

BASIC FACTS ABOUT SLOVENIA (YEAR 2006)

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- Number of population: cca 2 million
- Area: 20.273 km²
- GDP per capita: 14.811 EUR
- GDP 2006: 29.741 mio EUR
- Tax to GDP ratio: 39,5 %
- Number of companies: 44.431 (42.924 small, 751 medium, 756 large)
- Number of personal business taxpayers: 63.675

Total number of SMEs (incorporated and unincorporated) is 107.305, they constitute 99 % of enterprises and employ 59,4 % of employees.

Slovenia is independent since 1991, member of the EU since 1 May, 2004 and member of EU Group since 1 January, 2007.

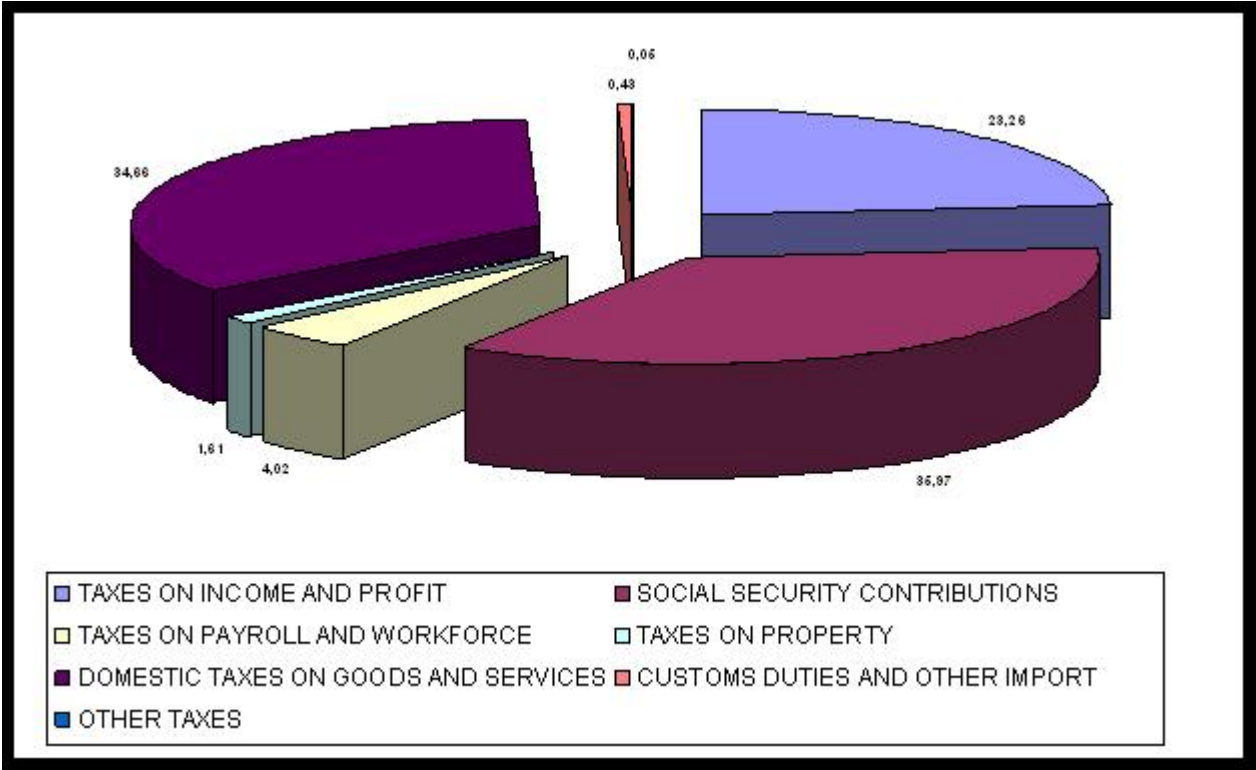
Tax Revenues Structure

Table: Tax revenues structure 2006

	in mio €	in %
taxes on income and profit	2.735,3	23,26
social security contributions	4.231,2	35,97
taxes on payroll and workforce	472,9	4,02
taxes on property	189,1	1,61
domestic taxes on goods and services	4.077,3	34,66
customs duties and other import	50,7	0,43
other taxes	5,4	0,05
Total tax revenues	11.762,0	100,00

