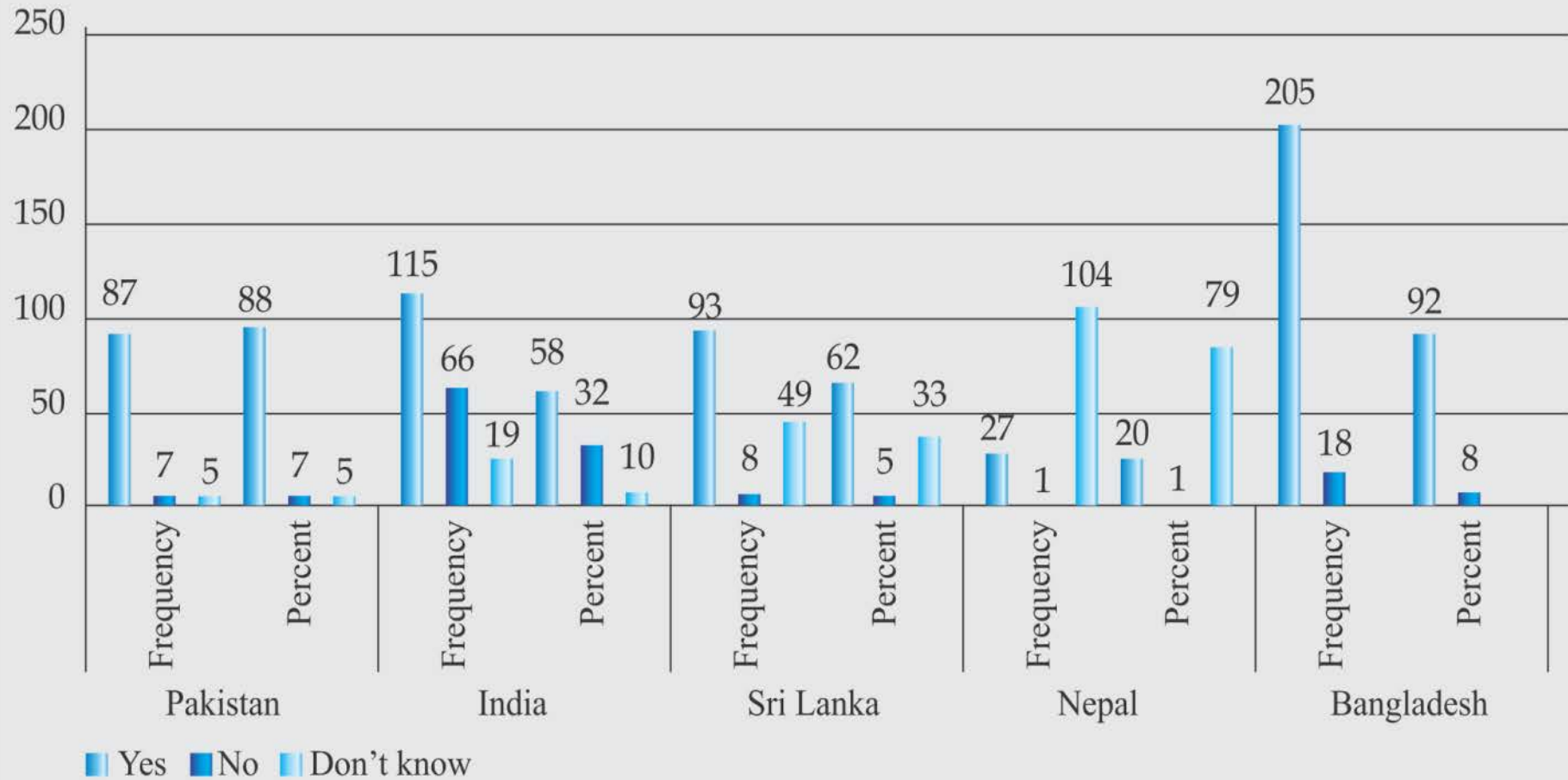
Does the Type of Property, you operate on, affect your Decision to Develop/Expand the Business?



