

# PRE-FILLED INCOME TAX RETURNS: REDUCING COMPLIANCE COSTS FOR PERSONAL INCOME TAXPAYERS IN SLOVENIA

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## *Abstract*

*Simplifying procedures and improving legislation generally lead to a reduction in the compliance costs. The introduction of pre-filled tax returns clearly simplifies the tax compliance procedure. Before the introduction of pre-filled tax returns for personal income taxpayers in Slovenia, tax legislation was also modified. This paper presents the results of research into the compliance costs for personal income taxpayers before and after the simplification of the compliance procedure in Slovenia, irrespective of tax legislation itself not being simplified. The results indicate that pre-filled tax returns reduce compliance costs for personal income taxpayers by around 73%. Nevertheless, this is only a tentative estimate, since several assumptions are taken into account.*

*Key words: compliance costs, personal income tax, pre-filled tax return, Slovenia*

## **1 Introduction**

Complying with regulations usually involves various costs for individuals, businesses and the voluntary sector: financial costs and compliance costs divided into substantive compliance costs and administrative costs (SCM Network, 2005). Financial costs are the result of a concrete and direct obligation to transfer a sum of money to the government or legislated authority. Compliance costs are all the costs to individuals, businesses and other institutions of complying with regulations excluding the financial costs. Substantive compliance costs are the costs that individuals, businesses and the voluntary sector pay in order

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to comply with the obligations that legislation and regulations require of a production process or a product. Administrative costs are the costs imposed on businesses, the voluntary sector, public authorities, and individuals in meeting the obligations to provide information in the broad sense (e.g. monitoring, assessment, getting licenses).

On the other hand, the administrative burden comprises the administrative costs that businesses incur simply because of regulatory requirements; it includes administrative activities that businesses, citizens, or the voluntary sector would not continue to pay if the regulations were removed. According to Sandford (1995), tax compliance costs are generally defined as costs incurred by taxpayers in meeting the tax requirements imposed on them by the law and revenue authorities, *over and above* the actual payment of taxes, and *over and above* any distortion costs inherent in the nature of the taxes. The measurement of tax compliance costs became an important research subject in most developed countries more than twenty years ago (Australia, Canada, the Netherlands, United Kingdom, United States), in countries in transition at the beginning of 2000 (Slovenia, Croatia, Czech Republic), and also in other countries in Asia (Singapore, Malaysia, Hong Kong, India), Africa (Tanzania, Ethiopia) and South America (Brazil) (see Evans, 2003). The research results on tax compliance costs (i.e. Sandford et al., 1989; Allers, 1994; Malmer, 1995; Pope, 1995; Evans et al., 1998; Tran-Nam et al., 2000; Ariff, 2001; Chittenden et al., 2003; Vitek et al., 2003; Klun and Blažič, 2005, Das-Gupta, 2003; OECD, 2001; EU, 2004, and others) indicate that tax compliance costs are regressive (low-income personal taxpayers bear a disproportionately higher burden than high-income personal taxpayers) and substantial (up to 2.5% of GDP) (see Evans, 2003) and therefore a significant part of tax-related costs.

With the revision of the European Union's (EU) Lisbon agenda for competitiveness, better regulation has become one of the priorities. Therefore, measuring compliance costs is becoming part of public policy in member states. At the end of 2006, a document was adopted at EU level calling for a 25% reduction in administrative burdens by 2012 (European Commission, 2006). Measuring compliance costs generally entails measuring such costs within business activities, i.e. for businesses and the self-employed. While more than twenty years ago measuring the compliance costs for various forms of regulation – primarily tax-related – was the concern of a limited circle of individual researchers, measuring these costs is now not only of interest to researchers, but primarily to central government institutions seeking to measure the impact of new or amended legislation on the economy. Reducing administrative burdens has become a vital indicator of competitiveness. The Standard Cost Model (SCM) Network in the EU has developed a standard model for measuring costs arising from regulation. Although the method is not intended for research purposes, as the cost assessments are carried out on a small sample only, it remains an attempt to assess any the unnecessary costs of individual pieces of legislation (for more, see SCM Network, 2005).

