INNOVATIONS FOR SUCCESSFUL SOCIETIES

KEEPING UP GROWTH: BUILDING A MODERN TAX ADMINISTRATION IN VIETNAM, 2004–2015

SYNOPSIS

As Vietnam gradually became a middle-income country during the early 2000s, its tax agency struggled to keep up. In the decade and a half following the Communist Party–led government's 1986 decision to establish a market-based economy, local entrepreneurs launched businesses, foreign investors poured into the country, and the average annual rate of economic growth soared to 7.5%. But during the same period, tax revenues declined as the General Department of Taxation (GDT), which previously collected almost all of the country's taxes from a small group of state-owned enterprises, strove to keep pace with the economic dynamism. In 2004, the department established an internal reform team and adopted a strategy to make sure those who could pay covered their fair share of the cost of government services. The GDT worked with the finance ministry's tax policy department and the parliament to implement a raft of legal changes. The department then reorganized each of its 758 tax offices along functional lines, rolled out a new IT system, improved staff training, and created a unit to bolster taxpayer compliance. It later adopted a personal income tax and tried—sometimes unsuccessfully—to close exemptions created earlier to attract foreign investors. Although its collection levels began to plateau after 2010, in the decade or so from 2004 to 2015 the GDT increased the number of registered taxpayers in the country to 15 million from 2 million and tripled the amount of taxes it collected annually, maintaining one of the highest tax-to-GDP ratios in East Asia.

Leon Schreiber drafted this case study on the basis of interviews conducted in Hanoi, Vietnam in May 2018. Case published in August 2018.

INTRODUCTION

From 1990 to 2000, Vietnam's economy more than doubled in size. The boom resulted from the Vietnamese government's 1986 decision to rescind a ban on private enterprise and introduce a package of reforms called Doi Moi (Renovation), in response to food shortages and runaway price inflation. The ruling Communist Party's decision to liberalize its economy opened the door to foreign investment—and domestic businesses prospered as well.

Although the Doi Moi reforms rescued the country's 80 million people from an economic and social crisis and spurred an average annual GDP growth of 7.5% in the 15 years that followed, the introduction of private enterprise also posed a weighty challenge for the country's General Department of Taxation (GDT). Created in 1990 as a department within the finance ministry, the GDT was charged with collecting all domestic taxes in Vietnam. (A separate customs department handled trade taxes.)

By the early 2000s, the government was deeply worried about the GDT. Even as the country's economy grew, the office collected less revenue. By 2000, total taxes collected by the GDT had declined to $5.8 billion from $6.3 billion in 1996, thereby lowering the country's tax-to-GDP ratio to 14.8% from 18.5%. Originally designed to collect revenues from a handful of state-owned enterprises in a tightly centralized economy, the GDT was simply not geared to interact with millions of taxpayers operating in a vibrant private economy. "Vietnam's tax administration in that period relied on traditional experience. [The systems] were not really methodical, advanced or compatible with international standards…One officer [each] was assigned to deal with specific [state-owned] enterprises," said Le Hong Hai, who joined the GDT in 1991 and rose to the rank of deputy director general in 2006.

Tax officials personally visited each of the country's taxpayers to calculate the taxes they owed, under a system known as *administrative assessment*. Even though this old model worked well when Vietnam had only about 1,000 taxpayers in the early 1990s, the model became increasingly impractical as the total number of taxpayers rose. The department projected that this number would skyrocket to more than 2 million by the mid 2000s.[1] "As the economy grew…We realized that it was not appropriate to [use the same model] for the private sector [that the GDT previously used for a centralized economy]. The number, size, scope, type and mode of businesses increased rapidly. [At the same time], tax administration was not based on the collection, analysis and assessment of taxpayers' data to classify and select risk management modalities that [were tailored to the] characteristics of [different] types of taxpayers," Hai said.

The pressure on the GDT mounted when the government adopted its 2001–2010 strategy for socioeconomic development, which aimed to boost investment in public services.[2] To help finance the government's spending plans, the new strategy therefore aimed "to modernize the state's tax collection and enhance its tax administration."[3]

The prospect of lower trade tariffs under a bilateral trade deal with the United States, which came into force in 2001, as well as the government's stated aim of joining the World Trade Organization (a goal it achieved in January 2007), amplified the pressure on the Vietnamese tax system to make up for lost customs revenues and conform with international standards.

At the beginning of 2004, the GDT's director general, Nguyen Van Ninh, appointed Hai to lead an internal GDT reform team charged with exploring ways to modernize Vietnam's tax system.

THE CHALLENGE

Before the reform team could begin work to improve the GDT's operations, the country's legislature, the National Assembly, took a hard look at Vietnam's tax policy framework. Although the legislature had replaced an ineffective general sales tax with a value-added tax (VAT) and created a corporate income tax in 1999, Vietnam still had a narrow tax base. There was no tax on personal income, and the GDT collected only a wealth tax on a small group of high-income earners.

Under existing laws, the GDT had no authority to issue a single identification number that taxpayers could use for all tax types. Taxpayers had to consult with different officials to register and pay for each type of tax separately, and the lack of a single set of identification numbers made it nearly impossible to maintain a single profile for each payer. To lay the foundation for reform, the GDT had to work with the finance ministry and the parliament to modernize the country's out-of-step policy framework.

Hai's team also had to address several serious organizational problems, the most pressing one of which was that the GDT neither trusted taxpayers to compute what they owed nor had the legal authority to empower individuals or companies to conduct self-assessments. As a result, tax officials were required to visit every payer, examine the payer's financial records, and calculate taxes due. And although the model was workable when the tax base was small, it was no way to administer a system for millions of new taxpayers.

The GDT's organizational structure was also fractured along tax types, with different units responsible for administering different taxes. Because each unit also issued its own identification numbers, it was nearly impossible to accurately track compliance or develop a complete picture of each taxpayer's affairs. A further complication was that each tax type had its own set of administrative procedures, and the GDT had no standard process for calculating penalties or identifying which taxpayers had to be audited. As a result, businesses made an average of 32 payments and spent 1,050 hours per year on complying with tax requirements.[4] Those figures compared poorly with neighboring Cambodia's averages of 27 payments and 121 hours and Laos's 31 payments and 180 hours.[5]

The Vietnamese GDT's lack of a central information database aggravated the organizational fragmentation. The tax office had a paper-based filing system, but "the paperwork was piling up," said Pham Minh Duc, a World Bank senior economist who worked closely with the GDT's reform team. "The number of registered enterprises alone quickly increased to 10,000, and tax administration was becoming so complicated that you couldn't manage without a more sophisticated IT system." The situation required an integrated system with modern database software.

