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in Spain: VAT and Excise**

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International Studies Program
Andrew Young School of Policy Studies
Georgia State University
Atlanta, Georgia 30303
United States of America

Phone: (404) 651-1144
Fax: (404) 651-4449
Email: ispaysps@gsu.edu
Internet: <http://isp-aysps.gsu.edu>

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The Reform of Indirect Taxation in Spain: VAT and Excise

José Sánchez Maldonado and J. Salvador Gómez Sala
Universidad de Málaga

Introduction

The role of indirect taxation in the Spanish tax system has a long tradition, as reflected perhaps by the fact that Spain was the home of the alcabala, the most ancient general form of indirect taxation¹. By the 1970s, indirect taxes accounted for around 65 percent of total tax revenue, in large part due to the continued delays and failed attempts to put in to place a modern personal income tax. However, after successive modifications to tax legislation (see Box 1) since the restoration of democracy, the share of indirect taxes fell to 55 percent of total tax revenue in 1986 and to 45 percent at the beginning of the present decade.

In this chapter we analyze the reform and evolution of consumption taxes in Spain over recent decades, paying particular attention to the new developments stemming from the introduction of the VAT in 1986 and the modifications carried out to excise taxes in order to bring the Spanish tax system into line with European Community legislation. In the second section we proceed to review the situation of consumption taxation in Spain in the years previous to the democracy's fiscal reform. The third section deals with a basic description of the before mentioned reform and includes an analysis of its main economic. It ends with the consideration of the role of indirect taxation in the financing of the territorial governments. The fourth section describes the evolution of the consumption taxation pattern in Spain in relation to other OECD countries, beginning in the year 1965. The fifth section analyzes the process of fiscal harmonization of the VAT and of excise taxes in the European Union. The incidence of indirect taxation in Spain is studied in the sixth section from a personal and territorial perspective, given the implications of this last one in the finance of regional and local governments (Comunidades Autónomas y Corporaciones Locales). In seventh section, we consider the main pending issues as well as a variety of future reform options. The last section of the paper offers some concluding thoughts.

Box 1: Important Tax Legislation Modifications

Law of Emergency Measures (Law 50/1977) - The public was first introduced to the idea of a total reform of the tax system.

General Law of the Indirect Tax Regime (1979) – Laid the groundwork for the VAT.

The Excise Tax Law 39/1979 - Dealt with the issue of modernizing these taxes.

Law 30/1985 on VAT and Law 45/1985 on Excise Taxes - The reforms of the VAT and excise tax laws in 1993 were made necessary by the introduction of the Single Market.

The Consumption Tax System before the 1977 Tax Reform

The consumption tax system before the fiscal reform of 1977 had been in force since 1964 and revolved around three main components: the general tax on “company trading” (sales), the tax on luxury goods, and excise taxes. These were complemented by other taxes of lesser importance, such as taxes on the income from the petrol and tobacco monopolies, advertising, radio and television duties and customs duties.

Within this fiscal framework, the General Tax on Company Trading (*Impuesto General sobre el Tráfico de las Empresas*, IGTE) was by far the most important in quantitative terms. This tax was basically a Spanish version of the multiple general sales tax which had been used in other European tax systems and whose earliest precedent can be found in the old Spanish alcabala tax. It has long been recognized that this form of taxation suffers from many problems, arising from both the type of sales tax chosen as well as the specific formulation of the tax. Thus, the accumulative multi-phase or “cascading” nature of the general tax on company trading gave rise to a series of problems: there was a severe lack of neutrality, which promoted the integration of firms; the tax burden was not uniformly distributed with respect to the value of the different goods; investment goods suffered from double taxation, on the one hand from their sale and on the other from the sale of final products whose price included the amortization of the investment goods; it gave rise to the well-known pyramidization effect on prices and gave rise to non-neutral tax adjustments at the borders for export and import activities. Moreover, the IGTE did not tax the whole production and distribution process up to the final acquisition by the consumer because retail trade was not subject to the tax. Finally,

the tax benefits conceded were very costly in fiscal terms and there were administrative problems which proved to be an obstacle to the efficient management of the tax.

To summarize, the multi-phase IGTE taxed all the phases or stages of the production and distribution processes from fabrication to final consumption (attempting, at the same time, to avoid levying the tax at the final retail stage) in such a way that at each stage the tax applied to the accumulated value including the tax paid in the previous stages, thus levying a tax on tax and leading to the pyramidization of the tax. Again, the results were the arbitrary creation of para-fiscal benefits, incentives for vertical integration, and in some instances export dumping².

The tax on luxury goods, on the other hand, was comprised of a large number of taxes on a list of goods and services which were classified as luxury commodities. On a first principle basis the existence of this tax was made compatible with other indirect taxes because of its specialized pursuit of the equity objective. However, from an efficiency perspective the tax on luxury commodities had important negative effects since it was levied on the production or distribution of certain goods and services which had previously been subject to other indirect consumption taxes, in particular the IGTE. This thereby accentuated the double taxation effects and the lack of uniformity with which the burden of the general tax on company trading was distributed across sectors. Moreover, because the tax on luxuries was comprised of numerous charges which were applied at various rates, the result was a further departure from neutrality for the entire set of consumption taxes.

The remaining component of consumption taxation in pre-reform Spain was formed by the excise taxes, which were taxes on specific goods which supposedly existed in their

own right (*sustantividad propia*) and their tax treatment at that time was independent of the treatment other goods. In particular, excise taxes and the IGTE were mutually exclusive. Excises applied to the fabrication of certain goods and the supply of particular services. In total, there were six excise taxes: tax on liquor, tax on sugar, tax on chicory, tax on beer and soft drinks, tax on petrol, and tax on telephone use. Different rates were applied for each, which again aggravated the lack of neutrality of indirect consumption taxes. Of course, some of the non-neutrality was intentional and in some cases, for example liquor or petrol, was justified because of the externalities the consumption of those commodities imposed on others. Nevertheless, the different effective indirect tax rates on commodities were arbitrary and hardly justifiable. The malfunctions of the consumption tax system grew to a crisis stage making clear the need for deep reform.

The principles underlying the future reforms of consumption taxes in Spain are documented in two comprehensive studies: The first, the “Report on the Spanish Tax System” (I.E.F., 1973), also known as the “Green Book”, and the second, “Spanish Tax System: Criteria for Reform” (I.E.F. 1976), known as the “White Book”. After undertaking a serious critical analyses of the existing regime, these studies proposed a new configuration for consumption taxation in the country built around two main levies, the Value Added Tax and (the new) Excise Taxes.

The Reform and Modernization of Consumption Taxes

The process of modernizing the consumption tax system in Spain began with the 1978 fiscal reform and was consolidated with the entry into the Common Market at the beginning of 1986. The initial stage covering the years 1978-85 was a transition period with some partial reforms of the consumption tax system.

The 1977 Reform

The tax system in place at the beginning of 1977 had two basic characteristics. On the one hand, fiscal pressure was at a level well below that of the average for EEC members. Total tax receipts amounted to 21.6 percent of GDP, 13.1 points below the average for the European Community (excluding Spain) and representing half of the fiscal pressure of countries with the highest taxes in that year (the Netherlands). Only Greece, Portugal and Italy had comparable fiscal pressure indices. On the other hand, the structural characteristics of the tax system converted it into an obstacle to the process of economic modernization which was to come.

At that time, half of the government's revenue (from coercive sources, that is) came from Social Security contributions, close to 30 percent corresponded to indirect taxation, and just under 20 percent came from personal income and profit taxes. Prominent among the indirect taxes was the IGTE, a "cascading" tax which plagued interior transactions with distortions and which was not neutral with respect to international trade as it gave rise to the need for complex frontier adjustments which, as already mentioned, facilitated protectionist practices.

Coinciding with the change in political regime, the urgent need to meet increasing social pressure in favor of increases in public expenditure made radical reform of the tax system necessary, and this became a priority in the political agenda. All political and social forces were in agreement over the need to tackle a profound reform of the tax system. This consensus took shape in an agreement called the Programme for Economic Overhaul and Reform, and known as the Moncloa Pacts, signed on the 25th of October, 1977.

The starting point of the 1977 reform goes back to a year earlier when the government approved on November 14th, 1977, Law 50/77 of Urgent Tax Reform Measures. This law had a major social impact and informed public opinion of the idea of the needed changes in the tax system. This first step was aimed above all at securing the objective of reforming the tax system and strengthening a new ethic of tax compliance (tax amnesty, abolition of bank secrecy, creation of a special patrimony tax and the introduction of criminal sanctions for fiscal offences).

Within this framework, the Transitory Indirect Tax Regime Law (*Ley de Régimen Transitorio de la Imposición Indirecta*) was passed in 1979 with the primary aim of preparing the way for the Value Added Tax which would inevitably come into force at a future stage. In the following years the IGTE tax rate was gradually increased to levels close to that of the future VAT so that excessive distortions were avoided; property transfers by companies and company income from property rental were subjected to tax; and taxes on the exportation and purchase of natural products were eliminated³. Also in preparation for deeper reforms in excise taxation, the government passed Law 6/79, changing various aspects of the Luxuries Tax, including the modification and elimination of taxable events, and the simplification of tax rates.

In January 1980, the new Excise Tax Law (*Ley de los Impuestos Especiales*) came into force, representing the first major change in the area of excise taxes. This reform had the aim of modernizing these taxes and was spurred on by two basic, concurrent needs: firstly, the need to adapt the structure of these taxes to the ideas prevailing at the time in the European Economic Community (EEC) with an eye to the eventual incorporation of Spain into the European Community; and secondly, the need to coordinate these taxes

with the future Value Added Tax in such a way that they would together constitute the basic pillars of indirect taxation. As a consequence of the above, the excise taxes on sugar and chicory were eliminated and those on soft drinks and telephone usage were maintained conditional on the coming into force of the VAT.

Furthermore, there was a notable rise in tax rates, fundamentally on Ethyl Alcohol and Alcoholic Drinks Tax. The same occurred with the Tax on Petroleum, Derivatives, and Similar Products, where the tax concept “Monopoly Income” (*Renta del Monopolio*) was replaced by the concept “Excise Tax”⁴.

Finally, the Tax on Manufactured Tobacco was given Excise Tax status. The effective introduction of this tax was also linked to that of the VAT, so in the meantime manufactured tobacco continued to be charged in accordance with the Luxuries Tax Law (*Texto Refundido del Impuesto sobre el Lujo*)⁵.

Thus, in this initial stages of tax reform the foundations were laid for the future, definitive, introduction of VAT and the modernization, technification and systematization of the excise taxes.

The 1985 Reform

The second stage of tax reform covered the years 1985 and 1986. The highlight of the reform was the adaptation of Spain’s consumption taxes to meet the demands for entry into the European Common Market.

The VAT was introduced into the Spanish tax system in Law 30/1985.⁶ After countless studies and three legal bills, the VAT came into force on January 1st, 1986, in a climate of distrust. Business taxpayers were concerned with its practical implementation while the public was afraid of the possible effects on consumer prices.

The Spanish VAT model followed the sixth Community Directive, whose philosophy is to tax economic fact, meaning the generation of value by firms which in turn determines the value of final consumption, rather than legal entities. VAT is, above all, a tax based on economic rationale whose operational features are carried out in an accounting context. In keeping with this, the main characteristics of Spanish VAT are the following:

- It is a consumption-type VAT, that is, an immediate deduction is permitted for the VAT associated with investment activity carried out during the period when the goods were acquired.
- It is applied using the tax credit method, that is, the VAT to be paid or returned is determined by the difference between VAT receipts and payments.
- Certain activities are exempt from VAT charges. Among these are the public postal service, medical services (except hospitalization in private clinics with no price controls), social work, education, insurance, gambling, leasing of real estate, services of plastic artists, writers, musicians, etc. These exempted activities only have the right to deductions for VAT paid, which means that this is just another cost for those companies which sell these types of goods and these will try to incorporate this into the sales price.
- Goods and services which are exported are also exempt from VAT charges in the country of origin. In this case, however, the exporter can deduct VAT paid. On arrival at the frontier of the exporting country, VAT payments which have been made by the exporter are returned to him, so the product crosses the frontier of the importing country free of indirect taxes. At the frontier, the products are charged with the VAT

of the destination country. This assures that all the products in a given market compete on the same conditions, thereby preserving efficiency with regard to the decisions of the consumer.

- In principle, three rates were contemplated: a general rate of 12 percent; a reduced rate of 6 percent for necessity goods; and a higher rate of 33 percent for luxury goods. At present, the general tax rate is 16 percent, and two reduced rates, one of 6 percent and another of 3 percent. The 6 percent rate is applied to food products; health material; housing; passenger transport; certain types of hotel and restaurant services; cinema, theatre and other cultural services; rubbish collection; waste treatment; and funeral services. The lower reduced rate of 3 percent is applied to certain foods; books, magazines and newspapers; certain pharmaceuticals; cars and prosthesis for the handicapped; and social housing.
- VAT paid on purchases can only be deducted when the goods acquired correspond to activities on which the tax is placed. This means that if a company carries out different activities, some exempt and others not, a pro-rata rule must be applied so that VAT is only deducted for purchases which correspond to taxed activities. There are a series of purchases for which deductions are not allowed for VAT payments made. The objective of this restriction is to prevent personal expenditure and expenditures which are not directly related with professional or firm activity from being converted into firm expenditure. Thus, there is no right to VAT deductions for, among other things, the purchase or hire of vehicles, travel costs and expenses which are considered remuneration as far as personal income tax is concerned, and expenditure on jewellery.

- There is no limit on the deduction for VAT paid on purchases. Thus, if in a given fiscal year the VAT paid on purchases was greater than that received on sales, the excess can be deducted in later fiscal years or the Treasury will reimburse the company.
- Special regimes exist for agriculture, small firms, used goods, antiques and valuable objects, travel agencies, and retail trade. The equivalent surcharge regime deserves a special mention. This consists of a surcharge applied by manufacturers or wholesalers to certain retailers in lieu of the VAT which should be charged. Merchants are not obliged to do the accounting needed to settle the difference between VAT payments and receipts. The dues which should be paid in are charged by the suppliers through the application of a surcharge to the sales price ranging from 0.5 percent to 4 percent depending on the type of good.

To summarize, it can be stated that Spanish VAT is a tax which is borne by the consumer, rather than the businessman or professional. Strictly speaking, it does not fall on value added, and its magnitude does not depend on the number of phases of transformation or distribution through which a good passes. Finally, the typical form of collection is the application of a rate of tax to the sale price to the final consumer.

Many taxes were absorbed by the Value Added Tax, including the General Tax on Company Trading (IGTE), the luxuries tax, certain excise taxes (those charged on soft drinks and telephone usage) and the compensatory scheme for internal charges. Similarly, when the VAT came into force the tax deductions on exports were abolished.

The Royal Decree-Law 6/85 adapted indirect taxation in the Canary Islands, Ceuta and Melilla. VAT is not applied in these Spanish territories and they maintained the

IGTE along with special provincial levies (*Arbitrios*). Afterwards, Law 10/1991 regulated the special position of the Canaries. As is well-known, the treaty covering Spanish accession to the European Community, signed in 1985, excluded the Canary Islands from the VAT regime, under a commitment to introduce taxes which would compensate for this exemption. When the transition period came to an end, the Canary Island's General Indirect Tax (IGIC) was created, as were the Dock Dues (*Arbitrio*) on Production and Exports. These are taxes which come under State law, and are usually modified on an annual basis through State budget legislation. This occurred through Article 11 of Law 24/2001 (December 27th) on fiscal, administrative and social order measures, which replaced the original excise tax with a new one called Dock Dues on Imports and Delivery of Merchandise to the Canary Islands (AIEMIC - *Arbitrio sobre importaciones y Entregas de Mercancías en las Islas Canarias*), that has been in force since the 1st of January, 2002.

In very simple terms, the IGIC is an indirect tax on sales which is somewhat similar to VAT but which has lower tax rates and is applied to fewer goods than VAT. The AIEMIC is an indirect tax on which each good is charged a specific tax rate in accordance with the structure of the European Community's customs tariffs. The regulation of the formal obligations surrounding the IGIC, the setting, within a predetermined band, of the tax rates applicable, and the administration, settlement, collection and inspection of the tax all correspond to the Autonomous Community. With regard to the AIEMIC, however, the Autonomous Community is only responsible for the tasks of administration, settlement, collection and inspection.

On the other hand, Law 8/1991 (25th March), through which the Dock Dues on Production and Exports was passed for Melilla and Ceuta⁷, adapted the local tax regime of these cities to the second Protocol of the Accession treaty. Article 25 of this Treaty covers the conditions under which the provisions of the EEC and ECSC Treaties regarding the free movement of goods are to be applied, as well as the acts of the Community institutions in relation to customs' legislation and trade policy in the Canaries and Ceuta and Melilla. This tax is basically an indirect tax of municipal character, which is charged on the production, manufacture and import of all types of movable goods, services provisions and the supply of immovable property situated in the cities of Ceuta and Melilla.

The second part of the 1985 reform also consisted of the adaptation of excise taxation to EEC standards. This was achieved in the same year through Law 45/85 on Excise Taxes, which was introduced due to the need to restructure indirect taxation. Excise tax reform is justified on several grounds. In the first place, there is coexistence with VAT generated problems of both compatibility and double taxation which had to be addressed. Similarly, the process of tax harmonization, which we refer to later, is a problem that needed to be resolved. In the third place, the very nature of the excise tax system gave rise to a series of deficiencies, including a lack of neutrality due to the different tax percentages applied to the final price of each product and the distortions arising from the use of excise taxes rates.

Different options for reform were possible which included: the elimination of the excise tax with its corresponding integration into the VAT; independent conservation of excise taxes, where these would have the characteristics of a tax on specific consumption

goods; or making all consumption goods subject to VAT while at the same establishing an excise tax on certain categories of consumption goods. The second of these options was adopted, in line, as we will see later, with the majority of developed countries.

After the approval of Law 38/1992 and subsequent partial reforms, Spanish excise taxes were organized as follows:

a) As a single stage tax on manufacturers in the following cases.

- taxes on alcoholic beverages:

- tax on beer
- tax on wine and fermented beverages
- tax on intermediate products⁸
- tax on alcohol and derived drinks

- tax on hydrocarbons

- tax on retail sale of certain hydrocarbons

- tax on manufactured tobacco

- tax on electricity

-tax on insurance premia

b) As a single stage tax at the retail stage in the case of the excise tax on certain means of transport

In the new regime Excise Taxes coexisted with the VAT in the sense that excisable commodities pay the excise tax first and on top of that they pay the VAT (on a price that includes the excise tax). This is a common international practice and is justified through the negative externalities argument: the consumption of certain goods (the excisable goods) is in some way detrimental to society in that it generates social costs which are not

included in the private costs or price of the goods. These additional social costs are “internalized” through a specific tax on the consumption of these products which provides disincentives to consumption as well as compensates for those social costs to the community at large generated by such consumption. Thus, these specific taxes serve not only to raise funds for the exchequer but also as policy tools in the areas of health, energy, environment, and so on.

Principal Economics Effects of the Reform

The aforementioned fiscal changes, especially the introduction of VAT, had important economic effects both with regard to the personal and sectoral incidence of indirect taxes as well as the modifications it implied to the mechanism for fiscal adjustments at borders. Regarding the consequences for the volume of the tax revenues, the political aim of the reform was to make it revenue neutral, leaving the tax burden unchanged in such a way that VAT would provide the same tax intake as the taxes which it replaced. In particular, the choice of the three tax rates of 6, 12, and 33 percent had this objective in mind. It can be checked that the elasticity of consumption tax revenue with respect to GDP rose as a consequence of these modifications. Concretely, using OECD data (“Revenue Statistics of OECD Member Countries”) we estimate that the elasticity in relation to consumption taxes as a whole was around 1.0054 for the period 1965-1985, rising to 1.051 for the period 1986-2001. If we consider general consumption taxes only, the introduction of the VAT in 1986 significantly raised the elasticity with respect to GDP – we estimate it was 0.994 during the period 1965-1985, rising to 1.195 in 1986.

Castellano and Raymond (1985) analysed the economic consequences of the introduction of the VAT in January 1986. Using Input-Output tables, these authors

argued that the introduction of the VAT would add between 2 and 4 percentage points to the private consumption deflator, based on the downward rigidity of prices and the different distribution across sectors of the tax burdens from the Tax on Company Trading (ITE) and the VAT. Later, Burgos *et al* (1992) analysed the effects on the main macroeconomic variables, especially inflation, of the reforms introduced in January 1992 on the VAT, hydrocarbons taxation, and tobacco taxation. They found that these taxes added 1 percent to the inflation rate.

González and Rey (1998) analysed the consequences of the changes to indirect taxation for prices. These authors found that reductions in VAT rates translated into an immediate and integral fall in prices, whereas the rises in prices when VAT rates were raised were either not maintained over time or were not integral. Among the various increases in VAT rates, they estimate that the rise which took place in January 1992 produced a practically integral rise in prices. In August 1992 and January 1995, on the other hand, they estimate that the inflationary impact was quite lower than that which would have been produced had there been an integral price rise. Their explanation for such asymmetry is the incidence of the cyclical position of the economy. Whereas in January 1992 national demand was still rising at rates of over 3 percent, in the summer of the same year there was a considerable weakening which led to a deep recession. The authors believe that in certain periods companies were unable to pass some of the tax increases onto prices, with the consequence that profit margins suffered during what were particularly difficult times.

Izquierdo, Melguizo and Taguas (2001) analysed the effects on the evolution of the Consumer Price Index (CPI) of the introduction of the VAT and subsequent legislative

changes to this tax, as well as the effects of changes in the three most important excise taxes – alcohol, tobacco and hydrocarbons – over the period from January 1983 to December 2000. The main methodological contributions of this study are that it employs a level of disaggregation beyond the five classical components of the CPI, which permits a more detailed analysis of the results, and that the sample period used covers all the modern reforms to indirect taxation in Spain. These authors estimate that the introduction of the VAT in 1986 caused an increase of two points in consumer prices. They also estimate that the three point increase in the normal rate in 1992 together with the reduction in the higher rate from 33 percent to 28 percent provoked a further increase of 1.3 points in consumer prices; the creation of the super-reduced rate of 3 percent in 1993 reduced prices by 0.3 points; the general one point rate rise in 1995 increased prices by 0.5 points; the reduction of vehicle registration tax in 1996 caused a reduction of 0.1 points; and, finally, the reduction of VAT on butane from 16 percent to 7 percent in 1999 reduced prices by 0.05 points.