In the Slovenian case, the simplification of tax procedures has become an important element in the policy to reduce administrative burdens, and is now the most frequently used tool for reducing such burdens. Other common tools to reduce burdens include (OECD, 2007):

- measuring potential costs before introducing legislation
- offering electronic services and one-stop shop services
- reducing the number of licenses and permits required
- codification (combining existing regulations in a particular area into a single piece of legislation).

As mentioned above, most of the actions are done for businesses, yet measuring compliance costs is also relevant for private individuals and non-profit organizations. This paper focuses on the impact of pre-filled tax returns on individuals. This paper presents a study of the impact of personal income tax reform on taxpayers' compliance costs. In Slovenia, these costs were measured for personal income taxpayers in 2001 – in relation to the 2000 tax year – which formed the basis for checking the research hypothesis that a simplification of the tax procedure will lead to a significant reduction in the tax compliance costs of personal income taxpayers. The 2004-2006 tax reform included a number of amendments to personal income tax legislation. By far the most important change from the point of view of tax compliance cost reduction was the introduction of pre-filled personal income tax return forms in 2006. The research evaluates the change in personal income taxpayers' compliance costs in 2007, when partial pre-filled tax returns were introduced, and estimates the expected change in these costs in 2008, following an additional change, as a result of introducing fully pre-filled tax returns.

The paper also presents the major changes in Slovenian legislation leading to changes in costs, followed by a presentation of the methodology and sample, and a comparison of compliance costs for the 2000 and 2006 tax years, and estimated compliance costs for the 2007 tax year.

## **2 International experience with pre-filled tax returns**

The pre-filled income tax return is not a new idea. Denmark, in the 1990s, was the first country in Europe to introduce pre-filled tax returns. The practice was followed in other Scandinavian countries. In recent years, pre-filled tax returns have been adopted in Belgium, Chile<sup>1</sup>, Portugal, Spain and France (OECD, 2008), and are planned for Australia<sup>2</sup> and US. The problem with introducing pre-filled tax returns is the complexity of tax systems. If no simplifications of tax system are made, pre-filled tax returns cannot be introduced. On the other hand, simplification itself leads to reductions in compliance costs, but not as much as when combined with pre-filled tax returns (Highfield, 2006).

Nevertheless, research on evaluating the compliance costs' reduction as a result of pre-filled tax returns is not undertaken in most countries. The only report in the literature concerns Sweden, where the introduction of prefilled tax returns reduced compliance costs of personal income taxpayers by 20% (Malmer, 1995). In other countries, estimates are not rigorous. In 2004-05, Australians spent over 1.2 million Australian dollars managing their tax affairs, mainly because 74% of taxpayers need professional help. Prefilled electronic individual tax returns would reduce these costs for the 9 million Australians who

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<sup>1</sup> Chile plans to use electronic accounts to introduce prefilled forms for value added tax as well.

<sup>2</sup> Australia has already provided prefilled tax returns for those who use e-tax filling.

use e-tax or lodge their returns electronically through a tax agent (Sampson, 2007). In Denmark, 87% of taxpayers received a pre-filled tax return in 2004, and for 67.5% of them no additional communication with tax authorities was necessary (Claps, 2006). According to the OECD E-Government Project (2006), pre-filled tax returns reduce income reporting 'errors', and the measured indicator showed annual savings of 200 million Euros. Some assessments of introducing pre-filled tax returns in the USA (Goolsbee, 2006) show that pre-filled tax returns would reduce taxpayers' costs by 2 billion US dollars, assuming that 40% of eligible taxpayers choose this method. As already mentioned, most of these assessments are not rigorous.

Slovenia introduced partially pre-filled tax returns in 2007, and completely pre-filled tax returns in 2008. The important changes that were needed in the regulations are presented in the next section. The aim of my research was to evaluate the reduction in tax compliance costs for personal income taxpayers in Slovenia after the introduction of pre-filled tax returns. The research was conducted in 2007, after partially pre-filled returns were introduced. It should be stressed that reductions in tax compliance costs are not only the result of pre-filled returns per se, but also part of regulatory changes. Therefore, the results should be treated with caution. Nevertheless, even only as an approximation, the results indicate that pre-filled tax returns substantially reduce compliance costs for personal income taxpayers.

