Tax Reforms: Experiences and Perspectives

HELENA BLAŽIĆ, KATARINA OTT AND HRVOJE ŠIMOVIĆ (Eds.)
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Pursuing the maximization of revenue collection or public good provision, governments enact tax reforms. A tax reform can be addressed to improve the tax system or tax compliance (*fairness-oriented*), to tackle better macroeconomic performance (*growth-oriented*) or to reduce the incentive to take on debt (*sustainability-oriented*).

Since the country's independence, the Croatian tax system has undergone numerous tax changes, but it was with the tax reform enacted in 1994 that its foundations were laid. Marking its 20th anniversary in 2014, the Institute of Public Finance, the Faculty of Economics and Business Zagreb and Faculty of Economics Rijeka jointly organized a conference to discuss and understand the economic implications of tax reforms from different standpoints. The book entitled *Tax Reforms: Experiences and Perspectives*, edited by Helena Blažić, Katarina Ott and Hrvoje Šimović, is a collection of sixteen papers presented at the aforementioned conference held in Zagreb on June 20th, 2014. Beside the papers, the book contains a foreword written by the editors, the conference program, information about the organizers and a list of donors, making a total of 293 pages.

The sixteen papers are of a miscellaneous character and therefore the book is not organized into well-defined parts or sections. Some works discuss tax reform issues subject to one of the three main objectives – fairness, growth and sustainability, some present country case studies that detail a specific tax system before and after all the enacted reforms, while others show opinion survey results regarding the tax system and tax reforms. Accordingly, the review will try to cover the main results and conclusions of the majority of the papers without following the order presented in the book.

As previously mentioned, the 1994 tax reform is considered fundamental in the design of the modern Croatian tax system. The focal point of this reform was the introduction of consumption-based direct taxation (interest-adjusted personal and corporate income tax), a concept consistently implemented during the nineties. However, subsequent tax changes enacted in the 21st century reveal a switch, or a propensity to switch, to income-based direct taxation (saving-adjusted personal and corporate income tax). Challenged by that fact, as well as by the necessity objectively to evaluate the advantages and disadvantages of the two concepts, Šimović, Blažić and Štambuk (*Perspectives of tax reforms in Croatia: expert opinion survey*) conduct a broad opinion survey among Croatian experts. Their results indicate that experts from the academic sector are not particularly in favour of any of the direct taxation concepts, while experts from the government sector seem to prefer the income-based concept. Moreover, authors' results indicate that (all) experts in Croatia solve the traditional equity-efficiency trade-off in favour of equity, whereas the government sector (again) expresses higher social sensibility than academia.

In a similar manner, Klun *(Slovenian experiences and lessons from tax reforms)* analyses the opinion of Slovenian experts about tax reform outcomes in Slovenia. She finds that all the experts are in great agreement that Slovenia's tax reforms were merely sustainability- rather than growth-oriented. As emphasized by Klun, it is interesting that all the experts point out that the effort to improve tax compliance falls down when it comes to the matter of enforcement and that the government is too loose with respect to tax avoidance, while being too hard with those willing to comply. Nerré, Dragojlović, Randjelović and Djenić (*Tax Reform in Serbia: experiences and perspectives*) suggest that reforming tax policy to improve sustainability and fairness or boost growth is worthless, if the tax administration stays unreformed. Although concentrating their analysis on the Serbian case, the authors pinpoint the fact that most of the transition economies focussed solely on tax policy reforms, neglecting the need to improve the tax administration at the same time. According to Nerré, Dragojlović, Randjelović and Djenić such a choice is positively correlated with the level of tax evasion and lack of transparency in transition economies.

Therefore, the fight against fraud and tax evasion presumes an efficient tax administration. Bronić and Bratić (*Can the efficiency of the Croatian tax authorities be improved?*) show that the efficiency level of tax authorities in Croatia improved in the 1997-2012 period. However, they proxy efficiency with the tax administration's costs-to-GDP ratio, which has to be distinguished from efficiency as measured in terms of the tax administrations' ability to detect and sanction tax evasion or to simplify tax compliance. Assessment of these is actually unfeasible, not only for Croatia, but also for most of the transition economies due to the insufficiency of statistical data. Nevertheless, finding an appropriate balance between tax avoidance and tax simplicity in practice proves to be difficult, especially if globalization and tax competition are brought into picture.

