

Value Added Tax is Not Always a Good Fiscal Lever

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Abstract

The development of national economies is oriented by each government using fiscal and financial levers. The most important issue represents determining what, when and what level these levers need in order to obtain the best result.

Keywords: *value added tax, levers, Ecologic Fiscal Reform*

Adjustment of Activities with Economic Implications by Means of Fiscal Levers

The issue of using fiscal levers is a very old one. The Keynesian School emphasizes the necessity of a substantial intervention of the state in the economy, unlike the liberal economic movement based on the conception “*laisser faire, laisser passer*”.

From the Keynesian point of view, the state can use these levers in order to develop economy. The most used lever is the fiscal one. According to the Keynesian conceptio, the optimal orientation of economy development is simple. When taxes increase, the benefits resulted from economic activities decrease.

Another important aspect is encouraging or discouraging polluting activities, which can only be adjusted by the state. The benefits are proportional to the consumption of resources. In many activities resources consumption has a predominantly natural component, this supposing intervention of man on environment.

Pollution – direct or indirect introduction, as a result of human activity, of substances, vibrations, heat or noise in the air or soil, likely to bring damage to material goods, or to affect or block the usage with a recreative purpose of the environment and/or some other uses, stipulated by the existing legislation.

The integrated vision on products life cycle is very important („nature-nature” cycle), especially when emphasizing the last segment of it, that is, wastes’ reintegration in the environment. Wastes resulted from using oil products, such as plastics, gaseous or liquid fuels, are reintegrated in the environment on longer or shorter periods, these sometimes irretrievably affecting the environment (such as damage of the ozone layer by the gas resulted from incomplete combustion of internal combustion engines. A certain activity is more or less pollutant according to the time which nature needs to recover itself, canceling the results of the human activity. As a result of major damages on environment, economic agents have to pay for helping the nature in the process of waste assimilation. These payments are also called eco-

taxes, and public administrations, private organizations and non – governmental ones are responsible for them.

This theory combined with the theory of world economic efficiency which shows „the matrix of economic efficiency indicators” succeeds in creating a broad vision of human activities, facilitating decision making on initiation, development or stoppage of these activities.

Besides, economic efficiency increase by means of resources economy represents the aim of the paper, „Factor four – doubling prosperity by half reduction of resource consumption”. The paper brings into discussion arguments for a rational resource consumption, such as: a better life, less pollution and deterioration, markets command and economic involvement, increase of capital usage, improving safety, equity and more jobs. [1].

After an extensive economic development with high resource consumption human kind has oriented to an intensive development. The main reason for choosing this development strategy was the increase of resource price, first of all due to reducing exploitable resources, but also to other factors that led to the increase of exploitation costs.

What has been identified and shown less is the fact that resource consumption increase rises proportionally to the damaging substances eliminated in the environment. Even the manufactured goods, being products of entropic processes, mostly represent pollution sources.

In the beginning of the millennium the most acute issue is that of environment health, which also depends on the human king survival, more on all living creatures of the Earth.

Unfortunately, man, by his psychological nature, acts in such a way that allows him to increase the level of his living style on a short term. Human behaviour is mainly based on individual interest, which, unfortunately, aims at earning money no matter the price paid. In the economic field it is based on an economic activity which usually consumes resources, so it is a polluting type of activity. Resource consumption may be extensive or intensive, both being approached in order to increase the entrepreneur’s benefits.

We can thus notice the fundamental contradiction between individual’s short terms interests and the long terms ones of the community.

In such a case, the administrative institutions of the community are assigned the difficult task of trying to keep a balance between the two tendencies. This balance is usually set by means of fiscal regulations imposed by the assigned institutions of the state. The state represents the institution that is allowed to act in this respect, knowing the fact that the market usually represents the short terms interest of economic agents.