### **3 Major income tax changes during the 2004-2006 tax reform in Slovenia**

Personal income tax in Slovenia applies to an individual's income, of which there are six categories:

- income from employment (salary, incentives, income earned under contracts for temporary work, pensions and other receipts);
- income from self-employment;
- income from agriculture and forest businesses (cadastral income of farmland and woodland);
- income from lending property and delivery of property rights;
- income from capital; and
- other income (i.e. gifts)

Each individual is treated as a separate taxpayer. The tax year is the calendar year. Provisional tax payments are made during the tax year. Those paying taxable income are required to calculate and pay an advance tax payment for the taxpayer.

Fundamental tax reform took place in Slovenia in 2004 with changes in the taxation of income for individuals and legal entities, and changes in the VAT system. A number of corrections and other amendments to these tax codes soon followed. The amendments to the taxation of personal income year by year are presented below.

The 2004 changes in legislation, which came into effect in 2005, introduced the following major changes to income tax (Čok, 2007):

- expansion to include global income (i.e. the taxation of income earned at home and abroad), and some other forms of income, such as interest on savings, staff stipends, selected bonuses;

- a reduction in the percentage of direct tax relief from 3% to 2%, and a reduction of standardised costs on certain types of income (e.g. copyright and rental income);
- a modest reduction in the number of tax brackets from 6 to 5, and a reduction in the lowest marginal tax rate from 17% to 16%;
- definition of fixed amounts of tax relief in advance (previously the scale and levels of relief were linked to percentages of average gross wage).

In this first phase, the amendments mainly led to additional compliance costs for taxpayers, as all those with income taxed by the new legislation had to collect data on more forms of income, and complete an expanded tax return.

In 2005, the Government created a tax action group to draft amendments to the 2004 tax reform. The major change in personal income tax was the introduction of schedular taxation, i.e. on passive incomes such as interest, dividends and capital gains. Administratively, this meant that dividends and similar income received in Slovenia were taxed at source and did not need to be entered in a tax return. However, the amendment also introduced additional administrative work for those receiving interest above the allowance threshold or income from abroad, and those making capital gains, as they were required to submit separate returns from 2007 onwards (Čok, 2007).

In 2006, additional amendments were introduced which would apply to the 2007 tax year, and hence only affect tax returns from 2008. The number of income tax brackets was again reduced, from five to three. The lowest marginal tax rate remained the same, but the top marginal tax rate was reduced from 50% to 41%. Another major difference was the abolition of non-standard forms of relief and an increase in general tax relief.

The simplification of the tax process adopted – pre-filled tax returns – was of significance to this research. Income information from third-party sources (employers, banks) in Slovenia was already required as control data by the Tax Administration in relation to personal income tax. This means that the tax administration has data on all of a taxable person's income received from payers in Slovenia, pension savings under pension plans and data on dependents. With this the Slovenian Tax Administration had 90% of the data required to pre-fill tax returns, excepting data on property rental, income from abroad, and non-standard relief. The change in the tax legislation in 2006, which abolished non-standard forms of relief, gave the tax administration the chance to introduce pre-filled tax returns, as income from abroad has to be declared to the tax administration within 15 days of receipt of income, and rental income by 15 January for the previous year. Pre-filled tax returns were not issued for schedular taxed income, i.e. for interest - dividends from abroad and capital gains - which taxpayers have to complete themselves.

Following the 2006 changes, the tax return forms, pre-filled with the data available to the tax administration, were distributed in 2007 to persons liable for income tax. Taxpayers had to add any data missing from the tax returns, correct any errors and input the non-standard forms of relief they wanted to claim. The signed tax return was then submitted to the tax administration via the internet, via post, or in person. In 2008, taxpayers received pre-filled tax returns which included a provisional calculation of their tax liability. If taxpayers do not appeal against the provisional calculation within 15 days, it then be-

comes the final decision on their income tax assessment. This means that taxpayers who agree with the tax administration's data do not have to submit tax returns or submit signed forms to a tax office. This type of pre-filled tax return reduces taxpayers' costs for both inputting data into the tax return and submitting the return to the tax administration. The major changes in tax legislation are presented in Table 1.