Gadžo and Klemenčić (*Time to stop avoiding the tax avoidance issue in Croatia? A proposal based on recent developments in the European Union*) show that Croatia can be considered an example that lacks a genuine and coherent anti-avoidance policy. They propose that as a first step Croatia should implement the so-called general anti-avoidance rule (GAAR) as endorsed by the European Commission. Gadžo and Klemenčić argue that GAAR, as a legislative framework, beside curbing tax avoidance, improves tax equity, tax efficiency and tax competitiveness. In contrast, Hybka (*Legislative proposal for controlled foreign companies regime in Poland from an international perspective*) writes that Poland introduced a number of measures to solve the tax avoidance problem. However, she finds the so-called controlled foreign company (CFC) legislation to be the most significant in controlling corporate income tax avoidance. Hybka explains that this measure applies to two specific groups of shareholders: those whose companies are located in countries using harmful tax competition, and those whose companies have registered offices in countries where passive income is taxed at a significantly lower rate than it would be if the shareholders' residence country tax rate is applied. Although she finds a number of benefits in this anti-avoidance measure, Hybka questions the overall net effect, fearing that the increased complexity of tax compliance could actually (again) favour tax avoidance.

Pendovska and Neshovska (*Tax reforms: experiences and perspectives – the case of the Republic of Macedonia*) show that the Macedonian tax system largely benefitted from the simplicity introduced with the flat tax reform: corporate income tax revenue in Macedonia grew much faster than planned and the enacted tax reforms provided significant economic stimulus to the private sector. Although focusing on personal income tax, Lazović-Pita (*Income, personal income tax and transition: case of Bosnia and Herzegovina*) shows that a flat tax system is the best solution for transition economies such as Bosnia and Herzegovina, at least during an "intermediate phase" before the enactment of a progressive income taxation system. She refers to the Slovak case, emphasizing that the move to a progressive income taxation is favourable only when the one percent of the wealthiest become visible.

The recent global economic crisis showed that a number of governments resorted to fiscal policies in stabilizing the economy, enacting thus growth- or sustainability-oriented tax reforms. Šimurina and Primorac (*The role of tax policy in the fiscal recovery of the European Union*) investigate the outcomes of tax policy measures implemented during the latest period of the Great Recession. They find that the tax measures enacted increased the overall tax burden in almost all EU member states. Moreover, Šimurina and Primorac show that income-, rather than consumption-taxation measures are more effective when the main objective is an increase in government revenues. Additionally, Jędrzejowicz and Sławińska (*Shifting from labour to consumption taxes: the impact on tax revenue volatility)* suggest that consumption (indirect) tax revenues are characterized by larger volatility, therefore shifting from income to consumption taxes increases the sensitivity of public finances to the business cycle.

Świstak, Wawrzak and Alinska (*In pursuit of tax progressivity: lessons from VAT rate structure adjustment in Poland*) seem to be in accord with Šimurina and Primorac. Namely, they argue that in Poland the increment in the standard VAT rate accompanied with the decrement in the reduced VAT rate only slightly improved the overall progressivity of the tax system, providing a minimal relief to the poor and a substantial subsidy to wealthier households. Świstak, Wawrzak and Alinska show that with a small change to the income tax structure the government could have secured more progressivity at a lower costs in terms of revenue foregone. On the other hand, Latvia's labour tax reform in response to the economic crisis served the targeted low-wage earners group (Šņucins and Kodoliņa-Miglāne in *Reform of Labour Taxes in Latvia*).

Altogether, the book *Tax Reforms: Experiences and Perspectives* certainly makes a contribution to the better understanding of tax reforms in general. Since a tax reform, no matter what its objective, is always an economic and political issue, the book combines the economic arguments for a tax reform with political and legal aspects. The book's writing is not particularly difficult to read, but requires knowledge of basic economics and/or public sector economics. However, along with researchers, students and experts, the general public can also benefit from the practical approach of the book. From a reader's point of view three main strengths emerge: (1) the book gives a fairly good theoretical background for a variety of tax reform-related topics, (2) it discusses tax reform issues under the lenses of two important contemporary contexts: the great recession and the European Union, and (3) it gathers information about changes in the tax bases and/or tax rates for a notable number of (post)transition economies (Croatia, Slovenia, Bosnia and Herzegovina, Serbia, Macedonia, Poland and Latvia) in one place. On the other hand, both the enclosed papers and accordingly the book as a whole are very often short on empirical testing and proofs for given positive economics statements, or, if they are present, the robustness of the results remains uncertain. Moreover, a number of papers seem to stop where one expects them to actually begin, leaving the policy implications discussion rather scanty. To conclude, the book (and conference) aimed to (a) compare experiences, and (b) draw lessons from tax reforms in different countries. It is possible to conclude that the first goal has been successfully reached, while the second is still left open. Drawing lessons from tax reforms is an extremely ambitious multidisciplinary task since it involves not only economic, but also political, legal and social aspects, made all the more challenging by globalisation.