

TONGA¹

(i) Status of Tax Treaties

Tonga is not party to any Tax Treaties

(ii) Status of VAT

Tonga passed its VAT legislation (Consumption Tax Act) in 2003 which then came into force on 1st April 2005.

Threshold	- \$100,000
Rate	- 15%
Return period	- 1 month
Registered	- 452 (total)
Volunt regist	- (38)
Revenue 05/06	- \$51,431,252.00
Revenue 06/07	- \$44.1m

Administration

Computer system	- Revenue Management System (Datatorque, NZ)
No. staff	- 9

(iii) Tax Reforms (a) implemented and (b) to be introduced

(a) Tax Reforms implemented

The revenue reform programme began in 2003 with the introduction of the Revenue Services Administration Act. That Act provided the foundation for a modern system of revenue administration based on self-assessment and voluntary compliance. In November 2004 the Revenue Services Department installed the Revenue Management System (RMS) to automate the processing and collection of tax. This represents a major **advance** in the capacity and capability of the Revenue Services Department to carry out its functions.

The next step in the revenue reform programme was the introduction of Consumption Tax on 1 April 2005. Consumption Tax (CT) replaced three former taxes—Port and Service Tax, Sales Tax, and Fuel Sales Tax. There will be a settling in period, as experienced by all tax administrations in both developed and undeveloped countries, which is expected to take up to 12 months before the merchant community, the public and Revenue Services are fully familiar with the operation of the new tax.

Consumption Tax (VAT)

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Since the Act came into force on 1st April 2005, there have been a few amendments to the Act, namely –

- (i) the reduction of the consumption tax period from 2 months to 1 month;
- (ii) the amendment to the definition of “enterprise” to the effect that it includes any independent economic activity **whether or not** undertaken for profit;
- (iii) amendment to the definition of “financial lease” which now includes a lease of goods, meaning that for higher purchase agreements, CT would be collected at each point the payment for the supply is due or received and not at the commencement of the lease; and
- (iv) amendment to the “reverse charge” provision by ensuring that consumption tax would apply even if the supplier and the taxable person receiving the service in Tonga is one and the same (i.e. banks management fees etc).

(b) Tax Reforms to be introduced

The final steps of the revenue reform programme are the changes being proposed for Income Tax, Company Tax and Customs Duty. We had aimed to implement the new changes on 1 July 2007, however with the political events of 16th November 2006 and the administrative challenges of bringing the new laws into effect, the new laws have not been brought into effect. Having said that, the Income Tax Act 2007, Consumption Tax (Amendment) Act 2007, the Revenue Services Administration (Amendment) Act 2007 and new Customs legislation were passed by Parliament on in June 2007 but have not been brought into effect pending the work currently being done on their respective regulations and rates.

The government has developed a set of principles to underpin the proposed changes to our tax system. This is to ensure that any changes are fair and do not hurt those that are most vulnerable in society. The principles that will provide a fair tax system are as follows:

- **Capacity to pay** - Income tax should be based on an individual's capacity to pay which is measured by their total income regardless of its source whether it is from salary or wages, profits or dividends, trading etc.
- **All income should be taxed** - If income is the measure of an individual's ability to pay tax then all income should be taxed alike.
- **Burden of tax should not be on the poor** - People on high incomes should pay more tax because they have more discretionary income and ability to pay.
- **Fair income distribution** - People have the opportunity to either spend or save but those on low income have less opportunity to save so we need a process to distribute the burden of tax fairly.
- **True measure of tax burden** – People need to understand that the true measure of the tax burden is not what the government raises in taxes but what it spends on providing public services.
- **Share the tax burden** – Bringing more income to the tax net will lower the tax rate which means people pay less tax. High tax rates acts as a discouragement to private investment because it increases the cost of doing business.

- **Not over-tax the formal sector** - The business sector represents a small share of total output but a higher proportion of the available tax base. The pressure to raise more tax to fund the cost of providing public services should not constrain private investment and undermine growth and sustainable public revenue.

New aspects of the Income Tax Act 2007 is the introduction of –

- (a) self assessment; and
- (b) PAYE as a final tax;

Proposed tax rates

Individuals -

Chargeable Income	Income Tax Rate
\$0-\$7,400	0%
exceeding \$7,400 but not exceeding 30,000	10%
exceeding \$30,000	20%

Company tax rate (including partnerships) 25%

Withholding tax (residents) (interest, dividends etc) 10%

(a) in the case of an insurance premium 5%

(b) in the case of rent 7.5% or

(c) in any other case 15%.

The Consumption Tax (Amendment) Act 2007 provides for the extension of the due date for consumption tax returns and payment from the 15th of the month to the 28th and other consequential amendments resulting from the new tax laws.

The Revenue Services (Amendment) Act 2007 provides for the registration of tax agents and other consequential amendments resulting from the new tax laws.