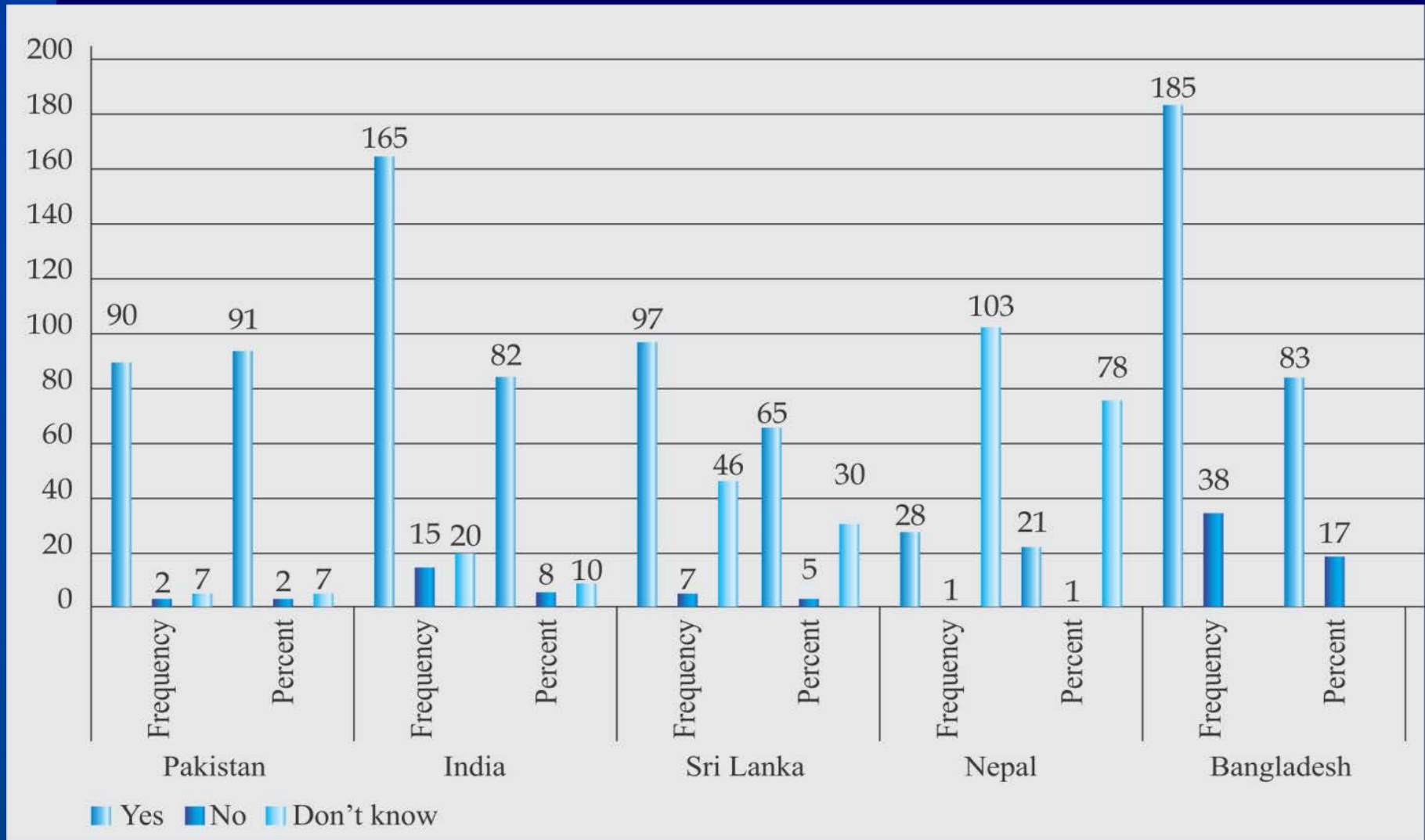
Problem(s) your Organization has Faced during Property Tax Compliance

