

January 2005

Response to QUESTIONNAIRE ON TAX REVENUE

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 on 3-4-5 March 2005 in Paris. The intention is to reach an agreement on the basic orientation and wording of this section in the future chapter dedicated to the public sector in the updated SNA.

The questionnaire is divided in 3 parts, corresponding to the three major identified issues: 1. Definition of tax revenue 2. Accrual recording of taxes 3. Recording of tax credits. The part 3 will be sent a little later.

Warning: the case of social contributions is not considered as such in this questionnaire. However, provisions in part 2 “Accrual recording of taxes” are relevant also for the recording of social contributions.

PART 1: DEFINITION OF TAX REVENUE

1. General presentation of the section

Question 1: *Do you agree* that the presentation should include:

Yes

- the definition (1§, see below), immediately followed by the list of main tax categories (as an illustration of the definition)
- additional provisions on the borderline with other fees and transactions (taxes and sale of services, taxes and sale of assets)

2. The definition

The following definition modifies slightly and completes the present one (see SNA93, §7.48 and 8.43). The main changes are related to:

- the specific character of taxes, as “compulsory” and “unrequited” payments (“nothing in return” being replaced by “nothing directly in exchange”), and as resulting of the “sovereign powers” of government (IPSAS)
- an illustration of the definition through the list of main tax categories

“Taxes are compulsory, unrequited payments, in cash or in kind, made by institutional units to government units exercising their sovereign powers. In most cases, the compulsory payment of taxes is conditioned by another noncompulsory economic event: earning of income, ownership of an asset, purchase of good or service, or, in some cases, request for a permit or a licence. Taxes are usually described as unrequited because, in most cases, the government provides nothing directly in exchange to the individual unit making the payment.

The acquisition of a permit or licence can sometimes constitute the acquisition of a service or of an asset (see below “Borderline with other fees and transactions”).

Classification of taxes (unchanged):

D.2: Taxes on production and imports

D.21: Taxes on products
D.29: Other taxes on production
D.5: Current taxes on income and wealth
D.51: Taxes on income
D.59: Other current taxes
D.91: Capital taxes”

Question 2: Do you agree with the above definition:

Yes

Question 3: The new definition uses the expression “nothing directly in exchange”. Would you refer more explicitly in the definition to the IPSAS concept of “non-exchange transaction”?

Yes

Question 4: Would you agree to show in annex of the chapter on the public sector in the updated SNA the detailed list of tax, according the SNA classification, which is the subject of table 0900 (disseminated by Eurostat and OECD)?

Yes

Other possible amendment to the definition: please see above proposed revisions to the text

4. The borderline with other fees and transactions

- Not all compulsory or unrequited payments are taxes. Some payments having these characteristics are to be recorded as other current transfers (D.7, e.g. fines and penalties).
- Moreover, the borderline between taxes and payments to government for services rendered or for acquiring an asset is not always clear cut in practice. The rationale developed in SNA93, §7.55 and 8.45 “Taxes versus fees”, is relevant and should be confirmed. Its implementation requires the following guidance:

a) The case of licences and permits delivered by the government.

- Record as tax: Whenever a licence or a permit is automatically granted to all applicants against payment (? Please see note below) of the amount due, while involving little or no work on the part of the government.

Example: licences to own or use vehicles, boats or aircrafts, and licences to hunt, shoot or fish

Note: “payments”- is this consistent with accrual recording?

- Record as a payment for a service: Whenever the issuance of the licence or permit implies a proper regulatory function of the government (exercising control on the activity, checking competence or qualifications of the persons concerned etc.). unless the fee is clearly out of proportion to the costs of providing the service;

Example: driving or pilot licences, firearm licences

- Record as payment for the transfer of an asset: Whenever the licence or permit meets a few conditions and characteristics of an economic asset (see SNA93, §13.12) to be used in the production of goods and services or as a store of value:

. over which ownership rights are enforced by institutional units

. from which economic benefits (in the form of income or holding gains) may be derived by the owner over a period of time, and, as a consequence, the licence being tradable on the market, the payment should be recorded as the corresponding to the transfer of an asset. (See note: “as a consequence”)

Example: licence for taxi company, licence for telephone company (in particular UMTS licences)

Note: “as a consequence” - I am not sure that the definition of an asset implies that it is tradable on the market. This implication is not in the SNA, I think.

Note: “purchase” – Why purchase and not sale, which is the term used to formulate question 1? [“(taxes and sale of services, taxes and sale of assets)”. Anyway, the choice of term would depend on whether the transaction is attributed to government or to other sectors.