Lack of staff capacity imposed another constraint on effectiveness. The headquarters in the capital city, Hanoi, which oversaw operations at the 63 provincial and 659 district tax offices, was understaffed; and the tax office had no standard training regimen. Only 10 to 15% of tax officials were trained to conduct tax audits.[6] Although, according to Dang Ngoc Minh, the deputy director general for international taxation and cooperation, the GDT's salaries were double those of other public officials, only 44.7% of the GDT's 44,000 staff members possessed university-level qualifications in 2006.[7]

The GDT further lacked the expertise needed to create and analyze strategic forecasts of revenues from different groups of taxpayers or assess compliance trends. The World Bank reported that "projections for the following year are primarily based on the growth rate of revenues during the current year, adjusted after consultations with line ministries and . . . field offices. No econometric or micro-simulation modelling tools are used, and the quality of the data is poor."[8]

All of those policy and operational weaknesses—including lack of systems for automatic information sharing with banks and other government departments—added to the problem of low compliance by taxpayers. Because only about 1,000 state entities formally paid taxes prior to the 1986 Doi Moi reforms, private citizens in Vietnam were not accustomed to paying taxes. In 2005, there were still only 2 million registered taxpayers out of a total population of more than 80 million.[9] That year, only 37% of Vietnam's 3.3 million businesses were registered with the GDT,[10] and the 673 largest taxpayers contributed more than 70% of total domestic revenues.[11]

Although low compliance was rooted partly in capacity constraints, the lack of clear and uniform procedures and low levels of computerization also served to fuel corruption. In an effort to reduce the temptation to exchange favors for bribes, the government had granted the GDT, shortly after its founding, the authority to pay higher salaries than the rest of the public service, but a 2006 World Bank diagnostic study rated the GDT as Vietnam's fourth-most-corrupt government agency, and an investment-climate survey conducted in the same year rated it as third most corrupt.[12] Frequent personal interactions between taxpayers and officials—as well as lack of a corporate identity, a rotation strategy, and clear incentives for good behavior—further contributed to the problem, according to the World Bank survey.[13]

Nguyen Thi Cuc, who served as the GDT's deputy director general of tax policy, administration, and international cooperation from 1995 until 2017, pointed out that low levels of compliance had deeper roots. She said that prior to the country's gaining its independence in 1954, French colonists had imposed "very high taxes to sustain their administration in Vietnam, which led to people's developing of an anti-tax mindset." She added: "My own father got upset when I told him I worked at the tax office. We had to explain to the public that it was now a different time and that we don't take money from the people to sustain the ruling class."

FRAMING A RESPONSE

Immediately after Director General Ninh appointed her to lead the reform team, Hai recruited a cohort of experienced and reform-minded officials from the GDT's national headquarters as well as from provincial and district offices.

Together with IMF consultants, the team turned to its first task, which was to conduct an analysis of the tax office's strengths, weaknesses, and opportunities, as well as threats to the office's operations. They then translated the analysis into a set of performance targets and presented the plan to the government. After the cabinet and Prime Minister Phan Van Khai endorsed the analysis, they directed the GDT to draw up a formal reform strategy under Hai's leadership.

In December 2004, the prime minister approved Hai's proposal for Vietnam's first comprehensive Tax Administration Reform Strategy. The plan, which would be in effect from 2005 until 2010, aimed to "develop a modern, fair and transparent tax administration, promote voluntary compliance with a balance between good taxpayer service and effective enforcement, and enhance revenue collection."[14] (Carlos Silvani, a tax expert in the IMF's fiscal affairs department, defined a modern tax system as one in which the vast majority of revenues are collected through a personal income tax, a corporate income tax, and a VAT.)

Based on the analysis the reform team conducted, the strategy pinpointed the key problems plaguing the GDT. Topping the list was fragmentation of the legal framework as it related to tax administration, which made it nearly impossible for the GDT to track individual taxpayers and build risk-assessment profiles. The strategy also noted the lack of effective coordination and information sharing between the tax administration and other government agencies. It further highlighted taxpayers' lack of knowledge about tax laws and compliance procedures as well as the public's negative perceptions toward the GDT. Other problems cited in the document included deficient professional skills, inadequate staff training, and the GDT's lack of a computerized system that could meet the requirements of a modern tax administration.[15]

The strategy set forth administrative priorities in response: to organize the GDT's sub-offices by function rather than by tax type; to hire and train more officers to deal with the expected increase in taxpayer numbers; to upgrade the department's IT systems; and to unify the legal framework related to tax administration. The strategy also called for more information sharing between the GDT and other state bodies and for more programs to inform taxpayers of their tax obligations—with the goal of increasing voluntary compliance.[16]

Soon after the strategy's adoption, in 2006 Vietnam's Ministry of Planning and Investment released its new five-year socioeconomic development plan. The document reinforced the GDT's proposals for tax administration reform with additional high-level backing by calling for measures to lower tax rates, expand the tax base, and improve compliance.[17]

Hai's reform team next set out to pilot a new organizational model built around the principle of taxpayer self-assessment, which meant that taxpayers would be able to calculate and declare their own tax dues. To implement the new model, the GDT first had to secure the legal authority to do so. Because existing laws specified that only tax officials had the power to assess payments, the GDT had to seek approval from the National Assembly before it could empower taxpayers to submit self-assessments.

When the pilot was launched, some officials feared that evasion might increase once the GDT stopped conducting assessments and allowed taxpayers to self-assess. "The finance minister was very worried, and only wanted the pilot done at one site, but we said that we needed two sites—one urban and one rural. If you only piloted in one location, you would have lacked the evidence that it was effective," Hai recalled.

