

20 December 2004

**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 No
- 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)

The list of tax categories must be linked to a list of compulsory, unrequited payments received by governments that are not taxes. See question 4 below.

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 economic event (not compulsory by nature): earning of income, **property ownership of an asset or purchase of good or service. Taxes are usually described as unrequited because, in most cases, the government provides nothing directly in exchange to the individual unit making the payment, although governments use the funds raised in taxes to provide goods and services to other units, either individually or collectively, or to the community as a **whole**.”**

However, in certain cases, the tax payment may also correspond to the acquisition of a permit or authorisation (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

No

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

No

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

No

Other possible amendment to the definition:

Add a statement that not all compulsory, unrequited payments received by government are taxes. In particular, most social security contributions, fines and penalties, and certain current and capital payments of compensation are not taxes.

4. The borderline with other fees and transactions

This paragraph belongs in the previous section.- 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:** If a licence or a permit is granted automatically to all applicants on payment of the amount due, involving little or no work on the part of the government, it should be recorded as a tax. **Example:** licences to own or use vehicles, boats or aircrafts, and licences to hunt, shoot or fish. **It would be useful to refer to the need for the government to have exercised its sovereign powers to require the permit.**

- **Record as purchase of a service:** If 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.), the payment should be recorded as the purchase of a service produced by the government, unless the payment is clearly out of proportion to the costs of providing the service;

Example: driving or pilot licences, firearm licences

- **Record as purchase of an asset:** If the licence or permit meets **all of the ~~a few~~** conditions and characteristics of an economic asset (see SNA93, §13.12), making it 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 purchase of an asset.

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

Question 5: Do you agree with this orientation?:

Yes

No

The examples given are from the current paragraph 8.54(c), but they should be indicated as examples that could be treated differently in different countries. If a convention is to be adopted that these specific fees should always be taxes or services, then they should be stated as such.

I agree with the comments of the UK/ONS that the phrase “clearly out of all proportion” is vague. The Task Force should consider whether it is possible or not to make the meaning more precise. Reference to a quasi-corporation would not be appropriate because a quasi-corporation cannot, by definition, receive any taxes.

It is not clear why an asset must be tradable. I think the condition can be deleted.

The reference to the purchase of an asset needs careful consideration. This statement does not distinguish between the payment of a multi-year tax which would create an financial asset equal to the taxes paid in advance, and the purchase of a permit that has the characteristics of a non-financial asset. It is far from clear that there are any permits that should be treated as non-financial assets. The example of UMTS licenses is especially problematic.

b) The case of certain fees

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

- **Museum or library admission fees:** they are a typical case of payments made by households (at a price which is not economically significant) for a service provided by a government unit. They are not tax but payments for a non-market service. Other payments for non-market output may be: Admissions to public universities, to public hospitals etc.

- **Waste collection and garbage disposal:** as a consequence of the above recalled definition (SNA93, §7.55 and 8.45) fees collected by the government for assuming this task (whether or not this task is then sub-contracted to a corporation) should be analysed as a purchase of 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 for the public service of radio-television are to be recorded as the purchase of a service (to the government or to a public corporation according to the sector classification of the public unit providing the service)

- **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 No

Possible amendment:

I agree in general, but the points made by the UK/ONS are valid and may require some revisions to the language.

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 No

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. If this principle would be understood as requiring to record *due amounts* of taxes (as the consequence of the underlying economic event, and under the existing tax law), this should not in any case lead to record uncollectible taxes. [The reference to chapter 2 does not seem necessary](#)

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 No

Possible amendment:

I agree with Søren Brodersen that the reference to uncollectible taxes is not clear.

Paragraph.2: Time of recording:

This is when the activities, transactions or other events occur which create the liability to pay taxes - 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 paid or when a transaction (purchase of goods and services etc.) generating the liability is made, to the extent that the tax liability can reliably be measured.

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

Yes No

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

- **Parallel economy**: some activities, transactions or events **permanently** escape the attention of the tax authorities¹. It is then difficult to put in relation the liability to pay taxes and the taxable economic event. The amounts to be recorded can be determined only when some tax assessment is made **or other documents are obtained evidencing the tax liability**. 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.

- **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 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). In the second case, the liability to pay income taxes is determined in a later accounting period than that 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. 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.

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

Yes No

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

Yes No

Possible amendment:

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”.

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

The paragraph on the parallel economy is about the amount to record, not the time.

I disagree with the final sentence of the paragraph on taxes on income. The time of recording should be stated as a simple principle as stated above. Implementation may require a divergence, but it should be considered an imperfect method of implementing the same principle.

Question 10 is two questions. I am not sure my answers would be the same to both because I do not fully understand the terms tax gap and uncollectible taxes. If used, both need to be defined in the SNA.

There is a casual reference to “final settlement” of income taxes. We need to specify how it is to be handled.

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) - at the time they are due or generated - should not lead to record amounts that are known to be uncollectible, or 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.

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

1. The time-adjusted cash method: available amounts are amounts actually paid. Nevertheless, these cashed amounts of taxes should be recorded, or shifted, at the time the tax liability was accruing.

2. Methods based on assessments of due taxes: there are two statistical methods which may eliminate the effect of uncollectible taxes on these assessments:

- amounts assessed as due are to be adjusted by a coefficient reflecting the assessments never collected in the recent past. Thus, the amounts of accrued tax are written down according to this adjustment, in such a way that uncollectible taxes are not recorded as government revenue.

- 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.

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, cumulated tax revenues are equal, whether compiled on the basis of cashed amounts or on the basis of assessed amounts. 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).

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

Yes

No

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

No

Other comment:

I strongly disagree with a capital transfer. I agree with Søren Brodersen to the extent that more details are needed in the SNA to explain the resolution of the problems he cites.

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

No

Compulsory is already used in the SNA. It should be retained and defined more explicitly.

John Pitzer
United States