David Ricardo states that „all taxes should be imposed on either capital or property” [2]. It is normal for 1821, when he wrote it in his book „ On Principles of Political Economy and Impositions”, that these taxes be a reality and at the same time an economic necessity, as at that time nobody cared about depletion of resources in such a relatively short time, or about the pollution resulted from resource exploitation and use. It was a time for capital accumulations and large properties and the fiscal regulations mentioned above were really necessary. In the same paper, David Ricardo explains how to use taxes as a fiscal lever: „without taxes, this increase of capital (in economy on.) would have been higher” [2]. After almost 200 years, the economic, social and environmental situation has radically changed. The tendencies that should guide world’s activity at the moment and especially in the future are those of creating less polluting advanced technologies as resources are fewer and fewer, and in order to get them we act on the environment more intensively and extensively and it recovers harder and harder or sometimes it does not recover at all.

Taxes aim at orienting the economic agent towards having the same interest as the community. This is immediately partially satisfied by redistributing the gross internal product to which the economic agent has financially contributed. At the same time taxes are long term levers by

means of which the society representatives try to achieve an economic and implicitly a social program. The interests of the community are not in accordance with the short term interests of the economic agent, more precisely with its will of being able to use its property rights completely and to exercise its right of deciding how to integrally use the property rights.

The art of building and using fiscal instruments by the representatives of the state actually represents finding those tax values that allow maintaining a balance between the possibility of satisfying the economic agent's interest and the community interest.

A major objective of any community economic policy is that of assuring a long term development taking into account the effects of economic-social phenomena globalization.

Usually, elaborating and selecting fiscal levers aims at supporting community interest, a common phenomenon, if we take into account those that are supposed to observe them. One can notice some questionable aspects as far as the correctness of functioning and applying the instruments

Ecologic Fiscal Reform (EFR) was issued in 1920 in Great Britain. Arthur Cecil Pigou stated that taxes should offer appropriate adjustment of prices. Ecological products are due to have lower prices adjusted by means of taxes.

In „Factor four – doubling prosperity by half reduction of resource consumption” the authors state that Europe should adopt a slow change of taxes, which should be neutral as far as the long term profits are concerned. The authors claim that the first regulation should deal with price increase for energy and primary resources, with approximately 5% per year for a period of over 20 years. Bob Repetto and Roger Dower from World Resources Institute in Washington, Charles Ballard and Steven Medema from Michigan State University, that have studied the effects of „pervert taxes”, agree with this point of view [1].

For example, Germany's Federal Environment Agency has published a report stating that the ecotax has reached its target and demanding the establishment of a broader ecological fiscal reform. According to the Environment Agency, the ecotax has advantages for business and employees amounting to billions of Euro – a much better outcome than its reputation would lead one to expect. The experts defend the ecotax as a steering mechanism for business and politics in their report.

The tax on petrol, diesel and other energy sources introduced in 1999, in Germany, certainly works as it was intended [3]. The aim of the ecotax was to cut energy use and relieve the pension funds – and, according to representative surveys and research carried out by the Berlin Institute Ecologic and the German Institute for Economic Research (DIW) – precisely this has been achieved. A representative survey carried out by Ecologic in September 2004 revealed that half of those asked have been more aware of their energy consumption since the introduction of the ecotax. The Environment Agency's report also revealed that economy has profited – ecotax benefited innovative, energy-saving companies and clearly reduced ancillary wage costs. Since 2003, there have been developments in some economic sectors that make it clear that the tax must be further developed for it to continue to be effective.

Ancillary wage costs fell, according to the study, by approximately 8 million Euros annually. Almost 90 percent of all funds raised by the tax were paid directly into the pension fund, to reduce pension payments. Without the ecotax, pension payments in Germany today would be 1.7 percent higher than their present levels – not 19.5 percent, but 21.2 percent [3].

Non-Linear Pattern of Taxing

As an example, the paper aims at analyzing a small part of the fiscal system in our country in order to identify a solution in the EFR spirit.

It can be said that VAT represents a double taxing of other taxes claimed by the state. For example, taxes applied to salaries are also taxed by means of VAT, salaries and expenditures being the main source of the added value basis. Obviously, VAT stands for discouraging economic agents from increasing the added tax and, implicitly, the salary funds (the number of employees and the average salary of the company). Correlating the theory of substitution of production factors, the economic agent will be encouraged to consume much more elements of the capital and implicitly natural resources, with all the negative aspects resulted from this phenomenon. A community that aims at its economic development considers VAT not to be one of its best options.