In 2004, the tax office launched the pilot in the context of Ho Chi Minh City, the country's southern economic engine, and in the rural northern province of Quang Ninh. In the two provincial offices, the reform team reorganized tax offices by function—registrations, declarations, payments, refunds, debt collection, appeals, and audit—rather than by tax type.

At first, only a small group of selected enterprises operating in the two regions was allowed to self-assess their VATs and income taxes. Most companies complied, welcoming the move, because it reduced their administrative burdens and required fewer time-consuming interactions with tax officials. After the GDT demonstrated to the cabinet that the project had enhanced tax collection, the project was scaled up in January 2005 to cover more taxpayers and all tax types; and the model was rolled out at three additional provincial offices, including Hanoi.

Hai regarded the pilot's success as "the most revolutionary change . . . [because] it proved that self-assessment was doable within our system. Due to the pilot's success, many local offices asked us to allow them to implement the new system. . . . Before the pilot, we were a very, very small minority [of reformers], but now you could feel the atmosphere of reform within the whole system. [The pilot] laid the foundation for further reforms."

GETTING DOWN TO WORK

Despite the newfound enthusiasm for taxpayer self-assessment and despite a reorganized business process classified by function rather than tax type, the GDT was unable to immediately expand the pilot reforms across the entire country. First, the National Assembly had to enact legal and policy changes that would empower the tax office to act. Once that new legal framework was in place, the GDT planned to overhaul its business processes at all 758 offices, roll out a modern electronic database system, embark on staff training, and focus on raising public awareness to improve compliance.

Creating a legal basis for reform

Armed with a comprehensive reform strategy and practical lessons from the pilot project, the GDT's leaders worked closely with the finance ministry's tax policy department on drafting a series of proposed legal amendments. In November 2006, the National Assembly adopted the most fundamental of the proposals when it passed a new tax administration law, which became effective on July 1, 2007. The law created the foundation for radical change by unifying administrative procedures for all tax types, making taxpayer self-assessment compulsory, mandating that the GDT use a single set of identification numbers across all tax types, enabling the office to issue tax clearance certificates that indicated whether a taxpayer's affairs were in order, and requiring other government departments as well as certain private institutions, including commercial banks, to share information with the GDT. The law also legalized the tax consultancy industry, which meant that "taxpayers for the first time were allowed to use private tax advisers," said Cuc, who became head of the Vietnam Tax Consultants' Association after retiring from the GDT in 2017.

(The rationale behind the legalization of private advisers was that private advisers had a clear profit incentive to enroll more taxpayers as customers. The potential downside was that advisers had a vested interest in the system's remaining overly complex, because complexity generated demand for their services.) Cuc further stressed the importance of the law's establishment of "basic procedures for registration, filing, paying, refunding, and auditing each tax type. The procedures became much more systematic."

But the legal changes did not end there. In 2007, the parliament for the first time introduced a universal personal income tax in Vietnam. (The law became effective on January 1, 2009.) The personal income tax replaced an existing wealth tax, which collected revenues from only a very small group of the country's richest people. By taxing even low earners at a rate of 5%, the personal income tax sharply expanded the country's potential tax base (figure 1).

In 2008, the National Assembly amended the law covering corporate income tax reducing the maximum rate from 28% to 25%. Amid growing concerns about land grabbing, it also required real estate developers to pay corporate tax based on the land *value* rather than land *area*. The 2008 law modified some of the qualification criteria for corporate tax breaks, but it continued the practice of granting generous concessions to large companies. The tax policy committee estimated that "resizing [corporate] incentives and reducing the [corporate tax rate] would lead to a decrease of 5 trillion Vietnamese dong (equal to about $290 million or 1.3% of total tax revenues at the time) in annual budget revenues but hopes such would help bring more foreign investment."[18]

Also in 2008, the National Assembly amended the VAT system originally introduced in 1999. The new law reduced the number of VAT rates applicable to different types of products from four (0%, 5%, 10%, and 20%) to three (0%, 5%, and 10%), which made it easier for the GDT to administer.

Even more important, the VAT law exempted microenterprises—referred to as *household businesses* or *business households*—from paying any VAT or corporate tax if their annual turnovers were less than D100 million (about US$5,800 in 2008). Household businesses with fewer than 10 employees and yearly turnovers of D100 million to D1 billion (US$58,000) did not have to keep detailed accounting books and were required to pay only a presumptive tax of either 1% (levied on businesses, like small shops, that distributed goods), 3% (levied on household businesses involved in transportation or building-material supply), 5% (levied on small construction

Figure 1: Personal Income Tax Rates in Vietnam (2015)

Annual Taxable Income (in Vietnamese dong)	Tax Rate
0 to 60 million (0 to US$2,600)	5%
60 million to 120 million (US$2,600 to US$5,200)	10%
120 million to 216 million (US$5,200 to US$9,360)	15%
216 million to 384 million (US$9,360 to US$16,640)	20%
384 million to 624 million (US$16,640 to US$27,000)	25%
624 million to 960 million (US$27,000 to US$41,620)	30%
More than 960 million (more than US$41,620)	35%

Source: PricewaterhouseCoopers, *Vietnam Pocket Tax Book 2015.*

companies), or 2% (levied on household businesses in any other sector).[19]

The simple presumptive turnover tax provided the GDT with a powerful tool to bring the country's millions of informal household businesses into the tax net. But it also posed a risk in that it could potentially incentivize household businesses to remain small in order to keep benefiting from its favorable rates and simple procedures.

Reorganizing the tax service

To enable the GDT to realize its ambitions, the government in 2005 approved the tax office's request to hire an additional 3,500 employees, most of whom it assigned to headquarters in Hanoi. The move boosted the total number of tax officials to 44,000 and aimed to raise the percentage at the head office from 1.1 to 5–7%[20]—closer to the 10% average for most modern tax offices.[21]

The government also provided the department with an injection of funding. The GDT was already permitted to keep up to 1.9% of revenues it collected to fund its own operations. (However, GDT leaders had to explain to the National Assembly every year how the department planned to use the money, and legislators could cut the department's budget.) In 2005, the government provided the tax office with an additional $153 million in funding from the state budget so the tax office could upgrade its facilities and physical infrastructure.[22]

Next, in line with the IMF's earlier recommendation, the GDT upgraded Hai's reform team into a permanent unit with overarching responsibility for rolling out business process reforms at all 758 offices across the country. Starting with the offices that generated the highest revenues, members of the reform team traveled around the country "to provide information and support for offices as offices moved to the one-stop-shop approach," Hai said.