*Table 1: An overview of Slovenian personal income tax reforms 2004-2007*

|   | <b>2004</b>   | <b>2006</b>   | <b>2007</b>   |
|---|---|---|---|
| Tax relief  | definition of fixed amounts of tax relief in advance      | rise in general allowance and reduction in non-standard reliefs | rise in general allowance and abolition of non-standard reliefs |
| Number of tax brackets                                      | 5   | 5   | 3   |
| Tax rates   | from 16-50%   | from 16-50%   | from 16-41%   |
| Schedular taxation of interest, dividends and capital gains | no  | yes   | yes   |
| Tax returns   | completion by taxpayers (electronic filing also possible) | partially pre-filled returns                                    | pre-filled returns  |

*Source: Čok, 2007*

The major income tax changes during the 2004-06 tax reform in Slovenia do not mean that tax legislation was rewritten in a simpler way. The important change was made when the compliance procedure of personal income tax was simplified. This simplification was possible after some changes in tax legislation, but the most important change was abolishment of tax reliefs which had to be reported by the taxpayer.

#### **4 Methodology**

As stated above, the aim of the research was to evaluate the reduction in tax compliance costs for personal income taxpayers in Slovenia after the introduction of pre-filled tax returns. The results are compared with the compliance costs of personal income taxpayers evaluated in 2001. The research assessed the reduction in taxpayer compliance costs for the partially pre-filled tax returns in 2007 and, based on cost distribution, it was also possible to estimate the reduction in tax compliance costs for 2008 under several assumptions, stated in subsection 5.2.

##### **4.1 The accounting framework for calculating tax compliance costs**

A questionnaire was used to assess tax compliance costs. The questionnaire was designed to capture all the information required for the analysis presented below. The anal-

ysis excluded tax planning costs<sup>3</sup> and psychological costs. The reason for excluding tax planning costs and psychological costs is that they are difficult to assess, and the same reasoning has led to their being excluded from most other research in this field.

The assessment of compliance costs includes the following taxpayer costs:

- time spent by both taxpayers and unpaid helpers in reviewing and completing tax returns
- tax agent/accountant's costs
- other cash expenditure (i.e. postage).

The time could be calculated in relation to spare time, work time or overtime at work. Net wage, gross wage and other values can therefore be used in calculations of the cost of that time. It was decided to take into account the values stated by the surveyed taxpayers. This approach is made under the assumption that taxpayers spent spare time on filling in tax returns, and therefore they stated the value of that time in questionnaires. Some researchers abroad (Sandford et al. 1989; Godwin 1995; Diaz and Delgado 1995; Pope 1995; Allers 1994; Blažič 2004) selected a similar approach for evaluating time, while some researchers have used a value based on average net or gross salary (e.g. Slemrod 1998; Vaillancourt 1989). The average value of one hour was assessed at € 14.81<sup>4</sup>, considering the evaluation of the time used to review pre-filled data and completion time, and excluding two values that deviated significantly from the mean.

#### **4.2 The questionnaire, conduct of survey, sample selection and response rate**

The questions relating to tax compliance costs were based on those used in 2001 in order to ensure comparability (Klun, 2004). The 2001 questionnaire was similarly based on the structure of questionnaires previously used abroad. As part of the planning phase, five taxpayers were interviewed in person to pilot test the comprehensibility of the questionnaire and availability of data. The questionnaire was redesigned on the basis of this pilot test, to make it simpler to complete. In addition to general questions on sex, age, and tax bracket, the questionnaire included questions on the time required by the taxpayer to complete the tax return, and also the time taken by family members, and friends. Time taken is also broken down into time spent on reviewing pre-filled data, and time used for inputting tax relief claims, as that is the only way to assess costs for the 2007 tax year. In addition to the statement of time taken, taxpayers also gave a figure in euros for the time taken, and estimated other costs relating to the tax return, plus the cost of consultancy services where relevant.

