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PFM LAC Strengthening Public Financial Management in LAC

Peru

Summary

- Tax revenues in Peru increased by 2.8% of GDP between 2003 and 2012. Revenues from taxes on income and profits nearly doubled as a percentage of GDP over the period, increasing from 4% to 7.5%, but were offset slightly by a decreased reliance on tax revenue from international trade. The increase in total tax revenue is attributed to strong economic growth and improved tax policy and administration over the period.
- A recent study[1] found Peru's tax effort[2] to be moderately below that of other countries in Latin America and the Caribbean (LAC). Peru's tax effort was 53.4% of tax capacity, whereas the average of the surveyed LAC countries was 61.1%. Peru's tax capacity, at 28.7% of GDP, was slightly below the average tax capacity of surveyed LAC countries, at 33.5%.
- Personal income tax effort and productivity figures in Peru are significantly below regional, income group, and world averages. The personal income tax rate is slightly above the regional, income group, and world averages.
- Peru's corporate income tax effort and productivity figures are above regional, income group, and world averages. The corporate income tax rate is slightly above the regional average and well above the income group and world averages.
- Peru's value added tax (VAT) effort is slightly above that of the regional, income group, and world averages. Productivity figures are below the comparators. The VAT rate is significantly above the regional, income group, and world averages.
- Suggested areas for further investigation include:
  - The low productivity figures from the personal income tax,
  - The impacts of the administrative reforms of 2012.

[1] Pessino, Carola and Ricardo Fenochietto (2010), "Determining countries' tax effort", *Hacienda Pública Española / Revista de Economía Pública*, 195-(4/2010): 65-87, Instituto de Estudios Fiscales. "Tax capacity" is the maximum tax revenue that can be generated given the country's economic, social, institutional, and demographic characteristics. "Tax effort" is the ratio of actual revenue to tax capacity.

[2] The definition of "tax effort" employed in the aforementioned study differs than the definition of revenue effort employed further below in this paper.

Major Developments and Features of Current Tax System

Evolution of Revenue

Peru's total tax revenue increased by 2.8% of GDP between 2003 and 2012. Over the period, the composition of revenue has changed significantly to reflect an increased reliance on taxes on income and profits, and from other taxes,[3] and a decreased reliance on revenue from international trade. Taxes on goods and services remained relatively stable over the period. Total revenue suffered a sharp decline after the 2008 financial crisis, declining by 2% in 2009; however, revenue figures have been increasing steadily since.

- Revenue from taxes on income and profits increased by 3.5% of GDP over the period.
- Revenue from taxes on goods and services decreased by 0.2% of GDP.
- Revenue from taxes on international trade decreased by 0.9% of GDP.
- Revenue from other taxes increased by 0.3% of GDP.

Peru Government Current Revenue
(% of GDP)

	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Taxes on Income & Profits	4.0%	4.0%	4.7%	6.5%	7.2%	7.0%	5.8%	6.4%	7.4%	7.5%
Taxes on Goods and Services	7.4%	7.3%	7.0%	7.1%	7.0%	7.4%	6.8%	7.3%	7.2%	7.2%
Taxes on International Trade	1.2%	1.2%	1.2%	0.9%	0.7%	0.5%	0.4%	0.4%	0.3%	0.3%
Other Taxes	0.4%	0.4%	0.4%	0.4%	0.3%	0.3%	0.4%	0.4%	0.4%	0.7%
Total Tax Revenue	**12.9%**	**13.1%**	**13.6%**	**15.2%**	**15.6%**	**15.6%**	**13.6%**	**14.7%**	**15.3%**	**15.7%**

Source: Economic Comission for Latin America and the Caribbean, CEPALSTAT

Summary of Reforms

Peru has benefitted significantly from strong economic growth and the rise in the banking, manufacturing, and mining sectors, which has accounted for a considerable share of collected taxes over the past decade. Tax reform efforts have focused on increasing transparency, enhancing the taxpayer registration system, simplifying procedures, and rationalizing tax rates.