To support the new one-stop-shops, the GDT replaced the different tax departments (corporate, VAT, etc.) with the organizational model used during the earlier pilot project. Back-office personnel in each office were reassigned to functionally-defined departments, and the GDT created a new, front-office taxpayer-services department (text box 1).

Transforming the offices in this way meant each taxpayer had to interact with only one front-office customer service representative, who could provide information and guidance on issues related to all tax types.

In some instances, the reform team also faced resistance from tax officials because, "in the past, the officers interacted with the payers, so they felt they had a lot of power. Now [some of them] were no longer allowed to interact directly," Hai said. The party and government's strong backing for the

Text box 1: A reorganized tax office

The GDT reorganized its tax-based departments into 11 new, function-based departments across all provinces and districts. In keeping with the one-stop-shop approach, Hai's reform team introduced a taxpayer services and information department that served as the first contact point for taxpayers regardless of their queries (the personal income tax department was the only exception). The other 10 departments all focused on back-office work and interacted with taxpayers only in rare cases, such as when conducting audits. General affairs, organization and personnel, and administration and finance departments dealt with internal administration, and an internal inspection team conducted monitoring and audits. Returns processing and arrears collection focused on basic tax processes; a dedicated department dealt with taxpayer audits; and an in-house IT department maintained the Tax Management System database.

model, based on the success of the pilot projects, enabled the reform team to move ahead.

Customer service representatives could consult specialists within the different functional departments if they were unable to deal with a particular issue. Cuc added that, based on the guidelines contained in the new tax administration law, "we designed clear new templates and forms for each department, as well as guides and manuals for how to use the forms." But the GDT made an exception for personal income tax as introduced in 2009. Because Vietnam had never before implemented a broad-based personal income tax, the senior management team elected to retain a separate personal income tax department until officials became comfortable with administering it. (The personal income tax department did not interact directly with payers.)

Alongside the introduction of a one-stop shop and the creation of a personal income tax department, the GDT eased the burden on taxpayers by creating a systematic risk assessment framework to classify companies according to the risk they posed to nonpayment, incorrect payment, and late payment.

According to Hai, "In the past, we used a subjective tax audit plan where certain enterprises were visited each year, while others were not visited in ten years." Using its newly-acquired ability to collect data from banks and other government institutions, "we now developed a risk assessment system to decide on which enterprises to visit based on the risk [that they would fail to pay]," she said. By classifying as low-risk the companies that always paid what they owed, the GDT aimed to free resources so they could focus on higher-risk payers.

Computerizing, integrating, systematizing

Even with a new legal framework and revamped business processes in place, lack of a modern, centralized IT system posed an acute risk to the GDT's ability to keep up with the country's steadily expanding tax base. To make full use of its newly acquired authority to issue a single set of identification numbers for the creation of a nationwide database and to implement its plans for building a data-driven risk assessment framework, the tax office urgently had to build and roll out an integrated IT system that would link all field offices with headquarters in Hanoi.

Under the existing distributed-database system, all transactions were paper based and were processed manually. Individual offices kept paper records on their premises and created spreadsheets by means of such database programs as Microsoft Excel to keep track of different transactions. District offices then e-mailed the Excel files monthly to their local provincial office, and the provincial offices compiled and submitted monthly, quarterly, and annual reports to the head office. However, without central control and real-time updating, the system was slow and riddled with errors because different offices used different formats and different conventions to compile their records.

With the GDT set to begin implementing a new personal income tax that would potentially bring millions of additional registrants into the system, the need for a database solution was more urgent than ever. The reform team turned to the local World Bank office, which had successfully assisted the customs department with rolling out that department's own database software.

From 2006 onward, Hai worked closely with World Bank senior economist Duc to design a project plan for obtaining a taxation database system. Hai's and the World Bank's work culminated in the World Bank's approval of the Tax Administration Modernization Project (TAMP), under which the bank committed $80 million to purchase and install an IT system, to provide staff training, and to help the GDT simplify and adjust business procedures in order to align them with the new digital system. But the GDT grew increasingly exasperated because of a series of delays that resulted from the complexity of developing an integrated tax administration information system, Duc said. A 2015 World Bank report said: "The GDT [project management unit] and the bank took a long time to agree on issues such as firm qualifications, price weight, and bid evaluation methodology. The disagreement created tensions between the task team and the procurement team, and between the task team and the GDT. . . . staff. Frustrations over procurement process built up."[23]

As the bidding process dragged on, the GDT's leadership team hedged their bets by purchasing, in 2007, a simpler, back-up IT system from FPT Group, Vietnam's largest IT company. The back-up would at least be able to manage the database for the personal income tax, which would come into effect on January 1, 2009. Once it was clear that "the World Bank was not yet ready for implementation, we adapted and installed [the software] using GDT IT staff," Hai said. The tax office met its deadline, and the software—called the Tax Management System (TMS)—was up and running across most offices in time for launch of the personal income tax.

As the TAMP procurement process for an off-the-shelf software solution fell further behind schedule, the GDT was forced to gradually expand the functions incorporated into the TMS software. By 2012, the GDT had a fully centralized database connected to all tax offices throughout the country. Working with contractors from the FPT Group, the GDT gradually rolled out services, such as electronic VAT declarations and electronic return filings for income tax, which enabled taxpayers to handle almost all of their tax affairs online. For example, in 2010, the GDT launched eFiling in 19 provinces and by 2014 had made it mandatory that all registered businesses submit their declarations electronically.

The delays in the TAMP process and the adoption of the TMS ultimately doomed the GDT's plans to install more-comprehensive, state-of-the-art software under its partnership with the World Bank. "The government felt that once the bank's system was up and running, everything else the [GDT] developed would have to be thrown away," Duc said. In September 2014, the Vietnamese government formally canceled the TAMP project.[24]

Despite his disappointment at the project's failure, Duc acknowledged that the GDT had been "very creative in developing for itself a kind of software that fit the regulations" and that the purchase of the TMS from a local company meant that "[the contractors] know the system very well and can tailor and change it more quickly than contractors hired under a World Bank-financed project [could]." But Duc also cautioned that the TMS software had become a patchwork of different functions that made it difficult for the GDT to use it for sophisticated data analytics and risk management work. "The use of a fragmented solution may end up with serious limitations, because it may not be capable of sophisticated data analytics, and the question is again whether to throw it all away and start over," Duc said.