Izquierdo, Melguizo and Taguas (2001) also obtain consumer price series for tobacco, hydrocarbons and electricity for which the variations due to changes in indirect taxes have been eliminated. Aggregating these results with the effects of changes to the VAT, they find that the consumer price level in the year 2000 was 5.6 percent greater than what it would have been in the absence of the legislative changes. This implies that the rate of accumulated inflation from 1983 to 2001, 142.6 percent, would have been 13 percentage points less than that observed.

With the introduction of the VAT in 1986, associated with accession to the European Community, a debate arose surrounding the possibility of substituting social

contributions with the VAT in an attempt to favor employment and exports. (Benelbas et al., 1987, Servén, 1988 and Zabalza, 1988). The argument used was the potential positive effect of the VAT on external trade in comparison with social contributions which were not “frontier-adjustable”. As Spanish producers have tended to be labor-intensive, the incorporation of social contributions into prices would damage the competitive position of companies. Thus, a policy of reducing these contributions, balanced by increases in VAT, would favor employment. According to Izquierdo, Melguizo and Taguas (2001), however, if the structure of the tax wedge is not important, and its level does not vary, the positive effect on employment and the potential benefits to the external sector would be eroded under the present provisional VAT regime and the large volume of intra-Community transactions.

Finally, the complex workings of the IGTE with cascading effects on prices made it impossible to determine the correct rates which should have been applied to compensate for internal tax payments and to tax deductions on exports⁹. Under the IGTE, the result, depending on the case at hand, was that imports were either penalized or subject to deductions and exports. These imports were either given hidden subsidies or compensated insufficiently since no one knew with certainty how much tax had been paid in the case of the exports and what was the right equivalent tax for the case of imports. This situation changed radically with the introduction of the VAT. One great advantage of the VAT is its external neutrality: precise calculations could be made of the needed tax adjustments which had to be made at borders in order to apply the principle of charging the tax in the country of destination. This is the standard treatment of indirect taxes in international relations, in general, and in the European Communities in particular.

Thus, the introduction of the VAT did away with a set of fiscal adjustments which particularly affected export sectors. Therefore, the change in the tax scheme would affect primarily the economy export sector through the alteration of border tax adjustments (Soto Guinda, 1982, p 132). If these adjustments, alongside with the substitution of the VAT for the IGTE, would mean a relatively higher burden for imports and a lower burden for exports, the implement of the VAT would bring an advantage for the commercial balance, and vice versa. According to the *Memoria* which accompanied the first *Proyecto de Ley de IVA* (bill on the VAT; published on the *Diario de las Cortes* from 14-9-1981), the most numerous group of exporters (concretely, around 75 percent, who took on more than the 60 percent of the total exports) was going to be favored by the implementation of the VAT, due to the neutrality and clarity of its border adjustments. On the other hand, the rest of exporters would experience a comparative loss from this perspective.

Indirect Taxation and the Financing of Autonomous Communities

The reform of the system of financing of the Autonomous Communities, stemming from Law 7/2001, granted for the first time a certain role for consumption tax as a financing tool for the regional governments. The previous lack of a such a role for indirect taxation was in sharp contrast with the reality in the majority of countries with decentralized tax systems, where taxation on consumption, and in particular tax applied at the retail stage, is widely used by intermediate levels of government.

Most studies which have addressed the issue of using indirect taxation in the financing of territorial entities have cast serious doubts on the advisability using the VAT as a decentralized tax. However, the experience of dual VAT use in Canada and certain

recent proposals (McClure, 2000) have significantly modified the possibilities for decentralizing the VAT.

Three forms of VAT which are capable of use in tax decentralization can be identified. Firstly, we highlight the experience of Quebec, known as dual VAT, where a central VAT coexists with a subcentral VAT which is employed for interprovincial operations along the lines the transitory regime of the European Union. Exports from Quebec to other provinces (and abroad) carry a zero subcentral VAT rate, while imports to Quebec from other provinces (and from abroad) follow the deferred tax procedure¹⁰.

Secondly, we can point to the compensating VAT (CVAT). This form was originally suggested by Varsano (1995, 2000) and adapted by McClure (2000a). The basic idea is to protect, in interjurisdictional sales, the zero rate/deferred tax of the subcentral VAT by introducing the CVAT alongside the centralised VAT. In McClure's version, the CVAT would be applied in interjurisdictional sales to both the payer of the tax (Varsano's proposal) as well as to the final consumers. However, whereas the CVAT is deductible, in interjurisdictional acquisitions, for the agent paying the tax (the same as for any VAT), for the final consumer it functions as a substitute for the subcentral VAT. The idea of the compensating VAT appears to be particularly appropriate for protecting interjurisdictional sales revenue in cases where a highly professional tax administration does not exist at all levels, as is the situation in developing countries. According to some experts in the field (Bird, 2000), the CVAT may become one of the main innovations in taxation techniques this century, in the way that pay-as-you-earn income tax or indeed VAT itself were important innovations in the past.

Finally, there is the proposal of Keen and Smith (1996), who suggested a new scheme known as Viable Integrated VAT (VIVAT). This is an attempt to address the situation in the European Union where a centralised VAT is not available. The proposal of Keen and Smith consists of a single-rate VAT to be applied to payers of tax (intermediate transactions) within the EU and a tax to be applied to sales to final consumers, where the form of the latter would be a question for each State to decide (17). This scheme can be interpreted in two alternative ways (Keen, 2000, 418-419):

- a) a centralised VAT (in theory) with a uniform rate plus a series of subcentral taxes on retailers at rates equal to the difference between these subcentral taxes and the centralised VAT;
- b) a common tax at an intermediate rate (which is charged and deducted at each phase without generating revenues) plus a tax on the final sales to consumers at the rate of the destination country.

As Pedraja and Salinas (2001) argue, formulas such as the CVAT and the VIVAT strengthen the possibilities of decentralizing VAT and of placing such a decentralization on the agenda for future tax reform. Both revolve around the role of consumption in decentralized financing and focus on the VAT, whose technical superiority makes it by far the most relevant sales tax in force nowadays and the use of which permits subcentral tax authorities to have control over what is considered the most strategic variable in the exercise of the principle of autonomy, namely the capacity to modify tax rates¹¹.

In the Spanish case, the retail phase does not come under the VAT. However, professionals and businessmen which are legal entities are not subject to the special regime of equivalent surcharge. Instead, VAT at the retail stage applies.

In the most recent reforms of 2002 the actual model for indirect taxation at the subnational level chosen in Spain, for the most part, has been revenue sharing with the regions of the collections of the central VAT and excise taxes.¹² The model of revenue sharing is applied to the financing of both Autonomous Communities (or regional governments) as well as local governments. On the other hand, the central government has also granted the Autonomous Communities some degree of tax autonomy with indirect taxes in the form of the Tax on Certain Means of Transport (*Impuesto sobre Determinados Medios de Transporte*). This tax gives the Autonomous Communities the possibility of increasing the tax on the retail sale of hydrocarbons (an option used up to now by very few Autonomous Communities, among which are Catalonia and Madrid).

More specifically, the current arrangements for revenue sharing of central government indirect taxes with the Autonomous Communities are as follows:

- i) A share of 35 percent of VAT revenues, distributed among the Autonomous Communities according to the index of territorial consumption elaborated by the National Statistics Institute (INE).
- ii) A share of 40 percent of revenues from the tax on beer, the tax on wine and fermented drinks, the tax on intermediate goods, the tax on alcohol and derived drinks distributed among the Autonomous Communities according to the indexes of territorial consumption elaborated by the National Statistics Institute¹³.
- iii) A share of 40 percent of the revenues from the tax on hydrocarbons, distributed among the Communities according to the territorial index of

deliveries of gasoline, diesel and fuel oils elaborated by the Ministry of Economics.

- iv) A share of 40 percent of revenues from the tax on manufactured tobacco, distributed among the Communities according to the territorial index of sales to tobacconists, elaborated by the Tobacco Market Commission.
- v) A share of 100 percent of revenues from the tax on electricity, distributed among the Communities according to the territorial index of net electric energy consumption elaborated by the Ministry of Science and Technology.

Regarding the revenue sharing for local governments with these taxes, the latest reform of the system of local finance in 2002 established that these bodies were entitled to a share of the collections from both the VAT and excise taxes¹⁴. Local corporations had a share of VAT and excise tax revenue with the percentages that follows:

- i) 1.0538% of the net VAT revenues.
- ii) 1.2044% of the net revenues from the Excise Taxes on Beer, Wine and Fermented Drinks, Intermediate Goods, Alcohol and Derived Drinks, Hydrocarbons, and Manufactured Tobacco.

These percentages are not applied to the total intake from these taxes, but rather to the part which corresponds to the State once the shares of the Autonomous Communities have been deducted¹⁵.

The sharing of these indirect taxes with local governments can be a complex task. For the sharing of VAT revenues, local entities are entitled to a portion of these revenues which will be determined through the application of the index of territorial consumption of the Autonomous Community that each local government belongs to. This index is

weighted according to the shares of population represented by each local government (in this case a province) within the Autonomous Community. The weighting is carried out as follows:

$$PVAT_t^p = 0,010538 \times NIVAT_t \times IC_t^i \times (P_t^p / P_t^i) \quad (1)$$

where:

- o $PVAT_t^p$ is the VAT return to province p in year t.
- o $NIVAT_t$ is the net VAT revenues to the State in year t, excluding those shared with the Autonomous Communities.
- o IC_t^i is the index of territorial consumption for the year t elaborated by the National Statistics Institute with the aim of allocating VAT among the Autonomous Communities, where i represents the Autonomous Community to which province p belongs.
- o P_t^p and P_t^i are the legal populations of province p and Autonomous Community i respectively, in accordance with the updated municipal register in force on the 31st of December of year t.

For the sharing of excise tax revenues (Excise Taxes on Beer, Wine and Fermented Drinks, Intermediate Goods, and Alcohol and Derived Drinks) with local governments, a similar approach is followed. The share is determined by weighting the net revenues of the State for each of these taxes according to the index of territorial consumption of the Autonomous Community to which the province belongs, with the result again being weighted by the population share of each province in its respective Autonomous Community. The calculation is carried out as follows:

$$PIIEE(h)_t^p = 0.012044 \times RLIIEE(h)_t \times IC_t^i(h) \times (P_t^p / P_t^i) \quad (2)$$

where:

- o $PIIEE(h)_t^p$ is the amount of Excise Tax h handed over to province p in year t .
- o $RLIEE(h)_t$ is the net revenues from Excise Tax h corresponding to the State in year t which excludes those shared with the Autonomous Communities.
- o $IC_t^i(h)$ is the index of territorial consumption, elaborated by the National Statistics Institute to allocate Excise Tax h to the Autonomous Communities, of the Autonomous Community i to which province p belongs.
- o P_t^p and P_t^i are the legal populations of province p and Autonomous Community i respectively, in accordance with the updated municipal register in force on the 31st of December of year t .

For the Hydrocarbons Tax, transfers to local governments are calculated using the index of deliveries of gasoline, diesel and fuel oils corresponding to that territory, using data from the Ministry of Economics, weighted by the corresponding tax rates. The same basic approach is used for determining revenue sharing for the Tax on Manufactured Tobacco. In this case, the calculation is carried out using the index of sales to tobacconists in that territory, according to data from the Tobacco Market Commission, weighted by the corresponding tax rates.

Consumption Taxes in Spain and the OECD Countries since 1965

This section reviews the evolution of the consumption taxes take in Spain, using OECD data. As a percentage of GDP, consumption taxes as a whole rose from 6 percent to 10.2 percent over the period 1965 to 2001 (Table 1), with taxes of a general nature rising from 3.3 percent to 6 percent of GDP and excise taxes rising less from 2.7 percent to 3.3 percent. From Figure 1 it can be seen that three stages can be identified in the evolution

of the two types of taxes. From 1965 to 1980, the share of both types in terms of GDP remained relatively stable, with a tendency towards convergence. From 1980 up to 1986, which was the last large reform of indirect taxation in Spain, both groups of taxes rose strongly (as happened with other taxes), but with general taxes rising faster (from 2.3 percent to 5.3 percent of GDP). From 1986 on, the two groups diverged, although not sharply, as happened in other developed economies (OECD, 2001, p.11). Thus, the take from general taxes, after the introduction of the VAT, rose from 5.3 percent to 6 percent of GDP, whereas the take from excise taxes fell from 4.2 percent to 3.3 percent. This differentiated behavior can be explained by the fact that the VAT replaced to the old tax on sumptuary consumptions and to other figures smaller than the special taxes.

Despite this, consumption taxes as a share of total tax revenues, have fallen, due to the fact that other public earnings have risen much faster as a percentage of GDP. As can be seen in Table 2 and Figure 2, taxes on goods and services went from representing 40 percent of total revenues in 1965 to 20 percent in 1980. The share of taxes of a general nature (the IGTE was still in existence) fell by almost 12 percentage points over this period (from 22.21 percent to 10.61 percent of the total intake) while that of excise taxes fell by more than 11 percentage points (from 18.42 percent to 7.38 percent in 1979). Since the beginning of the 1980s, the share of total revenues corresponding to excise taxes has remained fairly stable at around 10 percent while that of taxes of a general nature has risen strongly since 1981, especially after the introduction of the VAT.

Table 1. Consumption Tax Revenues as a Percentage of GDP: Spain 1965-2001

	<i>Goods and services</i>	<i>Production and sales</i>	<i>General</i>	<i>VAT</i>	<i>Excise taxes</i>	<i>Use</i>
	<i>5000</i>	<i>5100</i>	<i>5110</i>	<i>5111</i>	<i>5120</i>	<i>5200</i>
1965	6.0	6.0	3.3		2.7	
1966	6.1	6.1	3.3		2.8	
1967	6.0	6.0	3.3		2.7	
1968	5.7	5.6	3.1		2.5	
1969	5.9	5.9	3.3		2.7	
1970	5.8	5.8	3.3		2.5	
1971	5.4	5.4	3.1		2.3	
1972	5.5	5.5	3.1		2.4	
1973	5.7	5.7	3.2		2.4	
1974	4.7	4.7	3.1		1.6	
1975	4.5	4.5	2.9		1.6	
1976	4.7	4.7	2.9		1.8	
1977	4.7	4.6	2.8		1.8	
1978	4.7	4.7	3.0		1.6	
1979	4.7	4.7	3.0		1.7	
1980	4.8	4.8	2.3		2.4	
1981	5.3	5.3	2.5		2.8	
1982	5.4	5.4	3.0		2.4	
1983	6.4	6.4	3.3		3.1	
1984	7.1	7.1	3.9		3.3	
1985	8.0	7.7	4.1		3.6	0.2
1986	9.8	9.4	5.3	4.4	4.2	0.2
1987	9.6	9.2	5.3	5.0	3.9	0.4
1988	9.7	9.3	5.4	5.2	3.9	0.4
1989	9.6	9.1	5.6	5.4	3.6	0.5
1990	9.4	8.8	5.3	5.2	3.5	0.6
1991	9.5	8.8	5.3	5.2	3.5	0.7
1992	9.8	9.0	5.7	5.6	3.4	0.7
1993	9.0	8.2	4.9	4.9	3.3	0.7
1994	9.5	8.7	5.3	5.3	3.4	0.7
1995	9.4	8.6	5.2	5.2	3.4	0.8
1996	9.4	8.6	5.3	5.3	3.3	0.8
1997	9.7	8.9	5.5	5.5	3.4	0.8
1998	10.0	9.2	5.6	5.6	3.6	0.8
1999	10.5	9.6	6.1	6.1	3.5	0.8
2000	10.5	9.6	6.2	6.2	3.4	0.8
2001	10.2	9.3	6.0	6.0	3.3	0.8

Source: OCDE

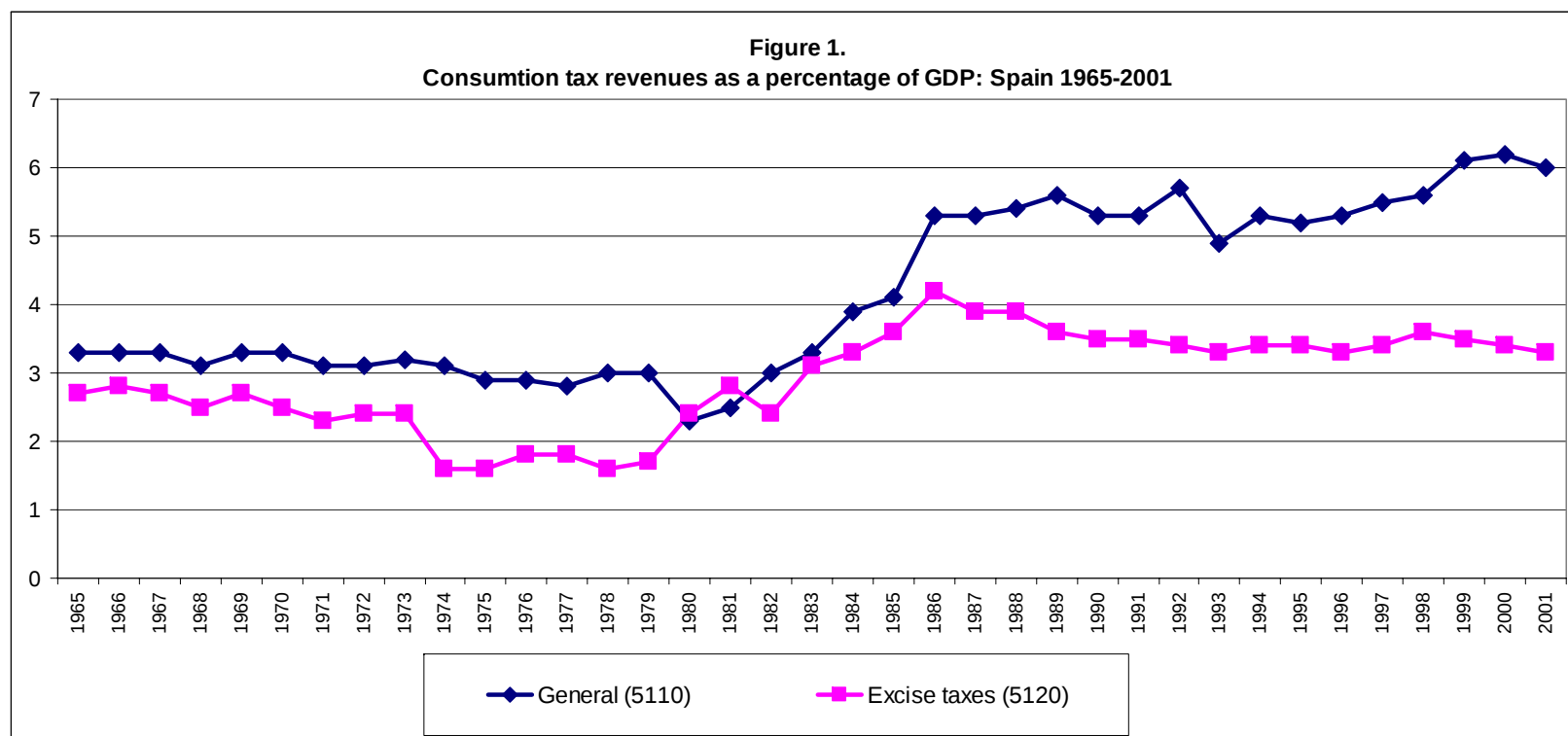
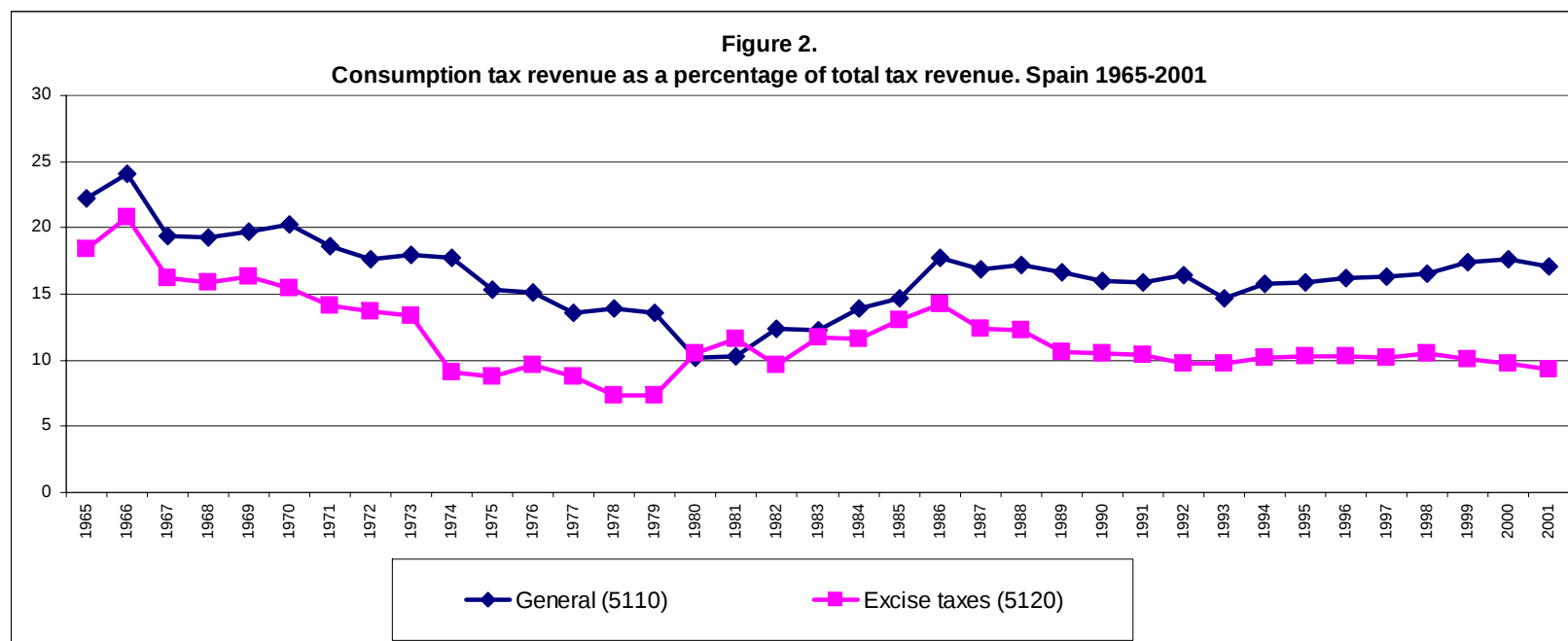


Table 2. Consumption Tax Revenue as a Percentage of Tax Revenue: Spain 1965-2001

	<i>Goods and services</i>	<i>Production and sales</i>	<i>General</i>	<i>VAT</i>	<i>Excise taxes</i>	<i>Use</i>
	<i>5000</i>	<i>5100</i>	<i>5110</i>	<i>5111</i>	<i>5120</i>	<i>5200</i>
1965	40.84	40.63	22.21		18.42	0.21
1966	45.02	44.96	24.14		20.82	0.06
1967	35.65	35.59	19.42		16.17	0.06
1968	35.17	35.11	19.22		15.89	0.06
1969	36.14	36.07	19.76		16.30	0.07
1970	35.87	35.77	20.29		15.48	0.10
1971	32.85	32.73	18.59		14.15	0.11
1972	31.50	31.36	17.63		13.74	0.13
1973	31.50	31.37	17.96		13.41	0.13
1974	26.92	26.78	17.73		9.05	0.14
1975	24.16	24.02	15.30		8.72	0.14
1976	24.92	24.79	15.12		9.67	0.13
1977	22.49	22.39	13.62		8.77	0.10
1978	21.39	21.30	13.90		7.39	0.09
1979	20.98	20.91	13.53		7.38	0.07
1980	20.69	20.69	10.16		10.53	0.01
1981	21.93	21.92	10.28		11.64	0.01
1982	22.07	22.06	12.40		9.67	0.01
1983	23.96	23.95	12.28		11.67	0.01
1984	25.51	25.51	13.86		11.65	
1985	28.71	27.68	14.67		13.02	0.62
1986	33.21	31.94	17.73	14.76	14.21	0.81
1987	30.59	29.28	16.90	16.03	12.38	1.24
1988	30.83	29.42	17.15	16.42	12.27	1.36
1989	28.81	27.35	16.68	16.29	10.67	1.41
1990	28.39	26.53	16.03	15.73	10.50	1.79
1991	28.36	26.34	15.89	15.59	10.45	1.93
1992	28.36	26.19	16.45	16.19	9.73	2.07
1993	26.87	24.51	14.72	14.65	9.79	2.22
1994	28.28	25.99	15.80	15.74	10.19	2.12
1995	28.62	26.14	15.87	15.85	10.27	2.32
1996	29.00	26.49	16.23	16.21	10.25	2.36
1997	28.88	26.50	16.34	16.34	10.15	2.25
1998	29.54	27.09	16.57	16.57	10.52	2.33
1999	30.03	27.51	17.42	17.42	10.09	2.41
2000	29.83	27.37	17.60	17.60	9.77	2.37
2001	28.83	26.35	17.06	17.06	9.29	2.39

Source: OCDE



From an international perspective, effective burdens from indirect taxation in Spain have been in the middle of the road. At the beginning of the 2000s, consumption tax burdens were lower for the non-European OECD countries (see Table 3 and Figure 3). In terms of the share of these taxes in GDP, the average for the European zone (at 12.1 percent of GDP in 2001) was higher than that of the American and Pacific zone (both barely up from 9 percent). However, if we consider the percentage that consumption taxes represent of the total tax revenues (Table 4 and Figure 4), we can observe that this share is higher for the non-European countries. This result is due mainly to the weight given to consumption tax in Mexico and Korea (53.1 percent and 39.6 percent, respectively, of total tax revenues corresponds to consumption taxes in those two countries). On the other hand, Japan, the United States and Switzerland are the countries where consumption tax is of lesser importance (in terms of both their share of GDP and the percentage of total tax revenues).