Question 5: Do you agree with this orientation?:

Yes

b) The case of certain fees

In all cases when fees are directly linked to a service - the service is provided in return for the fee - the payment is to be recorded as a sale of a service by government (consistently with SNA93, §7.55 and 8.45: “Taxes versus Fees”). A few examples are:

- Admission fees charged by government controlled museum or library: whenever these fees are at a price which is not economically significant, they constitute payments made by households for a non-market service provided by a government unit rather than a tax. Other payments for non-market output may be: admissions to public universities, public hospitals etc.

Note: should the case of fees at economically significant price be mentioned?

- Waste collection and garbage disposal: as a consequence of the above definition (SNA93, §7.55 and 8.45), fees collected by the government for providing a service (whether or not the service is then sub-contracted to a corporation) should be analysed as constituting a payment for a service to the extent that:

- . they are mainly assessed on the value of the work to be carried out and not to the value of the property as such
- . it is possible to identify the value of the fees

- Television and radio fees: payments by households for the public service of radio-television are to be recorded as the payment for a service (to the government or to a public corporation according to the sector classification of the public unit providing the service), rather than as a tax.

- Road tolls: they are normally to be recorded as the purchase of a service (the use of a road).

Question 6: Do you agree with this orientation?:

Yes

Possible amendment: See proposed above revisions to the text.

PART 2: THE ACCRUAL RECORDING OF TAXES

Question 7: Do you agree that in the updated SNA, SNA 9, §7.59-60 and 8.49-50 should be replaced by the following wording, exposed in the three new paragraphs below:

Yes

Paragraph.1: Like most transactions in the SNA, taxes (and social contributions) are to be recorded on an accrual basis (see also SNA chapters 2 and 3). Accrual recording means that flows are recorded when economic value is created, transformed, exchanged or extinguished and not when cash payments are made.. This principle encompasses all the taxes due that can be expected to be collected one day. Taxes that are not expected to be one day collected must not be recorded.

Note: collectible or collectable do not exist in the sense used above. At any rate “collectable” and “not collectable” would be preferable to “collectible” and “uncollectible”.

The implementation of this general recommendation for taxes (and for social contributions) leads to consider successively the two questions:

- the time of recording
- the amounts to be recorded

Question 8: Do you agree with the draft paragraph 1?:

Yes

Possible amendment: See proposed revisions above

Paragraph.2: Time of recording:

This is when the activities, transactions or other events that create the liability to pay taxes occur - in other words, when the taxable events occur - and not when the payments are actually made. In the case of taxes (and social contributions), this usually means when income is received or when a transaction (sale of goods and services etc.) generating the tax liability is made, to the extent that that the liability can reliably be measured.

Question 8: Do you agree with this principle (in paragraph 2)?

Yes

Some flexibility is permitted in two cases where this assessment cannot be made in a reliable way before the time of assessment:

- **Parallel economy**: In some instances, the activities, transactions or events at the origin of the tax liability may escape the attention of the tax authorities¹. In such cases, it is difficult to relate the tax liability to the underlying economic event, and the amounts to be recorded can only be determined at the time of assessment. If it cannot be the time of the taxable economic event itself, the relevant time of recording may be then the time of the tax assessment. (Not necessarily, please see note below)

Note: This phenomenon is not limited to the parallel economy and one should distinguish between the parallel economy and the recorded economy. In the case of the recorded economy, the moment

¹ Parallel economy is a major factor explaining the difference between what the government is entitled to collect under the tax law and what is really collectible. This difference is often referred to as the “tax gap”.

point at which the underlying economic event occurs can be usually identified. Therefore, while the amount to be recorded should be the one determined at the time of assessment, it should be attributed to the accounting period of the underlying event. In the case of the parallel economy, the relevant time of recording may be the moment of the assessment whenever the underlying economic event cannot be dated.

- **Taxes on income:** taxes on income may be paid 1/ in the same time as the revenue (pay-as-you-earn type) or 2/ at a later point in time, depending on the tax system (set-up of a roll (I do not think this term exists) or other form of tax assessment). In the first case, the link between the tax liability and the taxable event is clear and the accrual recording straightforward (except for the final settlement), as long as the lag between the tax payment and the underlying economic event is short. In the second case, the liability to pay income taxes is determined in a later accounting period other than the period in which the income accrues and becomes taxable. The moment of the tax assessment is the time when the tax liability is measured and known in a reliable way, taking into account possible changes to the tax rates and the final settlements.