Limiting corruption, building capacity

Even though the World Bank's project had failed to procure a comprehensive database system, TAMP made a valuable contribution to helping improve anticorruption measures and staff capacity. A large share of the $5 million ultimately spent on the project (of the initially planned $80 million) went to the training of staff and the development of a more-robust performance-monitoring system.

Although the earlier adoption of a new organizational framework and a modern IT system had reduced the amount of staff interaction with taxpayers (except in the case of household businesses), the GDT still had to do more to respond to survey findings that citizens viewed the agency as one of the nation's most corrupt. A new anticorruption law adopted in 2005, as well as the creation of an anticorruption committee chaired by the prime minister, reinforced that imperative.

Hai's team focused on introducing new practices to further limit the exchange of bribes between officials and taxpayers.[25] The tax office adopted a staff code of conduct that stipulated tough disciplinary measures. And the office developed a clear staff-rotation policy. With the exception of certain specialist positions, "25% of staff have to move every year, which means no one should spend more than three years in one position," Minh said. The rotation policy would thereby reduce opportunities for officials to transform particular offices or departments into their own personal fiefdoms.

The GDT further upgraded its internal audit function from a regular operational unit to a full-fledged department that systematically monitored the office's internal governance and financial controls and made recommendations for improvements. Cuc pointed out that the head office and each local office had its own internal audit team: "They will check whether tax officials followed the right procedures. For example, did they calculate a VAT refund correctly, or did they create unnecessary obstacles for the taxpayer?" If the audit team identified a mistake or fraudulent activity, "it will be treated according to the seriousness [of the offense]. The first step is to reduce salaries, the second calls for dismissals, and the most serious cases can be prosecuted," she said.

To enhance staff capacity, the GDT also upgraded its training department from a unit within the human resources department to a full department. Previously, Minh said, "different offices did everyday training by themselves. But when we changed to the functional model, we realized we also had to centralize the training function because all of the policies came from central." Because the GDT often changed tax-processing procedures, the office decided to centralize training so that its regulations would be enforced uniformly across all offices.

In addition to ad hoc training conducted under TAMP, the GDT launched a partnership with the Japan International Cooperation Agency in 2005 for the development of training materials and the launch of a comprehensive training program for all staff members.[26] Cuc explained that under the new program, "after you become a tax officer, you undergo standard induction training and get regularly retrained on advanced [aspects]." The training drive culminated in the construction of a dedicated tax-training institute, opened in the central city of Hue in 2014. The institute had space for more than 2,000 students at a time, and the government equipped it with state-of-the-art facilitates and full-time lecturers.

Finally, under TAMP, the GDT developed a performance-monitoring framework (figure 2). Although "revenue collections will remain the core criterion," the new framework broadened the scope of the office's performance monitoring by more heavily emphasizing "the quality of operations, the reduction of compliance costs, improvements in good governance, and cost efficiency," a 2011 World Bank report noted.[27]

Improving compliance

The GDT used both incentives and penalties to make sure that the millions of newly eligible taxpayers registered and complied. The task of ensuring that compliance was relatively easy when it came to large, mostly-foreign-owned companies, including the fewer than 1,000 largest that contributed more than 70% of total domestic revenues.[28] Sebastian Eckardt, who became the World Bank's lead economist in Vietnam in 2015, said that "in the formal sector, you have a very large part that is from foreign direct investment, as well as state-owned enterprises. It's relatively easy to register those" because they needed government licenses to operate in the country.

Nonetheless, to "change the [broader] public's attitude toward revenue collection," the GDT in the mid 2000s reintroduced itself to the public, Minh said. It upgraded its small communications unit to a full department for communications and taxpayer support. And with

Figure 2: GDT Results Monitoring Framework

Area	Performance Indicators
Improving governance and increasing the level of voluntary compliance	• Perception of the integrity of staff as measured by periodic internal and external stakeholder surveys • Public perception of the quality of tax administration performance as measured by periodic surveys • Tax revenues paid voluntarily/total tax revenues collected • Number of active taxpayers • Compliance with major taxes: corporate income tax, personal income tax, VAT
Institutional development	• Perception of taxpayers and other stakeholders regarding the level of honesty of GDT staff • Perception of managers and staff regarding the level of professional skills in selected functional areas
Operational development	• Perception of taxpayers regarding the quality of services provided by the tax administration • Percentage of written queries answered within 30 days • Operational costs/tax collected • Percentage of tax audits resulting in additional tax assessments • Additional tax collected as a result of tax audits/additional tax assessed through tax audits • Tax arrears recovered during the year/total tax arrears at the beginning of the year • Average time taken to process a VAT refund request • Percentage of taxpayers filing electronically • Average time required to settle administrative disputes

Source: Gangadha Prasad Shukla, Duc Minh Pham, Michael Engelchalk, and Tuan Minh Le, *Tax Reform in Vietnam: Toward a More Efficient and Equitable System*, World Bank, September 30, 2011.

the department housed at headquarters providing oversight and supervision, each provincial and district office also created a communications team.

The team seized upon a possible new vehicle for engaging with the public: by means of the private tax adviser, an occupation permitted under the tax administration law that became effective in mid 2007. Because tax advisers had an incentive to recruit taxpayer customers, "we used the 4,000 tax advisers in the country to our advantage," Minh said. By coordinating training courses with the Vietnam Tax Consultants' Association (Cuc, head of the association, even had an office at the GDT's headquarters), the GDT made sure that "taxpayers received a high-value service" through tax advisers, which helped bolster the image of the tax system, Minh said.

The communications team focused on building a relationship with tax advisers. "Our first audience consisted of tax advisers and [finance managers]. The department has a major focus on publicizing [the GDT] in newspapers and on television and radio stations. We also have a tax magazine that goes out to financial professionals," Cuc said.

Another core function of the communications team was "to translate laws and regulations into normal language to inform the public. If [taxpayers] have any difficulties, they can also ask their local service representatives," Minh said.