In 2001, Spain, after Switzerland, was the European country of the OECD for which this group of taxes represented the smallest share of GDP, with a share of 10.2 percent compared to 15.8 percent for Denmark, 14.9 percent for Hungary. The average for the European OECD members was 12.1percent while that for the 15 members of the EU prior to the recent enlargement was 11.9 percent (see Figure 3). Despite the relatively low fiscal pressure in Spain corresponding to this group of taxes, it is clear that the gap with neighbouring countries has been reduced significantly over the last twenty-five years. In 1980, consumption taxes represented 4.5 percent of GDP compared with an average of 10.4 percent for the European OECD members.

Table 3. Consumption Taxes as a Percentage of GDP (5000)

	1965	1970	1975	1980	1985	1995	2001	Variation
OECD Total	9.7	10.0	9.7	10.1	10.9	11.4	11.5	1.8
OECD Europe	10.3	10.8	10.4	10.9	11.8	12.4	12.1	1.8
European Union (15)	10.4	10.8	10.2	11.0	12.0	12.2	11.9	1.5
OECD America	8.0	7.6	7.7	7.7	8.8	7.7	9.2	1.2
OECD Pacific	6.4	6.3	7.0	7.7	7.8	8.5	9.1	2.7
GERMANY	10.4	10.3	9.5	10.2	9.5	10.7	10.6	0.2
FRANCE	13.3	13.0	11.9	12.4	13.0	12.1	11.4	-1.9
ITALY	10.1	10.1	7.7	8.1	8.7	11.2	11.0	0.9
NETHERLANDS	9.4	9.9	10.1	11.0	10.9	11.4	12.3	2.9
BELGIUM	11.6	12.6	11.0	11.6	11.6	11.5	11.2	-0.4
LUXEMBOUR	6.8	3.6	7.9	8.4	10.8	11.2	11.4	4.6
UNITED KINGDOM	10.1	10.7	8.8	10.3	11.9	12.3	11.7	1.6
IRELAND	13.1	15.1	13.5	13.7	15.6	13.3	10.3	-2.8
DENMARK	12.2	15.2	13.5	16.4	16.2	15.9	15.8	3.6
SPAIN	6.0	5.8	4.5	4.8	8.0	9.4	10.2	4.2
GREECE	9.8	10.8	10.2	10.0	12.2	13.3	13.9	4.1
PORTUGAL	7.0	8.6	8.5	10.8	11.4	14.1	13.8	6.8
UNITED STATES	5.6	5.5	5.3	4.8	4.9	4.9	4.7	-0.9
MEXICO				8.3	11.0	9.0	9.7	
CANADA	10.4	9.8	10.2	10.0	10.4	9.1	8.8	-1.6
KOREA			9.3	11.1	10.1	8.8	10.9	
JAPAN	4.8	4.5	3.7	4.1	3.8	4.2	3.9	-0.9
AUSTRALIA	7.6	7.2	7.8	8.5	9.6	8.6	8.7	1.1

Table 3. Consumption Taxes as a Percentage of GDP (5000) (Continued)

	1965	1970	1975	1980	1985	1995	2001	Variation
NORWAY	12.2	14.8	14.8	15.1	16.3	16.0	14.1	1.9
NEW ZEALAND	6.9	7.3	7.4	7.2	7.6	12.5	12.4	5.5
SWEDEN	10.9	10.9	10.3	11.4	12.9	11.5	11.1	0.2
FINLAND	12.9	12.6	11.9	12.9	13.6	13.3	13.6	0.7
ICELAND	16.4	16.5	18.5	17.4	17.3	15.4	14.8	-1.6
SWITZERLAND	6.0	6.1	5.6	5.9	5.8	6.3	7.1	1.1
AUSTRIA	12.7	12.9	12.9	12.6	13.6	11.5	12.4	-0.3
TURKEY	5.7	6.2	6.6	4.6	5.6	8.5	13.9	8.2
CZECH REPUBLIC						13.2	11.9	
SLOVAKIA							11.0	
HUNGARY						17.2	14.9	
POLAND						14.0	12.5	

Notes: (*) In all tables the last data entry for Portugal, the UNITED STATES, Australia, Iceland and Poland corresponds to the year 2000.

Source: OCDE

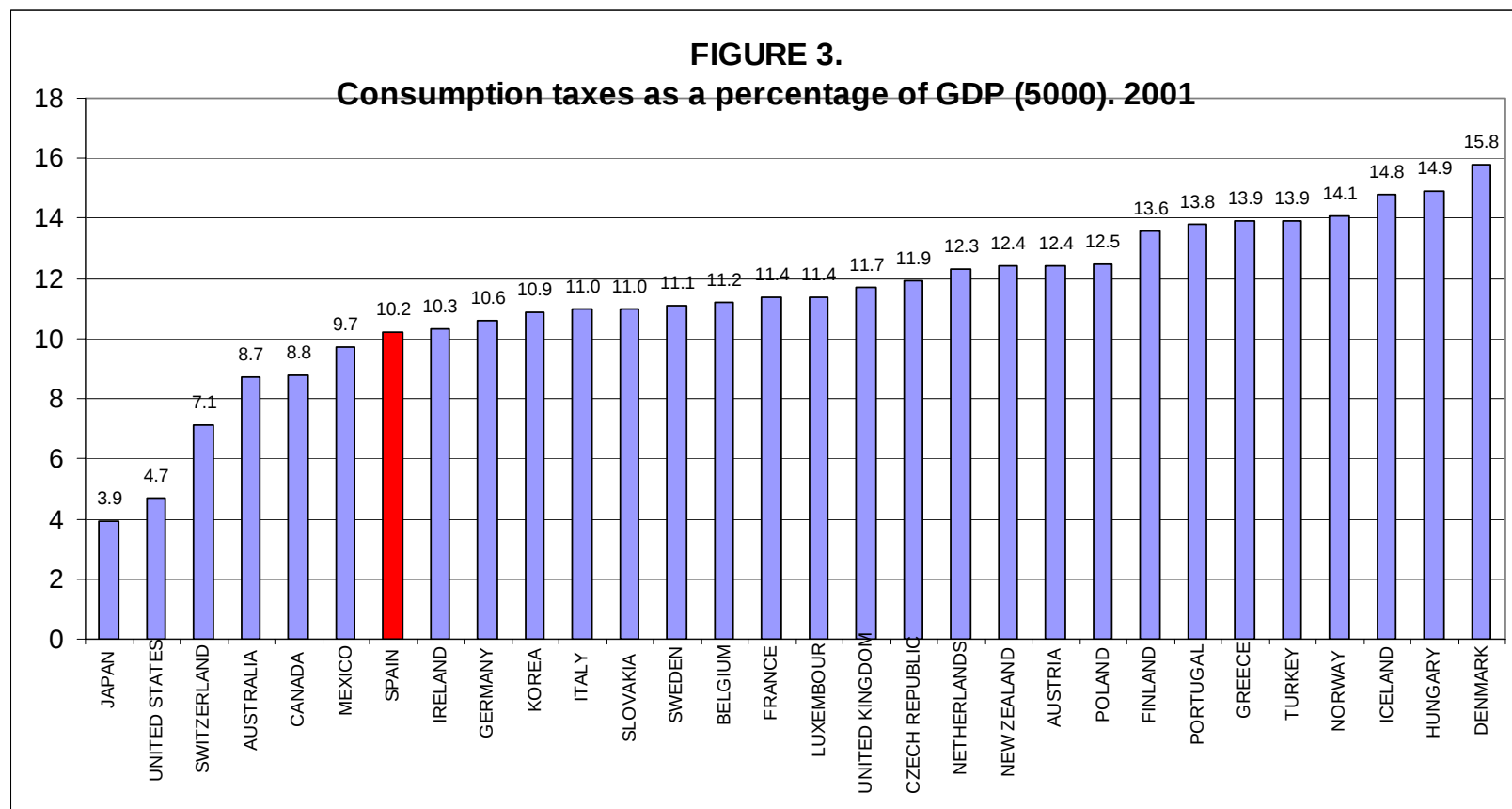


Table 4. Consumption Taxes as a Percentage of Total Tax Revenue (5000)

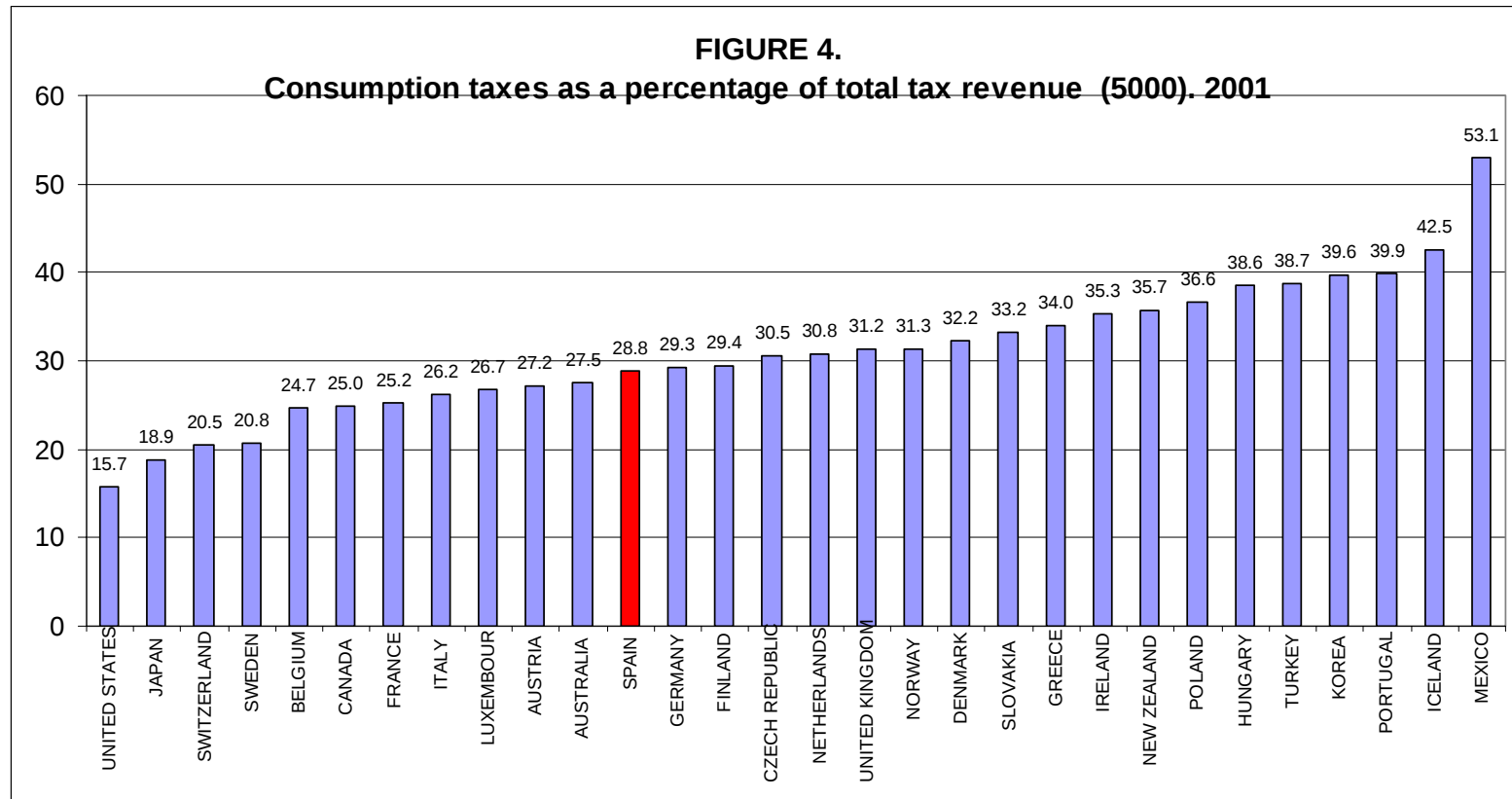
	1965	1970	1975	1980	1985	1995	2001	Variation
OECD Total	38.05	35.61	32.63	32.34	33.54	32.31	31.84	-6.2
OECD Europe	40.05	37.98	33.28	31.95	33.01	32.68	30.34	-9.7
European Union (15)	38.18	36.08	31.36	31.05	31.55	31.1	28.7	-9.5
OECD America	31.62	25.81	25.78	33.81	38.47	32.48	39.01	7.4
OECD Pacific	29.63	27.19	32.98	33.1	32.37	30.13	37.52	7.9
GERMANY	32.97	31.81	26.9	27.11	25.65	27.98	29.28	-3.7
FRANCE	38.41	38.13	33.29	30.42	29.67	27.44	25.18	-13.2
ITALY	39.47	38.69	29.36	26.46	25.38	27.29	26.24	-13.2
NETHERLANDS	28.64	27.78	24.17	25.25	25.65	27.16	30.77	2.1
BELGIUM	37.17	36.47	27.44	27.24	25.33	25.75	24.7	-12.5
LUXEMBOUR	24.74	14.33	21.12	20.93	24.1	26.69	26.74	2.0
UNITED KINGDOM	33.07	28.78	25.02	29.2	31.53	35.42	31.24	-1.8
IRELAND	52.64	52.42	46.51	43.71	44.42	40.75	35.25	-17.4
DENMARK	40.62	38.8	33.63	37.39	34.18	32.21	32.24	-8.4
SPAIN	40.84	35.87	24.16	20.69	28.71	28.62	28.83	-12.0
GREECE	48.84	48.18	46.8	41.24	42.72	42.13	33.96	-14.9
PORTUGAL	44.24	44.63	40.75	44.88	42.79	43.46	39.93	-4.3
UNITED STATES	22.76	19.95	19.55	17.63	18.82	17.87	15.72	-7.0
MEXICO				51.23	64.8	54.15	53.06	
CANADA	40.49	31.68	32.01	32.58	31.81	25.43	24.96	-15.5
KOREA			61.07	62.65	59.48	43.07	39.64	
JAPAN	26.25	22.36	17.31	16.34	14.02	15.17	18.87	-7.4
AUSTRALIA	34.71	31.97	29.33	31.1	32.85	29.02	27.52	-7.2

Table 4. Consumption Taxes as a Percentage of Total Tax Revenue (5000) (Continued)

	1965	1970	1975	1980	1985	1995	2001	Variation
NORWAY	41.16	42.81	37.66	35.4	37.61	38.61	31.29	-9.9
NEW ZEALAND	27.93	27.23	24.22	22.3	23.14	33.26	35.66	7.7
SWEDEN	31.18	28.25	24.35	24.01	26.6	24.23	20.79	-10.4
FINLAND	42.46	39.64	32.37	35.66	33.92	29.62	29.37	-13.1
ICELAND	62.73	61.25	62.98	59.9	61.06	48.79	42.52	-20.2
SWITZERLAND	30.48	26.94	19.96	20.52	19.29	18.84	20.47	-10.0
AUSTRIA	37.38	37.36	34.52	31.52	32.57	27.69	27.18	-10.2
TURKEY	53.93	49.37	41.29	25.61	36.02	37.57	38.74	-15.2
CZECH REPUBLIC						32.93	30.55	
SLOVAKIA							33.17	
HUNGARY						40.63	38.62	
POLAND						35.23	36.62	

Notes: (*) In all tables the last data entry for Portugal, the UNITED STATES, Australia, Iceland and Poland corresponds to the year 2000.

Source: OCDE



In terms of the current weight of consumption taxes in total revenues (Figure 4) as opposed to fiscal pressure, Spain, for which these taxes contribute 28.8 percent of public revenue, is closer to the average than the other European countries.

If we focus on excise taxation, we can observe that as a percentage of GDP Spain has converged towards its peers (Table 5 and Figure 5). The figure for Spain rose from 2.7 percent of GDP in 1965 to 3.3 percent in 2001 whereas the OECD average fell from 5.8 percent to 4 percent over the same period. There has also been a convergence in terms of the share these taxes represent of the total public revenue, due primarily to a substantial reduction in the figure for all countries (Table 6 and Figure 6). Despite this, in the year 2001 Spain occupied the twenty-fourth position out of the thirty two OECD countries under consideration in terms of the specific fiscal pressure of excise taxes, and was twentieth in terms of their contribution to the total tax revenues.

With regard to consumption taxes of a general nature (Tables 7 and 8, Figures 7 and 8), the distance of Spain from the developed countries has been substantially reduced, though a gap still persists. Whereas the average fiscal pressure for OECD-Europe rose from 3.7 percent to 7.4 percent of GDP between 1965 and 2001, the corresponding rise for Spain was from 3.3 percent to 6 percent. Spain is considerably closer to the other countries considered when it comes to the share these taxes represent of fiscal resources as a whole.

Table 5. Excise Taxes as a Percentage of GDP (5120)

	1965	1970	1975	1980	1985	1995	2000	2001	Variation
OECD Total	5.8	5.5	4.8	4.8	4.9	4.5	4.2	4	-1.8
OECD Europe	6.2	5.8	5	4.9	4.9	4.8	4.3	4	-2.2
European Union (15)	6	5.6	4.6	4.6	4.9	4.6	4.2	3.9	-2.1
OECD America	4	3.7	3.5	3.9	4.9	3.9	3.7	4.5	0.5
OECD Pacific	4.7	4.5	4.9	5.1	4.9	3.5	3.6	3.3	-1.4
GERMANY	4.6	4.2	3.8	3.5	3.3	3.6	3.3	3.5	-1.1
FRANCE	4.9	4	3.2	3.4	3.8	4	3.7	3.5	-1.4
ITALY	6.2	6	3.6	3	3.1	4.6	4.2	3.8	-2.4
NETHERLANDS	4.8	4.1	3.4	3.2	3.1	3.8	3.7	3.6	-1.2
BELGIUM	4	4.3	3.7	3.7	3.7	3.8	3.2	3.2	-0.8
LUXEMBOUR	3.1	2.3	3.1	3.9	5	5.1	5.3	4.8	1.7
UNITED KINGDOM	7.7	7.4	5.2	4.7	5.2	5.1	4.7	4.4	-3.3
IRELAND	10.8	10.5	8.6	8.9	7.7	5.7	4.4	3.5	-7.3
DENMARK	8.7	7	5.9	5.9	6.2	5.7	5.5	5.4	-3.3
SPAIN	2.7	2.5	1.6	2.4	3.6	3.4	3.4	3.3	0.6
GREECE	6.8	6.1	5.2	6.1	6	5.3	4.4	4.3	-2.5
PORTUGAL	6.6	6.5	5.6	6.6	7.6	6.3	5.2	5.2	-1.4
UNITED STATES	3.7	3.3	2.7	2.2	2.2	2.1	1.9	1.9	-1.8
MEXICO				5.6	8.2	6	6.2	5.9	0.3
CANADA	4.3	4.1	4.3	4	4.2	3.5	3	3.1	-1.2
KOREA			7.2	7	6.3	4.5	5.1	5.8	-1.4
JAPAN	4.6	4.2	3.2	3.5	3.3	2.2	2.1	1.6	-3
AUSTRALIA	5	4.6	5.1	6.2	6	4.3	4.4	4.4	-0.6

Table 5. Excise Taxes as a Percentage of GDP (5120) (Continued)

	1965	1970	1975	1980	1985	1995	2000	2001	Variation
NORWAY	5.5	6.2	6.3	6.9	7.9	6.7	5.3	5.2	-0.3
NEW ZEALAND	4.6	4.6	4.2	3.6	3.8	3.2	2.6	2.6	-2
SWEDEN	6.7	6.3	4.5	4.4	5.6	4.2	3.6	3.6	-3.1
FINLAND	7.1	6.3	5.6	6	5.6	5.2	4.9	4.8	-2.3
ICELAND	11.8	10.2	9.9	8.7	7.5	4.4	4.6	4.6	-7.2
SWITZERLAND	3.7	3.9	3	2.8	2.5	2.4	2.5	2.5	-1.2
AUSTRIA	6.1	6.2	5.2	4	4.2	3.3	3.4	3.4	-2.7
TURKEY	5.7	6.1	6.5	4.5	1.9	1.4	5.3	5.4	-0.3
CZECH REPUBLIC						5.4	4.3	4	
SLOVAKIA							4.8	3.4	
HUNGARY						8.8	5.4	4.7	
POLAND						7	4.8	4.8	

Notes: (*) In all tables the last data entry for Portugal, the UNITED STATES, Australia, Iceland and Poland corresponds to the year 2000.

