

13 January 2005

**Response to
QUESTIONNAIRE ON TAX REVENUE**

Continuation: TAX CREDITS

This questionnaire is first sent to the members of working team C (tax and tax credit) in preparation of the TFHPSA meeting to be held in Paris on 2-3-4 March 2004.

The first two parts of the questionnaire were sent in December 2004. This is Part 3: "Recording of tax credits".

PART 3: RECORDING OF TAX CREDITS

1. Definition:

"a) Most tax systems include elements of social redistribution, through the tax schedule (increasing tax rate), the choice of tax unit (individual or family taxation) and tax reliefs. Tax reliefs aimed at redistribution may be designed to reduce the amount of tax that households pay according to certain characteristics, such as the number of children. Moreover, tax reliefs may also be designed to encourage certain activities, such as participation in the labour force or investment in research and development.

Tax reliefs can generally take the form of a tax allowance, exemption or deduction - which is subtracted from the tax base - or of a tax credit - which is subtracted directly from the tax liability. Tax credits can sometimes be payable, in the sense that any amount of the credit that exceeds the tax liability will be paid to the taxpayer (or non-taxpayer). In contrast, some tax credits are non-payable, and so are limited to the size of the tax liability.

A tax relief that is embedded in the tax system should be recorded as reducing tax revenues. This is the case of tax allowances, exemptions and deductions, as they enter directly into the calculation of the tax liability. This is also the case for non-payable tax credits, as their value to the taxpayer is limited to the size of their tax liability."

Question 1: Do you agree with the above definition a)?

Yes

No

Possible amendment:

HM Treasury and the tax authorities note that this section mixes a definition of tax credits with how to record them. Perhaps the section should be split into two, with the first two paragraphs being the definition and the third paragraph noting how to record the tax credits. It might be worth adding that where, exceptionally, a non-payable tax credit is not embedded in the tax system, it should be treated wholly as a government expense.

Comment: The Public Sector Committee of IFAC has a different definition and recommendation (see the majority view in the “Invitation to comment” on “Revenue from non-exchange transactions”). The PSC steering committee recommends to gross up the tax revenue in respect of all “expenses paid through the tax system” (benefits available to entities irrespective of whether or not they pay taxes, in other words: payable tax credits)

“b) However:

Payable tax credit can result in the government making a net payment to the taxpayer. This occurs in cases where the total amount of the credit exceeds the amount of tax liability (tax due) and so the element of the credit in excess is paid by the government to the taxpayer. The sum of such individual net payments is to be recorded as government expense and not as negative tax revenue.”

Question 2: Do you agree with the above specification (b) However:...)? Yes No

Possible amendment:

2. Relevant conditions and criteria :

“The recording of tax credits as negative tax in national accounts should meet some conditions and criteria:

- a) Tax consistency: the tax credit measure must appear as part of the tax law, tax calculation and of tax statements.

- b) Could be deducted only from a given tax, amounts that are calculated on the same base as the tax - usually the income – and over the same period of time. For example, possible VAT reimbursements to specific categories of the population, should not be recorded in national accounts as a deduction from their tax on income.

- c) By contrast, if the amount can be calculated independently of the procedure for calculating the tax payable, then it is unlikely to be a tax credit.

- d) Individual character of tax credits: the amount recorded as negative tax – to be deducted from tax due – cannot exceed the amount of tax due by the beneficiaries on an individual (or household) basis. Thus, individual tax information must be used in order to calculate the amount of credit to be expensed. The element due in excess is an expenditure of government (see also 1 b) above), and will not be deducted in the reporting of global tax revenue.”

Question 3: Do you agree with the above conditions and criteria?

a) Yes No
b) Yes No
c) Yes No

d) Yes No

Other possible conditions and criteria:

We do not agree with criterion (a) because it is too restrictive – it is too much tied to administration and is too country-specific.

On (c), we believe that the criterion could be made clearer by amending it to read “..if the amount to be treated as negative tax can be calculated...”.

Although we agree with criterion (d), we wonder whether it belongs to the previous section since it is about recording rather than about whether something is a tax credit.

We also attach the criteria which we have previously shared with the task force.

3. Possible supplementary criterion:

Not all transactions that might be, in practice, netted from the amount of tax due to be paid should be recorded as tax credits in national accounts: in particular credits which would cover income substitute benefits, related to typical income risk, like pensions for retirement, disability or unemployment, are always recorded as expense rather than negative tax.”

Question 4: Would you agree to introduce this supplementary restriction (drawing the line in a more constraining way between negative tax and certain social benefits – having the character of income substitute)?

Yes No

Possible amendment:

We believe that the issue is how closely the tax credit is related to the tax system, not what it is for. It is important, therefore, that the criteria in Q3 are properly applied.

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