The GDT further modified a set of technical regulations to make it easier to pay. Among other steps, from 2011 the tax office allowed small and medium-size companies to submit VAT declarations every three months rather than monthly (large companies still had to submit declarations every month).[29] The GDT also published risk assessment criteria that enabled companies to substantiate that they posed little risk of falling behind on VAT payments. By dedicating more resources to higher-risk companies, the assessment system made the VAT refund process quicker and easier.[30] The tax office consequently shortened the turnaround time for unexamined VAT refunds from 15 working days to 6, and for refunds that it examined first, from 60 working days to 40.[31]

Finally, the GDT launched an electronic invoicing service that required VAT-registered businesses to use electronic bank transfers for all supplier transactions valued at more than D20 million (US$870). To enforce the new measure, the tax office determined that non-electronic transactions higher than that amount were not eligible for VAT refunds and were not income-tax deductible.

But the office also applied other methods to induce behavior change and improve compliance: Provincial and district *tax offices* reported to the GDT's national headquarters on all administrative issues, but provincial *governments* were responsible for political oversight of offices located in their regions. And provincial authorities kept a share of the taxes collected by their local offices, which gave them a powerful incentive to sustainably maximize revenue collection.

Because of Vietnam's centralized political system, the ruling Communist Party exercised significant control over subnational governments. "One unique thing about the tax administration strategy is that it is approved by the Politburo of the [Communist Party], so we used the party to do public relations for the GDT," Hai said.

The government similarly ensured that companies and individual taxpayers complied. "We have a big network of local tax offices, which means that enterprises that must be registered cannot escape," Minh said. With 44,000 officers serving a total labor force of 55 million, the GDT had one staff member for every 1,250 taxpayers—a better ratio than South Korea (1,421), South Africa (1,486), and the United States (1,621).[32]

To ensure that the country's 4.66 million business households paid their fair shares of the presumptive lump-sum tax, local officials posted outside the tax office as well as in front of local government offices and other public places its lists of all of the people who had to pay. "We then request you to compare with your neighbor and report any inaccuracies or complaints [through an anonymous feedback system]. Based on the [feedback], we then do some examinations," Minh said. Making tax information public enabled the GDT to more accurately estimate the amount of revenue it could expect from the presumptive tax while it ensured that communities helped identify possible evaders and boost compliance.

OVERCOMING OBSTACLES

By the time the GDT adopted its new reform plan for 2011 to 2020, it had already made substantive progress in improving tax administration. However, the government now confronted fresh challenges because the domestic private sector had stagnated. The problems arose from two of the government's attempts to fix earlier problems. The first followed from the decisions to offer generous tax incentives (which allowed certain companies to pay lower tax rates) and grant exemptions (which excluded certain companies from the requirement to pay any taxes for a specific period). These measures were designed to attract foreign direct investment and to compensate for "a number of negative factors still inherent in the country's investment climate, such as lack of adequate infrastructure and a wellfunctioning legal system," as a 2016 report from Oxfam and UN Women noted.[33] The second problem was that the presumptive tax on household businesses had begun to backfire.

On one hand, the government's friendly policies toward foreign business had produced spectacular results by helping fuel economic growth and turning Vietnam into one of the most economically open countries in the world. Although not the only factors in generating the investment boom, the government's offers of generous tax incentives and tax exemptions for foreign companies contributed to the expansion.

A law that took effect in 2015 specified that tax incentives applied to both foreign and domestic businesses in 57 different "encouraged" and "especially encouraged" sectors, to businesses in 53 geographic districts, and to more than 300 individual industrial parks, high-tech manufacturing areas, and export processing zones.[34] In certain cases, such as when Samsung expanded its operations into Thai Nguyen province in 2014, individual foreign investors received tailor-made incentive packages that yielded additional benefits. In the case of Samsung, the government threw in a 50% reduction in corporate tax over three years—on top of existing incentives.[35]

But the scale and extent of the government's tax holidays and incentives for big foreign businesses came at a price for local companies. Although a 2006 law in principle banned tax discrimination between foreign and domestic firms, in practice foreign companies still benefited disproportionately from tax breaks. The system favored large investment projects, with the biggest tax breaks going to those valued at more than $280 million, which was out of the reach of most Vietnamese companies.[36]

As a result, Vietnamese manufacturers struggled to compete in the increasingly wealthy local market with multinationals that enjoyed substantial tax breaks and could thus sell products at lower prices. "The government used incentives from the beginning to attract investment, and they had success," Duc said. "But it seems like they've now reached a point of decreasing returns. There is now a dual economy in Vietnam: the [foreign direct investment] economy and domestic firms. The task now is to create close linkages between the two."

Although the GDT lacked definitive statistics, a 2014 IMF report noted that Vietnam's tax base "has eroded, reflecting in part exemptions and incentives."[37] The government estimated that tax incentives in 2014 reduced the corporate tax take by about 1.85%.[38] Beyond directly reducing the tax take, the breaks benefiting foreign companies stunted the development of domestic enterprises.

Fraud in the application of the presumptive tax on household businesses also aggravated problems in the domestic private sector. Although the tax had succeeded in bringing millions of additional household businesses into the GDT's net, it required enforcement to counter evasion and served as a further disincentive for domestic companies to grow. Le Dang Doanh, a Vietnamese economist who helped draft some of the laws that ushered in the Doi Moi era, explained that "according to the enterprise law, a household business with more than 10 employees had to formally register and obtain a business license. But many businesses with more than 10 employees will claim to be smaller because they want to continue paying the lump-sum tax."

The yearly presumptive 1 to 5% turnover tax regime levied on household businesses was much simpler and much easier to abuse than the complex corporate tax and VAT systems. Once a household business obtained a formal license that required it to pay income tax, it had to keep records of its invoices, draw up formal accounting records, and make regular VAT payments and corporate income tax payments at a rate of 22%

(the government lowered the rate to 20% in 2016). Household businesses faced no similar requirements.

