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Introduction

There are many ways to tax individuals and corporations. Taxes may be levied on consumption (such as the VAT, sales or excise taxes), flows of income (such as enterprise and individual income taxes), or wealth and assets (such as property taxes, assets taxes, and some income taxes). In fact, the tax systems of most countries are a combination of these different types of taxation. Developed tax systems tend to tax income according to relatively complex structures which utilize sophisticated accounting, record keeping, and tax administration in order to balance various goals of the tax system including equity and efficiency. Consumption taxation in more developed systems consists of excise taxes, value-added taxes and sales taxes, with varying degrees of complexity.

In all countries, some enterprises and individuals remain outside of the tax system through use of different types of evasion or avoidance. In many cases, it is easier for individual taxpayers and small enterprises (versus large corporations) to remain outside of the tax net for the simple reason that they can remain inconspicuous to the tax administration. For these types of entities, complicated and administratively burdensome tax systems further discourage compliance with the tax laws. Tax administrations are often left with the choice of “going after” large firms where the potential tax revenue pay-back is higher or going after less lucrative smaller taxpayers. Additionally, complicated tax systems make it difficult and expensive for start-up firms (particularly small enterprises) to act in good faith in terms of tax compliance due to the costs associated with record keeping and the need for specialized information to comply with complex tax laws. At the same time, large and small taxpayers find it beneficial to take advantage of loopholes in the tax system in order to minimize their tax payments.

These factors, tax avoidance, tax evasion, and the expense and difficulty for start up enterprises to comply with complex tax laws, have led many countries to adopt specific tax regimes to counter these problems. In many countries, imputed or presumptive taxation has traditionally been used as a way to get some tax revenue from these taxpayers which might otherwise go completely untaxed. These systems calculate the tax base via easy-to-obtain indicators or other methods, instead of relying on taxpayer self-assessment. This method of taxation can accomplish two things: it can reduce the cost of compliance by the taxpayer as the tax base is easier to calculate than that of the income or corporate tax, and, once the system is determined, it reduces the costs of tax administration. Once part of the simplified system, it theoretically becomes more difficult to “disappear” from the view of tax administrators by going to the shadow or underground economy. Imputed or presumptive taxation is therefore often regarded as a stepping stone to the regular tax system, such that a taxpayer would be subject to this simplified regime for a limited period of time and then become part of the regular tax system under which income can be taxed according to the country’s law regarding individual and corporate taxation.

In the last decade, presumptive taxation has been increasingly used to combat tax avoidance by large taxpayers as well. In Latin America in particular, there has been a move to use presumptive taxation to generate minimum taxes on corporations. These minimum taxes are used to reduce tax avoidance which is generated by complicated tax structures, particularly in enterprise or corporate income taxes. The taxes are typically

levied on assets and are creditable against regular corporate income taxes. Rajarman (1995) points out that these minimum taxes may also reduce tax evasion vis-a-vis transfer pricing. By taxing assets, the Government can collect revenue regardless of the level of transfer pricing activity and the impact of such activity on reported income (subject to the caveat that the taxable assets need to be present within the country). These minimum taxes are not transition systems, rather they are most typically permanent features of some tax systems.

The successes of country's in using the imputed or presumptive systems as stepping stones are difficult to quantify. In many countries, the imputed tax has become a staple of the tax system (more so in developing countries than in developed countries). In other countries, the taxes were eventually phased out as part of a long-term strategy and alternatives brought back (Italy), while in still others the taxes were simply dropped.

The experiences of the presumptive tax as a minimum tax are newer. Some believe that these types of presumptive taxes, especially those based on assets, have been more successful than more traditional presumptive or imputed taxes which estimate income bases for the hard-to-tax.

It is difficult to conclude a set of consistent lessons from countries that have used simplified tax systems. There are about as many different simplified systems as countries that have used them. Differences are due to taxes that are folded into the system (in some countries only income and wealth taxes are rolled in, in other countries consumption taxes are also part of the simplified system, like in Russia); tax bases (some countries use assets, others turnover or gross receipts, others simply define by the type of business and industry); tax levies (lump-sum, or flat or even progressive rate structures); and eligibility requirements (size of taxpayer defined by assets, turnover, gross sales or receipts, number of employees, etc.). Yet, given this diversity, there are some obvious lessons to be taken from the experiences of other countries:

- One of the primary benefits of imputed systems on small entrepreneur is to bring these taxpayers onto the tax rolls. Once these taxpayers enter the system, the tax administration must be ready to follow up so that these taxpayers don't "disappear" once again.
- It is difficult to transition away from imputed-presumptive taxation. Countries with long traditions, such as France, have transitioned away simply due to the impacts of inflation.
- It is easier to transition individual taxpayers off of an imputed or presumptive system to the regular tax structure by imposing time limits for simplified filing (for example, three years of simplified filing, then a move to the regular system).
- Worldwide, there have been many court challenges to non-rebuttable imputed-presumptive systems. A rebuttable tax is one that can be challenged by the taxpayer. In such cases, the taxpayer is able to present evidence to the tax administration to substantiate a lower tax liability. A non-rebuttable tax can not be appealed. Legislating these taxes as rebuttable increases their acceptance by the taxpayers and reduces costs associated with legal battles. Making the tax rebuttable so that the

taxpayer may calculate tax under the regular tax system and pay that amount instead, also reduces the need for discussions and negotiations between the tax administration and individual taxpayers.

- Presumptive minimum taxes have become a popular way to combat tax evasion by larger corporations. These taxes are typically creditable against a company's enterprise profits tax liability. As such, they are not necessarily a transition tax scheme, but may remain as long-term component of a tax system.
- If presumptive or imputed taxes are not charged as minimum taxes, there should be an eligibility requirement associated with an enterprise's turnover. If this is not done, then the presumptive or imputed scheme becomes a hard-to-eliminate alternative tax structure.

Forms of Imputed and Presumptive Taxation

Imputed or presumptive taxes are taxes based on notional income. There are subtle differences between imputed and presumptive taxes among countries. Imputed systems tend to calculate taxable income based on key factors which are associated with income generation. These might be sales, turnover, number of employees, size of firm, assets of the taxpayer, etc. Imputed tax bases are typically calculated based on coefficients for different factors applied to specific taxpayers or specific types of taxpayers (certain sized enterprises in particular industries). Presumptive taxes tend to be calculated based on more aggregate indicators, such as industry and region, or external indicators of income, with less specific calculations for particular taxpayers. In both cases, the tax bases take advantage of data that are easier to come by than data required to calculate actual taxable income as specified by law. In this report, we will use these terms interchangeably. In many countries, taxes derived via presumptive or imputed measures are rebuttable--that is, the taxpayer can prove a lower tax liability through a full disclosure to the tax authorities.

Another form of presumptive taxation is referred to as the presumptive minimum tax. Such a tax is imposed on a presumptive base--most typically based on the value of gross assets, gross receipts, or turnover. In some countries, allowances are made for some deductions (these are discussed in detail below). This type of tax is designed to reduce tax evasion for all regular taxpayers by imposing a minimum level of tax (which is typically creditable against regular tax liabilities). This form of taxation is not designed to facilitate compliance and enforcement for small taxpayers.

Two specific examples of imputed or presumptive systems are the *forfait* (France and others) and the *tachisv* (Israel and others). The *forfait* (contractual system) has been established for certain taxpayers whose income falls below a set threshold: sole proprietorships, individuals and unincorporated businesses. The taxpayer must agree with the tax administration to be taxed based on estimated income versus actual income. The actual estimation of income is well developed in tax administration procedures manuals. The taxpayer must supply the following to the tax administration: purchases, sales, value of closing inventory, number of employees, wages paid, and number of cars owned. Expenses are estimated by the tax administration. The tax administration

calculates income based on a sophisticated and detailed estimation procedure, by industry.

The tachshiv of Israel is another widely referred to method of presumptive taxation. Tachshivim are standard assessment guides, produced for a variety of industries. The assessments are based on a variety of factors including physical location, size of store-front, etc. The assessments may be negotiated with industry representatives, but not with individual taxpayers.

Imputed and Presumptive Taxation: Mechanisms

In practice, there are many ways to impose a simplified tax regime based on the principle goal of the tax: small businesses, all businesses, or individuals. Based on international experience, presumptive and imputed tax calculations may be classified into four basic groups although there are certainly others (Buotogoli, 1995):

1. Systems which estimate taxpayer income and apply a formula to all taxpayers (by type of taxpayer or by individual taxpayer). Estimation of taxpayer income may be a very simple calculation (such as a lump sum tax based on the average income of a particular profession) or a more complex calculation using information on sales, employees, assets, location, etc. Albania and Kazakhstan have used presumptive taxes levied as lump-sum taxes based on profession;
2. Systems which apply an assets tax (used more generally for all businesses and as a minimum tax);
3. Systems which apply a gross receipts or turnover tax (used more generally for all businesses and as a minimum tax);
4. Systems which base the tax on external indicators of income (personal expenditures, wealth, etc.).

