

Changes and additions to the Tax Code: possible effects of reducing the Value Added Tax (VAT) rate to certain categories of benefits

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Abstract: *Through this initiative we intend to actually achieve a critical approach to bringing about an extension - through legislation - the scope of the reduced VAT rate, without sufficient substantiation of that measure. Risks that may occur are related to the issue of sustainability of public finances. However, in the final part of the thesis we reveal a number of aspects regarding the budgetary impact of the legislative measure at issue here, given the extremely mitigated fiscal space of the adoption of such formulas of fiscal relaxation, reporting to the current targets of budget deficit in context of restrictions (preventive action) derived from the Growth and Stability Pact.*

Keywords: *Council tax; initiative legislative; budgetary receipts; reduced VAT rate; the sustainability of public finances.*

1. Introduction

Based on the teachings of Adam Smith [1], Laffer concluded that tax rate changes may have on tax revenues and other economic arithmetic effect [2]. As already stated in a previous work of ours [3], the first effect is explained by the decrease in the tax rate attracts clearly a loss of tax revenue and otherwise, increase it will cause revenues tax collected per unit of taxable income to grow.

As for the economic effect, it causes a positive impact of lower tax rates on labor and production and thus the tax base, but an increase in the tax rate has opposite economic effect, namely the participation of subject's penalty taxable activities.

In practice, as it notes and other Romanian scholars have problems taxation [4, 5], the effect of arithmetic will always act to reverse the economic effect and the question that arises is the difficulty in determining that point of optimum respectively tax burden optimal clearly located between two extremes of the tax rate - "very small" and "large", but hard to say where.

Obviously, a reduction of taxes / duties would be, in many respects, as is very welcome, but when attempting fiscal easing should be considered a multitude of constraints. As an EU member state, Romania, beyond the question of whether the margin realistic sliding tax / budget should consider restrictions (preventive) derived from the Stability Pact and Growth [6] and the Treaty on Stability, Coordination and Governance in the Economic and monetary (fiscal compact) [7] implemented in national space on fiscal responsibility Law no. 69/2010 [8].

However, it is certainly in the case of the Romanian economy [3], that politics reduce the level of taxation remains conditional on the development of the real economy, marked by such GDP growth "that can support increasing budget revenues that otherwise would be done by increasing existing tax rates or introducing new taxes" [5].

2. Tests fiscal relaxation on the way of settlement of extending the application of reduced VAT rate of 9% for some services

As adopted in 2015, Law no. 227/2015 regarding the Fiscal Code [9] does not provide for the application of reduced VAT rate of 9% for services such as sanitation, production, transmission, distribution and supply of heat in a centralized system, electricity supply, gas supply and public service localities sanitation.

But after a parliamentary initiative in the current year was targeted modification of the Fiscal Code. This legislative initiative targeting several changes and additions to Law no. 227/2015 regarding the Fiscal Code.

Punctual, according to the text already adopted by the Romanian Senate, they are [10]:

- Increasing the deductibility ceiling for expenditure on sponsorship and private scholarships and introducing the possibility of taxpayers to decide on the destination of an amount of 4% of their annual income tax to support private providers of social services;
- Changing the tax base and tax rate related to the transfer of real estate from the personal property;
- Broadening the scope of the reduced rate of VAT (9%) for sewerage, production, transmission, distribution and supply of heat in a centralized system, electricity supply, gas supply and public sanitation service of the localities;
- Extension of the tax exemption on land and buildings public or private property of the administrative territorial units for carrying out sports activities;
- The annual update by the local authority of the value of non-residential buildings owned by individuals;
- Giving the assimilation of arable land around the building (up to 400 sq m) as construction and land taxation of arable;
- Returning to the first of the month following the month in which the documents were submitted for the application of exemption / reduction of tax payment / tax.

In September 2016, the Romanian Senate has already voted in favor of these changes. In deciding on the imposition of the reduced VAT rate of 9% for services like sanitation, production, transmission, distribution and supply of heat in a centralized system, the delivery of electricity, supply of natural gas and public sanitation service of the localities, it took considering a potential positive element. Namely that reducing VAT in previous years has influenced the living standards of taxpayers and the wider economy through the multiplier effect.