Source: Bulletin of government finance

Graph: Tax revenues structure 2006



Tax Wedge

Table: Tax wedge for the average wedge in July 2007

	Average wedge in July 2007	IN % OF GROSS WAGE	IN % OF LABOUR COSTS
Gross wage	1.254	100,0	84,5
Employee's SSC	277	22,1	18,7

Allowances	233	18,6	15,7
Tax base	744	59,3	50,1
Tax rate	27%	0,0	0,0
Tax	138	11,0	9,3
Net wage	839	66,9	56,5
Employer's SSC	202	16,1	13,6
Payroll tax	29	2,3	1,9
Labour cost	1.485	118,4	100,0

Table: Structure of revenues from social security contribution

health fund	35,13
pension fund	63,82
social security contributions from state budget	1,05
TOTAL	100,00

TAX REFORM IN SLOVENIA - BASIC OBJECTIVES

Slovenia adopted tax reform package in 2006. It became effective on January 1, 2007 and consists of 7 tax acts: Personal Income Tax Act, Corporate Income Tax Act, Tax Procedures Act, Value Added Tax Act, Inheritance and Gift Tax Act, Immovable Property Transfer Tax Act, Act on Taxation of Vessels. Major changes were introduced in the field of personal income taxation, corporate income taxation and the tax procedures.

Tax reform was a part of a broader social and economic reform programme prepared by the Government already in 2005 and is a continuation of changes in tax legislation prepared in late 2004 and in 2005.

Major objectives were Lisbon strategy objectives, improvement of competitiveness of the Slovenian economy on international markets by alleviating administrative burden and decreasing level of taxation of labour, and protection of the sustainability of public revenues in the light of introduction of euro as national currency.

As administrative barriers are obstacles to entrepreneurship (aswell as to activities of all citizens) the tax reform package solutions were studied carefully in order to eliminate the barriers to the largest possible extent.¹ Besides eliminating the administrative barriers, there

¹ It is to be stressed that the Slovenian Government adopted in late 2005 the Programme of Elimination of Administrative Barriers. The Programme had been coordinated with all ministries, the Council for business-friendly administration and the Chambers of economy and crafts, taking into consideration also proposals from citizens and the interested public. The Government asked all implementing bodies (i.e. ministries and government services) to consider this Programme when preparing their regulatory and work programmes for 2006, 2007 and 2008. The Government entrusted the coordination and monitoring of the implementation of the Programme to the Ministry of Public Administration and asked it to prepare the first report on its implementation by 31 July 2007.

The objective of the Programme for Elimination of Administrative Barriers is to create a friendly and efficient administration and to regulate better the field of drafting and adopting regulations. It focuses on the following: simplification of procedures relating to urban planning and issuance of building permits, elimination of backlogs in solving complaints in tax matters, simplification of public procurement procedures, and drastic reduction in the number of activities for which a craft permit is required.

The Ministry of Public Administration has already introduced more than 50 simplifications, including:

are other tax factors that promote tax compliance, as will be seen further on (for example, the tax burden is lower, tax administration is more taxpayer oriented, etc.).

REASONS FOR ENCOURAGING COMPLIANCE

The result of informal economy is weakening of social welfare. Informal economic operators do not pay taxes and social security contributions, supply consumers with goods and services that are cheaper than those produced by formal economic operators, jeopardise health by omitting respective standards, exploit workers that are usually on social margin, etc. Therefore, informal economy erodes the tax base, shifts the tax burden to compliant taxpayers, distorts market competition and has other negative implications.

In accordance with Article 2 of the Constitution of Slovenia (hereinafter: the Constitution) Slovenia is a state governed by the rule of law and **a social state**. Right to social security, right to health care, rights of disabled persons, right to education and schooling are some of the basic rights guaranteed by the Constitution.