Source: OCDE

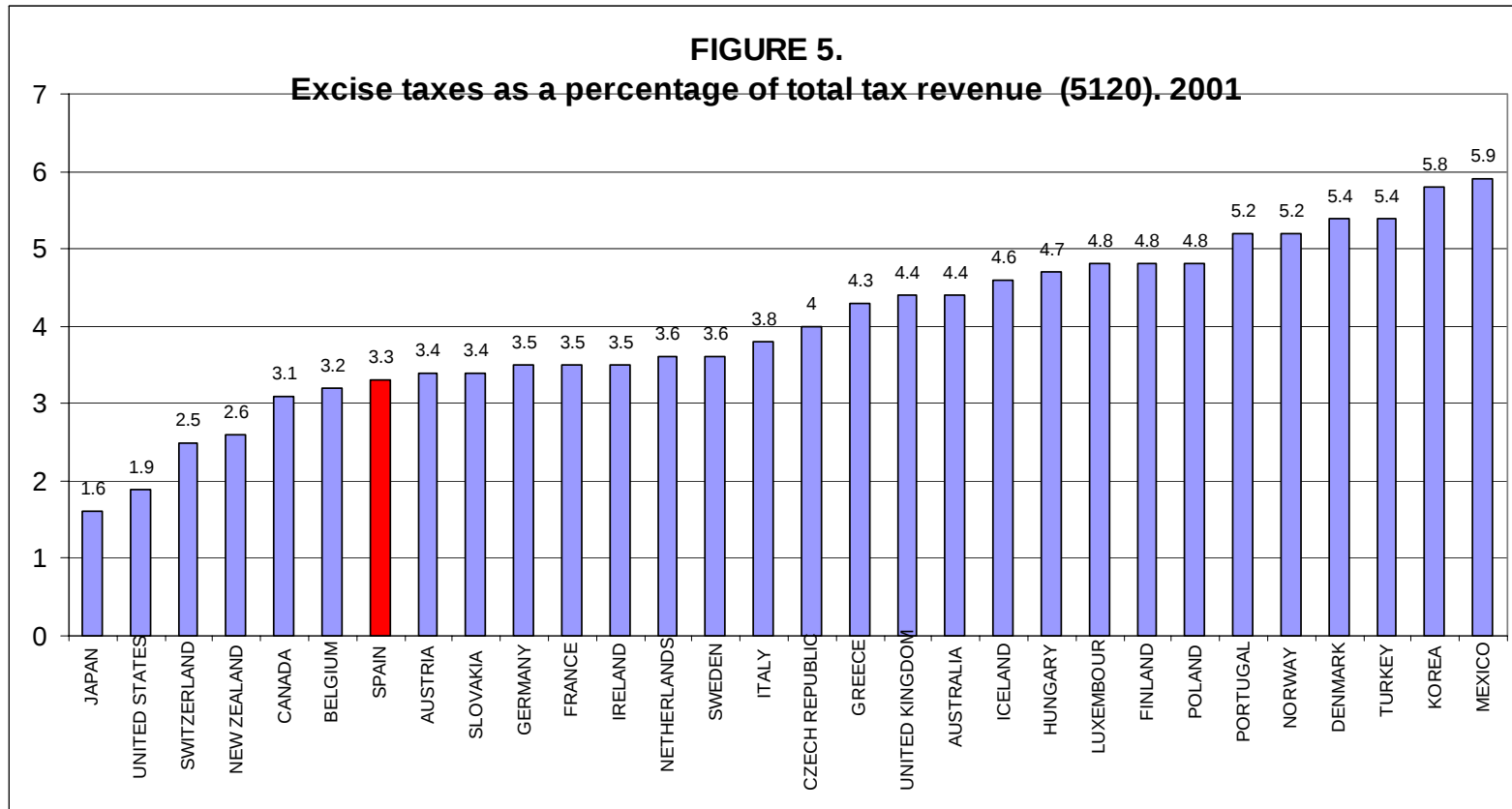


Table 6. Excise Taxes as a Percentage of Total Tax Revenue (5120)

	1965	1970	1975	1980	1985	1995	2000	2001	Variation
OECD Total	24.07	20.46	17.54	16.57	16.05	13.08	11.78	11.4	-12.67
OECD Europe	25.24	21.46	16.82	15.14	13.97	12.4	11.13	9.99	-15.25
European Union (15)	22.92	19.07	14.55	13.78	13.33	11.84	10.33	9.5	-13.42
OECD America	15.99	12.5	11.81	18.56	23.31	17.85	16.07	20.47	4.48
OECD Pacific	22.07	19.49	23.84	21.85	20.46	13.21	12.24	14.69	-7.38
GERMANY	14.62	12.89	10.8	9.27	8.75	9.49	8.81	9.61	-5.01
FRANCE	14.28	11.63	9	8.38	8.75	9.14	8.18	7.81	-6.47
ITALY	24.11	23.16	13.97	9.74	9.12	11.1	10.04	9.11	-15
NETHERLANDS	14.73	11.57	8.11	7.32	7.24	8.98	8.85	9.12	-5.61
BELGIUM	12.96	12.59	9.26	8.63	8.1	8.6	7.08	7	-5.96
LUXEMBOUR	11.1	9.32	8.43	9.69	11.1	12.07	12.65	11.4	0.3
UNITED KINGDOM	25.21	19.92	14.82	13.28	13.85	14.58	12.44	11.76	-13.45
IRELAND	43.38	36.37	29.68	28.26	21.99	17.51	14.12	11.92	-31.46
DENMARK	29.17	17.86	14.68	13.4	12.97	11.48	11.28	10.96	-18.21
SPAIN	18.42	15.48	8.72	10.53	13.02	10.27	9.77	9.29	-9.13
GREECE	33.8	27.37	23.87	25.08	20.87	16.65	11.74	15.17	-18.63
PORTUGAL	41.45	33.83	26.98	27.2	28.75	19.48	15.17	15.17	-26.28
UNITED STATES	15.14	11.74	10.03	8.28	8.4	7.66	6.32	6.32	-8.82
MEXICO				34.37	48.56	35.99	33.37	32.21	-2.16
CANADA	16.84	13.27	13.58	13.02	12.97	9.89	8.51	8.72	-8.12
KOREA			47.3	39.53	37.39	21.92	19.66	21.09	-26.21
JAPAN	25.02	20.95	15.09	14.13	12.08	7.98	7.79	15.45	-9.57
AUSTRALIA	22.65	20.35	19.15	22.56	20.69	14.45	13.99	13.99	-8.66

Table 6. Excise Taxes as a Percentage of Total Tax Revenue (5120) (Continued)

	1965	1970	1975	1980	1985	1995	2000	2001	Variation
NORWAY	18.39	17.84	16.11	16.21	18.25	16.2	13.27	11.63	-6.76
NEW ZEALAND	18.53	17.17	13.81	11.17	11.67	8.49	7.52	7.55	-10.98
SWEDEN	19.15	16.29	10.71	9.19	11.57	8.73	6.72	6.8	-12.35
FINLAND	23.4	19.81	15.3	16.63	13.95	11.58	10.4	10.25	-13.15
ICELAND	44.99	37.9	33.57	29.8	26.47	14.05	12.44	12.44	-32.55
SWITZERLAND	18.97	17.1	10.64	9.77	8.36	7.25	6.99	7.36	-11.61
AUSTRIA	17.96	17.98	13.98	10.07	9.94	7.9	7.73	7.43	-10.53
TURKEY	53.44	48.77	40.94	25.22	12.39	6	16.04	15.12	-38.32
CZECH REPUBLIC						13.42	10.96	10.33	
SLOVAKIA							13.4	10.13	
HUNGARY						20.86	13.85	12.27	
POLAND						17.54	14.15	14.15	

Notes: (*) In all tables the last data entry for Portugal, the UNITED STATES, Australia, Iceland and Poland corresponds to the year 2000.

Source: OCDE

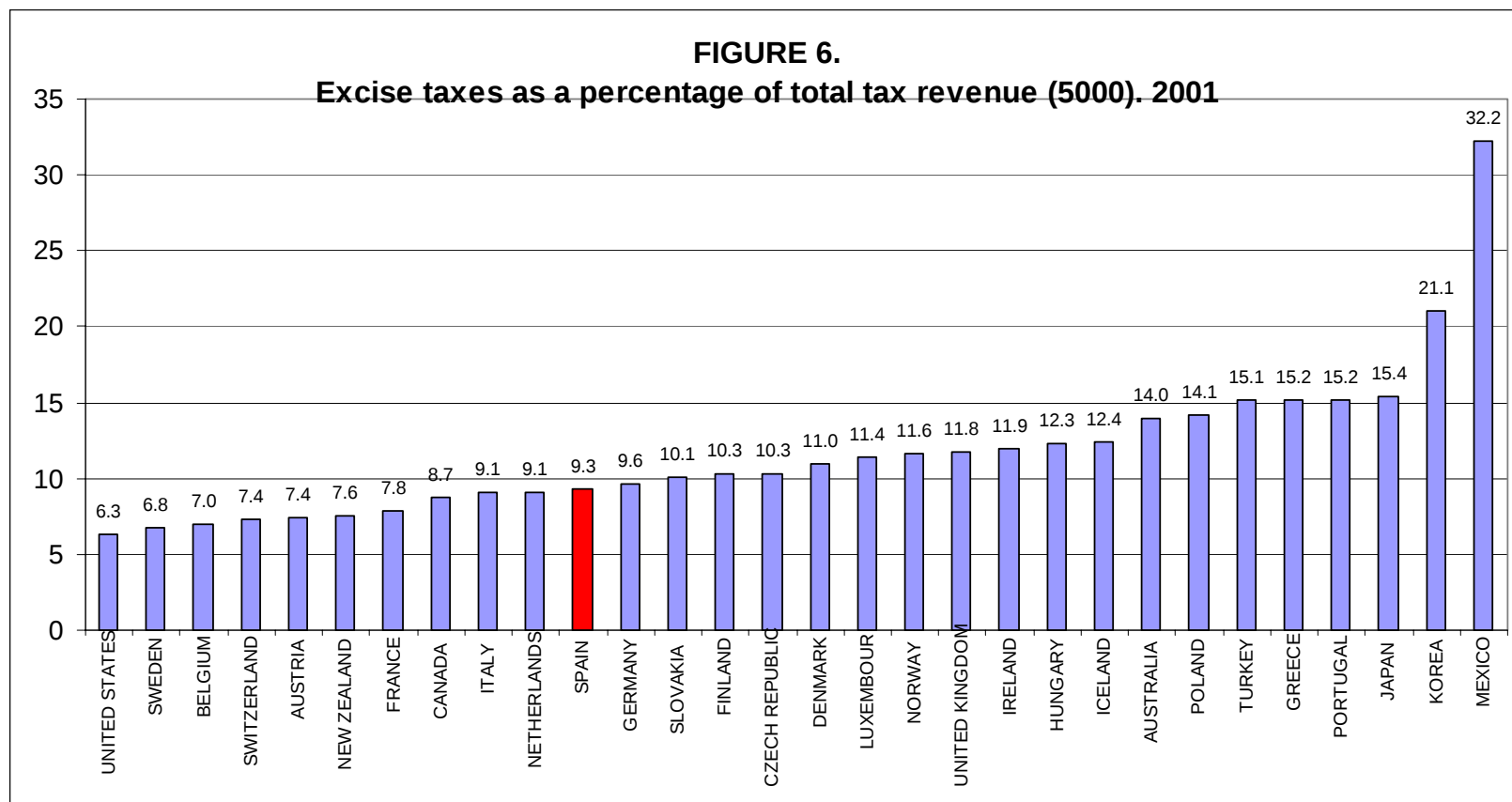


Table 7. General Consumer Taxes as a Percentage of GNP (5110)

	1965	1970	1975	1980	1985	1995	2000	2001	Variation
OECD Total	3.3	4	4.3	4.8	5.4	6.3	6.9	6.9	3.6
OECD Europe	3.7	4.5	5	5.6	6.4	7.1	7.7	7.4	3.7
European Union (15)	3.8	4.6	5.1	5.9	6.5	7	7.5	7.3	3.5
OECD America	2.9	3	2.9	2.7	3	3.3	3.6	4.4	1.5
OECD Pacific	1.2	1.3	1.6	2.2	2.3	4.1	4.8	5.3	4.1
GERMANY	5.2	5.5	5.2	6.2	5.9	6.7	7	6.7	1.5
FRANCE	8	8.7	8.4	8.6	8.7	7.6	7.7	7.6	-0.4
ITALY	3.3	3.4	3.7	4.8	5	5.7	6.6	5.9	2.6
NETHERLANDS	4.1	5.2	6	6.9	6.9	6.5	7.2	7.5	3.4
BELGIUM	6.6	7.4	6.5	7.3	7.2	6.8	7.4	7.1	0.5
LUXEMBOUR	3.4		4.5	4.3	5.6	6	6	6.4	3
UNITED KINGDOM	1.8	2.5	3.1	5.2	6	6.6	6.9	6.8	5
IRELAND	1.4	3.8	4.3	4.6	7.2	7	6.7	6.4	5
DENMARK	2.7	7.4	6.8	9.8	9.5	9.5	9.6	9.6	6.9
SPAIN	3.3	3.3	2.9	2.3	4.1	5.2	6.2	6	2.7
GREECE	2	3.8	4	3.2	4.9	7.3	8.6	8.5	6.5
PORTUGAL		1.6	2.3	3.9	3.3	7.6	8.3	8.3	6.7
UNITED STATES	1.2	1.6	1.9	1.9	2	2.2	2.2	2.2	1
MEXICO				2.5	2.7	2.8	3.5	3.6	1.1
CANADA	4.6	4.5	4	3.5	4.3	5	5.2	5.2	0.6
KOREA			1.9	3.9	3.6	3.9	4.5	4.7	-1.9
JAPAN						1.4	2.4	2	2
AUSTRALIA	1.6	1.7	1.8	1.4	2.3	2.6	3.9	3.9	2.3
NORWAY	6.4	8.2	8.1	7.8	7.9	8.8	8	8.2	1.8
NEW ZEALAND	1.9	2.1	2.8	3.3	3.4	8.5	8.7	9	7.1

Table 7. General Consumer Taxes as a Percentage of GNP (5110) (Continued)

	1965	1970	1975	1980	1985	1995	2000	2001	Variation
SWEDEN	3.6	4	5.1	6.3	6.8	7.1	7.3	7.1	3.5
FINLAND	5.6	6.2	6.2	6.8	7.8	7.8	8.5	8.5	2.9
ICELAND	4.4	5.9	8.4	8.4	9.3	10	11	11	6.6
SWITZERLAND	1.9	1.8	2.2	2.6	2.9	3.4	4.1	4.1	2.2
AUSTRIA	6.3	6.4	7.4	8	8.8	7.6	8.3	8.2	1.9
TURKEY					3.6	7	7.8	8	8
CZECH REPUBLIC						6.9	7.5	7	
SLOVAKIA							8	7.6	
HUNGARY						8.2	10.2	10	
POLAND						6.8	7.6	7.6	

Notes: (*) In all tables the last data entry for Portugal, the UNITED STATES, Australia, Iceland and Poland corresponds to the year 2000.

Source: OCDE

Table 8. General Consumer Taxes as a Percentage of Total Tax Revenue (5110)

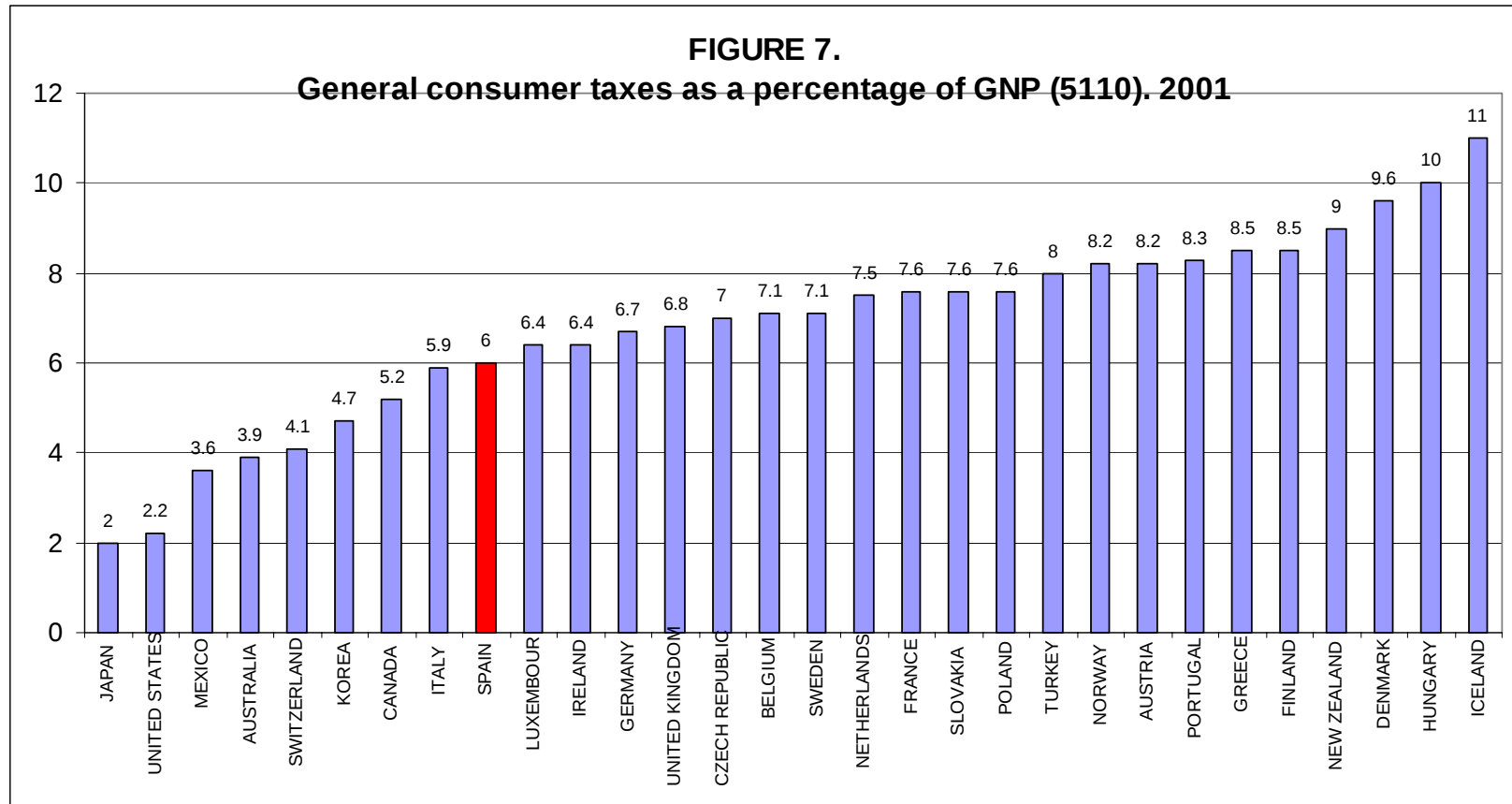
	1965	1970	1975	1980	1985	1995	2000	2001	Variation
OECD Total	11.85	13.06	13.34	14.17	15.79	17.54	18.34	18.51	6.66
OECD Europe	12.99	14.62	15.03	15.61	17.59	18.83	19.42	18.27	5.28
European Union (15)	13.28	14.95	15.25	16.02	16.68	17.75	18.22	17.58	4.3
OECD America	11.31	10.14	9.75	11.42	12.33	13	13.54	17.27	5.96
OECD Pacific	5.01	5.14	7.09	9.37	9.84	13.87	15.72	20.9	15.89
GERMANY	16.49	17.14	14.63	16.63	15.81	17.44	18.37	18.52	2.03
FRANCE	23.26	25.51	23.4	21.14	19.95	17.34	16.92	16.66	-6.6
ITALY	12.89	13.15	14.31	15.62	14.5	13.82	15.76	14.13	1.24
NETHERLANDS	12.37	14.61	14.36	15.83	16.18	15.6	17.34	18.81	6.44
BELGIUM	21.11	21.51	16.29	17.1	15.72	15.33	16.25	15.64	-5.47
LUXEMBOUR	12.35		11.93	10.68	12.52	14.22	14.29	15.02	2.67
UNITED KINGDOM	5.91	6.83	8.91	14.66	15.88	19.08	18.37	18.25	12.34
IRELAND	5.68	13.1	14.68	14.76	20.59	21.25	21.49	21.78	16.1
DENMARK	9.11	18.77	16.9	22.25	20.12	19.32	19.58	19.53	10.42
SPAIN	22.21	20.29	15.3	10.16	14.67	15.87	17.6	17.06	-5.15
GREECE	10.26	16.82	18.32	13.16	17.16	23.11	22.66	20.93	10.67
PORTUGAL		8.38	11.16	16.16	12.58	23.39	24.21	24.21	15.83
UNITED STATES	4.8	5.85	7.04	7.02	7.88	8	7.45	7.45	2.65
MEXICO				15.69	15.95	17.01	18.72	19.75	4.06
CANADA	17.82	14.43	12.46	11.54	13.16	13.99	14.45	14.78	-3.04
KOREA			12.66	22	21.07	18.88	17.02	17.25	-12.66
JAPAN						5.21	8.89	19.6	19.6
AUSTRALIA	7.36	7.44	6.67	5.27	7.93	8.69	12.25	12.25	4.89