	Pakistan		India		Sri Lanka		Nepal		Bangladesh	
	Frequency	Percent	Frequency	Percent	Frequency	Percent	Frequency	Percent	Frequency	Percent
No problem non-payment or payment at a little amount	49	48	55	55	125	83	42	34	98	51
Absence of self-assessment scheme	18	18	26	26	64	43	23	19	23	12
Discretionary valuation of property by taxmen	45	44	18	18	25	17	57	46	39	20
Frequent asking for increased volume of tax	22	21	30	30	12	8	38	31	71	37
Frequent asking for submission of various documents	24	23	31	31	8	5	47	38	31	16
Frequent visits of tax officials causing business disturbance	27	26	15	15	2	1	20	16	3	2
Absence of dedicated revenue officer for collection of property tax	20	20	2	2	1	1	11	9	10	5

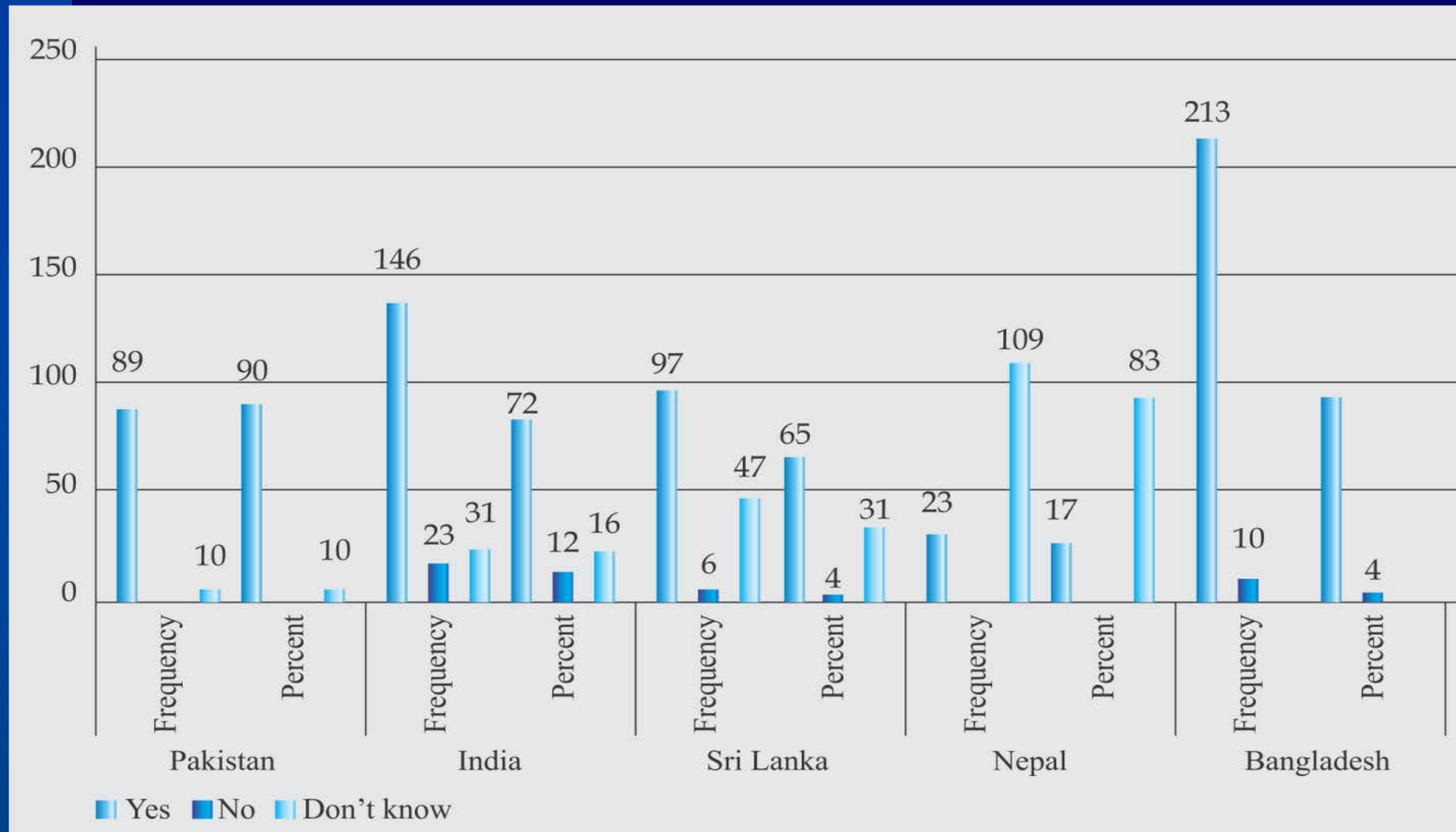
Do you think that the Procedure of Land Acquisition is Complex?