Due to lack of formal accounting records, tax officers also had to estimate a household business's annual turnover in order to calculate the lump sum it owed. But as a World Bank study reported in 2011, "The administrative processes for presumptive taxation result in extensive direct contact between taxpayers and tax administrators, which increases compliance costs and the risk of collusion and corruption."[39] Doanh agreed: "[Business owners] make friends with tax bosses, so tax agents negotiate a very symbolic amount. . . . But because [business owners] pay bribes into the pockets of tax officials, they actually do pay high taxes. The taxes just don't go into the state budget."

Household businesses that abused the presumptive system further reduced the GDT's collections. By 2015, Vietnam had an estimated 4.75 million household businesses—10 times the number of domestic enterprises paying the higher, corporate income tax. However, although household businesses—many of which falsely claimed to have fewer than 10 employees—accounted for 17% of the country's annual GDP, the money collected from them amounted to only 2% of Vietnam's total domestic revenues in 2014.[40]

The World Bank study also found evidence that larger businesses abused the presumptive task system, organizing their operations so that they remained within the threshold of eligibility.[41] To encourage household businesses to graduate from the presumptive tax to the formal corporate tax and VAT systems, the GDT in 2014 abolished the requirement that companies file corporate returns on a quarterly basis and reduced the number of documents required in order to benefit from certain VAT-deductible expenses.[42] The finance ministry's tax policy department launched a comprehensive review of the country's tax policies, which culminated in an August 2017 proposal to create a separate, lower corporate income tax rate of 15% (instead of the regular 20%) for enterprises generating annual revenues of less than $130,000.[43]

The proposal also included a call to reduce the number of tax incentives and to clarify and streamline eligibility criteria—in another effort to boost domestic firms.[44] However, the plans did not immediately result in legal changes. As the government continued with plans to grant incentives to investors across three new special economic zones, public protests flared up periodically in dozens of cities over fears that Chinese investors would crowd out Vietnamese businesses.[45]

ASSESSING RESULTS

Vietnam's first-ever tax administration reform plan, which guided the GDT's work from 2005 to 2010, yielded impressive results. According to a 2011 IMF report, as a share of GDP the country's tax revenues increased from an annual average of 19.6% during 2001–2004 to an average of 23.7% for 2005–2008[46] before leveling off at 22.38% in 2010. Thanks in part to the introduction of a presumptive turnover tax that let household businesses pay simple annual lump sums, the number of registered taxpayers in the country also grew rapidly from 2 million in 2005[47] to 15 million by 2014.[48]

The IMF praised the GDT's "tax policy reforms [as] positive steps toward building a tax system conducive to economic development and dealing with increased exposure to the global economy." It similarly pointed out that the reforms made to the tax office's operations "have better-positioned the GDT to administer an increasingly market-oriented economy."[49]

However, fueled partly by the cost of tax loopholes and by small businesses' failure to graduate into the formal corporate tax system, the tax-to-GDP ratio reversed after 2010, declining from 22.38% to 18.22% in 2015. That was well short of the target of 23 to 24% that the government had set in its 2011–2015 socioeconomic development plan. Nonetheless, overall tax revenues (in constant 2010 US dollars) nearly tripled in a decade, increasing from US$11.7 billion in 2005 to US$26 billion in 2010 and to US$32 billion in 2015.

Under the leadership of Hai's reform team, the GDT underwent a transformation within a decade—from being a tax collector built to manage a minuscule group of taxpayers in a centrally controlled economy to becoming a modern revenue agency that collected taxes in a dynamic, market-based economy. Working with the finance ministry and the National Assembly, the GDT had completely overhauled Vietnam's tax policy framework. The 2007 tax administration law introduced a uniform set of procedures for all taxes; the country created a personal income tax; and it improved corporate-tax and VAT operations.

The policy reforms helped boost compliance, with corporate income tax and VAT generating revenues equal to 6% of GDP.[50] Driven partly by the move to encourage online payments as well as the high percentage of taxes paid by a small group of big foreign-owned companies, the World Bank reported that Vietnam's VAT was "extremely efficient," with Vietnam's VAT productivity indicator exceeding the average for industrial countries.[51]

Guided by the new legal framework, the GDT had reorganized its business processes by introducing self-assessment and arranging tax offices according to function rather than tax type. Despite delays, all tax offices also became connected to a central network database the GDT used as a springboard to introduce electronic services. By 2015, 97% of enterprises registered in Vietnam were filing their taxes electronically.[52] According to Minh, "95% of companies also pay online, and 30% of our refunds are done online." The share of tax officers with university qualifications increased from 44.7% in 2006 to 53.1% in 2010, and the creation of a dedicated tax-training college further boosted staff capacity.

But corruption remained a problem. In 2015, a quarter of all companies participating in a World Bank enterprise survey reported that they were expected to give "gifts" in meetings with tax officials, which was higher than the 20.3% average reported for East Asia.[53] (However, given the importance of interpersonal relationships in Vietnam, gift giving is a common practice, and it can be difficult to distinguish bribes from tokens of appreciation.) The problem was particularly acute when it came to household businesses, which relied on tax officials to calculate the turnover tax owed.

In its Public Financial Management Performance Assessment conducted in 2013, the Public Expenditure and Financial Accountability program gave Vietnam's GDT a C+ score for its transparency and effectiveness in registering taxpayers and collecting revenues.[54] The report warned that some tax regulations were still not uniformly implemented across all tax offices and that "there is no dedicated independent tribunal to resolve disputes between taxpayers and the authorities apart from the [normal court system]."[55]

Another unresolved issue was that despite the GDT's reorganization, compliance with formal corporate tax procedures (excluding the presumptive turnover tax) still required as many payments and nearly as much time from firms in 2015 as in 2006: 32 payments and 872 hours per year instead of 32 payments and 1,050 hours per year.[56] That was still more time spent on compliance than in most countries in the East Asia and Pacific region, including Cambodia (40 payments and 173 hours per year) and Laos (35 payments and 362 hours per year).[57]