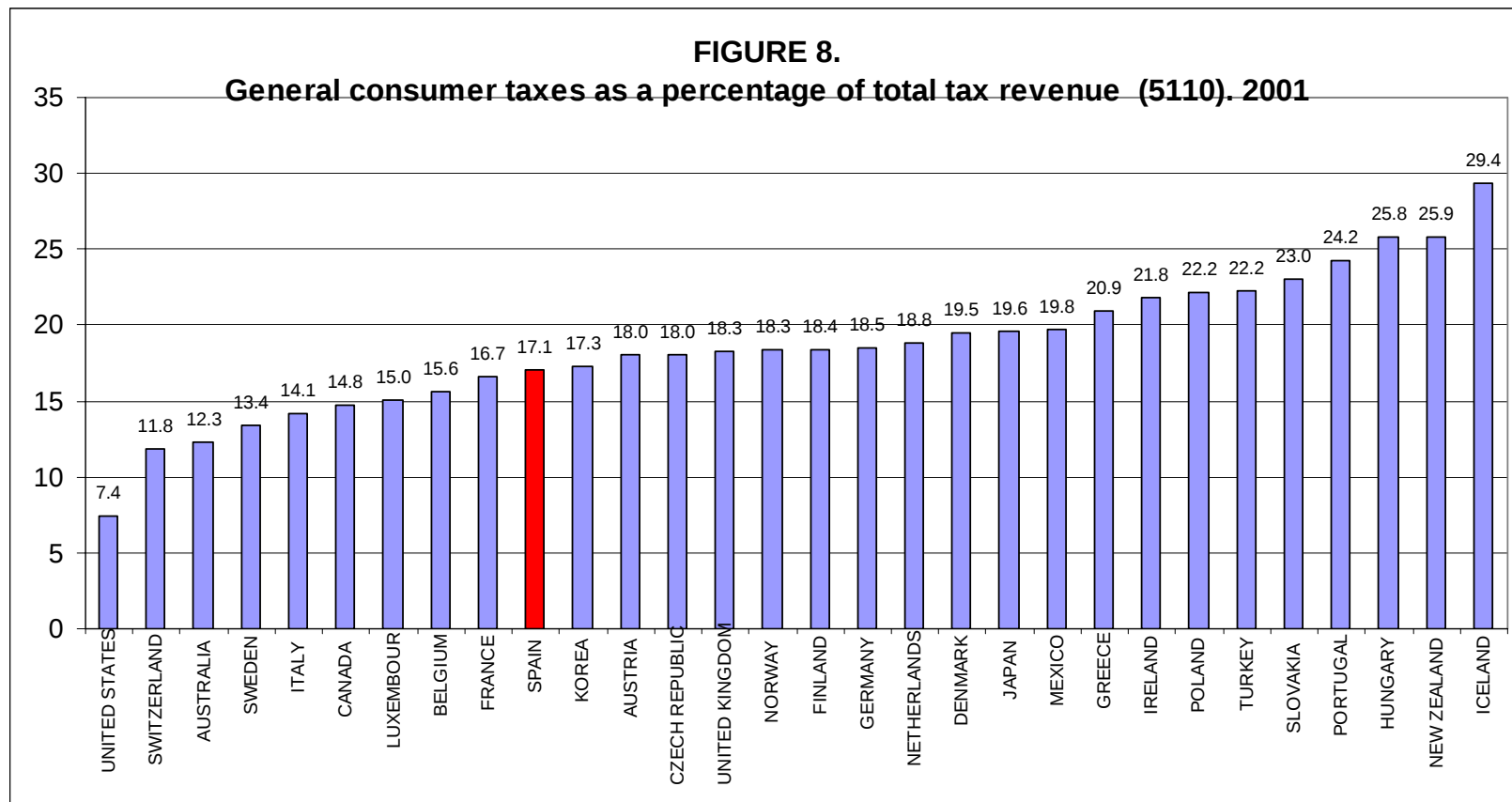
Table 8. General Consumer Taxes as a Percentage of Total Tax Revenue (5110) (Continued)

	1965	1970	1975	1980	1985	1995	2000	2001	Variation
NORWAY	21.51	23.75	20.49	18.22	18.19	21.21	19.74	18.34	-3.17
NEW ZEALAND	7.65	7.99	9.02	10.21	10.36	22.72	24.71	25.85	18.2
SWEDEN	10.37	10.26	11.98	13.36	13.96	15	13.38	13.38	3.01
FINLAND	18.46	19.31	16.79	18.66	19.54	17.32	18.03	18.39	-0.07
ICELAND	16.71	21.98	28.59	28.92	33.05	31.75	29.38	29.38	12.67
SWITZERLAND	9.45	7.82	7.76	9.16	9.46	10.32	11.49	11.84	2.39
AUSTRIA	18.68	18.53	19.84	20.11	20.99	18.23	19.04	18.01	-0.67
TURKEY					23.29	31.07	23.3	22.23	22.23
CZECH REPUBLIC						17.16	18.89	18.05	
SLOVAKIA							22.25	23.05	
HUNGARY						19.43	26.08	25.82	
POLAND						17.06	22.19	22.19	

Notes: (*) In all tables the last data entry for Portugal, the UNITED STATES, Australia, Iceland and Poland corresponds to the year 2000.

Source: OCDE





The appearance and the increase in importance of the VAT in those OECD countries where this tax exists, namely all except the USA, is detailed in Tables 9 and 10. The generalization of the VAT goes a long way towards explaining the rise observed over recent decades in the intake derived from consumption taxes. Australia introduced a Goods and Services Tax in 2000; Greece, Spain and Portugal introduced the VAT in the 1980s as a consequence of joining the EU; Iceland, Japan and New Zealand introduced the VAT around the same period; and Switzerland did the same at the end of that decade. The economies of the former Soviet bloc have also introduced the VAT as an important source of tax revenue in most cases starting with the beginning of the transition to a market economy.

In the European countries, VAT represented some 7 percent of GDP in 2001, while the figure for Spain was about 6 percent, though VAT as a percentage of total tax revenue was similar at over 17 percent.

Interestingly, countries tend to apply quite different VAT rate structures (Table 12)¹⁶: Denmark has a single rate; there are two rates in Germany, Holland and the UK; and structures with multiple rates in Greece, France, Italy, Ireland, Spain, Austria, Portugal, Finland and Sweden. Nominal rates also vary widely, whereas Sweden and Denmark have rates of 25 percent and Iceland has a rate of 24.5 percent, Canada has a rate of 7 percent and Switzerland a rate of 7.5 percent. For the EU countries as a whole the standard tax rate fluctuates between 15 percent and 25 percent, while for the OECD it fluctuates from 5 percent (Japan) to the aforementioned 25 percent in Sweden and Denmark. Moreover, in the last twenty years all countries have raised their standard nominal rates, such that the EU average has risen from 17.5 percent to 19.4 percent.

Table 9. VAT as a Percentage of GDP (5111)

[illegible]

Table 9. VAT as a Percentage of GDP (5111) (Continued)

	1965	1970	1975	1980	1985	1995	2000	2001	Variation
NORWAY		8.2	8.1	7.8	7.9	8.8	8	8.2	8.2
NEW ZEALAND						8.5	8.7	9	9
SWEDEN		4	5.1	6.3	6.8	7.1	7.2	7.1	7.1
FINLAND	5.6	6	5.8	6.3	7.3	7.4	8.1	8.2	2.6
ICELAND						9.5	10.3	9.3	9.3
SWITZERLAND						2.4	4.1	4.1	4.1
AUSTRIA			7.4	8	8.8	7.6	8.3	8.2	8.2
TURKEY					3.5	5.5	7.8	8	8
CZECH REPUBLIC						6.9	7.5	7	
SLOVAKIA							8	7.6	
HUNGARY						7.5	8.8	8.7	
POLAND						6.7	7.6	7.6	

Notes: (*) In all tables the last data entry for Portugal, the UNITED STATES, Australia, Iceland and Poland corresponds to the year 2000.

Source: OCDE

Table 10. VAT as a Percentage of Total Tax Revenue (5111)

	1965	1970	1975	1980	1985	1995	2000	2001	Variation
OECD Total	1.61	5.84	8.1	9.77	10.77	16.12	17.54	17.46	15.85
OECD Europe	2.03	7.38	10.66	11.39	12.79	18.05	19.05	17.34	15.31
European Union (15)	2.57	7.77	12.13	13.22	13.5	17.48	18.02	15.81	13.24
OECD America				5.19	5.31	7.88	8.65	13.56	13.56
OECD Pacific				5.5	5.27	11.7	15.48	20.9	20.9
GERMANY		17.14	14.63	16.63	15.81	17.44	18.37	18.52	18.52
FRANCE	20.07	25.46	23.1	20.88	19.68	16.99	16.49	16.2	-3.87
ITALY			13.68	15.62	14.5	13.82	15.76	14.13	14.13
NETHERLANDS		14.61	14.36	15.83	16.18	15.6	17.34	18.81	18.81
BELGIUM		11.28	16.29	17.1	15.72	15.29	16.14	15.57	15.57
LUXEMBOUR			11.93	9.71	10.78	12.25	13.28	14.12	14.12
UNITED KINGDOM			8.91	14.66	15.88	19	18.37	18.25	18.25
IRELAND			14.68	14.76	20.59	21.25	21.49	21.49	21.49
DENMARK		18.77	16.9	22.25	20.12	19.32	19.58	19.53	19.53
SPAIN						15.85	17.6	17.06	17.06
GREECE						22.49	21.96	20.2	20.2
PORTUGAL						23.39	24.21	24.21	24.21
MEXICO				15.56	15.94	17.01	18.72	19.75	19.75
CANADA						6.62	7.24	7.37	7.37
KOREA				22	21.07	18.88	17.02	17.25	17.25
JAPAN						5.21	8.89	19.6	
AUSTRALIA							11.31	11.31	11.31

Table 10. VAT as a Percentage of Total Tax Revenue (5111) (Continued)

	1965	1970	1975	1980	1985	1995	2000	2001	Variation
NORWAY		23.75	20.49	18.22	18.19	21.21	19.74	18.34	18.34
NEW ZEALAND						22.72	24.71	25.85	25.85
SWEDEN		10.26	11.98	13.36	13.96	15	13.29	13.28	13.28
FINLAND	18.46	18.96	15.72	17.33	18.32	16.35	17.35	17.67	-0.79
ICELAND						30.07	27.67	26.79	26.79
SWITZERLAND						7.35	11.49	11.84	11.84
AUSTRIA			19.84	20.11	20.99	18.23	19.04	18.01	18.01
TURKEY					22.34	24.32	23.3	22.23	22.23
CZECH REPUBLIC						17.13	18.89	18.05	18.05
SLOVAKIA							22.25	23.05	
HUNGARY						17.82	22.45	22.48	
POLAND						17.02	22.19	22.19	

Notes: (*) In all tables the last data entry for Portugal, the UNITED STATES, Australia, Iceland and Poland corresponds to the year 2000.

Source: OCDE

There is also significant variation in effective rates. Table 11 and Figure 10 show the effective rates derived from the application of VAT (column 5). To calculate these rates we have divided the revenue from this tax by family expenditure on final consumption, that is used as measure of the potential base of the VAT for each country.

In the final column of Table 11 (column 6) we present calculations of the consequences arising from the existence of exemptions, minimum allowances and reduced rates by country, thereby relating the aforementioned effective rates with the standard nominal rate for each country. It can be seen that for Luxembourg, Switzerland, Japan and Norway the effective rates are quite similar to the nominal rates; in most cases, however, the effective rates range from 60 percent to 80 percent of the nominal rates. For Spain, the efficacy of the tax in this regard is quite low (see Figure 10), since he is estimated an effective rate of the IVA of 10.58 percent, that, in front of 16 percent of the legal rate, it represents 66.1 percent of the same one, that would be the productivity of this tax.

In the ambit of the EU, the lack of neutrality between countries which is reflected in the large differences between effective and nominal rates highlights the need to make advances in the area of reducing distortions which affect competition within states, e-commerce and cross-border purchases.

The consequences of the different VAT regulations and the difference degrees of compliance for tax-collection are reflected in the productivity of VAT by country (column 4 of Table 11; Figure 9). VAT productivity has been calculated by dividing the specific fiscal pressure of VAT for each country by the standard nominal rate in place

that country. The values for Switzerland, Turkey, Portugal, Korea and Greece are high but those of the remaining countries vary from 30 percent to 40 percent (Figure 9).

Table 11. VAT Productivity and Effective Tax Rates

	<u>Revenue</u>	<u>Nominal</u> <u>rate</u>	<u>productivity</u>	<u>Effective rates</u>		
	% share of public revenue			% of nominal		
	% GNP					
	2001	2001	2001	2000		
	(1)	(2)	(3)	(4) = (1)/(3)	(5)	(6) = (3)/(5)
GERMANY	6.7	18.52	16	41.9	12.31	77.0
FRANCE	7.3	16.2	19.6	37.2	13.93	71.1
ITALY	5.9	14.13	20	29.5	11.02	55.1
NETHERLANDS	7.5	18.81	19	39.5	14.60	76.8
BELGIUM	7.1	15.57	21	33.8	13.94	66.4
LUXEMBOUR	6	14.12	15	40.0	14.50	96.7
UNITED						
KINGDOM	6.8	18.25	17.5	38.9	10.91	62.3
IRELAND	6.7	21.49	17.5	38.3	14.60	83.4
DENMARK	9.6	19.53	25	38.4	20.53	82.1
SPAIN	6	17.06	16	37.5	10.58	66.1
GREECE	8.2	20.2	18	45.6	11.94	66.3
PORTUGAL	8.3	24.21	17	48.8	13.84	81.4
MEXICO	3.6	19.75	15	24.0	5.16	34.4
CANADA	2.6	7.37	7	37.1	4.93	70.5
KOREA	4.7	17.25	10	47.0	7.99	79.9
JAPAN	2	19.6	5	40.0	4.39	87.8
AUSTRALIA	3.6	11.31	10	36.0	5.92	59.2
NORWAY	8.2	18.34	23	35.7	19.58	85.1
SWEDEN	7.1	13.28	25	28.4	14.82	59.3
FINLAND	8.2	17.67	22	37.3	17.24	78.3
ICELAND	9.3	26.79	24.5	38.0	17.90	73.1
SWITZERLAND	4.1	11.84	7.5	54.7	7.06	94.1
AUSTRIA	8.2	18.01	20	41.0	15.08	75.4
TURKEY	8	22.23	15	53.3	10.88	72.6
CZECH						
REPUBLIC	7	18.05	22	31.8	13.85	62.9
SLOVAKIA	7.6	23.05	23	33.0	15.03	65.3
HUNGARY	8.7	22.48	25	34.8	17.25	69.0
POLAND	7.6	22.19	22	34.5	11.74	53.4

Notes: Productivity: collection of the VAT in percentage of the GDP divided by nominal type.

Effective types: Collection of the VAT in percentage of the expense in final consumption of the families.

Source: OCDE and Own Elaboration

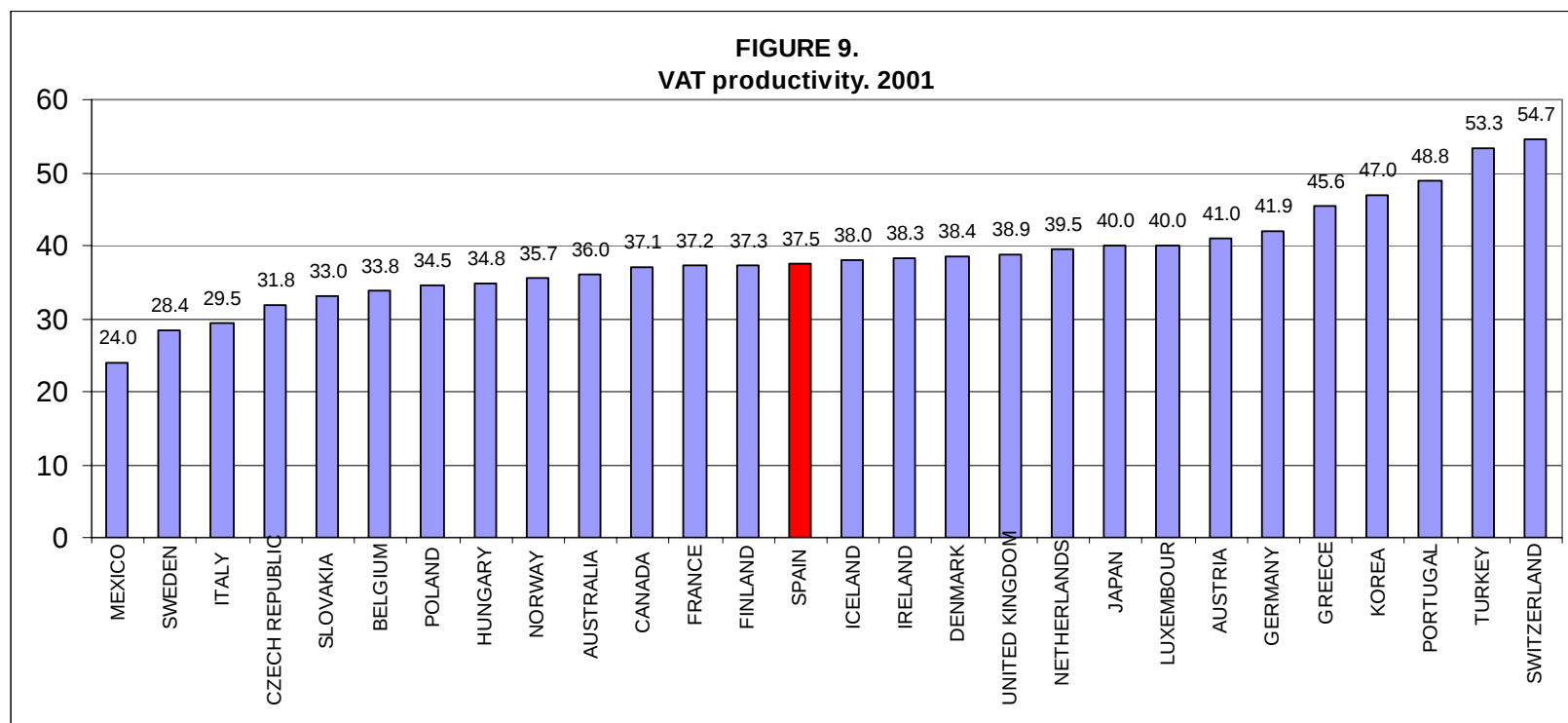


FIGURE 10.
Effective VAT rate as a percentage of nominal VAT rate. 2000

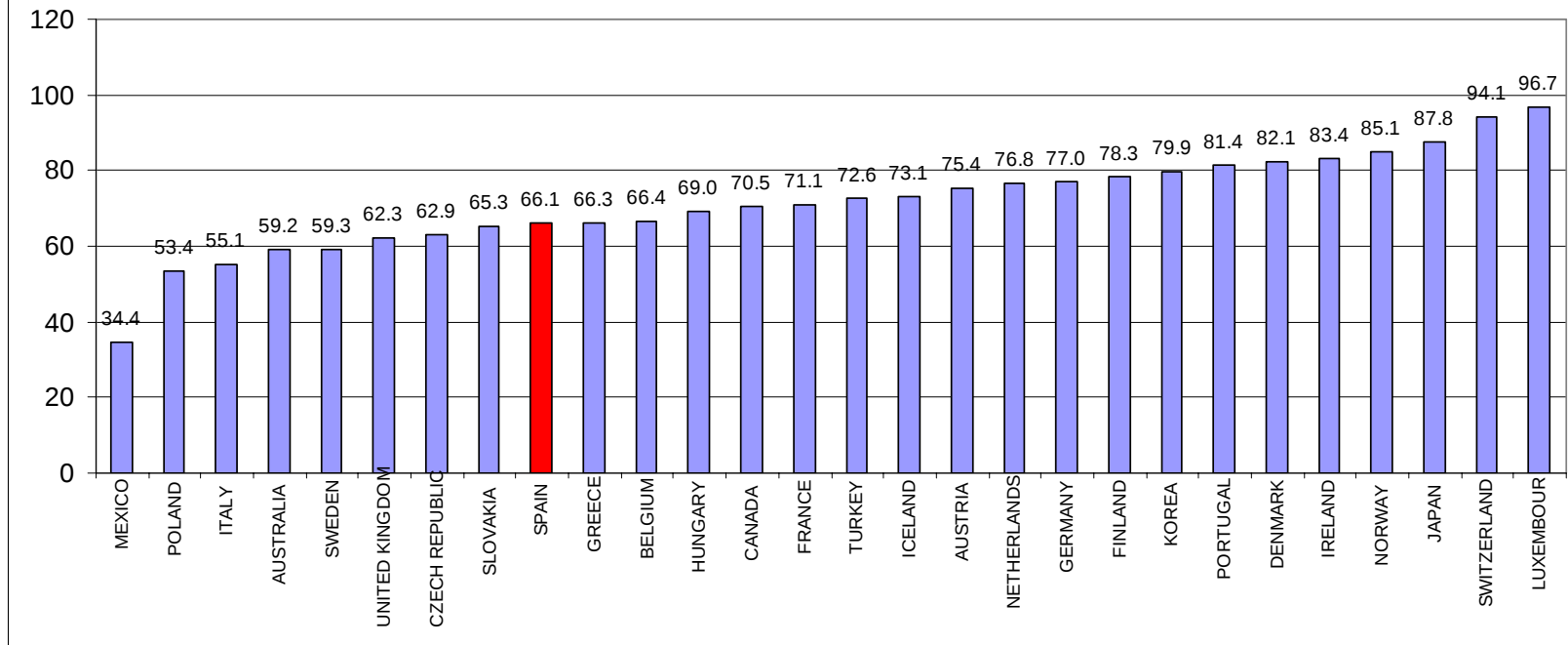


Table 12. VAT Rates in the EU (15) (As of May 2002)

	<i>Super Reduced</i>	<i>Reduced</i>	<i>Standard</i>	<i>Rate Parking</i>
GERMANY	-	7	16	-
FRANCE	2.1	5.5	19.6	-
ITALY	4	10	20	-
NETHERLANDS	-	6	19	-
BELGIUM (*)	-	6	21	12
LUXEMBOUR	3	6	15	12
UNITED KINGDOM (*)	-	5	17.5	-
IRELAND (*)	4.3	12.5	21	12.5
DENMARK (*)	-	-	25	-
SPAIN	4	7	16	-
GREECE	4	8	18	-
PORTUGAL	-	5/12	17	-
SWEDEN (*)	-	6/12	25	-
FINLAND (*)	-	8/17	22	-
AUSTRIA	-	10/12	20	-

Evolution in Spain				
	<i>Super Reduced</i>	<i>Reduced</i>	<i>Standard</i>	<i>Rate Parking</i>
1/1/1986		6	12	33
1/1/1992		6	13	28
8/1/1992		6	15	28
1/1/1993	3	6	15	-
1/1/1995	4	7	16	-

Note: (*) Countries that use the zero tax rate.