- In 2002, Peru underwent a major decentralization reform, which divided the country into macro regions with regional governments and limited taxing authority to the central government and municipalities.[4]
- In 2004, the Mining Royalties Law introduced a monthly royalty assessed on the value of the mining extract. The law was then amended to permit revenue from royalties to be

[3] Other taxes includes primarily revenue from taxes levied on bases other than the ones described in other categories or revenues that cannot be attributed to a single tax category. According to IMF's Government Finance Statistics Manual 2001, examples include taxes on persons that are not based on income (e.g., "head" taxes) and stamp duties that do not apply primarily to a single class of transactions or activities covered by the other tax categories (http://www.imf.org/external/pubs/ft/gfs/manual/pdf/all.pdf).
[4] Bustad, Erik, and Glimeus, Linn, Evaluating Fiscal Decentralization in Peru, Lund University, 2011.

distributed to provinces and municipalities. Later in the same year, a new Mining Tax was introduced that applied progressive rates (between 1-3%) on operational profit.[5]

- In 2006, a new Single Simplified Regime was adopted, allowing micro and small-sized enterprises to remit tax on a monthly basis according to their tax bracket based on gross income. The new regime simplified the taxation system and replaced both the income and VAT tax for small businesses.[6]
- In an effort to promote industry growth, three new laws were passed in 2008-09. The laws permitted accelerated depreciation on renewable energy products, petrochemical plants, and new buildings.
- In 2010, a new 5% flat tax was introduced to standardize capital gains taxes for local and foreign investors.
- In 2010 and 2011, various tax rates were adjusted. The VAT rate was lowered by one percentage point from 19% to 18%. The tax on financial transactions was lowered first from 0.06% to 0.05%, and then to 0.005%. Customs duty rates were lowered from 8% to 6.5%, and tariffs were lowered for over 3,000 items, reducing the average tariff rate to 3.4%.[7] A fuel excise tax was also introduced, while the tax on natural gas was lowered.[8]
- In 2011, three additional laws aimed at increasing tax revenues from mining companies were passed, expected to increase tax revenues by $5.5 billion in five years.[9]
- In June 2012, the government enacted a broad tax reform package focused on strengthening compliance and enforcement. Administrative measures included granting tax authorities the power to initiate partial tax audits to examine specific aspects of a taxpayer's tax liability and introducing harsher penalties for customs and tax law infractions.[10]
- The 2012 reform also abolished tax exemptions on interest and capital gains, and expanded the withholding tax to include dividends.[11] The 2012 reform also tightened transfer-pricing rules and introduced tax rules for foreign-owned companies.

Tax System Profile (2010-11)

The tables in Annex 1 provide a high-level description of Peru's tax system and draw comparisons with the Latin America and Caribbean (LAC) region, upper-middle-income (UMI) countries,[12] and the rest of the world. The data in this section are from the 2012-2013 release of

[5] KPMG Peru Country Mining Guide, 2013. http://www.kpmg.com/Ca/en/industry/Mining/Documents/Peru.pdf
[6] Inter-American Development Bank, Recommendations and Best Practices on Taxation of SMEs in Latin America.
[7] Economic Survey of Latin America and the Caribbean 2010-2011, Peru. http://www.eclac.org/publicaciones/xml/2/43992/1-2011_Peru.pdf
[8] Comisión Económica para América Latina (2013), Fiscal Panorama of Latin America and the Caribbean, http://www.eclac.org/publicaciones/xml/7/49287/2013-106_Fiscal_Panorama_WEB.pdf.
[9] KPMG Peru Country Mining Guide, 2013.
[10] Deloitte Global Services Limited 2012. World Tax Advisor. Peru: Broad Tax Reform Package Enacted. August 24, 2012. http://newsletters.usdbriefs.com/2012/Tax/WTA/120824_6.pdf
[11] CEPAL 2013, Fiscal Panorama of Latin America and the Caribbean.
[12] Derived from the World Bank's Country and Lending Group classifications, http://data.worldbank.org/about/country-classifications/country-and-lending-groups.

USAID's Collecting Taxes database.[13] **The most recent comparative data in this section are from fiscal year 2011, and do not reflect the most recent reforms or data discussed above.**

Revenue Effort

- "Revenue Effort" is the amount of revenue as a share of GDP.
- Peru's overall tax revenue effort, at 15.8%, is below the world average of 17.9%, and well below the LAC regional and income group comparator averages of 19.5% and 19.4%, respectively.
- Peru's revenue effort from personal income tax, at 1.7%, is significantly below – less than one half – that of the LAC regional, income group, and world averages of 4.1%, 4.8%, and 5.5%, respectively.
- Corporate income tax revenue effort, at 5.2% of GDP, is well above all corresponding comparator averages, which are in the 3.3% to 3.7% range.
- The revenue effort from VAT, at 6.6%, is in line with the LAC regional and income group averages of 6.4% and slightly above the world average of 6.1%.