REFLECTIONS

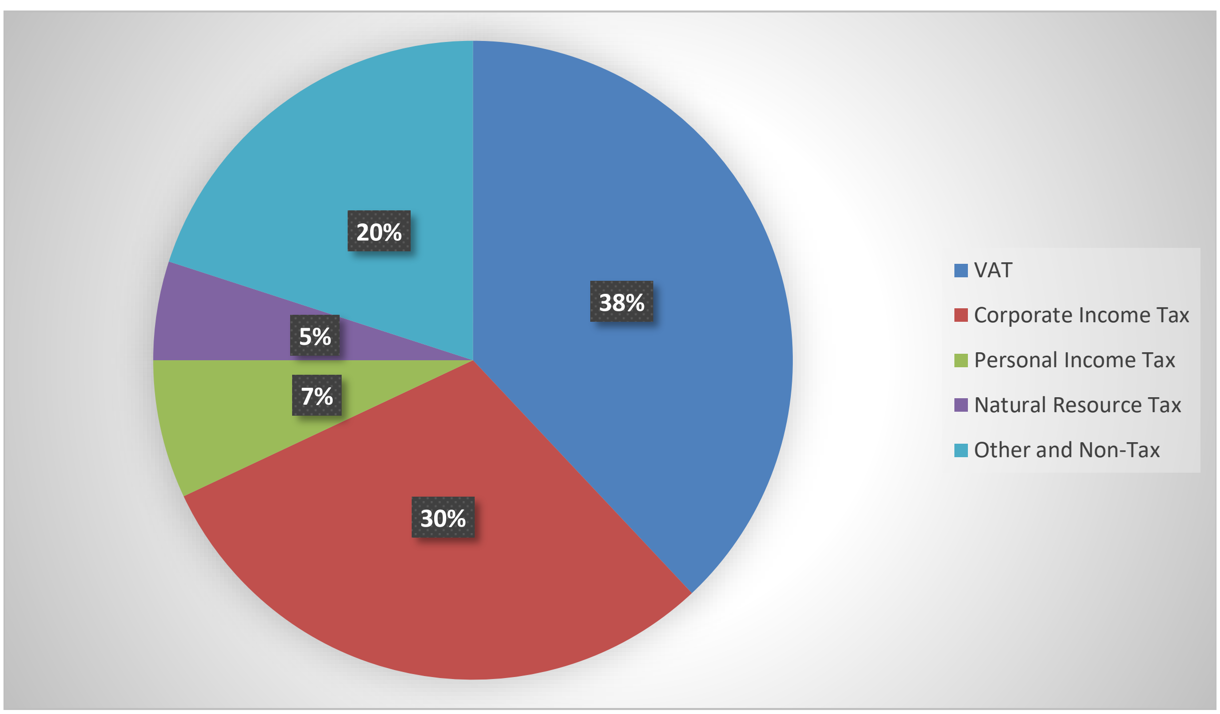
Looking back over a decade of reforms that overhauled and modernized Vietnam's tax system, Le Hong Hai, a deputy director-general who led the General Department of Taxation's reform team from 2004 to 2015, stressed the importance of domestic political will: "We could only do the reforms successfully once we ourselves really wanted it. When the IMF initially advised us [to reform in the 1990s], we didn't agree. Only when we really wanted it ourselves, did we do it." But as the government became increasingly concerned about the tax office's inability to handle millions of taxpayers using an outdated system divided by tax type and based on administrative assessment, GDT leaders became convinced of the need for reforms. To Hai, it was clear that "Only when we really wanted it ourselves did we do it."

Nguyen Thi Cuc, deputy director general of tax policy, administration, and international cooperation from 1995 to 2015, added that "the reality that the tax base expanded so much that the GDT couldn't [keep administering taxes manually] was a big motivation for the prime minister, who pushed the finance minister, who then pushed the GDT" to reform. Cuc added that Vietnam's position near the bottom of the World Bank's Doing Business index also "hit [the government's] self-respect," further fueling the desire for reform. (In 2007, Vietnam ranked 104th out of 190 in overall ease of doing business. In 2015, it was up to 79th.)[58]

Once the finance ministry and the GDT's leadership team realized that the tax office's ability to collect revenues risked being completely outstripped by the growth of the private economy, "the next element was to choose tax leaders who were reformist," Hai said. "The leader of the GDT assigned me to the reform group because I really wanted to do it, and when we did the piloting we chose locations where local leaders were reformist. If we had assigned the wrong people, we would have failed," Hai said.

For Sebastian Eckardt, who became the World Bank's lead economist in Vietnam in 2015, one of the GDT's primary strengths was that "compliance management works," as illustrated by the sixfold increase in registered taxpayers. "The intake is quite good—also by regional standards. But it's a reflection not just of the tax

Figure 3: Tax Revenue Composition, 2015



Source: Pham Thi Huong Ly, *Viet Nam 2016*, Keio University, accessed July 16, 2018; http://www.ic.keio.ac.jp/en/doc/3_Vietnam_2016.pdf administration in isolation but also that [Vietnam has] a functional state apparatus more broadly" (figure 3).

There was still work left to do, however. Aside from the needs to (1) streamline and equalize foreign and domestic companies' access to tax exemptions and (2) make it easier for household businesses to graduate into full-fledged enterprises that paid their fair shares in corporate taxes and VAT, Vietnam's exposure to the global economy left the country vulnerable to evasion by multinational companies.

Dang Ngoc Minh, deputy director general of international taxation and cooperation, said, "We have been successful in attracting foreign direct investment, but a big problem is base erosion and profit shifting," which enabled big companies to avoid paying taxes in Vietnam by moving their profits to no-tax jurisdictions. "Although we now have a system of double-taxation treaties that enables us to coordinate with other countries, we need to increase our international cooperation," Minh said.

To better track large companies, the GDT in 2013 established a large taxpayer department, and planned to further refine its structure by segmenting into different offices serving large, medium, and small taxpayers. For the tax office to ramp up its data analytics capacity to better track taxpayers and effectively implement its new risk assessment framework, it would have to revisit the contentious issue of whether its homegrown software solution was up to the task.

With Vietnam's economy still growing by nearly 7% in 2015, there was no time to stand still. "Currently, we have 675,000 registered enterprises, but . . . as the government formalizes household businesses . . . by 2020, it will already be one million," Minh said. As was the case in the mid 2000s, the GDT "will have to cope with a further rapid increase in number of taxpayers as well as the challenges of the digital economy," he added. But with an improved policy framework, a revamped organizational structure, and modern tools in place, the tax office was much better equipped than ever to keep up with Vietnam's vibrant economy.

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