It was further envisaged that the reduction in billings related utility costs will cause "both timely payment of bills and prevent accumulation of debt chain suppliers" [11].

Although to be effectively operational draft law that would have to meet and vote Chamber of Deputies still do some references to the position expressed by the Fiscal Council [12] related to the initiative.

3. The budgetary impact of decrease rate of VAT for certain categories of benefits

In this section of our approach we focus on the intention to amend the VAT regime (through regulation extending the scope of the reduced VAT rate) relating to Fiscal Council position in this regard. Bending Our only on possible changes to the legal regime of VAT (of all measures subject to legislative initiative addressed) is justified by the fact that, as assessed institution mentioned (Council Tax), here comes the negative impact the higher the revenues.

In this context it must be stated that the Council, according to art. 53 parag. (2) let. e) of the Fiscal Responsibility Law no. 69/2010 [8] must write and submit an opinion on a parliamentary initiative to amend the Tax Code.

Moreover, the duties of the Fiscal Council also cover "analysis and elaboration of opinions and recommendations, both prior Government approval and before transmission to Parliament, the annual budget laws, the budgetary adjustments, as well as other legislative initiatives that may have an impact on the volume of spending, and assess their conformity with the principles and tax rules (...)", and "preparing estimates and issuing opinions both on the budgetary impact of the draft legislation, other than those specified (...) and on the amendments made to the annual budget laws during parliamentary debates ..." [8].

By processing certain data and information statistical and economic order, with the intention of determining the impact on budget revenues, the Fiscal Council praised the 'first-round effect of the proposed extension of the reduced rate of 9% (...) is valued at year 2017 - assuming that VAT would be reduced from 19% to 9% - at a level between 1.200 mil. lei (...) and 1.480 mil. lei" [12].

As stated by the institution, it was considered the relevant expenditure in 2014, determined on the basis of the investigation INS [13], after which extrapolated costs relevant dynamics predicted by CNP consumption nominal aggregate service.

In terms of general hypotheses work, I note that the starting point in estimating the loss of revenue caused by the possible adoption / implementation of that draft law "was represented by household spending in Romania with services envisaged for applying a reduced VAT extracted from publication INS (the aforementioned - n.ns.)" and "input data refers to spending money on electricity, gas, water, sewerage, sanitation and communal services (...), which have been deducted from household expenditure for water supply (already falling under the scope of the reduced VAT rate)" [12].

The result of calculations made by the Fiscal Council, taking into account the NIS data on certain consumption [14] and applying the average tariff to the distribution of cold water to the number of persons (individual consumers), considering the VAT rate of 24%, lead by the numbers worthy of attention. Thus, the impact of applying a reduced VAT of 9% for the above services would lead to an annual revenue loss of 1480,9 mil. Lei in 2017 (assuming that the measure would apply from the beginning of that fiscal year).

In the years 2018 and 2019, such losses would 1590,7 mil. Lei and 1700,5 mil. Lei, amounts reached by taking the "loss of revenue estimated at the level of 2014 (which - n.ns.) it was extrapolated to the dynamics of household final consumption expenditures for services registered or designed by Personal Identification Number (PIN) for the period 2015-2019 and taking into account that in 2017 the standard VAT rate will be 19%" [12].

4. Conclusion

The legislative measure extending the reduced VAT rate of 9% for services such as mentioned in the present approach, though it would have a positive impact on the living standards of the population, raises reserves attitude from specialists for taxation.

Mainly it occurs as an explanation why that would widen the structural deficit, risking Romanian economy is entering a significant budgetary slippage, which would determine - according to the European regulatory framework - re-entering our country in excessive deficit procedure.

Therefore, further supporting the measure requires new approaches addressed / countervailing budgetary instruments designed to bring as tax revenues - located only at the level of 2017 - at a rate of over 1480,9 mil. Lei.

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