Tax Structure

- The maximum personal income tax rate in Peru, at 30%, is above the LAC regional, income group, and world averages, which are in the 24% to 28% range.
- Peru's corporate income tax rate, at 30%, is above the LAC regional average of 27.2%, and significantly above the income group and world averages of 23.5% and 24.1%, respectively.
- The VAT rate, at 18%, is well above the regional, income group, and world averages, which are in the 13.5% to 14% range.
- The tax wedge on labor income, at 22.6%, is in line with the regional, income group, and world averages, which range between 20% and 24%.

Revenue Productivity

- "Revenue productivity" measures the revenue share of GDP mobilized for each point of the tax rate.
- Personal income tax productivity, at 0.06, is significantly below the LAC regional, income group, and world averages of 0.15, 0.23, and 0.22 respectively.
- Corporate income tax productivity, at 0.17, is slightly above the regional, income group, and world averages, which are 0.15, 0.16, and 0.15.
- VAT productivity, at 0.37, is below the regional, income group, and world averages of 0.47, 0.45, and 0.42, respectively.

[13] USAID's Collecting Taxes Database, http://egateg.usaid.gov/collecting-taxes.

Tax Administration Structure

- The *Superintendencia Nacional de Aduanas y de Administración Tributaria* (SUNAT) is responsible for the administration of all taxes in Peru. SUNAT operates as a semi-autonomous revenue authority under the Ministry of Finance. In 2002, SUNAT absorbed the National Customs Superintendency, which administers taxes on international trade.
- Tax administration in Peru is organized along functional lines and includes a Large Taxpayer Unit (LTU).
- SUNAT's ratio of active taxpayers to staff, at 691 taxpayers per staff, is above the income group average of 589 taxpayers per staff, and in line with the world average of 677. It remains significantly below the LAC regional average of 982.

Taxpayer Burden and Corruption Evidence

- The 2010 World Bank Enterprise Surveys indicated that the percentage of Peru business taxpayers "expected to give gifts in meeting with tax officials" was 8.4%, which was slightly above the LAC regional average of 6.1%, but significantly below the world average of 14.1%.
- The 2014 World Bank Doing Business survey estimates that the average time to pay taxes expended by a medium-sized company in Peru amounted to 293 hours per year, which is below the LAC regional average of 369 hours, and broadly in line with the world average of 285 hours per year. Peru has improved significantly from its 2009 average of 424 hours per year.

ANNEX 1: Peru's Collecting Taxes Indicators

Total Tax Revenue	**TAXY**[14]
	Tax Revenue as % of GDP (%)
Peru	15.8
Latin America and the Caribbean[1]	19.5
Upper-Middle-Income Economies[2]	19.4
World	17.9

Company Income Tax	**CITR**	**CITY**	**CITPROD**
	Tax Rate (%)	**Revenue as % GDP (%)**	**Revenue Productivity**
Peru	30.0	5.2	0.17
Latin America and the Caribbean[1]	27.2	3.7	0.15
Upper-Middle-Income Economies[2]	23.5	3.7	0.16
World	24.1	3.3	0.15

Income Taxes on People	**PITMINR**	**PITMAXR**	**PITMINL**	**PITMAXL**
	Minimum Tax Rate (%)	**Maximum Tax Rate (%)**	**Minimum Income Level (Multiples of GDP per capita)**	**Maximum Income Level (Multiple of GDP per capita)**
Peru	15.0	30.0	0.00	7.10
Latin America and the Caribbean[1]	13.4	27.5	0.52	3.58
Upper-Middle-Income Economies[2]	11.5	24.2	0.29	2.63
World	10.9	27.8	0.40	6.38

[14] A glossary of terms for the selected indicators is found in Annex 2.

