

Chapter 18

The Perception of Tax Complexity Within Local Authorities' VAT Framework: Evidence From Portugal

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ABSTRACT

The relevance of the impact of tax complexity on tax noncompliance justifies the study of tax complexity in the scope of several taxpayers, including local authorities. This chapter analyses the case of the value added tax (VAT), a typical example where the misuse of exemptions and no subjections imply the no payment of taxes by citizens. Therefore, this chapter tries to assess, qualitatively and quantitatively, the levels of tax complexity perceived in local authorities' administrations through the amount of binding tax information those organizations request. The results suggest a high degree of perception of tax complexity and uncertainty as well as a lack of transparency associated with the tax framework of the activities of local authorities. It is pointed out that the perceived complexity is essentially legal. Moreover, the findings establish a relation between some more complex legal changes with great tax impact within these entities and the increase of the number of binding tax information requested on their subjects.

INTRODUCTION

Tax complexity is a worrying phenomenon, which has been earned the attention of political decisors, tax policy makers and academia, since several studies highlight the existence of a positive relation between the high levels of tax systems complexity and the intentional and the unintentional tax noncompliance. Moreover, a very complex tax system tends to be less transparent, to have high levels of tax illusion and

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that increases the public expenditure (see Puviani, 1903; Buchanan & Wagner, 1977; Mitias & Turnbull, 2001; Becker & Mulligan, 2003; Afonso, 2014).

Thus, tax complexity is a problem of public financial management and public governance, since its consequences may expose public policy.

In the Portuguese case, despite the efforts to simplify the Portuguese tax system in order to make it more transparent and easier to deal with, it continues to be classified, both nationally and internationally, as very complex, particularly by the Portuguese Working Group for Tax Simplification (MF¹, 2007), the Working Group for Tax Policy (Santos & Martins, 2009), as well as by the OECD (Organisation for Economic Cooperation and Development) (2010a) and the World Bank (2011), which classifies Portugal as one of the European countries with greater tax complexity and tax bureaucracy.

Moreover, this is not a Portuguese problem, this is a phenomenon common to most countries. In many countries, studies reinforce that taxpayers display tax noncompliant behaviours as a result of difficulties in interpreting tax laws, such as Australia, United Kingdom, Spain, France, USA, Canada, Central Asian Republics and so on. (see Gammie, 1996; James & Wallschutzky, 1997; Tran-Nam, 1999; Lopes, 2003; McKerchar, 2002a, 2002b; McKerchar *et al.*, 2008; Freedman, 2009; Evans & Tran-Nam, 2010; Saw & Sawyer, 2010; Lopes, 2012a; Evans, 2012; Galbiati & Zanella, 2012; Mokhtari & Ashtari, 2012; Borrego, 2015; Borrego *et al.*, 2015).

Although this positive relation is more evident in the private sector, it could also be a problem in the public sector, especially in local authorities, with consequences in unintentional tax noncompliance.

The relevance of this issue in the Portuguese local authorities' tax environment mainly centres on the collection of taxes from citizens, especially in the VAT (Value Added Tax) case, where the improper application of exemptions and no subjections implies the taxes that should be paid by the citizens are not collected.

As a rule, the State appears in most studies as legislator and tax collector, however the State and public bodies (namely local authorities) are also taxable persons (taxpayers) in the majority of taxes (however, as it is well known public entities are very often exempt from taxes). Therefore, in this chapter the local authorities are analysed in the perspective of VAT's taxable person.

Based on a qualitative approach, this paper analyses the level of perception of tax complexity and uncertainty associated with the Portuguese local authorities' tax framework in VAT by using legislative analyses. We believe that the high number of IRS's binding tax informations concerning local authorities' VAT framework² is associated with a high degree of perceived tax complexity and an uncertainty, in particular as regards tax law interpretation.

It should be noted that the requests for binding information are sent by taxpayers - in this case by the local authorities and their suppliers - to the IRS, which processes them and responding to taxpayers.

The binding tax informations do not have force of law, they only bind the IRS to the situation in concrete that was exposed in the request (with the taxpayer(s) involved). However, those requests are used by other taxpayers to know the Portuguese IRS's tax understanding, in order to avoid conflicts with the IRS. It is important to note that taxpayers paid the binding tax information requested to IRS.-

Thus, we selected for tax complexity analyses four articles from the Portuguese VAT Code, Art. 2 (subjective incidence), Art. 9 (exemptions), Art. 18 (tax rates) and Art. 23 (mixed taxable persons³), which for local authorities represent the main sources of request of binding tax information.

This paper is divided into three parts, excluding this introduction. Firstly, there is a brief tax literature review on tax complexity; secondly, the framework of VAT taxation of local authorities is described, emphasizing the areas of greater complexity; finally, we draw our main conclusions and suggest further lines of tax research.

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