A major difficulty encountered in defining the taxpayer sample was the fact that the personal income tax payer register is confidential, which meant that it was not possible to create a representative sample<sup>5</sup>. Therefore, the sample of 600 potential personal taxpayers was selected at random from the telephone directory. The letter enclosed with questionnaires sent by mail includes information that the questionnaire can be filled online, since

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<sup>3</sup> Planning costs usually refer to costs the taxpayer spend in order to minimise his/her tax bill.

<sup>4</sup> An average net wage in year 2007 was 4.80 EUR per hour. Using an average net wage per hour, assessed compliance costs would be much lower.

<sup>5</sup> The same problem also arose in 2001.

they are prepared electronically and can be completed online. The Ministry of Public Administration and the Tax Administration of the Republic of Slovenia also cooperated in the distribution and promotion of the questionnaire, placing it on their websites. Although internet use has increased significantly in Slovenia<sup>6</sup>, the researchers did not want to neglect people who do not make frequent use of the internet, so some questionnaires (5% of 600) were completed on the basis of telephone interviews<sup>7</sup>. The survey of the entire sample was carried out in the second half of May 2007 and the beginning of June 2007.

A total of 481 taxpayers completed the questionnaire; the “self-employed”<sup>8</sup> were analysed separately, and excluded from the analysis, along with two questionnaires that could not be used because the answers were incomplete. A total of 439 completed questionnaires were therefore included in the analysis. It was not possible to calculate response rate because responses were received from both the mail-out sample and the websites. It was impossible to determine how many people saw the questionnaire on the websites where the questionnaire was promoted.

A total of 439 is a relatively small sample (population coverage – 0.042%). Nevertheless, the research was comparable to similar surveys abroad, as the proportion of the sample size to the overall population was comparable to previous foreign and Slovenian research (the lowest was in the UK and Germany, 0.008%; Sandford et al. 1989; Tielbe 1986) and the highest was in the Netherlands, 0.09% (Allers 1994); the coverage achieved by the 2001 research was 0.022% (Klun 2004)).

### ***4.3 The use of population weighting***

Testing whether the sample was representative indicated that the proportion of taxpayers in the lowest income bracket in the sample was lower than the proportion in that bracket in the overall population. On the other hand, the proportion of high income taxpayers was higher. The other difference from the total population was the distribution of the sample according to number of income sources. In the sample, the proportion of those with up to two income sources was much higher than in the total population, and those with three income sources was much lower (see Table 2).

The correlation between estimated compliance costs and the number of income sources and income level was measured using Pearson’s correlation. The results show that both correlations are positive, but not statistically significant<sup>9</sup>. Since in the research from 2001 compliance costs were weighted according to income level only, the calculation of weighted total compliance costs for personal income taxpayers for the 2006 tax year was carried out in the same way.

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<sup>6</sup> In the first quarter of 2007, 58% of households had access to the Internet. 44% of the households used broadband Internet access. In the first quarter of 2007, 56% of persons aged 10 to 74 used the Internet (Statistical Office of the Republic of Slovenia, 2007).

<sup>7</sup> Interviews were done among people aged 55 and above.

<sup>8</sup> The fulfilment of tax obligations for this income taxpayer group requires a different form of recordkeeping and tax return completion, despite the fact that tax law treats them as personal income taxpayer. Their responses deviated too much from other personal income taxpayers. These taxpayers were also excluded from the 2000 analysis.

<sup>9</sup>  $R(\text{costs and income level})=0.177$  and  $R(\text{costs and number of sources})=0.205$ , in both cases with sig. (2-tailed)=0.000.