Personal Income Tax	PITY	PITPROD	SSR	WEDGE
	Revenue as % GDP (%)	Revenue Productivity	Mandatory Combined Social Contribution Rates (%)	Combined Rate of Personal and Labor Taxation (%)
Peru	1.7	0.06	22.6	22.6
Latin America and the Caribbean[1]	4.1	0.15	17.1	20.1
Upper-Middle-Income Economies[2]	4.8	0.23	22.2	24.1
World	5.5	0.22	20.8	22.4

Value Added Tax	VATR	VATY	VATGCR	VATPROD	THRESHOLD
	VAT rate (%)	Revenue as % GDP (%)	Gross Compliance Ratio (%)	Revenue Productivity	Mandatory registration/ filing (annual turnover in USD)
Peru	18.0	6.6	57.4	0.35	N/A
Latin America and the Caribbean[1]	13.5	6.4	66.2	0.47	34,149
Upper-Middle-Income Economies[2]	13.7	6.4	69.8	0.45	61,098
World	13.8	6.1	65.9	0.42	57,598

Tax Administration	Tax Staff	Payer to Staff	Function	LTU	Customs
	Tax staff per 1000 population	Number of tax payers per tax staff	Functional Organization (1 = Yes, 0 = No)	Large Taxpayer Unit (1 = Yes, 0 = No)	Customs and Tax Administration Combined (1 = Yes, 0 = No)
Peru	0.25	691	1.00	1.00	1.00
Latin America and the Caribbean[1]	0.33	982	0.80	0.78	0.30
Upper-Middle-Income Economies[2]	0.57	589	0.88	0.82	0.37
World	0.65	677	0.88	0.81	0.30

Footnotes:

1. LAC countries include: Anguilla, Antigua and Barbuda, Argentina, Bahamas, Barbados, Belize, Bermuda, Bolivia, Brazil, Chile, Colombia, Costa Rica, Cuba, Dominica, Dominican Republic, Ecuador, El Salvador, Grenada, Guatemala, Guyana, Haiti, Honduras, Jamaica, Mexico, Nicaragua, Panama, Paraguay, Peru, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, Suriname, Trinidad and Tobago, Uruguay, and Venezuela.
2. Upper-Middle-Income Countries include: Albania, Algeria, Angola, Azerbaijan, Belarus, Belize, Bosnia and Herzegovina, Botswana, Brazil, Bulgaria, China, Colombia, Costa Rica, Cuba, Dominica, Dominican Republic, Ecuador, Fiji, Gabon, Grenada, Hungary, Iran, Iraq, Jamaica, Jordan, Kazakhstan, Lebanon, Libya, Macedonia, Malaysia, Maldives, Marshall Islands, Mauritius, Mexico, Montenegro, Namibia, Palau, Panama, Peru, Romania, Serbia, Seychelles, South Africa, St. Lucia, St. Vincent and the Grenadines, Suriname, Thailand, Tunisia, Turkey, Turkmenistan, and Venezuela.

ANNEX 2: Collecting Taxes Indicators Glossary

CITR is the general rate applied for the corporate income tax. In most countries, only one corporate income tax is applied to corporate profits. In most countries, business enterprises that are owned by sole proprietors or unincorporated partnerships pay tax under the personal income tax system.

CITY is the level of corporate income tax collections as percentage of GDP.

CITPROD represents how well the corporate income tax does in terms of revenue collection, given the tax rate. CITPROD is the portion of GDP in revenue that is mobilized for each point of CIT rate.

PITMINR is the lowest non-zero positive tax rate applied to the lowest income group in the personal income tax system.

PITMINL is the lowest level of income at which the lowest marginal personal income tax rate (PITMINR) is imposed, expressed as a multiple of per capita GDP.

PITMAXR is the highest tax rate applied under the personal income tax system.

PITMAXL is the lowest level of income at which the top marginal personal income tax rate is imposed, expressed as a multiple of per capita GDP.

PITY is the level of personal income tax collections as percentage of GDP.

PITPROD provides an indication of how well the personal income tax in a country does in terms of producing revenue. PITPROD is the portion of GDP in revenue that is mobilized for each point of the average PIT rate.

SSR is the combined rate for employer and employee social security contributions.

WEDGE is an estimate of the overall taxation of labor income, represented as a percentage of gross salary. It combines social contributions with personal income tax. The tax wedge represents the ratio of total labor taxes to total labor costs to the employee.