Source: European Commission (2003)

The Process of Harmonization of VAT and Excise Duties with the European Union

Since its origins, the European Common Market has progressed with the ultimate objective of achieving free circulation of goods and services. With this aim, tariffs were eliminated among the participant states and the neutrality of indirect taxes was declared a fundamental goal. In this regard, Articles 95 and 96 of the Treaty of the European

Economic Community embody two principles which must be respected in all cases: the principle of equal treatment of goods, and the principle of no discrimination. Article 99, on the other hand, explicitly contemplates the harmonization of indirect taxes.

After the elimination of tariffs, the European Community began to harmonize the structure of sales taxes and their rates. In 1967 the Council decided to substitute the taxes on company trading with a VAT on consumption applicable on a destination principle, partly to prevent the manipulation of adjustments at frontiers aimed at favouring national exports or substituting imports, which are practices that are incompatible with the objectives of the Common Market. Since then there have been over twenty directives on harmonization, of which the most important was the Sixth, in 1977, which provided a large step towards greater uniformity of the tax base and was partly driven by the decision to convert VAT into a tool for financing the European Community budget.

VAT Harmonization

It is well known that the establishment of a common market implies, among other things, that fiscal frontiers and border controls should be eliminated for intra-community transactions. That is, goods should circulate between two community countries with the same freedom with which they circulate between two locations in the same country. In common with standard practice in international trade, VAT was subject to the destination country criterion in Europe and the administration of this was carried out at the physical borders between community countries (indeed, this still occurs for trade with the rest of the world). Thus, the fiscal adjustment occurs at the border. The exporter has the right to a VAT credit and the importer is charged the VAT of the destination country.

The elimination of fiscal frontiers within the European Community meant that the system had to change so that intra-Community operations occur in the same way as those carried out within individual Member States. One possibility in this respect would be to apply origin-destination VAT within the Community. In other words, the agent acquiring the good in the importing country is charged the VAT of the exporting country, and the importer has the right to deduct the payments made to the origin country at the standard rate.

This solution gives rise to serious difficulties, the most fundamental being that the VAT intake does not correspond to the level of final consumption within each country. Under origin-destination VAT, the exporting country receives a return which the agent acquiring the good in the importing country uses as a deduction; the countries within the Community which export more, increase their VAT intake at the expense of the countries which import more, and these see their VAT intake reduced. However, VAT intake should basically depend on a country's consumption. This problem thus requires the creation of a compensation mechanism between Member States which would permit the destination country to be compensated for the VAT received by the origin country and deducted by the destination country.

Since January 1st, 1993, the European Union opted to provisionally maintain the destination principle despite the elimination of VAT controls at intra-Community borders. This provisional regime was developed in Directive 91/680/EEC (16th of December), which regulates the legal framework of intra-Community trade and which modified the Sixth Directive of 1977; in Regulation 92/218/EEC (27th of January) on administrative cooperation in the field of indirect taxation; and in the agreements reached

on the harmonization of tax rates. As a technical solution, the taxable event of acquisition of intra-Community goods was created. This permitted the elimination of customs procedures (formally, imports and exports do not exist between Member States), with verification of VAT payments now being performed through company accounting. Under the taxable event of intra-Community acquisition of goods, each intra-Community transaction is divided into two operations: a delivery, exempt from tax, but with the right to a VAT deduction for the person making the delivery; and an acquisition, subject to tax, whose VAT is borne by the acquirer who in turn deducts it, initiating the VAT chain in the destination country.

As the European Council has not made any declaration on this subject, the provisional system has been automatically extended and remains in force at present. As already mentioned, this system was laid out in Directive 91/680/EEC, Regulation 92/680/EEC, and the agreements reached on the harmonization of tax rates. The contents of these agreements can be summarized as follows: the standard rate of VAT cannot be lower than 15 percent; one or two reduced rates may be applied, provided they are no lower than 5 percent; higher VAT rates may not be applied. However, there are some exceptions: Spain and Luxembourg can apply a special reduced rate no lower than 3 percent; the UK and Ireland can maintain their traditional zero-rates; and the rights of States which had been applying rates below 5 percent are generally respected.

In summary, the system is too complex, excessively combining the origin and destination principles. This leads to insecurities and uncertainties with regard to fiscal responsibility and increases the administrative burden. This situation makes it advisable to move from the provisional regime to a more definitive regime, and it is in this

direction that the European Commission has focused much of its harmonization effort in recent times. For this transition, a series of fundamental measures must be made regarding two issues: (a) the general application of the taxation principle of destination or origin, and (b) greater or lesser harmonization of tax rates.

Recent Commission proposals aimed at achieving the establishment of a definitive VAT system based on the origin principle include:

- the elimination of the present distinction between interior and intra-Community operations and, as a consequence, the elimination of the taxable event of intra-Community acquisition of goods and the exemption applied to deliveries of goods whose destinations are other Member States.
- the possibility to deduct certain VAT instalments on goods used for both company and personal activity, such as, for example, cars.
- VAT revenues collected by Member States where taxpayers have their fiscal residence will be entirely redistributed between Member States in function of the consumption of goods and services subject to the tax which has taken place in their respective territories, as determined by statistical data.¹⁷
- regarding the harmonization of the rules regulating the structural elements of the tax, it will be necessary to establish a single standard VAT rate band (between 15 percent and 25 percent) as a preliminary step, with a view to reducing the width of this band. At present, the only obligation is to respect the minimum of 15 percent for the standard rate. The number of reduced rates should be limited to the minimum, and if possible to only one, with a band as narrow as that envisaged for the standard rate.

- each Member State should be responsible for the management, collection and control of tax corresponding to taxpayers whose fiscal residence is in the territory of that State and to that due for imports of goods into that territory. States who, due to a lack of diligence, endanger VAT receipts may be obliged to redress the corresponding losses.
- the establishment of standard methods to ensure more efficient control and collection. This will determine the need to create new instruments and methods of cooperation and to perfect the present system of information exchange.
- a study is due on the legal instrument (directive or regulation) which will be used, and a modification of Article 99 of the Treaty to substitute the principle of unanimity now required to adopt such measures with that of a qualified majority.

In June 2000, the Commission presented a Communication in which it set out its strategic program to improve the workings of the VAT regime within the framework of the internal market. The program proposed a series of pragmatic measures centered around four main objectives; the simplification and modernization of existing rules, a more uniform application of existing regulations, and cooperation at administrative level. This strategy was based on the observation that it was unlikely, given the reluctance of the Member States, that significant advances would be made in the near future on the establishment of a common VAT regime based on the origin principle.

The main objective of the strategy was to provide a new impulse to the European Council with the aim of achieving concrete and necessary improvements to the existing tax regime in the short run, without calling into question the long-run objective of a definitive regime based on taxing in the origin Member State. Since the new strategy was

put into place almost three years ago, the Council has put forward several proposals on the issue of the VAT. However, as pointed out by the Commission (European Commission, 2003a) the maintenance, in an enlarged Union, of the principle of unanimity when taking decisions on taxation represents a serious threat to this incipient progress. If future work is carried out within the framework of Article 93 of the Treaty, the Member States will more than ever have to show flexibility at negotiations in order for progress to continue. This flexibility will be even more necessary when it comes to measures aimed at a key element of the VAT system, namely the determination of where operations should be taxed.

A more extended and better use of electronic means of communication between operators and the tax administration, as well as between the tax administrations of different Member States, would allow the VAT regime to be simplified for operators, safeguarding and even extending control measures. In effect, through the creation of a one-stop-shop mechanism, an operator established in the European Union can contact the Administration of the Member State in which he is established in order to comply with his obligations regarding tax declarations and payment. The introduction of this mechanism greatly facilitates procedures in cases where an operator carries out taxable transactions for which he appears as a debtor in other Member States where he is not established. The use of this mechanism would reaffirm the principle of taxing in the place of consumption (the destination principle), without generating administrative burdens for Community operators or hindering the workings of the internal market. Moreover, taxing in the place of consumption, at the VAT rate which is applicable in the Member State where consumption has taken place, guarantees the correct functioning of the internal

market while at the same time permitting that the Member States preserve certain sovereignty when it comes to setting the VAT rates to be applied in their territory.

On the other hand, the Commission is continuing with efforts to modernize the present regime and to guarantee its more uniform application. In particular, the proposals towards providing legal substance to the debates of the VAT Commission¹⁸ as well as the planned initiative aimed at introducing a mechanism for managing individual cases should contribute to settling cases of double taxation, a practice which has no place in an authentic internal market.

The observation that the present regime has defects which can give rise to fraud is not a new one. Carousel fraud exploits these defects inherent to the basic principles which constitute the foundations of the present regime.

As is known, in the present provisional VAT regime of the European Union transactions involving deliveries of goods between companies of different EU member States are subject to VAT through the application of a system under which transactions are exempt in the origin member state. VAT fraud on intercommunity transactions occurs in many varieties but basically functions somewhat as follows. A company, which we call Firm 1, registered in an EU member state which we call State X, carries out an inter-Community delivery of goods to Firm 2 located in another State Y. Firm 2 acquires these goods free of VAT and immediately carries out a delivery to another firm, Firm 3, in the same state as itself, State 2. Firm 2 (the “missing trader”, which is the name commonly given to these types of fraudulent operators) charges the VAT from the previous delivery to Firm 3, but does not lodge it and after a short while disappears. Firm 3 (“broker”) deducts the VAT it has paid on its acquisitions from 2 and sells the goods in the internal

market of State Y, charging VAT. The loss in VAT revenue is equal to the payment made by Firm 3 to Firm 2, which the latter has not lodged. At times, and with the objective of obscuring the relationship between Firm 2 (missing trader) and Firm 3 (broker), the goods are supplied from one to the other through one or more intermediary companies (“buffers”).

The scheme just outlined turns into “carousel fraud” when, instead of selling the goods in the internal market of State Y, Firm 3 carries out an inter-Community tax-exempt delivery to a company in the origin state, State X. Once in this State, the operation can be repeated indefinitely. The fraud is therefore manifest in the application for a VAT return made by Firm 3. In the so-called “document” carousel fraud, the merchandise does not even exist and there is only a circulation of invoices. However, the Commission is of the opinion that an ever-increasing collaboration between the Member States, with the support of the Commission, should make it possible to keep fraud within acceptable limits¹⁹. If in spite of the efforts of the authorities carousel fraud becomes so intense as to affect the normal functioning of the economic market, causing unacceptable distortions to competition for honest operators, a need will arise for a debate at Community level on the future common VAT regime.

With regard to the future path of VAT harmonization, attention should be drawn to the stagnation into which the definitive VAT regime has fallen, with the consequent major slowdown in the process of tax harmonization in Europe that this has caused. The uncertainties which hang over the existence, conditions and terms of the origin system are generating an impasse even with regard to the changes which are needed to maintain the present provisional system. Spain, in its position as a net importer within the EU, is

comfortably positioned within the great majority of member states against change, given that a significant share of tax revenue would be lost in a macroeconomic “clearing” with uncertain results. The large differences in opinion between member states with regard to the need to carry out serious progress in the field of tax harmonization combined with the requirement of unanimity in the Council to adopt proposals in this area make it unlikely that the so-called definitive regime will be put in place in the next few years.

The Commission itself recognizes the incoherence of some of its proposals in relation to the objective, more and more theoretical as time goes by, of taxing in the State of origin which should have been complied with on the 31st of December, 1996. Taxation in the state of origin only pins down the territory in which the taxpayer has to pay the tax, and only a system of reallocation would guarantee that each member state would receive the revenue corresponding to it, given the distortions which could arise from the fact that the taxpayer belongs to one state whereas final consumption takes place in another. The problem is that this would require the differences between tax rates to be reduced, practically to the extent they were unified. The main obstacle is not technical, but political, so that as long as States are unwilling to abandon the principle of taxing in the destination country, any improvements in the common VAT regime can only be aimed at guaranteeing strict compliance with the present structure. This is manifest in the almost definitive confirmation that the future of tax harmonization is going to be centered on technical modifications to the Sixth Directive (with a large impulse given to inter-administrative cooperation), and that there are two steps which are not going to be taken in the medium term: the transition from the destination principle to the origin principle, on one hand, and the unification of tax rates on the other. This opinion is reinforced not only

by the pessimism of the Commission itself but also by the fact that this pessimism arose in a Union with 15 member States, leading us to the conclusion that it will only get worse with a Union of twenty-five members and with the amplified Union from 2007 on.

Finally, motivated by the year 2002 financing reform of the Autonomous Communities, the central government put forward the alternative of a partial ceding of VAT, in particular the retail phase. To this end the European Commission was consulted for its opinion on this possibility.

The position of the Commission can be summarised as follows. With regard to handing over part of VAT revenue, no restrictions are placed by the EU on member states. The member states are sovereign, and can distribute their tax revenue according to their needs provided that this does not have any affect on its own resources derived from VAT.

On the other hand, Community VAT provisions currently in place do not permit the Autonomous Communities to fix differential VAT rates. Article 12, Paragraph 3a, of the Sixth Directive stipulates that a single normal rate be set for each member State. Member states can then apply one or two reduced rates. Moreover, the possibility that the Autonomous Communities charge a supplementary tax which would act as a tax on the volume of business is not allowed either given the provisions of Article 33 of the Sixth Directive. In light of the above, it can be asserted that the possibilities for future changes will be restricted to the percentage share in the tax intake.

Excise Taxes

Regarding excise taxes, the trend towards maintaining the destination based principle of taxation is likely to continue, as has been mentioned above. This brings with it a need for

harmonization of the tax rates in force in the Member States as well as a minimum harmonization of the structures (taxable events, systems of collection, tax exemptions, etc.) if fiscal frontiers are to be effectively eliminated. Over the years, the Commission has put forward many proposals, mainly related to the harmonization of tax *structures* rather than tax *rates*. However, progress has been slow, primarily due to the budgetary impact.

Community norms on the harmonization of excise taxes regulate the structure of these taxes and establish the minimum rates applicable for each product category. This has permitted the member states to maintain large differences in tax rates. Up to now these differences have not generated unbearable distortions because it is only on sales to private agents (for the satisfaction of their needs and transported by them) that the principle that the tax be received in the country where the goods are acquired and at the rates applicable in that country applies. Otherwise, the tax is generated and paid in the destination country.

The delay in bringing minimum excise tax rates up to date is damaging the process of harmonization of excise duties on hydrocarbons – tainted by the controversy over the CO₂ tax – and alcohol and tobacco. The story of the “CO₂ tax” begins in 1992 when the Commission proposed the creation of a harmonized tax on energy consumption in order to comply with the Community commitment to reduce CO₂ emissions. Two years later, and faced with the impossibility of arriving at an agreement on the obligatory establishment of an “ecotax” (which some defended on environmental ground while others were opposed on grounds of competitiveness), the Essen summit seemed to have abandoned the project, although it did establish the setting of some common parameters

so that states who wished to introduce taxes of this nature could do so without distorting the functioning of the Single Market.

The Commission has not presented proposals corresponding to the revision of excise duties on alcohol and tobacco either. These have been blocked by the full body of the Commission due to the eternal disagreements surrounding the taxation of these goods. There is a division between the States which produce cheap manufacturing tobacco, who defend ad valorem rates, and those who produce expensive tobacco, who defend a lump-sum tax. There are also divisions between wine-producing States, who defend the present zero rate and limited control, and non-producers, who wish to tax wine the same way as other alcohol products.

On the other hand, the member states have created non-harmonized excise duties to get around the limitations imposed by the the harmonization of VAT and to take advantage of its shortcomings. In some cases, these excise duties have compensated the obligatory elimination of higher VAT rates, such as the Spanish vehicle registration tax. In other cases consumption tax was extended beyond the straitjacket of VAT to certain sectors for which Community directives permitted exemptions. An example of this is the tax on insurance premia recently introduced in Spain and which had already been introduced in the majority of member states.

The changes which can be expected in the coming years and which can be gathered from the proposals awaiting approval presented by the Commission are not particularly important, and will not achieve (nor is it their aim) the unification of rates of taxes on specific consumption goods nor even the establishment of tax bands. It will thus remain

the norm that large differences exist among member states with regard to the tax burden borne by products subject to the regime of taxes on specific consumption goods.

With regard to the use of excise taxes in the financing of the Autonomous Communities, the future could be marked by the creation of new national taxes under certain conditions, which include: i) that the objective pursued be not primarily budgetary; and ii) that the tax be claimed only at the point of consumption. These taxes could then be handed over to the territorial governments, as has happened with the excise tax on fuels.

The current solution of imposing excise duty on manufacturing in the country where consumption takes place, in force since the 1st of January, 1993, is likely to be maintained in the medium term. Excise taxes are subject to what has come to be known as a “suspension system”, which is defined in the Spanish Excise Tax Law (*Ley Española de Impuestos Especiales*) as the “regime applicable to the manufacture, transformation, holding, and circulation of products subject to excise taxes for which the taxable event has occurred but the tax has not accrued, and hence the tax is not demandable”.

At present, therefore, under the “destination-based principle of taxation” the circulation of goods in EU territory is carried out freely under duty suspension arrangements up until they arrive at the tax warehouses (*depósitos fiscales*) in the destination country, where the excise tax is paid (at the tax rates in force) at the moment the product is consumed. This is the same as before with the difference that there have been no controls at internal frontiers since January 1st, 1993. Despite its problems, the system does not seem to be in need of radical reform.

In summary, we note that there are serious defects in the provisional VAT regime still in place. We believe it will not be long before there is an origin-destination system in place in the Community where the repercussions of the VAT will not interrupt transactions between business people and professionals of the Member States. As we have commented, however, it is unlikely that the definitive origin country regime will be adopted in the medium term.

A reduction of the dispersion of existing tax rates is also possible. On the other hand, the present structure of excise taxes can be maintained, and perhaps extended to an environmental tax.

Incidence of Indirect Taxation

As predicted by theoretical analysis, Spanish indirect taxes on the whole are markedly regressive in nature. From a personal point of view, the fact that these taxes basically fall on consumption suggests that this is indeed the case. This conjecture has been confirmed by numerous empirical studies which have been carried out for Spain on the distribution of indirect tax burdens across income levels. Both the studies carried out before the introduction of VAT²⁰ and those carried out after its introduction²¹ conclude in all cases that indirect taxation is regressive. This is so, in spite of the radical changes carried out to the structure of this class of taxes, the constant evolution of Spanish consumption patterns, and the changes in income distribution over this long period.

The comparison of the results in Avellaneda (1998), for the year 1991 for the set of all consumption taxes, with those in Argimón, González-Páramo and Salas (1987) for the year 1980 also for the whole set of indirect taxes, allows us to calculate the variation of effective average tax rates over the decade. Thus, over this period the average rates as a

percentage of expenditure rose from 7.34 percent to 8.805 percent and as a percentage of income from 8.43 percent to 11.293 percent²². Though the tax structures corresponding to both years are quite different, the comparison is reasonable due to the fact that consumption taxes accounted for practically all indirect taxation in 1991.

If we focus exclusively on VAT, the rates found by Avellaneda (1998) for 1991 are lower than those found by González-Páramo and Salas (1991) for 1986. As a percentage of expenditure, the rate fell from 7.88 percent in 1986 to 6.571 percent in 1991, while as a percentage of income the rate fell from 9.02 percent in 1986 to 8.558 percent in 1991. The changes in the VAT rates²³ brought about a rise in fiscal pressure from 1993, with the average rate as a percentage of expenditure rising 0.615 points from 8.805 percent to 9.420 percent and the average rate as a percentage of income rising by 0.801 points from 11.923 percent to 12.094 percent. While taxes increased across the board, Excise Taxes increased much more than VAT as a consequence of the elimination of the higher VAT rates and the introduction of the new Vehicle Registration Tax.

Although consumption taxes as a whole are regressive, VAT is somewhat less so than excise taxes. However, two excise taxes, namely the fuel and vehicle registration taxes, seem to be progressive. This is a consequence of the fact that the consumption of these goods is highly conditioned on income levels. The high prices of motor vehicles, the possession of which determines the consumption of oil-based fuels, imply that families with higher incomes are the ones buying them. Alcohol and tobacco duties, on the other hand, are extremely regressive. The consumption of these goods, which are accessible to people at all income levels, given that their prices are low, is determined above all by cultural factors. However, it is likely that those sectors of the population

which are better-informed will consume less of these products given the prejudicial effects they have on health. As there is a high correlation between information levels and income, low-income families tend to consume more of these products and thus contribute more than high-income families to this tax (Avellaneda and Sánchez Maldonado, 1999).

Serrano (2003, p.80 and thereafter) examines the redistributive impact of the present VAT arrangements in Spain. With regard to VAT payments, the present system is characterized by the fact that the tax burden is not spread proportionally across income distribution. The concentration index is 0.2268, whereas the Gini index is higher (0.2964). In other words, the tax payments concentration curve lies above the Lorenz curve of pre-tax income, for every percentile, which implies that indirect taxes are globally regressive. The negative value of the Kakwani index (-0.0696) confirms the regressiveness of VAT, again from a global point of view. As an illustration, the poorest 30 percent of the population has 14.59 percent of income but pays 20 percent of the VAT burden. The richest 10 percent of the population, on the other hand, receives 23.47 percent of the income but only pays 17.06 percent of the VAT. The reduction of the average effective rate as income rises is another indicator of the regressiveness of the present VAT regime in Spain.

The studies by Avellaneda and Sánchez Maldonado (1999) and Sánchez Maldonado, Gómez Sala and Avellaneda (1999) analyze the distribution of the fiscal burden from consumption taxes across individuals according to the Autonomous Community of residence as well as income. The comparative analysis of the rates of the different taxes in the different regions for two different years allows us to compare the relative incidence of each tax in each region and to measure the impact of the 1993 reform on each region.

These studies show that regional tax rates are far from homogeneous. There is a significant variation of rates both as a percentage of expenditure as well as income, with the dispersion in income terms being higher, and there are also variations across the individual taxes. The increase in tax as a result of the 1993 reform also affected different regions quite differently. Their expected conclusion is that the taxes are regressive on the whole, and that the effective rate of taxation is higher in lower-income regions than in higher-income regions. Again, this result is to be expected if we extend the finding that consumption taxes are regressive at the level of household income to the territorial level.