Right to social security (Article 50 of the Constitution): citizens have the right to social security, including the right to a pension, under conditions provided by law. The state regulates compulsory health, pension, disability and other social insurance, and ensures its proper functioning. Special protection in accordance with the law shall be guaranteed to war veterans and victims of war.

Right to health care (Article 51 of the Constitution): everyone has the right to health care under conditions provided by law, the rights to health care from public funds are provided by law, and no one may be compelled to undergo medical treatment except in cases provided by law.

Rights of Disabled Persons (Article 52 of the Constitution): disabled persons shall be guaranteed protection and work-training in accordance with the law. Physically or mentally handicapped children and other severely disabled persons have the right to education and training for an active life in society which shall be financed from public funds.

Right to education and schooling (Article 57 of the Constitution of Slovenia): freedom of education shall be guaranteed. Primary education is compulsory and shall be financed from public funds. The state shall create the opportunities for citizens to obtain a proper education.

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- one-stop procedure for the establishment of activity as self-employed persons,
 - elimination of double automobile documents (stickers and vehicle registration documents),
 - the possibility of accessing a series of services from any location and not only from the place of residence,
 - abolishment of certification by a notary public for a number of procedures,
 - extension of the period for the first technical examination of a new vehicle from three to four years,
 - reduction by half of projects that need to go through the lengthy and demanding process of environmental impact assessment,
 - possibility of on-line extension of driving permits,
 - shortly the Government will abolish the obligation for the founder of a company to register in the court register and then again in the tax register.

Details can be found on the:

<http://www.mju.gov.si/en/splosno/novice/news/article/14/5195/?cHash=bc8542332a>

Within the context of the principles and rights described above, contribution of economic operators to public finance revenues should be in line with their economic power.

Social security contributions

The role of the social security contributions and the implications on the informal economy mainly depends on the social history of the country. As can be seen from the principles and rights of the Constitution we have a strong system of the social insurance. The goal of the system is to include all permanent residents into social insurance net. Besides employed, also self-employed, including farmers, and others who are not insured by their status, are included in the system.

SMEs - reasons for non compliance

In general, there are two possible causes from the tax point of view why tax payers do not want to pay taxes:

1. taxes are for them too high (illegimate taxation)
2. administration of taxes is overcomplicated.

Sometimes taxpayers feel that taxes are so high that do not allow them to cover their and theirs family members living expenses. If it is true the legislation forces them to be out of the legal net or they hide their income.

At this point, in Slovenia we do not discuss problems of that kind. We tackle the administration of taxes on business income. The administration of taxes must take into account the following two points:

1. administrative costs of small economic unit can be relatively high compared to greater units,
2. small economic units are in most cases run by individuals with relatively low skills; complicated administrative structure of bookkeeping and reporting for tax purposes presents another obstacle for the inclusion into formal economy.

There are different methods how to solve the problem of administration of taxes but the main idea is that the taxpayers should not keep any books or in a very small extent if we take as a standard the **net basis for the taxation of business income**. Considering the starting points, the administrative burden should be in so many cases as possible transferred to the economic unit that can administer the taxes. At the same time taxes are being collected (an advantage for tax administration). This is a ratio behind the withholding tax on business income.

The way of Slovenia

The presentation will lead us through major solutions designed with the aim to proper treatment and thus encouragement of SMEs (as well as other taxpayers).

IDENTIFYING THE NEEDS OF SMES

The Slovene Chamber of Craft annually issues »Demands of Slovenian Craft and Entrepreneurship« which cover various fields, such as administrative requirements, stimulative business environment, taxation, labour market. It is very important for the

Government to consider the demands, discuss and explain the tax policy and administration issues - i.e. to run a dialogue with SMEs. Identifying the needs of SMEs (as well as other taxpayers) and responding to their proposals is a good practice for promoting compliance.