*Table 2: Sample and population according to distribution among tax brackets and number of sources*

| Tax bracket | Tax brackets   |            | Number of income sources |                |            |
|-------------|----------------|------------|--------------------------|----------------|------------|
|             | Population (%) | Sample (%) | Number of income sources | Population (%) | Sample (%) |
| 1           | 55.4           | 14.7       | 1 – 2                    | 37.0           | 70.1       |
| 2           | 28.7           | 27.2       | 3 – 4                    | 45.9           | 24.2       |
| 3           | 12.3           | 39.2       | 5 – 6                    | 6.6            | 5.5        |
| 4           | 2.9            | 15.7       | more than 6              | 0.4            | 0.2        |
| 5           | 0.7            | 3.2        |                          |                |            |

*Source: Slovenian Tax Administration internal data (2007) and survey*

## 5 Estimate of personal income tax compliance costs

### 5.1 Tax year 2006

On average, taxpayers stated that they took just 28.6 minutes to review the pre-filled data and enter tax relief claims, while family members took an average of 12.9 minutes, and friends, 8 minutes. On average, taxpayers took 4 minutes to complete separate income tax returns (for interest exceeding the allowance threshold, capital gains, and income from abroad), which takes into account the fact that most taxpayers are not required to submit separate returns<sup>10</sup>. The average total time taken to complete all income tax-related requirements was 53.5 minutes. On average, male taxpayers aged between 25 and 45, and taxpayers with a higher number of income sources took more time to complete their tax returns. Taxpayers from the highest tax bracket, i.e. with the highest income, took the most time. People from the highest and the lowest education level also took more time to complete their tax returns. The structure and average value of compliance costs relating to income tax are given in the Table 3. Although the structure changed slightly compared to 2000, the time taken by taxpayers is still the highest share of costs. It is noteworthy that tax agent/accountant costs remain a relatively low proportion of overall costs<sup>11</sup>, whereas they are generally much higher in foreign studies.

The analysis continued by defining the weighted average value per taxpayer, in order to produce the total figure for taxpayer compliance costs. As already mentioned, costs were weighted according to the number of taxpayers in each tax bracket. The weighted average cost per taxpayer was derived by multiplying the average cost value for an individual income tax bracket by the proportion of taxpayers in the individual tax bracket in the overall population. The weighted average cost per taxpayer is €15.40, which means that in 2006 tax year the total cost for all taxpayers was €16.02 million. Taxpayers' compliance costs for personal income tax therefore represented 0.89% of personal income tax revenue, and 0.05% of GDP in 2006.

<sup>10</sup> The zero was used for those who did not file separate tax returns.

<sup>11</sup> The proportion of taxpayers that pay for help from tax agents (4.6% of respondents) is also lower than in 2000 (10.9% of respondents).

Table 3: Structure of personal income taxpayers compliance costs in 2007

|                            | Average cost<br>per taxpayer (€) | Proportion<br>(%) |
|----------------------------|----------------------------------|-------------------|
| Cost of time spent         | 15.16                            | 69.5              |
| Tax agent/accountant costs | 0.91                             | 4.2               |
| Other expenditure          | 5.75                             | 26.3              |
| Total                      | 21.82                            | 100.0             |

Source: Survey of personal income taxpayers, 2007

Like other research into compliance costs, this study indicated that the costs are regressive. They represent 0.42% of income for those in the lowest tax bracket, 0.21% for the second tax bracket, 0.16% in third, 0.09% in fourth and 0.13% for those in the highest tax bracket, despite the fact that taxpayers with a higher income have higher compliance costs.

### 5.2 Estimate of costs for tax year 2007

Changes in legislation mean that in 2008, personal income taxpayers received pre-filled income tax return forms for income from the 2007 tax year. The pre-filled tax returns include a provisional calculation of the taxpayer's tax liability, which also serve as the tax administration's final decision, unless the taxpayer finds an error. If taxpayers discover any errors, they must appeal within 15 days and inform the tax administration of the correct data<sup>12</sup>.

The taxpayer questionnaire distinguished between the time taken to review the pre-filled data, and the time needed to input tax relief items, and the surveyed taxpayers also had to define in detail any cash expenditure relating to sending or delivering signed income tax returns. Dividing the time used by taxpayers, family members, and friends, and separating expenditure in this manner enabled the researchers to estimate the 2007 income tax compliance costs that taxpayers incurred in 2008.

The assessment of average costs per taxpayer was based on the following assumptions:

- the same amount of time was used to review pre-filled data;
- the compliance costs of separated tax returns remained unchanged, as the proportion of taxpayers submitting the separate tax returns did not differ significantly;
- the evaluation of time remained the same;
- tax agent/accountant costs remained unchanged;
- expenditure was reduced by the amount used for sending and delivering signed tax returns to the tax administration, while expenditure on acquiring information remained the same.