The specific systems used by countries are based on the goal of the tax (to alleviate evasion and avoidance by all taxpayers or to simplify the system for small taxpayers), the sophistication of the tax administration, and a judgement regarding the availability of reliable data. Country examples are discussed below.

Advantages and Disadvantages of Presumptive/Imputed Systems

Presumptive or imputed taxes may reduce tax evasion by reducing the compliance burden for taxpayers and reducing the cost of enforcement by the tax administration. Such taxation may also encourage new enterprises to start off as legitimate taxpaying enterprises at the very beginning. In many countries, a simplified system of taxation is the only reasonable, cost-effective way to get some level of taxes from certain types of taxpayers. Typically, tax evasion is very high among small enterprises or sole proprietorships and many of the simplified tax structures are developed with these taxpayers in mind. If presumptive or imputed bring more taxpayers into the tax net, the

perceived fairness of the system increases, which has long-term benefits to a country. Additionally, if a presumptive minimum tax is successful at reducing the tax avoidance of large firms, once again, the fairness of the system is enhanced.

Presumptive minimum taxes based on assets may also be efficiency enhancing in that taxes are based on average returns; taxpayers earning higher returns are not necessarily taxed on the additional margin.

Disadvantages of presumptive or imputed systems are also obvious. These types of taxes are by design approximations of taxes on income. The procedures used to estimate income through various proxies could be expensive to develop and maintain, may involve negotiations between taxpayers and tax authorities, and may significantly over or understate income. Depending on the goal of the tax, the advantages of expanding the tax net may outweigh the disadvantages of the system. Given the number of countries imposing some type of presumptive or imputed tax, the chance of positive benefits of these taxes outweigh the potential costs.

International Experiences

Greece:

Individuals may be taxed according to imputed income when imputed income is higher than actual income declared, and the taxpayer can not substantiate the difference. Imputed income is calculated based on criteria such as: rent of second home, operating expenses of vehicles, planes, costs of domestic servant, assets (cars, boats, ships, planes). Additions to imputed income as of January 1, 1995 include the purchase of enterprise shares, purchase or construction of immovable property (excluding first residence of up to 120 square meters), and loans to personal enterprises, partnerships, and limited liability companies. (Coopers and Lybrand, 1997 International Tax Summaries).

France:

The forfait is described above. For small businesses selling goods, the threshold is FF 500,000; for other small businesses (mostly service providers), the threshold is FF 150,000. The income thresholds used under the forfait system have not been adjusted for inflation. Over time, the result is that there has been a natural transition from the forfait as fewer taxpayers fall below the income threshold.

Indicators determine income versus checking assessments or reported income. Those covered include: farmers, unincorporated businesses, professionals whose gross receipts fall below a certain threshold.

Mexico:

Mexico adjusted its tax scheme for small businesses after a major tax reform in 1988. Prior to 1988, there was a Special Basis Taxpayer regime (for transport, primary and publishing enterprises) and a Minor Taxpayers Regime (for all sectors, with a threshold of gross income below \$100,000). Under the first scheme, taxpayers were divided into two groups: those below a turnover threshold were taxed based on an asset-

based lump sum levy and those above the threshold were taxed based on a profit coefficient on actual turnover. The second scheme applied to all other industries, with the limited threshold. The form of taxation was similar. A variant of these schemes is now in place in Mexico. The base is cash flow, and the tax is a set percent of cash flow.

As part of the 1988 Tax Reform, Mexico also introduced a presumptive minimum tax effective since 1989. Business assets were taxed at 2 percent until 1997, and are now taxed at 1.8 percent of gross assets. The tax liability is creditable against regular corporate tax liability.

Bolivia:

Bolivia instituted a number of changes to their tax code in the mid-1980s. In the 1986, a simple tax on gross sales replaced direct and indirect taxes on small enterprises. Additionally, Bolivia introduced a 3 percent levy on net worth, as a form of presumptive final tax. Bolivia's case was fairly unique in that there was no additional corporate income tax. This has since be changed, and the tax is now levied as a presumptive minimum tax.

Other Experiences:

Uruguay, Angola, Cameroon, and Morocco all have experience with presumptive taxes, specifically on small businesses. In these countries, small businesses are defined by turnover (Uruguay and Angola), or include a large component of the service sector (Cameroon and Morocco). These systems are of the most straightforward presumptive systems where few calculations are required and administration is relatively inexpensive.