Another relevant fact is that if we take the composition of households into account then the taxes are even more regressive in terms of their territorial distribution. The extent of this is such that the only two progressive taxes, namely fuel and vehicle registration taxes, become regressive. This is an important factor when it comes to analyzing the equity of the indirect tax system because for a given income level a household with more members has less capacity to pay such taxes. Finally, the 1993 reform slightly reduced territorial regressiveness both for the taxes as a whole as well as for each individual tax with the exception of the tax on alcoholic drinks, which became much more regressive than before.

Some Outstanding Problems and Options for Reform

As has been stated (Cnossen, 1998), the introduction of Value Added Tax (VAT) on an almost universal level should be considered as the most important event of the second half of the twentieth century as far as the evolution of tax systems is concerned. Since the end of the nineteen-sixties, VAT has become the main consumption tax in 123 industrialised and developing countries. At present, the most notable absences from the

list of countries where VAT exists are the USA and India. For different reasons, in these jurisdictions traditional consumption taxes have been relied upon. The motives for adopting VAT varies from one given country to another, though the main reason in all cases has been the realization that a correctly-designed value added tax is capable of generating greater public revenues than any other broad-based general consumption tax, and with lower economic and administrative costs.

However, a large number of problems persist with regard to VAT in many of the countries where it has been introduced (Cnossen, 1998, 2001; Ebril *et al*, 2001). Among these, the following can be highlighted. Firstly, on many occasions, and as happens in the Spanish case, VAT does not extend to the retail consumption stage. Secondly, it has been noted that many countries generalize the practice of exempting certain services, ignoring the costs of doing so in terms of economic distortions and administration problems. Noteworthy in this regard is the treatment given to public services (postal services, telecommunications, public transport), which often remain exempt without any theoretical or practical justification. The same occurs with a large portion of cultural services (books, DVDs, etc) and the activities of education and health.

Thirdly, many countries find it difficult to tax real estate, financial services, agricultural activity and small enterprises.²⁴ In the case of real estate, subjection to tax is clearly preferable to exemption. No clear solution to the treatment of financial services appears in sight²⁵, while different ad hoc systems are used to tax the agricultural sector.

Fourthly, there is the problem of the number of tax rates. In high-income countries the establishment of a reduced VAT rate for basic products is not a good system of aid for the underprivileged due to the convergence produced in consumption patterns – it is

better to apply a single rate. In low-income countries, on the other hand, where administrative capability is more limited, the existence of reduced rates and exemptions on basic foods does contribute to mitigating the regressiveness of VAT. However, the equity gains which can be achieved through differentiated VAT rates depend on the level of other instruments available. For example, excise duties on goods with inelastic demands can destroy the main equity gains achieved through differentiated VAT rates. The greater the restraints on the redistributive role of other government taxes and expenditure, the stronger the justifications for differentiated VAT rates on the grounds of equity. Obviously, these justifications will be weaker when an effective income tax can be used. While the benefits from differentiated VAT rates can be large in developing countries, it is also true that the administrative and compliance costs associated with a differentiated structure can be high. In any case, the existence of a heterogeneous tax scale complicates the management of and compliance with VAT. However, as Ebrill et al (2001) state, the importance of differentiated rates seems to have been exaggerated on many occasions. Even leaving aside other instruments, there are aspects of the VAT structure, such as exemptions, which can generate much more damaging effects than having a variety of rates.

Fifthly, the interjurisdictional aspects mentioned earlier are becoming more and more important, especially in the case of countries that are growing or part of an economic union.

Finally, and as mentioned above, in the case of common markets where no customs controls exist, the adjustments which were previously carried out at the frontier are substituted by the control of agents' accounting, through a system of deferred payments,

which seems to be working well in the EU. Cross-border control is possible thanks to a system of information exchange. Dual VATs, such as in Canada, are probably more effective, but would require a supranational VAT in the EU which is at odds with the fiscal subsidiarity of the member states. In the Commonwealth of Independent States, exports are taxed and a tax credit is given on imports. However, this system appears unstable unless accompanied by a well-functioning compensation mechanism.

Table 13. Comparison of VAT Proposals for the EU Single Market

	National VAT rate autonomy	Incentive compatibility	Avoidance of break in VAT chain (VAT rate on intra- community supply)	Compliance symmetry	Clearing requirement (*) characterization of clearing regime
Draft directives 1987/89	Yes	No	Yes (country of supply rate)	Yes	High (micro-or macro- clearing)
1996 VAT proposal (Commission 1996)	No	No	Yes (uniform rate)	Yes	High (VAT revenue sharing)
VIVAT (Keen and Smith)	Yes	Yes	Yes (uniform Euro- VAT rate)	Yes	Low (multilateral intra- Community trade imbalances)
CVAT (McLure)	Yes	No	Yes (uniform CVAT, zero national rate)	No	Low (multilateral intra- Community trade imbalances)
Dual VAT (Bird and Gendron)	Yes	Yes	No (zero rate)	No	Low (special regimes)
Prepaid destination VAT (Vanistendael)	Yes	No	Yes (country of acquisition rate)	No	High (bilateral VAT- transfers to destination states)

Notes: (*) National VAT revenue is allocated in line with national consumption, apart from tolerable cross-border purchases.

Source: Genser (2003).

Various proposals have been made by the European institutions as well as scholars of this issue to address interjurisdictional problems of trade adjustments and overcoming the provisional regime (tables 13), of which the following can be highlighted:²⁶

a) Draft directives 1987/1989

These attempts by the Commission to produce a new model of VAT, which like the 1996 proposal were rejected, tried to get around the problems of breaking the VAT chain and the asymmetric treatment of Community trade by taxing sales according to the rates in the country of origin. In this framework, taxpayers in the destination country have the right to deduct VAT paid on their purchases. To ensure that the VAT collected on these inter-Community transactions flows to the destination country, that is, to the administration in whose territory the consumption of taxed goods takes place, the administration of the origin country would be obliged to compensate the administration of the destination country for the quantity of VAT charged by its companies.

The most glaring drawback of this system is the creation of adverse incentives for the administrations in destination countries or importers with regard to the examination of VAT payments which can be deducted, as these will be reimbursed by the administration of the origin country or exporters who, at the end of the day, are the ones that suffer the consequences of any fraudulent deductions that may occur. Consequently, the introduction of such a system requires the reinforcement of the control and harmonization of the collection systems.

With regard to the system of compensation between countries, in 1987 it was proposed that this be based on the invoices of the different transactions, whereas in 1989

it was proposed that this compensation be also based on aggregate EU trade and consumption data.

b) 1996 commission proposal

This proposal broadly coincides with the previous ones. Now, however, a greater uniformity of the bases and the rates of the tax throughout the different EU countries is advocated in order to achieve a symmetric treatment for trade and to facilitate the compensation mechanism. This mechanism would include a clearing house which would centralize VAT collection and from which the redistribution would be made in accordance with aggregate data on national consumption. One of the requirements of this proposal is the intensification of cooperation between administrations and the harmonization of norms of control and collection.

The main drawback of this proposal, apart from the adverse incentives explained in relation to the above proposals, is that the requirement of uniform tax rates, aimed at avoiding distortions when the origin principle is applied, comes at the expense of the degree of fiscal autonomy provided to the national administrations up to this point by VAT regulation.

The introduction of any of the Commission proposals implies a greater harmonization of VAT throughout the EU. In particular, it is necessary to harmonize the VAT base in order to extend the system of invoices to inter-Community transactions, as well harmonize the tax rates in order to simplify the compensation mechanism.

c) VIVAT

The proposal of Keen and Smith (1996, 2000) requires a simpler compensation mechanism due to the fact that the common or supranational VAT is the same for the set

of EU countries. It is sufficient to have a multilateral compensation to compensate for possible collection deficits caused by intra-Community transactions, which are taxed at the same rate at all times.

d) CVAT

The proposal by McClure (2000) also consists of a dual VAT, where the present heterogeneity of tax rates can be maintained for domestic operations, while intra-Community sales would be subject to a common CVAT for all EU countries.

e) Dual VAT

Bird and Gendron (1998, 2000 y 2001) propose a system similar to that of the Canadian province of Quebec: a central VAT which allows a certain degree fiscal autonomy to this regional autonomy. The system operates in a similar way to the present provisional regime (and does not overcome the drawbacks associated with the interruption of the tax chain). Its advantage is that the common supranational VAT would act as a mechanism for controlling fraud in intra-Community transactions, as well that associated with each country's own VAT.

f) Prepaid destination VAT

Vanistendael (1995) proposes that buyers in intra-Community transactions be taxed according to the tax rates prevailing in their country of residence. It follows that the tax authorities in each country would be obliged to immediately transfer the revenue collected from these transactions to the administrations of the countries of residence of the buyers.

Genser (2003) carries out a comparison of the six proposals above with the present provisional regime in terms of five objectives which he considers the new EU VAT regime should aim towards achieving (table 14):

Table 14. Coordination Requirement of VAT Proposals in the EU Single Market

	Harmonized VAT base	Harmonized VAT rate(s)	Harmonized revenue-sharing mechanism	Harmonized VAT control
Transitional VAT regime (since 1993)	No	No	No	Yes (zero-rating, tax fraud)
Draft directives 1987/89	Yes	No	Yes	Yes (undersupply of control effort)
1996 VAT proposal (Commission 1996)	Yes	Yes	Yes	Yes (undersupply of control effort)
VIVAT (Keen and Smith)	Yes	Partial (supra national VAT rate)	Low	Low (small clearing volume)
CVAT (McLure)	Yes	Partial (VAT on cross border trade)	Low	Yes (undersupply of control effort)
Dual VAT (Bird and Gendron)	No	Partial (supra national VAT rate)	No	Yes (zero-rating, tax fraud)
Prepaid destination VAT (Vanistendael)	Yes	No	Yes	Yes (undersupply of control effort)

Source: Genser (2003)

- 1) it should permit a certain degree of fiscal autonomy at national level with regard to the establishment of tax rates.
- 2) it should incorporate incentives for efficient tax management in the control of invoices on the part of the administrations involved.
- 3) it should avoid breaking the tax chain in the internal market.

- 4) it should bring with it a symmetric treatment of trade in the whole of EU territory, such that transactions between different EU countries should be treated identically to those carried out within a single country.
- 5) the revenue collected should be allocated on the basis of consumption made in each country.

Genser (2003), while recognizing that any evaluation of these alternatives depends on the relative importance attributed to the objectives, notes that VIVAT scores comparatively higher than the other options.

The second comparison made by Genser (2003) is aimed at evaluating the various alternatives on the basis of the degree of coordination or harmonization of national policies their introduction would require. Greater coordination and harmonization of national policies amounts to a loss of fiscal autonomy for member states. The harmonization of the VAT base is a requirement of all the proposals except Dual VAT, where national VAT bases may be different from the common or supranational VAT.

Regarding the harmonization of rates, this is necessary only for the supranational VAT in the cases of VIVAT, Dual VAT and CVAT.

As far as collection and compensation mechanisms are concerned, the coordination and administration needs corresponding to each alternative are directly proportional to the volume of tax revenue which has to be redistributed. The requirements of VIVAT and CVAT in this sense are limited as bilateral disequilibria tend to offset each other to a large extent, while any remaining collection deficits are compensated on a multilateral basis.

In short, the provisional regime, as Genser (2003) states, has obvious virtues but is capable of improvement. However, it will always have the essential characteristics of a zero rate for intra-Community transactions and asymmetry. Therefore, either the Commission should revise its goals (and abandon symmetry and the abolition of a zero rate in order to implement in a credible manner a reform of the provisional regime) or it should continue supporting both elements. If it chooses the latter, VIVAT will probably be backed at the expense of the provisional regime, as long form of VAT superior to VIVAT appears.

In regard with excise taxes it is to be expected that in next years we will see a growing interest. Cnossen (2005)²⁷ observes a greater academic attention paid to this issue lately, which might have been brought about for three reasons. In the first place, the greater awareness about environmental problems, such as the greenhouse effect of gases emissions or acid rain, has developed an expanding literature on the economic mechanisms, such as excises, that help to internalize the externalities caused by polluting activities. In the second place, the recognition of the health problems caused by smoking has prompted worldwide campaigns against tobacco consumption, which include an increase in tobacco excises. In the third place, this author calls to attention to the difficulties arising in the taxation of capital income due to greater capital mobility, as well as to the disincentive effects of high taxes on labour supply and demand, which has led governments to make a wider use of excise taxes to raise more revenues.

Conclusions

The 1978 Fiscal Reform and the later introduction of the VAT in 1986 completely transformed indirect taxation in Spain. In a short space of time indirect taxation in Spain

went from having a traditional structure to a modern one more in line with its European peers. This transformation basically came about through the introduction of a modern VAT and the substitution of traditional “fiscal monopolies” by also modern excise taxes.

The future role of indirect taxation in Spain will be conditioned by both the process of tax harmonization within the single market within the EU, as well as the way in which it will be used in financing regional and local authorities (Autonomous Communities and Local Corporations). In this context, it is worth highlighting that VAT is applied in a very complex fashion in the majority of European countries and that it has been the object of a multitude of special schemes²⁸. This situation, along with the successive extensions of the provisional regime, is a serious obstacle to tax harmonization and for the implementation of the origin-country principle. At this point it should also be noted that any advances in the area of indirect taxation with regard to the harmonization of national legislation and/or tax rates will entail, at minimum, a rise in the fiscal pressure of these taxes in Spain

VIVAT appears to be one of the plausible alternatives for a radical future change in the VAT structure in the hypothetical situation of surpassing the provisional regime. In the longer term, and if the present provisional regime is consolidated in the European Union, the introduction of some of the VAT alternative such as Dual VAT, CVAT or VIVAT could be considered.

With regard to the financing of regional and local authorities, it would appear likely that any future legislative changes will bring about, on one hand, an elevation of the tax rates or an increment of the participation percentages in the collection of the indirect taxation and, on the other, the creation of new specific taxes on the consumption of

alcohol and tobacco, to the likeness of the tax retailers have to pay on the sales of hydrocarbons..

In relation to the incidence of this type of taxation, Spain is no different at present from its peers. Consumption tax as a whole maintains its predictably regressive character, although VAT, as a result of the application of the differentiated tax rates, is considerably less so than excise taxes as a whole.

In terms of their share of GDP, the relative importance of consumption taxes in Spain has risen from 6 percent to 10.2 percent over the period 1965-2001. Consumption taxes of a general nature rose from 3.3 percent to 6 percent of GDP, whereas excise taxes rose from 2.7 percent to only 3.3 percent. From 1965 to 1980, the share of GDP of both these tax categories remained relatively stable with a tendency towards convergence. From 1980 up to the last major reform of indirect taxation in 1986, the contribution of both groups rose strongly (as occurred with the other taxes), especially that of taxes of a general character (which rose from 2.3 percent to 5.3 percent of GDP over this period). From 1986, and in line with what occurred in the other developed countries, the contribution of these tax groups diverged somewhat. Revenues from the general taxes rose from 5.3 percent to 6 percent of GDP as a result of the introduction of VAT, while excise tax revenues fell from 4.25 percent to 3.3 percent of GDP.

Despite the above, and as a consequence of the fact that the share of GDP of the remainder of public revenue grew much faster than that of consumption taxes, the share of the latter in tax revenue as a whole fell significantly. Goods and services taxes fell from representing 40 percent of public revenue in 1965 to 20 percent in 1980; those of a general character fell by almost twelve percentage points in these terms over this period

(22.21 percent to 10.61 percent) while excise taxes fell by over eleven points (from 18.42 percent to 7.38 percent in 1979). Since the beginning of the 1980s, the relative importance excise taxes have stabilized, maintaining a share of fiscal revenue of around 10 percent, whereas that of the general tax has risen strongly in importance, especially since the introduction of the VAT.

At present, and with the exception of Switzerland, Spain is the European member of the OECD for which the share of GDP of this set of taxes is the lowest, although the distance from other members has been reduced significantly over the last twenty-five years. With respect to the share of these taxes in total tax revenue, the Spanish figure of 28.8 percent is now close to the European average. More specifically, regarding VAT, the average contribution of this tax in European OECD countries was 7 percent of GDP in 2001, whereas the figure for Spain was 6 percent. The share the VAT represents in total public revenue in Spain, at over 17 percent, is similar to the current European average. For Luxembourg, Switzerland, Japan and Norway, the estimated effective VAT rates are close to the nominal rates, although in most cases the range varies from 60 percent to 80 percent. For Spain, the efficacy of the tax in these terms is not very high.

If we focus on excise taxation, we can observe that as a percentage of GDP Spain has converged towards its peers: the figure for Spain rose from 2.7 percent of GDP in 1965 to 3.3 percent in 2001 whereas the OECD average fell from 5.8 percent to 4 percent over the same period.

Appendix

The importance of VAT and the structure of the Excise Taxes since 1986.

In the following tables and figures we detail the evolution of consumption taxes in Spain since the introduction of VAT and accession to the EC in relation to tax revenues net of Social Security returns.

We consider the tax-take as the sum of revenues corresponding to Chapters I and II of the State Budget (*Presupuestos Generales del Estado*) with the exception of Social Security payments for basic pensions. With regard to excise taxes, we distinguish, from 1993 on, between excise duties on manufacturing and the Excise Tax on Certain Means of Transport. We provide individual information for each tax, with the exception of the Intermediate Products Tax: this became a tax in its own right from 1993 but is still collected jointly with the Tax on Alcohol and Derived Drinks, so we do not treat it separately in the interest of maintaining the homogeneity of our comparisons.

With this same aim of making comparisons between homogeneous values, the tax-take from the Hydrocarbons Tax and the Petroleum Monopoly Income are reported jointly. The Hydrocarbons Tax had been gradually replacing the Monopoly Income up until June 1990. In that month, the State stopped selling petroleum products which came under the Monopoly and hence such tax revenue was no longer generated (with the exception of quantities pending from previous years). The table includes the revenues from Monopoly Income imputable to each year.

Table A1. Evolution of Tax Revenues in Spain (millions of Euros)

	1986	1988	1990	1991	1992	1993	1994	1995	1996
DIRECT TAXES	12,780.2	20,861.3	29,631.8	32,882.2	35,538.3	35,429.4	36,107.8	39,047.2	40,067.3
INDIRECT TAXES	16,720.30	25,872.70	26,898.50	25,930.80	29,141.80	27,118.50	30,907.90	32,838.30	35,191.80
- VAT (*)	9,728.90	12,642.40	15,129.10	16,255.70	18,872.40	16,670.50	19,201.50	20,308.00	21,899.10
- Excise Taxes	4,825.30	10,311.90	9,189.60	7,975.60	8,715.50	9,566.20	10,810.40	11,502.60	12,404.40
Hydrocarbons									
(1)	3,868.20	8,979.60	7,498.10	6,225.00	6,673.20	6,719.60	7,293.50	7,745.40	8,216.20
Manufactured									
Tobacco (2)	713	844.3	1,122.70	1,189.10	1,447.20	1,591.50	2,048.00	2,292.30	2,687.70
Alcohol and									
Derived Drinks (3)	197.4	411.3	481.5	476.1	510.7	416.8	529.4	546.9	624.4
Beer	46.7	76.7	87.3	85.4	84.4	140.5	179.8	190.3	199
Electricity	---	---	---	---	---	---	---	---	---
Tax on Certain									
Means of Transport	---	---	---	---	---	697.8	759.7	727.7	677.1
- Foreign Trade	1,311.30	2,308.00	2,020.30	1,741.20	1,254.00	594.5	566.5	730.7	581
- Other Indirect Taxes	854.80	610.4	559.5	-41.7	299.9	287.3	329.5	297	307.3
TAX REVENUE	29,500.50	46,734.00	56,530.30	58,813.00	64,680.10	62,547.90	67,015.70	71,885.50	75,259.10

Table A1. Evolution of Tax Revenues in Spain (millions of Euros) (Continued)

	1997	1998	1999	2000	2001	2002	2003	2004 pto
DIRECT TAXES	46,770.4	44,229.7	46,350.0	50,757.0	54,598.0	67,173.0	69,367.0	75,384.0
INDIRECT TAXES	37,601.40	42,154.00	47,776.20	51,267.30	53,187.90	56,204.00	59,602.00	62,982.00
- VAT (*)	24,052.6	26,253.7	30,733.8	33,394.5	34,697.9	36,913.0	40,579.0	42,874.0
- Excise Taxes	12,439.60	14,380.8	15,428.9	16,056.9	16,611.3	17,330.0	16,854.0	17,758.0
Hydrocarbons (1)	7,922.7	8,399.9	8,946.8	9,077.8	9,243.9	9,505.0	9,790.0	10,164.0
Manufactured Tobacco (2)	3,014.3	3,679.7	3,811.5	4,186.2	4,513.2	4,919.0	5,243.0	5,672.0
Alcohol and Derived Drinks (3)	582.6	710.0	734.9	771.7	795.2	817.0	833.0	887.0
Beer	163.6	177.7	181.1	193.1	197.4	208.0	229.0	228.0
Electricity	---	505.3	598.4	648.9	657.9	692.0	759.0	807.0
Tax on Certain Means of Transport	756.4	908.2	1,156.20	1,179.20	1,203.70	1,189		
- Foreign Trade	660.3	800.1	865.7	967.2	956.8	923.0	1,020.0	
- Other Indirect Taxes	448.9	719.4	747.8	848.7	921.9	1,038.0	1,149.0	2,350.0
TAX REVENUE	84,371.80	86,383.70	94,126.20	102,024.30	107,785.90	123,377.00	128,969.00	138,366.00

Notes:

(*) Includes the former General Tax on Company Trading (I.G.Tráfico Empresas) and the Luxuries Tax (Impuesto sobre el Lujo).

(1) Includes the Petroleum Monopoly Income.