ENCOURAGING INFORMAL FIRMS INTO FORMAL ECONOMY – A POLICY MIX

Informal economy is a complex problem affected by various factors. Fight against informal economy must be endorsed by a policy mix, such as elimination of administrative barriers in the process of registration, issuing work permits, various licenses. Transparency in public finance (use of public finance, work of the government and its bodies) strengthens confidence in government and can be used as a tool to promote compliance. Better regulation helps to better understanding of sometimes complicated laws and regulations. From the tax policy and administration perspective proper tax treatment and taxpayer oriented tax administration play the key role.

TAX TREATMENT

Business income of individual taxpayers is subject to personal income tax.

Personal Income Tax (PIT) is divided into 2 parts:

- synthetic :
includes income from employment, business income (including agriculture and forestry), rental income, income from royalties and any other income
- schedular :
passive income.

As a general rule, the tax basis of business income of individual taxpayer is determined in accordance with the rules that apply to corporate income taxation as regulated by the Corporate Income Tax Act (accrual basis, book keeping compulsory). The tax installments that are paid during the tax year are based on the previous tax year base. As an exception to the general principle, small unincorporated business may choose a simplified tax treatment (special regime combined with compulsory withholding), subject to special conditions:

- the possibility of the withholding tax on business income is allowed if:
 - the revenues in the calendar year are less than 42.000 euros,
 - the unincorporated business does not employ any person,
 - cash basis accounting,
 - there are no book keeping requirements under regulations other than tax regulations, the expenses allowed are equal to 25% of the payment.

The withholding tax is 25%.

It is to be explained that one of the basic tax policy objectives of Slovenia is to bring as many taxpayers as possible under the tax net. The principle of a broad tax base is applied, recognising the possible overload of the administration by small unincorporated taxpayers. Slovenian tax policy has taken the possible overload of the administration into account since

1991 and Slovenian tax legislation has passed several different periods in which different models of taxation have been used. In the field of personal income taxation special measures tailored to small unincorporated business taxpayers have been introduced.

From 1991 to 2004 selected activities (artists, journalists, farmers, bee-keepers), were not obliged to keep accounting records, the tax basis was defined on cash basis; a lump sum of 40% on the account of the expenses was recognized. The tax was withheld at the rate of 25% on 60% basis.

The major change was done in the period from 2004 to 2006. The administrative requirements for small business were carefully studied. The tax policy choice was then to broaden the possibility of the withholding tax on business income but only under certain conditions. The result is the tax treatment that is described above.

I am primarily focusing on administrative procedures as a potential obstacle for compliance because in Slovenia we do not discuss the problem of a too high tax burden as a reason for informal economy. However, moderate tax burden combined with simplifications, taxpayer friendly administrative procedures and taxpayer oriented tax administration creates stimulating tax environment. Reshaping personal income taxation (less progressivity, number of brackets lowered, tax rates lowered in the higher income), and corporate income taxation (statutory tax rate gradually lowering from 23% in 2007 to 20% in 2010, withholding taxes lowered from 25% to 15%), other solutions in the field of income taxation, and improving administration of taxes are by no doubt factors that we can count on in tackling informal economy.

Slovenia introduced dual income taxation in 2005, effective from January 1, 2006 (active income taxed progressively on a synthetic basis, passive income - schedular taxation).

Personal income tax rates:

YEAR 2006		YEAR 2007	
Tax bracket	% of taxpayers	Tax bracket	% of taxpayers
16 %	62,43	16 %	71,12
33 %	24,09	27 %	19,95
37 %	10,31	41 %	8,93
41 %	2,57		
50 %	0,60		

Basic personal income tax allowance was raised from 2522 EUR to 2800 EUR, allowance for various purposes was abolished.

Schedular system of passive income taxation is as follows:

- interest: tax rate 15% in 2007, and 20% afterwards (interest on savings deposits in banks in EU are tax exempt up to 1.000 euros)

- dividends: tax rate 20%

- capital gains: The tax rate for capital gains depends on the holding period: 20% for a holding period of up to 5 years, 15% for a holding period from 5 to 10 years, 10% for a holding period from 10 to 15 years, 5% for a holding period from 15 to 20 years and 0% for a holding period longer than 20 years. The alienation of residential property, if the holding period is more than 3 years, is tax exempt.