Lessons Learned from International Experience

The results of imputed and presumptive taxes used in various countries are difficult to quantify. However, there are some general lessons which pertain among countries:

- Governments must decide on their goals for presumptive or imputed taxation since the best structure for one goal may or may not be different for others. The goals in general are: reduce tax evasion/avoidance of small, hard-to-tax firms; reduce compliance costs for taxpayers; reduce tax avoidance in general; or reduce tax evasion/avoidance of individuals.
- It is difficult to transition away from imputed or presumptive systems aimed at capturing the small taxpayers. If a goal is to use such a system to bring a taxpayer into the tax net and then to transition the taxpayer to the regular tax system, the tax laws need to keep this in mind. This might be accomplished by setting tax rates under the simplified system at a reasonable rate (not too high nor too low) and creating incentives to move to the regular system (for example, allowing certain deductions only under the regular tax), or imposing a limit regarding the number of years that a taxpayer of a particular size--measured by economic activity--may remain

on the simplified system. Finally, the French method of non-indexed thresholds may also be a natural way to move taxpayers off of the imputed or presumptive system to the regular tax system.

- Collective assessment is likely less corrupted than individual assessment. Presumptive assessment on a taxpayer-by-taxpayer basis might be more accurate, but it doesn't outweigh the corruption.
- Taxpayers should be able to appeal their tax assessments which are based on presumptive or imputed means and they should be able to convert to the regular tax system without an ability to move back to the imputed or presumptive tax structure.
- In general, thresholds should be indexed for inflation. Lump-sum taxes should be indexed for inflation to maintain the integrity of the system. The case for non-indexation when the government allows inflation to transition taxpayers to the normal tax system.
- Presumptive minimum taxes have been relatively effective at raising taxpayer awareness. In some countries (Mexico), these taxes appear to have encouraged an increase in compliance with the regular tax system.

Changes Russia Might Consider

Russia's current tax laws include a Single Tax Law (No. 222-FZ) and an imputed tax law (No. 148-FZ). The Single Tax is aimed at reducing the complexity of the tax system for small businesses by replacing many taxes with one tax, and also reduce accounting and reporting costs. Small businesses qualify for the Single Tax based on thresholds of the number of employees and gross receipts. The system is optional for small businesses and is largely regulated by regional authorities. The current threshold (100,000 minimum monthly wages) is relatively high by international standards. Individual entrepreneurs pay a patent fee, which differs based on industry and region. Legal entities are taxed based on gross receipts or an alternative income calculation (at the discretion of the regional authorities). The alternative income base allows deductions for some inputs, but not all.

The current law on the Uniform Tax (imputed income tax, Federal Law No. 148-FZ: Imputed Tax) specifies the requirements for imposition of the uniform tax. The tax applies to a variety of industries, and imposes eligibility restrictions based on number of employees only for certain industries (public catering, retail trade, and transportation services; taxi cab services were added later). A tax rate of 20 percent is applied to imputed income, which is calculated via a complex formula. The formula is based on the following factors (among others): location, quality of services, quality of premises, distance from highway, inflation, and seasonality. The actual calculation is at the discretion of regional authorities. The tax takes the place of most taxes, with the major exceptions of: state duty and customs duty, land tax, tax on purchase of foreign currency, and withheld income tax and VAT.

Given the international experience with presumptive and imputed taxes, there are some changes to the current simplified and imputed tax laws in Russia that the Government might consider. In particular:

- The Government might consider the simplified system of taxation (Federal Law No. 222-FZ: Single Tax) as the tax used to bring small businesses into the tax net. The current law could then be adjusted to take the follow issues into consideration:
 - The different treatment of entrepreneurs and legal entities may bias one type of taxpayer against another; entrepreneurs pay a patent fee as total liability, legal entities pay a patent which is creditable against the Single Tax. Since the actual cost of the patents is set by the regions, it is difficult to say which type of taxpayer is disadvantaged. Additionally, legal entities under the Simplified System of Taxation pay the Single Tax on a base of either gross receipts or aggregate income. The choice is at the discretion of the regional authorities, which is not necessarily bad if the same rules apply uniformly throughout the region. However, such discretion may invite negotiation of the tax paid and therefore remove some of the potential gains of such a system.
 - The Law could be amended to allow credits only for those taxpayers filing a regular income tax form. This would encourage a movement from the simplified system to the regular system.
 - A Qualifying Small Business subject to the Single Tax must pay value-added tax and sales tax on its inputs, but may not charge VAT or sales tax when goods are sold. Thus, these businesses can not receive a credit for VAT paid. These firms become less competitive as a result vis-a-vis firms selling to VAT and sales tax payers. The law may be amended to exclude the VAT and sales tax from the Single Tax. Alternatively, a threshold may be set to exempt small entities from the VAT all together.
 - The threshold for the Single Tax is relatively high at 100,000 times the minimum wage. The threshold is potentially unpredictable if the official minimum wage is not adjusted in a timely fashion. The threshold may be based in currency equivalent units, tied to the exchange rate of the Central Bank. The Government may want to consider that certain taxpayers may not ever transition to the regular tax structure, and as such, the threshold should not be too high.
 - The income definition could be adjusted to consider currently non-deductible costs.
 - A permanent incentive to move to the regular tax system may be created by establishing a tax liability under the simple tax that is higher than average for the regular tax. An additional incentive may be introduced to encourage taxpayers to move to the regular system via a one-time credit or deduction for the individual or enterprise income tax once the taxpayer moves off of the simplified system to the