Therefore, in these two cases, the relevant time of recording the taxes may be not the time when the economic event generated the obligation to pay taxes, but the time when the taxes were assessed as due with sufficient certainty. (I do not agree: please see note below) This is not necessarily similar to the accounting period of the payment. In the specific case of prepaid taxes on income, the accounting period of the payment may be considered as the relevant one.

Note: I think the last paragraph needs to be redrafted, notably the last 2 sentences. More importantly, I do not think that, in both cases, the relevant time of recording is the time when the taxes are assessed. In the second case, the time of recording is still determined by the date of the underlying economic event, even though the amount is determined only at the time of assessment. One should not confuse time of assessment with time of recording.

*Question 9: Do you agree with the drafting on flexibility in paragraph 2?*²

No See note

above

Question 10 (with IPSAS): is the tax gap equivalent to the amount of uncollectible taxes?. Should this be clarified?

Yes No

Yes this should be clarified. I am not sure that the “tax gap” was defined. It should be. Is this an IPSAS concept? I could not find it.

Possible amendment: Please see remarks and proposed revisions

Paragraph.3: Amounts to be recorded

Accrued taxes may be understood as due amounts of taxes (or amounts of taxes due to be paid), especially when they are made available as such by tax assessments. However, recording accrued amounts of taxes (and social contributions) should not lead to record amounts that are not expected or are unlikely to be collected. The balancing items of the general government should not be artificially improved by the recording of amounts of taxes which are not collected.

² This is a redrafting but not a change brought to SNA93 (see §8.49 and following, and in particular 8.52)

There are two basic methods of valuating accrued amounts of taxes:

1. The time-adjusted cash method: are amounts actually received, but attributed to the period during which the tax liability accrued.

2. Methods based on assessments of due taxes: there are two possible methods to eliminate from the assessment taxes that are not expected to be collected:

- amounts assessed as due are to be adjusted by a coefficient reflecting the assessments never collected in the recent past and the amounts of accrued tax are reduced accordingly.

- amounts assessed as due are entirely recorded as taxes (and social contributions). But the discrepancy between this theoretical amount and the actual cash receipts shall be treated as a capital transfer in favour of defaulting payers. Note; why capital transfer? Taxes are current transactions; why should the correcting entry be a capital transaction?

A combination of methods is possible, according to the different types of taxes (and social contributions). In principle, statistical methods used to achieve accrual recording of tax should ensure that, in the long-term, cumulative assessment and receipts of tax revenues are equal. However, the shifting of recording tax backwards over time may have the consequence that cumulated tax revenue is higher on an accruals basis than on a pure cash basis, as a result of the general economic growth (in volume and in price). I do not quite understand since the “shifting” consists in taking cash amount and treat them as if they were accrual amounts. The two should therefore be equal. This last sentence must be clarified or eliminated.

Question 11: Do you agree with the draft paragraph 3?

Yes

I agree with the broad content, but would suggest of proposed revisions to be taken into account.

We agree in general with the draft paragraph 3 and particularly with the core idea, that the balancing items of the general government should not be artificially improved by recording of amounts of taxes which are not collected. Referring to methods based on assessments of due taxes, we consider that **amounts assessed as due should not be entirely recorded as taxes, (and social contributions)** as we do not consider prudent treating the discrepancy between the amount of taxes accrued and the actual cash receipts as capital transfer from the government to the debtors. Recording amounts assessed as revenue implies that the so called “tax gap” is recorded as government subsidy. In that line we suggest to drop out the following wording: “- **amounts assessed as due are entirely recorded as taxes (and social contributions). But the discrepancy between this theoretical amount and the actual cash receipts shall be treated as a capital transfer in favour of defaulting payers.**” from paragraph 3, item 2. OK

Question 12: should it be considered that “An adjustment on the revenue side of the general government is preferable to an adjustment on the expenditure side”?

Yes

What “adjustment” is being discussed? The adjustment for uncollected taxes? Yes, it should be made to the revenue side.

Note: The word “revenue” is used. Should’nt the words “government resources” be used instead? There is no concept of government revenue in the current SNA.

Other comment: Please refer to the comment stated in the answer to question 11.

Appendix:

International comparisons are currently made on the tax burden, or rate of compulsory levies to gross domestic product. These assessments are more and more based on national accounts data.

Question 12: *Should the notion of compulsory levies be defined in the updated SNA?*

Yes

Yes: but this is unrelated to the previous statement on tax burden. It is nice to define compulsory levies in the SNA but not necessary, either from a methodological standpoint or for consistency's sake.

Vincent Marie
Statistics Department
International Monetary Fund
United States