In the field of **corporate income taxation (Corporate Income Tax Act (CIT))**, statutory tax rate is very moderate, 23% in 2007, 22 % in 2008, 21% in 2009, 20% in 2010, loss carry forward is allowed without time limitations, determination of revenue and expenses in principle follows commercial accounting rules (exceptions regulated by the Corporate Income Tax Act, reporting by the Tax Procedures Act).

As a rule, determination of the tax base as prescribed by the CIT is also applied to determination of the tax base of individual business income.

Administrative burden of SMEs has been relaxed with respect to the transfer pricing documentation requirements.

Payroll tax is being under the process of gradual elimination. It will be finally eliminated per January 1, 2009.

Value Added Tax

A taxable person must apply for registration as a taxable person if the value of its supplies within the period of the last 12 months exceeds the threshold of EUR 25,000. There is separate threshold for registration in the VAT system for agricultural activities exceeding EUR 7,500 in accordance with the cadastral income of agricultural and forestry land. Small businesses (including farmers) may apply for voluntary registration, which should be valid for at least a five-year period.

Simplifications, taxpayer friendly procedures

In addition to the simplified taxation of small unincorporated individuals as described previously, presumptive costs of 70% of the revenues are allowed to individual taxpayers with respect to their agricultural and forestry activity, supplementary activities on a farm and for production of home craft and applied art products.

A new procedure, well established in developed tax environments, advance ruling, has been established with the new Tax Procedure Act.

Furthermore, a new procedural option, self-declaration of tax liabilities, was envisaged with the objective of promoting voluntary compliance with tax obligations.

E-business is promoted in all fields of communication between taxpayers and the Tax Authority.

Declaration of personal income for tax purposes will no longer be necessary, due to a pre-completed form that the Tax Authority will send to taxpayers. The possibility of installment payments of the tax liability has improved.

The tax return can subsequently be changed in the case of error.

Tax Administration

Good tax administration is taxpayer oriented, efficient, transparent in performing its functions and responsibilities and using public funds, and treats taxpayers equally. In the case of Slovenia, the Slovenian Tax Administration's website is becoming important way of communication with the public, information on new tax laws and regulations is regularly provided to the public, explanations of the laws and regulations and taxpayers rights and obligations are provided to the taxpayers. Tax Administration also publishes its annual report where it makes public the data on collected taxes and other revenues, performing its tasks, professional qualifications and technical equipment, expenditure of the Tax Administration and supervision over Tax Administration work.. The Tax Administration is devoting its resources to detection and prevention of informal economy and submits tax assessments in the case of unreported income.

E-VEM (E - One Stop Shop)

E - one stop shop system in Slovenia enables individual entrepreneur to register (business register, tax register) via an e - entering point, identify for VAT, etc.

DETECTION AND PREVENTION OF INFORMAL ECONOMY (EMPLOYMENT)

In Slovenia, prevention of illegal work and employment is regulated by the Prevention of Illegal Work and Employment Act (Official Gazette of the Republic of Slovenia, No. 36/2000, 118/06. Supervisory bodies are Labour Inspectorate, Market Inspectorate, Transport Inspectorate and Tax Administration.

Coordination of activities is provided for by the Government Commission. With reference to the Commission's 2005 Annual Report ², industries where the extent of informal employment increased, were construction, pubs, trade, passenger and cargo transport, security, driving instruction, economic activities of associations. Also baby-sitting, giving instructions, cleaning are activities that are often run informally.

CONCLUSION

² Source:

http://www.mddsz.gov.si/fileadmin/mddsz.gov.si/pageuploads/dokumenti__pdf/delo_crno_porocilo05_ess.pdf

The tax system itself is not the only factor influencing informal economy. Different policies in coordination are a way forward. Countries should support education of citizens, taxpayers and consumers.