regular system. The credit may be justified on the basis of supporting the initial fixed costs faced by a business of complying with the more complicated regular structure. This should be extended to all taxpayers who move from the simple tax to the regular tax.

- The Uniform Tax on Imputed Income (Federal Law No. 148-FZ: Imputed Tax) may serve as a presumptive minimum tax on all legal entities. This could be accomplished by considering the following changes to the current law:
 - Amend the law to so that the tax base is gross assets or gross revenue instead of the complicated tax base currently found in Article 5 of the law. In Russia, gross assets may be quite difficult to estimate and therefore gross revenue may be a better measure for the next five years. As an alternative, the tax base may be based on an imputation method that is simpler than that in Law 148-FZ. Regions should not be allowed to alter the basic calculation. This could then serve as the presumptive minimum tax base.
 - Eliminate the industry classifications; extend the tax to all businesses (legal and entrepreneurial).
 - Create a deduction (or possibly a credit) of this presumptive minimum tax for enterprise profit tax and individual income tax (for entrepreneurs). The deduction (or credit) could only be taken for cash-tax paying enterprises. This creates two incentives: first, to comply with filing for the income taxes, and second, to pay the enterprise profits tax in cash.
 - Changing the Imputed Tax to a presumptive minimum tax could be introduced as a revenue neutral package by eliminating one or both of the current turnover taxes. The revenue sharing issue could be addressed by allocating a portion of the presumptive minimum tax to the regional/local budgets.

Table 1
Presumptive/Imputed Tax Treatment: Small Businesses

Country	Tax Treatment	Conditions
Belgium	Small businesses: Flat rate for three years	Forfait scheme applying to small businesses based on profession (1992) for income below BF 100,00
Greece	Small businesses: Flat rate applied to purchases and receipts	1992
Spain	Small businesses: Forfait scheme for twenty-eight industries	Began in 1992
	Other small businesses covered by a standard flat rate tax	Tax base: sales minus limited expenses
Bolivia	Small businesses in two sectors: Transport (no threshold)	Tax Base: Turnover
	Retail and artisans (threshold of \$4,000 turnover)	Tax Base: Total income
Israel	Small businesses and professionals (no threshold): Tachiv applies to 140 occupations	Tax Base: a mix of total turnover and inputs
Mexico	Small businesses and professional: all industries at a standard percentage	Tax Base: cash flow
Uruguay	Small businesses: all industries with turnover less than \$22,000; taxed as a flat amount (unindexed)	Tax Base: Turnover
Angola	Small businesses: all industries with turnovers less than \$20,000	Tax Base: Turnover
Cameroon	Small businesses: service sector	Tax Base: Flat presumptive amount
Morocco	Small businesses: service sector	Tax Base: Turnover, taxed as a fixed percentage

Table 2
Presumptive Minimum Taxes

Country	Tax Treatment	Conditions
Mexico	Total assets taxed at 2 percent	All sectors except financial
Argentina	Total assets taxed at 1 percent (all except financial) Total assets taxed at 0.4 percent (financial sector)	All sectors
Nigeria	Total assets taxed at 0.5 percent	All enterprises greater than 4 years old are liable
Nicaragua	Total assets taxed at 1 percent	All sectors
Bolivia	Net worth taxed at 3 percent	Replaced in 1997 by an alternative minimum corporate tax

Sources: Rajaraman (1995) and Shome (1999)

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Endnotes

1. Technically, the alternative minimum tax (AMT) used in the United States corporate income tax does not fall into this category as it is not a presumptive tax. However, the philosophy behind the use of the U.S. AMT is quite similar.