VATR is the general rate at which most goods and services are taxed under the value added tax system. Most countries have a variety of reduced rates for certain basic goods, such as basic food stuffs. Also, all countries have a zero rate on exported goods.

VATY is the level of VAT collections as a percentage of GDP.

VATGCR is the VAT gross compliance ratio which is the ratio of potential VAT collections—if all final household consumption had been taxed at the standard rate--to actual VAT collections.

VATPROD is a measure of how well the VAT produces revenue for the government, given the VAT rate. It is the portion of GDP in revenue that is mobilized for each point of VAT rate.

Threshold indicates the amount of annual turnover, in US $ terms above which taxpayers must register for VAT and file regular VAT returns.

Functional Organization is a binary indicator where 1 indicates that the tax administration is organized along functional lines.

Large Taxpayer Unit is a binary indicator where 1 indicates that there is a large taxpayers unit.

Customs and Tax Administration Combined is a binary indicator where 1 indicates that revenue is administered jointly by a single customs and tax administration.

Peru Highlights

Currency: Nuevo Sol (PEN). Peru also uses the "tax unit", a figure set annually by the tax authorities to determine applicable rates and deductions, among other uses.

Foreign exchange control: No restrictions are imposed on the import or export of capital. Funds may be repatriated in any currency, and both residents and nonresidents can hold bank accounts in any currency.

Accounting principles/financial statements: IAS/IFRS. Financial statements must be prepared annually.

Principal business entities: These are the corporation, closed corporation, public corporation, limited liability company and branch of a foreign company.

Corporate taxation:

Residence – An entity is considered domiciled for tax purposes if it is incorporated in Peru.

Basis – Domiciled corporations are taxed on worldwide income. Non-domiciled corporations and branches of foreign entities are taxed only on Peruvian-source income. Foreign-source income derived by residents is subject to corporation tax in the same way as Peruvian-source income, but it is calculated separately. Branches are taxed at the corporation tax rate, plus a remittance tax. Subsidiaries are taxed at the normal corporation tax rate.

Taxable income – Taxable income is comprised of all profits derived by a company, including capital gains. Normal business expenses may be deducted in computing taxable income.

Taxation of dividends – Dividend distributions between resident entities are not taxed. Foreign dividends received by a Peruvian entity are included in taxable income and subject to the normal corporate tax rate, but with a tax credit for foreign tax paid on the dividends. Dividends and other profit distributions, as well as a branch remittance of net profits abroad, are subject to a 4.1% withholding tax when paid to resident and nonresident individuals and nonresident entities.

Capital gains – Capital gains are generally included as income and taxed at the normal corporate rate.

Losses – A taxpayer has the option to carry forward all net operating losses for 4 years or carry the losses forward indefinitely, but only up to 50% of the taxpayer's taxable income of each subsequent year. Loss carryback is not permitted.

Rate – 30%

Surtax – No

Alternative minimum tax – No

Foreign tax credit – A tax credit is available for income tax paid on foreign-source income equal to the actual foreign tax paid or the Peruvian tax liability on the income, whichever is less. Excess credits may not be carried forward.

Participation exemption – No

Holding company regime – No

Incentives – Investors in large mining and oil or gas operations may conclude tax law stability agreements with the government for periods of 10 to 15 years.

Withholding tax:

Dividends – Dividends paid to nonresident entities (companies) and to resident and nonresident individuals are subject to a 4.1% withholding tax.

Interest – Interest payments to a nonresident related party that satisfies certain requirement are subject to a 4.99% withholding tax; otherwise, the rate is 30%.

Royalties – Royalties paid by a Peruvian resident are considered Peruvian-source income and, consequently, subject to a 30% withholding tax.

Branch remittance tax – The remittance of net profits abroad is subject to a 4.1% withholding tax. Branches of foreign companies are subject to the 30% standard rate of corporate income tax, plus the 4.1% tax on the remittance.

Other taxes on corporations:

Capital duty – No

Payroll tax – No

Real property tax – The municipal authorities levy real estate property tax at progressive tax rates of 0.2%, 0.6% and 1%, depending on the value of the property. The tax is a deductible expense for income tax purposes.

Social security – An employer pays a 9% social security contribution for its employees.