<sup>12</sup> 7.6% of taxpayers appeal, 76.6% of these appeals were due to changing information on child allowance (Tax Administration of the Republic of Slovenia, 2008).

Based on these assumptions, in 2008 the average time taken by taxpayers would be 14.4 minutes, the time taken by family members would be 6.7 minutes, and the time taken by friends, 4.4 minutes. Since other tax returns are unchanged, the time used to complete them would remain 4 minutes. The average time required per taxpayer is therefore assessed at 29.5 minutes, which is almost half of that in 2007 (45% less, to be precise). Taking into account the estimated time per taxpayer, tax agent/accountant's costs and cost expenditure for information acquisition, total personal income tax-related compliance costs for 2008 would be €8.98 per taxpayer, which is €12.84 less than in 2007. Average total costs for all personal income taxpayers would be 9.1 million euros. As the number of income tax brackets was reduced to three for 2007, an estimate of the weighted average value per taxpayer was not possible. The cost saving for the overall population would be 13.6 million euros in comparison with 2006 if we take into account the same total population as in 2006. If we use the total population number for 2007, average total personal income tax compliance costs are almost the same (9.09 million euros) since the number of taxpayers did not decrease substantially<sup>13</sup>. Nevertheless, we must stress that the introduction of totally pre-filled tax returns is not the main reason for the reduction in compliance costs. The difference between the 2006 and 2007 personal income tax compliance costs is in general the result of the abolition of non-standard tax-reliefs, since a very small part of the reduction is the result of lower expenditures for delivering tax returns to the tax administration<sup>14</sup>. Therefore, the results from 2006 tax year are compared to the 2000 tax year, when taxpayers filled in the entire tax return themselves. Even this comparison should be treated carefully. Some other changes in legislation could also lead to a reduction in compliance costs (i.e. withholding tax on dividends, which is final), since some other changes could increase them (i.e. separate tax returns on interest and capital gains, number of changes in a short time). The comparison is an approximate indicator of the effect of pre-filled tax returns. All of these factors should be taken into account when interpreting the results.

### **5.3 Comparison with the tax year 2000**

Personal income tax-related compliance costs were also assessed for the 2000 tax year, on the basis of a survey carried out in 2001. The sample was determined in the same way. The questionnaire followed that from 2001. The major difference is in the availability of online questionnaires.

Comparing the results of the two studies shows that the partially pre-filled tax return offers a significant reduction in compliance costs. Table 4 shows the different values for comparing the results between all years. The most appropriate is the comparison of average compliance costs per taxpayer to separate population size effects on aggregate values. If we compare only time spent, other expenditures and tax agent costs would be excluded from the comparison. Using the same value for time evaluation (in this case, the value stated in the 2007 survey), it is also important to exclude the impact of different time evaluations between both surveys. Average personal income tax compliance costs per taxpay-

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<sup>13</sup> The number decreased by 27336 tax returns.

<sup>14</sup> On average €0.34.

er for 2000 amount to €37.93, and €21.82 for 2006. The costs are lower by around 73%. As already mentioned, the difference between the 2007 tax year is in general due to other simplification in the administrative procedure. We could estimate that the simplification of the administrative procedure for personal income taxpayers reduced compliance costs per taxpayer by more than 300% from 2000 to 2007, and by more than 100% from 2006 and 2007, when totally pre-filled tax returns did not substantially influence the decrease in compliance costs.