This is one of the reasons for which I consider wrong the present economic policy of states that use as main taxing basis employees' work and exercising the property rights. The main income source to the state budget in Romania is represented by indirect taxes (VAT and excises represent 65% of budgetary incomes) [4]. Under these circumstances, extraction, processing and natural resources consumption are encouraged at present and this contributes to the occurrence and emphasis of pollution risks. What is more important is the fact that we can contribute to the correction of this negative aspect by issuing relatively high taxes on extraction and natural resources consumption, or even null to the labor factor and the added value.

Taking into account the pitfalls of the taxing classical systems, I have thought of a non-linear taxing pattern for an economic agent's profit. The pattern aims at better answering the necessary requirements and principles for economic organizing of a modern state. The pattern starts from a classical, linear formula for calculating the taxes, in which an efficiency coefficient has been added. Taken as an example the calculation formula for tax on profit, the following result has been obtained:

$$I = P \times K_1 \times \left[K_2 + \left(\frac{C}{Va} \right)^{K_3} \right] \quad (1)$$

where:

- I – value of profit tax;
- P – value of exercised profit;
- C – total cost recorded during the exercised;
- Va – added value;
- K1 – adjustment coefficient of tax value;
- K2 – amplifying coefficient;
- K3 – slide correction coefficient.

The adjustment coefficient of tax value can be used in order to establish a correlation between profit value and tax value.

Amplifying coefficient aims at emphasizing the efficiency indicator influence on the final result of the formula.

By using the K3 coefficient a dependence relation can be determined between the change of added value and the change of tax value, in this case, the relation being an exponential one.

The K2 and K3 coefficients give the possibility of adjusting the pattern in accordance with some particular aspects of economic branches. More precisely, we refer to the variable percentage of the average added value within the total specific incomes of a certain branch.

The advantages of using this pattern are:

- encouraging the creation of new jobs, that will lead to development and increase of the added value;

- discriminating and discouraging raw material consumption and goods on condition of low added value;

Economic agents that are great consumers of natural resources (raw materials, goods, energy) are those that contribute to environment pollution. This leads us to the conclusion that tax reduction for those that aim at realizing a optimal balance between general consumption and added value represent an advantageous process in accordance with national and global desiderata regarding encouragement of reducing pollution and unemployment

Superiority of non-Linear Taxing Pattern

One can state that this pattern tries to move a part of the tax weight point, from profit to consumption. While profit represents an engine of economic development, the unadjusted consumption, directly uncontrolled by society, may become a negative factor in the economy of a community.

Obviously, the profit has to be taxed, but the present pattern of profit taxing encourages consumption. This, together with the pitfalls of other taxing systems and taxes exercised so far have determined a certain economic evolution of the environment at global, but also European and national levels.

In all previous analyses, the value of the indicators whose change has been stimulated has had a linear variation. It is well known the fact that, in reality, the phenomena especially evolve non-linearly, their linearity being only accepted as a theoretical pattern.

The pattern is difficult to apply in present conditions, as the calculation formula is not a very accessible one. But, taking into account the development of calculation techniques we tend to believe that it will not take long till many economic agents will use computers in order to keep accounts and, implicitly, finances.

However, the pattern can be simplified, without mainly affecting its fundament. Although Romania is part of international agreements and legislation is adapted to the community, the pattern remains a theoretical issue that can be discussed and thought as an economic way of thinking in the fiscal field. At the same time it can be analyzed following some simulations and a comparative study that can be the objective of a previous analysis.

I therefore consider that this pattern is the result of a way of thinking oriented towards less developed economy support and, implicitly, Romanian economy, to which they represent an immediate, a real and substantial support in their development. The pattern is important for the economic agent behavior, which is oriented towards psychological factors.

References:

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Taxa pe valoarea adăugată nu este totdeauna o bună pârghie financiară

Rezumat

Dezvoltarea economiilor naționale este orientată de fiecare guvern utilizând pârghii financiare și fiscale. Un aspect foarte important îl reprezintă determinarea tipului pârghiilor, a ariei lor de aplicare și a nivelului la care trebuie stabilite aceste pârghii, astfel încât să se obțină cel mai bun rezultat.