Stamp duty – No

Transfer tax – The transfer of buildings (real estate property) are subject to a 3% transfer tax, with the first 10 tax units being exempt.

Other – A Temporary Net Assets Tax (TNAT) is imposed on the value of total assets exceeding PEN 1 million at a rate of 0.4%. A "Financial Transactions Tax" is imposed primarily on debit and credit transactions with Peruvian bank accounts at a rate of 0.05% before (0.005% from) 1 April 2011.

Anti-avoidance rules:

Transfer pricing – Transactions between related parties or between a Peruvian person and an entity in a tax haven jurisdiction must be carried out at arm's length prices. If the price agreed upon is not arm's length, the tax authorities may adjust the price. Jurisdictions that are deemed to be tax havens are set out in a list issued by the tax authorities. Transfer pricing documentation is required.

Thin capitalisation – Interest paid by resident taxpayers to economically related or associated enterprises may not be deducted if a debt-to-equity ratio of 3:1 is exceeded. However, the interest is not recharacterised as a dividend.

Controlled foreign companies – No

Other – A transaction that exceeds USD 1,000 must be paid via check or other means of verifiable payment.

Disclosure requirements –No, other than transfer pricing documentation.

Administration and compliance:

Tax year – Calendar year

Consolidated returns – No

Filing requirements – Companies are required to make 9 monthly advance payments of income tax based on a percentage of net assets (TNAT) and 12 payments on account based on monthly taxable income. An annual self-assessment tax return must be filed, and final tax must be paid by the first week in April following the end of the tax year.

Penalties – Penalties apply for late filing or failure to file.

Rulings – No

Personal taxation:

Basis – Residents are taxed on worldwide income and nonresidents are taxed only on Peruvian-source income.

Residence – Peruvian individuals living in the country and foreign individuals who are in Peru for more than 183 calendar days in any 12-month period are deemed to be resident for tax purposes. All individuals who qualify as resident on 1 January are subject to income tax for that fiscal year; any changes in residence status after that date will take effect for the next fiscal year.

Filing status – Spouses can choose which spouse will file the return.

Taxable income – Taxable income is divided into specific categories: labour income (derived from employment), income from independent personal services) and capital income (interest, royalties, capital gains and income from the leasing of assets). Business income earned by an individual is subject to the corporate tax regime.

Capital gains – Capital gains are taxed at a rate of 6.25%. Gains derived by nonresident individuals from the transfer of securities outside the country are taxed at a 30% rate. Transfers in Peru are taxed at a 5% rate. Gains derived by nonresident individuals from the transfer of real property are taxed at a 30% rate.

Deductions and allowances – An individual is allowed a deduction from capital income and labour income.

Rates – Progressive rates apply to employment income according to the following schedule: 15% up to the first 27 tax units, 21% for 27-54 tax units and 30% on the excess. Nonresident individuals are subject to different rates depending on the type of income. Capital gains tax is levied at a flat rate of 6.25%.

Other taxes on individuals:

Capital duty – No

Stamp duty – No

Capital acquisitions tax – No

Real property tax – Tax is imposed on the total value of real property owned by a person.

Inheritance/estate tax – No

Net wealth/net worth tax – No

Social security – Only the employer is required to contribute. The employer pays a 9% social security contribution for its employees.

Administration and compliance:

Tax year – Calendar year

Filing and payment – An annual income tax return must be filed within 3 months of the end of the tax year.

Penalties – Penalties apply for late filling or failure to file.

Value added tax:

Taxable transactions – VAT is levied on the sale of goods, the provision and use of services, the first sale of real estate by a contractor and imports.

Rates – 18% (reduced from 19%) effective 1 March 2011.

Registration – Taxpayers are required to keep accounting books (such as purchase and sales books).

Filing and payment – VAT returns must be filed on a monthly basis.

Source of tax law:
Income Tax Law, VAT Law

Tax treaties:
Peru has 3 bilateral agreements (Canada, Chile, Brazil) and an agreement with the Andean Community (Colombia, Ecuador and Bolivia).

Tax authorities:
Tax Administration (SUNAT), Tax Court (Tribunal Fiscal)

International organisations:
Andean Community

SOURCE: Deloitte International Tax Source: Tax Highlights, http://www.deloitte.com/taxguides.