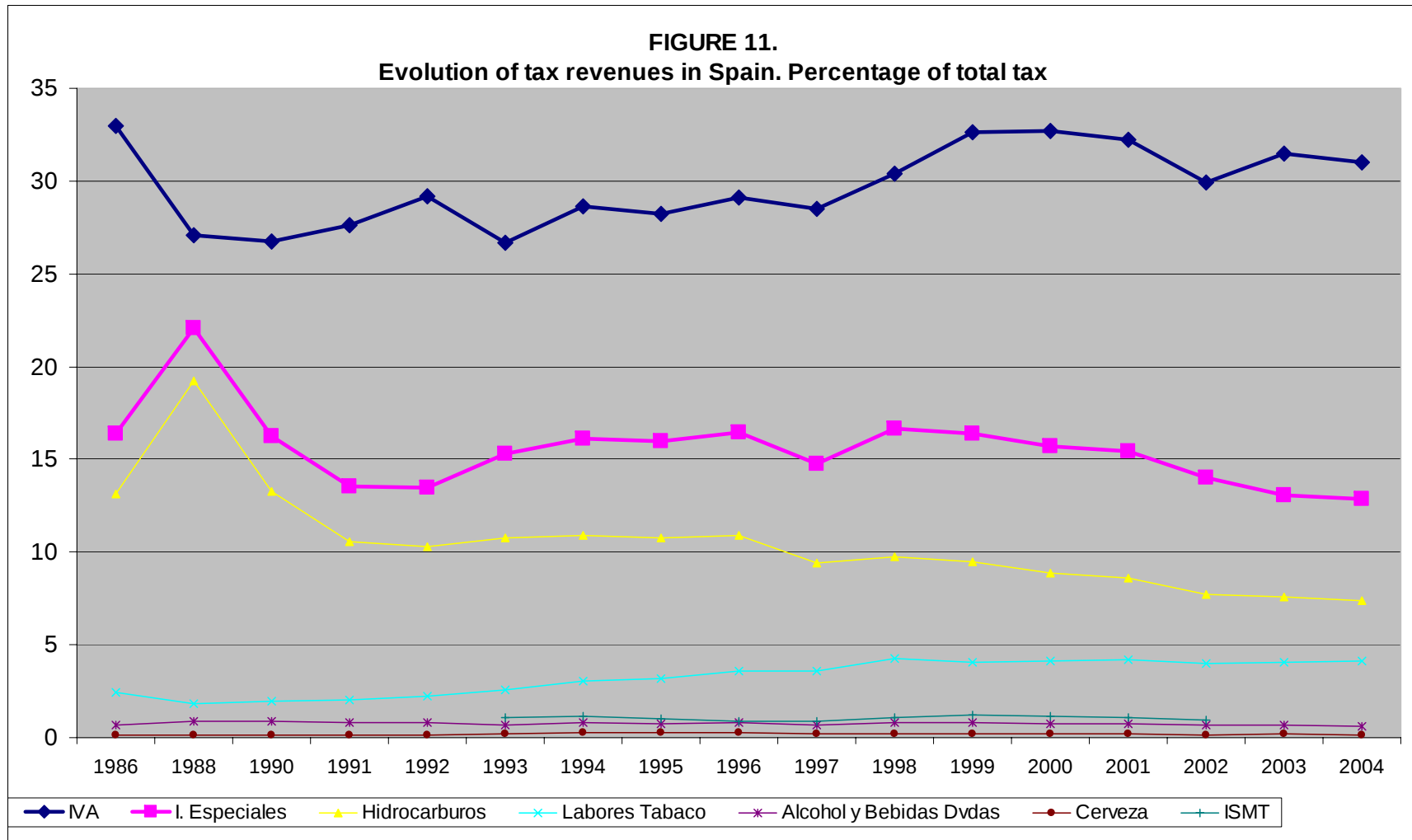
(2) Includes 44.054 million euro from Tobacco Tax in año 1986.

(3) From 1993, this includes payments corresponding to the Tax on Intermediate Products (Impuesto sobre Productos Intermedios).

Source: AEAT: “Estudio sobre los impuestos especiales (2001)” and “Informe Anual de Recaudación Tributaria 2003” for the years 1999-2003. “Presupuestos Generales del Estado. 2004” for this year.

Table A2. Evolution of Tax Revenue in Spain (Percentage of Total Tax) (Continued)

[illegible]



Tables A.1. and A.2. show that from 1986 to the beginning of the present decade indirect taxes have decreased from 55 percent to 45 percent as a share of the total public revenues under consideration. It can be seen in Figure 11 that VAT shows an upward trend, except for the decreases in 1993 and 2001-2002, and accounts for 31 percent of total revenue. The decreasing weight of indirect taxes as a whole can be basically explained by the decline in the tax-take relating to external trade (which fell from 5 percent of the total to less than 1 percent) and general decline in excise taxes (which went from over 16 percent during the 1990s to less than 13 percent at present).

The Hydrocarbons Tax has traditionally been the most important of the excise taxes, and the decline in the importance of this tax goes a long towards explaining the reduced importance of Excise Taxes as a whole. The Hydrocarbons Tax accounted for 7.59 percent of the total tax-take in 2003, whereas it accounted for over 13 percent in 1886. Second in importance among the excise taxes is The Tax on Manufactured Tobacco, whose share rose steadily up to 1998 when it reached its maximum of 4.26 percent of total tax revenue compared with a percentage of only 1.81 percent in 1988.

The Tax on Certain Means of Transport is third among the excise taxes with revenues corresponding to almost 1 percent of the total in 2002. The revenue from Alcohol and Derived Drinks and Intermediate Products represents 0.65 percent of the total over recent years. Finally, the revenue from the Electricity Tax, which was incorporated into the excise taxes in 1998, represented 0.59 percent of the total in 2003, well above that obtained by the Beer Tax, which holds last place among the excise taxes.

Table A.3. offers a breakdown of the State tax-take from VAT from 1999. This permits us to differentiate between revenues corresponding to internal transactions, on

one hand, and those relating to imports and transactions assimilated under imports on the other, as well as to identify the volume of refunds and the discrepancies with respect to the budgeted figures.

Table A3. VAT: Evolution of Revenues (millions of Euros)

	1999	2000	2001	2002	2003
Budgeted	28,890	33,987	36,194	37,017	39,181
Tax revenues	30,735	33,389	34,673	36,913	40,579
Imports	7,972	10,196	10,683	10,724	11,594
Internal transactions	22,763	23,193	23,990	26,189	28,985
Returns	9,693	12,437	14,701	16,004	18,537
Gross revenue	40,427	45,826	49,374	52,917	59,117
Departure from Budget	1,845	-598	-1,521	-104	1,398
Percentage of budget execution (%)	106.4	98.2	95.8	99.7	103.6

Source: AEAT

It can be seen that VAT on imports and assimilated transactions, which accounted for 26 percent of VAT returns during the 1990s, has risen since the year 2000 to account for over 30 percent of VAT. The VAT on transactions assimilated to imports, for which disaggregated data are available only from 1996, reached 5,083.7 million euros in 2001, representing 47.5 percent of import tax revenue and 14.7 percent of the total net VAT take compared with figures of 40.8 percent and 10.2 percent respectively in 1996.

With regard to possible discrepancies between the actual and budgeted VAT takes, it has generally been the case that the former has been higher than the latter, as occurred in 1999 and 2003, although in the years 2000 and 2002 the tax-take was below the budgeted amount. With the information provided by the annual VAT declarations, the State Tax Collection Agency (*Agencia Estatal de Administración Tributaria*, AEAT) publishes

statistics on this tax on its web-page (AEAT, 2003). The data available from 1997 to 2002 indicate that the weighted-average effective rate calculated from tax declarations fell from 11.4 percent in 1997 to 10.7 percent in 2002. Over this period, the average rate rose in only one year, and fell in the rest, implying that there was an average annual reduction of 1.3 percent. This source also indicates that the aggregate tax base of VAT rose by an average of 9.5 percent.

In a recent study, González-Calbert and Frutos-Vivar (2004) attempt to explain the reasons why VAT revenue rose at an annual rate of 9.1 percent over the period 1995-2003, which was much higher than the 6.8 percent average growth of GDP. As changes in tax regulations do not appear to explain this growth, attention is focused on the aggregate tax base of VAT from a macroeconomic point of view. In particular, they consider this base to comprise three fundamental components: household expenditure on final internal consumption, expenditure on the purchase of housing, and expenditure by public administrations.

From the analysis carried out, the authors highlight the important role played by housing in explaining the growth in the tax-take, given that expenditure on new housing multiplied by a factor of 3.4 over the eight-year period considered whereas expenditure on internal consumption rose by a factor of 1.6. They estimate that 35 percent of the growth of VAT fiscal pressure can be explained by the relative growth of the prices of housing compared to those of GDP as a whole. The authors also argue that the growth in the effective rate of VAT, an average of 1.4 percent, can be explained by the fact that the tax base and the tax-take from VAT are pro-cyclical in nature, so that there exists a crowding-out effect whereby consumption of necessity goods (which are generally taxed

at reduced rates) is displaced by consumption of goods taxed at standard rates. This crowding-out effect is intensified in periods of high economic growth. Data on consumption, disaggregated by products, from the National Accounts confirm this phenomenon, showing that in the latter half of the 1990s there was a significant shift in consumption from food products to other goods and services such as automobiles and telephone services.

Tables A.4. and A.5. show a breakdown of the recent evolution in the census of VAT declarers, obtained from the aforementioned source²⁹ (AEAT, 2003). In 2003, 2,815,770 declarations were made by companies and organisms from all economic sectors. This represented an increase of 85,000 from the previous year and continues the trend from the years before. The most numerous collective of declarers comprises those under the general deduction scheme (52.23 percent of the total), although its relative weight has been declining due to the growing importance of those subject to reduced rates. By economic sectors, the greatest number of declarers come from construction and property services (34.75 percent of the total), followed by the retail trade sector (15.72 percent), with the first of these being by far the most dynamic. On a territorial basis, and excluding taxpayers who declare exclusively to the territorial administrations of the Basque Country and Navarra, the greatest number of declarers are from Catalonia (21.7 percent), Andalusia (15.5 percent) and Madrid (15.1 percent).

Table A4. Number of VAT Declarers. 1999-2002

	Simplified scheme	Reduced rates	Special deduction	General deduction	Total
1999	362,109	693,253	25,933	1,484,049	2,565,344
2000	360,102	762,867	27,941	1,491,453	2,642,363
2001	365,407	808,119	30,694	1,525,625	2,729,845
2002	371,866	940,656	33,239	1,470,009	2,815,770
BIG COMPANIES					
1999	-	6,415	2,076	7,963	16,454
2000	-	7,222	2,288	8,993	18,503
2001	-	8,090	2,416	10,135	20,641
2002	-	8,978	2,616	11,177	22,771
SMALL COMPANIES					
1999	362,109	686,838	23,857	1,476,086	2,548,890
2000	360,102	755,645	25,653	1,482,460	2,623,860
2001	365,407	800,029	28,278	1,515,490	2,709,204
2002	371,866	931,678	30,623	1,458,832	2,792,999

Note: (*) Grandes Empresas: volumen de facturación anual superior a 6.010.121,04 € (1.000 millones de ptas)

Source: AEAT (2003).

Table A5. Number of VAT Declarers by Sectors. 1999-2002

	1999	2000	2001	2002	%
TOTAL	2,565,344	2,642,363	2,729,845	2,815,770	100.00
ENERGÍA Y AGUA	3,822	4,045	4,211	4,215	0.15
INDUSTRIA	227,495	229,551	231,327	231,686	8.23
CONSTRUCCIÓN Y S. INMOB.	860,758	895,219	950,588	978,428	34.75
COMERCIO	416,586	424,661	434,160	442,562	15.72
TRANSPORTE Y COMUNIC.	197,039	196,582	197,406	198,754	7.06
HOSTELERÍA Y RESTAURACION	241,161	242,797	245,754	249,372	8.86
ENT. FINANCIERAS Y ASEGUR.	10,592	10,931	11,569	11,901	0.42
SERVICIOS A LAS EMPRESAS	232,081	246,372	262,234	275,631	9.79
ENSEÑANZA Y SANIDAD	30,413	31,916	30,367	31,728	1.13
OTROS	345,397	360,289	362,229	391,493	13.90
Number of VAT declarers by CCAA. 1999-2002					
TOTAL	2,565,344	2,642,363	2,729,845	2,815,770	100.0
ANDALUCIA	385,900	401,102	417,792	435,681	15.5
ARAGÓN	100,023	101,242	103,433	105,675	3.8
BALEARES	83,525	87,115	90,764	93,509	3.3
CANTABRIA	35,051	35,996	37,013	38,247	1.4
CASTILLA - LA MANCHA	109,334	112,701	116,030	120,130	4.3
CASTILLA Y LEÓN	173,770	176,969	179,267	181,785	6.5
CATALUÑA	559,899	575,093	593,822	611,988	21.7
EXTREMADURA	56,817	58,789	60,317	62,067	2.2
GALICIA	188,778	193,716	196,887	200,734	7.1
LA RIOJA	22,963	23,491	24,156	24,850	0.9
MADRID	382,131	393,615	410,778	424,842	15.1
R. MURCIA	72,609	75,794	79,218	82,713	2.9
C. VALENCIANA	320,174	330,665	342,729	355,098	12.6
P. ASTURIAS	71,960	73,572	74,831	75,553	2.7
T. FORALES	700	707	749	755	0.0
RESTO	1,710	1,796	2,059	2,143	0.1

Source: AEAT 2003

Notes

1. This was the name given to the tax which was charged on the value of all movable goods and real estate which were sold or exchanged. The alcabala appeared during the middle ages (there are references which date back to the reign of Alfonso X) as a local tax. It was generalized during the epoch of Alfonso XI (1342), although it was of a temporary character and limited to 5%. During the time of the Trastámara dynasty (1369) it became permanent and was raised to 10% of the value of merchandise, although the Crown was unable to prevent the nobility from appropriating it in many of the feudal estates. The Court of Cádiz abolished the alcabala along with many other indirect taxes, but it did not disappear completely until the fiscal reform of Mon (1845). In America, the tax was not charged during the early period of the conquest but the needs of the Treasury brought about its gradual imposition. It was first charged in Mexico in 1574, and limited to 2%. In the following years it was extended to New Galicia and Guatemala and in 1591 to the Viceroyalty of Peru. Finally, it should be noted that the Castilian alcabala was not strictly a sales tax in the sense that we understand it today, rather a tax on all sales in that it was applied not only to the exercise of an economic activity (acts of commerce) as we now perceive it but also to incidental and isolated sales (civil acts) and the sale of real estate. Stretching the imagination a little, we thus see the beginnings of future real estate VAT.
2. Given that goods which are inputs in productive processes are taxed under the IGTE both when they are sold as well as when they are incorporated into the final sale price of other good of which they form part, the IGTE can be considered as a cascading tax on goods until the final stage of consumption. This gives rise to a non-uniform and arbitrary distribution of the tax burden in relation to the price of finished goods and impedes the correct determination of compensating taxes on imports and fiscal reductions on exports. This in turn gave rise to fiscal adjustments at frontiers which were of a non-neutral character. In effect, the compensating tax rates applied were generally higher than the tax burden suffered by equivalent national goods, while the fiscal deductions on exports were generally higher than the tax burden implicit from the price of goods which were exported. Thus, the frontier tax adjustments made in Spain were incorrect and the compensating tax could be considered to some extent as a tariff while the tax deductions on exports could be partly considered as a subsidy to exporting sectors.
3. These two measures had the objective of preparing the way for the introduction of VAT, where exports were exempt and where a special regime was foreseen for the purchase of natural resource products.
4. The resources obtained from petroleum products were channelled through three concepts: the gains from the Petroleum Monopoly Income; excise taxes on petroleum products (excise tax on petroleum and derivative products, created by the law of March 17th, 1932) and luxury taxes on high-grade fuel gasoline and the gains from shares of the State-owned company CAMPSA. The gains from Petroleum Monopoly Income were included in the excise taxes, thereby increasing fiscal transparency and preparing the way for the future elimination of this monopoly.
5. While in the case of tobacco a monopoly existed, the tax was entirely articulated through the luxuries tax.
6. The immediate consequence of Law 30/1985 was the repeal of the IGTE and the Luxuries Tax.
7. Later to become the Tax on Production, Services and Imports (Impuesto sobre la Producción, los servicios y la importación) from 1997 on due to Law 13/1996.
8. There shall be deemed intermediate products those with an alcoholic degree over 1,2° and under 22°, and not subject to tax on beer or tax on wine and fermented beverages.
9. The system previous to the implement of VAT used the country of destination principle by means of the *Desgravación Fiscal a la Exportación* (DFE; tax credit for exports) and the *Impuesto de Compensación de Gravámenes* (ICGI; compensation of inner levies tax). In general and for each item in the tariff of costumes, the compensation rate established the amount to pay for the imports so that they carry the same fiscal burden as the goods and services produced internally. On the other hand, the rate of the tax credit to the exports sought to alleviate the internal fiscal burden incorporated in their price. This system implied the coincidence between the rates of the tax credit for exports and the compensation of inner levies tax. Nevertheless, there were a fair amount of exceptions to before mentioned rule, which respond to political economy reasons. So, the different rates of the tax credit might be considered as mean values for each economic sector. In some cases the rate of the tax credit could be higher than that resulting from the cascade turnover tax, which meant an implicit subsidy to the exports and a penalization to the imports.
10. Vid. Bird and Gendron (1998, 2000 and 2001).
11. Piffano (2003), after analyzing the advantages and disadvantages of the various forms of VAT which can be used in a multi-level government context, recommends the option of combining a national VAT with another decentralized VAT applicable to retail sales.
12. For a more detailed analysis of the role that consumption taxes could play in regional financing in Spain, see Sánchez Maldonado and Gómez Sala (1995, 1996a, 1996b and 1999).
13. A different index is elaborated for each of the taxes according to the territorial distribution of respective consumption.
14. Law 51/2002 and Legislative Royal Decree 2/2004, 5th March, which passed the recast text (*texto refundido*) of the Law on the Regulation of Local Finance.
15. The Central Government has not explicitly revealed how these respective percentage shares are calculated.
16. Of the fifteen considered countries seven apply the type zero instead of the exemptions, to allow the deduction of the IVA supported in the acquisitions. Vid. European Commission (2003).
17. The Commission is aware that this demands major efforts and progress to be made on the issue of coordinating statistics.
18. The VAT Committee debates issues related to the application of the common VAT regime. Normally the results of these debates are put together to form guidelines. However, the VAT Committee is not empowered to make these guidelines binding. In this setting, in 1977 the Commission presented a proposal to modify the statute of the VAT Committee. However, the Council did not come to an agreement on this matter and it is unlikely that significant progress be made in the near future. Indeed, the

adoption of application measures in the area of taxation, in accordance with established procedure, remains the main obstacle to the adoption of this proposal. A modification of the Treaty is the only way a new impulse could be given to this subject.

19. Vid. European Commission (2003) y (2004).
20. Among these are Perona (1972), Pérez Morales (1974) and Lagares (1975). See also Argimón, González-Páramo and Salas (1987).
21. See González-Páramo and Salas (1991), Avellaneda (1998), Briones, Estrada and Hernando (1993), Manresa et al. (1996), Mayo (1995) and Serrano Mancilla (2003).
22. The apparently contradictory fact that the rates estimated for expenditure are lower than those for income is due to the fact that in the Family Budget Survey (EPF - *Encuesta de Presupuestos Familiares*) many social groups tend to underdeclare their income but have no such problems when it comes to declaring their expenditure. According to Ruiz-Castillo and Sastre (1998), over 60% of households report higher expenditures than revenues. This concurs with the work of Sanz (1996) on the 1990-91 EPF according to which EPF incomes are undervalued by some 40% when aggregate incomes are compared with the comparable total from the National Accounts.
23. In 1992 the normal VAT rate rose from 12% to 13% (Law 31/1991) and in August of that same year (Royal Decree 5/1992 and Law 28/1992) to 15%. From 1995 it was 16%. On the other hand, the higher VAT rate, which was 33% from 1986 to 1991 and 28% in 1992, disappeared in 1993 (Law 37/1992) and the Tax on Certain Means of Transport was introduced so that vehicles were now taxed by VAT at the normal rate and by the new tax (Law 38/1992 on Excise taxes). The super-reduced rate came into force on the 1st of January, 1993. In 1993 and 1994 it was 3%, and from the 1st of January of 1995 it was 4%. The reduced rate was 6% from 1986 to 1994 and 7% from the 1st of January 1995.
24. In the case of small enterprises, it seems clear that size alone does not appear to be a relevant issue with regard to the appropriateness or not of being subject to VAT, except in those cases where the smaller average size of taxed firms would lead to a situation where collection costs would be higher than those generated by other types of tax.
25. On this issue see Huizinga (2001).
26. We base this section on the work of Genser (2003).
27. Cnossen (ed.) (2005) examines carefully the characteristics and particularities of modern excise taxes on tobacco, drinking, game, pollution and driving.
28. In Spain, apart from the general regime there are seven special value added tax regimes: 1. Simplified regime. 2. Special regime for agriculture, livestock and fisheries. 3. Special regime for used goods, objects of art, antiquities and collectors' items. 4. Special regime applicable to operations with investment gold. 5. Special regime for travel agencies. 6. Special regime for the equivalent surcharge.

The simplified regime is applied under certain conditions to physical persons and entities who are attributed as rent earners under the regime of the Income Tax on Physical Persons (IRPF). Its objective is to determine the amount of VAT to be paid or the equivalent surcharge. Thus, it does not follow the general criterion of collecting the difference between VAT charged and paid.

The special regime for agriculture, livestock and fisheries applies to the owners of holdings in these categories, unless they opt to remain outside the regime, provided they comply with certain requirements. It functions in a different way from the general regime as the taxpayers are reimbursed by the Treasury at the standard rate (for operations outside the territory where VAT is applied) or by the receiver of the goods or services.

The special regime for used goods, objects of art, antiquities and collectors' items is applied on a voluntary basis to resellers of these goods. Regarding the special regime for travel agencies, this is obligatory for operations carried out by the travel agencies when they act in their name with respect to travellers and use goods or services of other firms or professionals in the operation of the trip.

Finally, the special regime of the equivalent surcharge is obligatory and is applied to firms dedicated to retail trade. The taxpayers subject to this regime charge VAT at the corresponding rate, and make VAT payments that they are charged plus a special surcharge. Thus they do not make VAT declarations, except in very particular cases, as it is supposed that the VAT quota they should pay is precisely the special surcharge which their supplier has charged them. The administrative burden on these firms is therefore reduced.

29. The transactions of subjects who declare exclusively to the Territorial Administrations of the Basque Country and Navarra are not included. Similarly, it should be noted that although VAT regulations excludes taxable persons under certain special schemes (Special Scheme for Agriculture and Fisheries and the Special Compensatory Charge Scheme) from the obligation of declaring and settling taxes, this does not imply that the transactions carried out by these collectives are excluded from the VAT statistics elaborated by the AEAT in relation to these collectives. On the contrary, the transactions carried out within the ambit of the Special Scheme for Agriculture and Fisheries are incorporated in the statistics through the compensations carried out by those who acquire the products corresponding to this scheme. The activities of retail traders carried out under the Special Compensatory Charge Scheme are incorporated through the increments and VAT instalments arising from the delivery of goods by taxable wholesalers to those taxable persons covered by the Special Scheme. These are declared in their annual reports along with any other transactions.

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