Does Land Acquisition Involve High Cost?



Perception about Corruption in Land Acquisition Process



Common Findings and Issues

- **The following commonalities emerged from the Literature Review, Focus Group Discussion (FGD) and Key Informant Interviews (KIIs):**
- **Lack of Standard SME Definition:**
 - **All South Asian countries find it difficult to standardize the criteria used to define SMEs across institutions that levy taxes, encourage investment, promote trade, provide credit and support to SMEs.**
 - **This makes the policy mix for institutions fragmented and incoherent while its net impact on SMEs becomes difficult to assess with any degree of certainty.**

- **Lack of Tax Awareness:**

- The level of awareness and understanding among SMEs of tax policies and administrative procedures is extremely low, and steps need to be taken to address this before firms can be expected to formalize and grow.

- **Value Added Tax (VAT):**

- Almost all SMEs face medium to high compliance costs with their respective VAT regimes
- This discourages registration, ultimately hampering their profitability and competitiveness.
- In certain countries except India and Sri Lanka, researchers have found strong arguments and support favoring the establishment of a multiple rate VAT system, rather than a single flat rate.
- However, in India the policy recommendations sought uniformity in VAT rates.

● **Concessions/Exemptions:**

- **It was found that tax expenditure policy is neutral vis-à-vis size, but prioritizes certain industries that are deemed significant with regard to investment or trade.**
- **These industries are invariably those where SMEs find it difficult to compete with larger, more established firms, due to a variety of reasons.**
- **In most cases, SMEs that can supply exporters are unregistered or exempt from VAT, which means exporters cannot claim input credits from them, and so have no incentive to buy from them.**
- **At the same time, exemption thresholds may encourage tax avoidance as firms prefer not to expand business but to establish a new business to remain under the exemption threshold**

● **Property Tax and Land Acquisition:**

- **Property tax does not affect enterprise development directly, as the local tax administration system is weak, valuation tables are obsolete and the tax rate is too low to affect earnings.**
- **At the same time it was found that commercial or residential area land use does affect the decision making of entrepreneurs, regarding growth and formality.**
- **As a corollary to the foregoing, the process for acquiring land is highly cumbersome, inefficient and costly for entrepreneurs seeking to establish businesses.**

Common Recommendations

- **There is a need to educate tax payers using methods such as:**
 - Practical and illustrative tax guides
 - Workshops and seminars on tax systems
- **To make tax regimes non discriminatory towards particular industries/sectors.**
- **There is a need to make provisions for self assessment of tax**
- **There is a need for transparent tax return calculation mechanism**
- **Improve the accessibility of Tax Administration's Service offices and enhance service quality:**
 - Operate fully automated e-return system
 - Appoint certified tax facilitators

Common Recommendations

- **Streamline both the tax design and the tax administration to reduce the compliance costs:**
 - Taxpayer friendly returns
 - Less frequency in filing of returns for small enterprises
 - Tax forms in local languages.
- **A broad consensus can be built to at least harmonize the sector-wise definitions of SMEs by public and private sector governing institutions.**

Thank You

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