Table 4: Comparison of time taken and assessed compliance costs for the tax years 2000, 2006 and 2007

|  | 2000                                     | 2006  | 2007  |
|--|--|-------|-------|
| Average time taken per taxpayer (in minutes)               | 141.60                                   | 53.50 | 29.50 |
| Average costs per taxpayer (EUR)                           | 28.14 <sup>a</sup><br>37.93 <sup>b</sup> | 21.82 | 8.98  |
| Total costs (millions EUR)                                 | 32.10                                    | 22.70 | 9.10  |
| Compliance costs as a proportion of income tax revenue (%) | 1.99 <sup>c</sup>                        | 0.89  | 0.50  |
| Compliance costs as a proportion of GDP (%)                | 0.133                                    | 0.05  | 0.03  |

<sup>a</sup> Adjusted figure (using revalorization<sup>15</sup>) for costs assessed in 2001

<sup>b</sup> Costs calculated using the value of one hour stated by taxpayers in 2007

<sup>c</sup> Not taking into account negative financial effects

Source: Survey of income taxpayers, 2007

A comparison of compliance costs as a proportion of personal income tax revenue<sup>16</sup> indicates that the proportion falls below 1% with the changes, which means that alongside Sweden, Slovenia has the lowest proportion of compliance costs in income tax revenue of all the countries studied<sup>17</sup> (for more see Klun 2004).

## 6 Conclusion

The research was used to evaluate the reduction in the compliance costs personal income taxpayers achieved with the introduction of several administrative procedure simplifications in legislation in Slovenia. The major change influencing the reduced tax compliance costs was the introduction of pre-filled tax returns. The research results indicate that simplifying the administrative procedure for taxpayers completing income tax return

<sup>15</sup> Revalorization was made by using revalorization calculator at Slovenian Statistical Office web page (<http://www.stat.si/>), which uses price indexes.

<sup>16</sup> Comparison should be taken as a very general approximation since the ratio is influenced by tax rates, tax reliefs, taxable income and other determinants of personal income taxation in a country.

<sup>17</sup> UK 3.6% (Sandford et al., 1989), Australia 4% (Tran-Nam et al., 2000), USA 5-6% (Slemrod and Sorum, 1984), Netherlands 3% (Allers, 1994), Canada 2.5% (Vaillancourt, 1989), Spain 3.3% (Diaz and Delgado, 1995), Sweden 1.7% (Malmer, 1995).

forms would result in a 73% reduction in taxpayer compliance costs. The research found that the abolition of tax allowances and the use of totally pre-filled tax returns led to additional reductions in taxpayer costs.

Despite the use of several assumptions, the research results are a good indicator to policymakers, i.e. the state, of the importance of eliminating superfluous administrative burdens, and the importance of evaluating the impact of legislative amendments. Research of this kind is also a significant indicator for efforts made by the European Union – and other OECD members – to reduce tax compliance costs, which they have been doing for some time by means of campaigns to “cut red tape”. This research clearly indicates that simplifying procedures leads to a significant reduction in costs for individuals, although it only provides an estimate of such costs.

The assessment of personal income taxpayer costs presented here for Slovenia is based on a set of assumptions that could also be considered as the study’s limitations. One of the major limitations is undoubtedly the fact that the research does not take into account additional costs incurred by taxpayers as a result of errors in the pre-filled tax returns (only 1.8% of taxpayers appealed about the pre-filled returns); nor are the costs evaluated for each of the “separate” tax returns, but only the average for all separated tax returns, as reported by taxpayers in the questionnaires. Since several changes in personal income tax legislation were made in the last three years, it is difficult to separate the influence of each change on compliance costs. The changes themselves have probably raised compliance costs, since taxpayers need to “learn” about the new rules.

Nevertheless, the research results provide a significant indicator of the benefits arising from measures relating to the simplified procedure. It would be of interest to supplement the data produced with figures on the savings the Tax Administration has achieved by introducing pre-filled tax returns. The fact that tax administration employees no longer have to input tax returns submitted by taxpayers into the information system probably means that the time needed to process income tax is at least halved. The delivery of pre-filled tax returns by regular post<sup>18</sup> also means an additional saving for the tax administration. The costs of information technology probably rose. The operational costs - i.e. the overall cost of administration for taxpayers and the tax administration - were significantly reduced compared to previous years. Each saving of this kind means an increase in the economy’s competitiveness. It represents both a direct saving on taxpayers’ disposable income and a reduction in public spending.

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<sup>18</sup> Before regulation changes Tax Administration was obliged to send tax returns to taxpayers with special delivery (confirmation of recipients needed), which cost 3.4 times more than regular delivery.

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