Trends in the fiscal policy in the countries of Central and Eastern Europe: taxation of enterprise income

Taxation systems in place in CEE are far from theoretically effective models. The current direct tax system in CEE countries comprises in fact diversified national tax systems. / Income taxes encumbering enterprises do not prevail in the tax revenue structure of CEE countries. / Fiscal instruments encouraging enterprises to undertake innovative activities, purchase or develop new technologies have been to a various extent applied by CEE countries. / Convergence research indicates that in times of crises income tax systems in CEE countries were usually becoming similar to each other.

The study analyses income tax solutions functioning in the CEE countries for almost 30 years. During this long period the factors that clearly left their stamps on the tax systems of Central and Eastern Europe countries included: various paths of transformation, reforms of public finance systems, EU membership and the necessity to harmonize taxes, the financial crisis, international capital mobility, international tax competition, pressure of fiscal and short-term needs of state budgets. All the surveyed countries carried out tax reforms in order to adjust their tax legislation to their current stage of social and economic development. The current system of direct taxation in the CEE countries is basically a range of diversified national tax systems. It is worth to pay attention to:

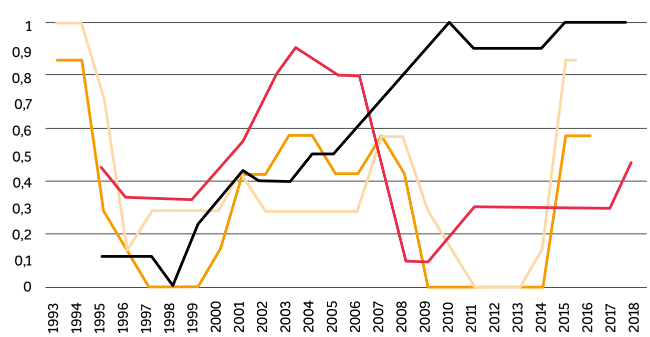
1) different basic taxation rules: taxation of profit (income) versus taxation of profits paid to owners (Estonian system, Latvian system);
2) diversified relations between balance sheet law and tax law (relation between tax income and balance sheet profit, permanent differences, temporary differences);
3) adoption of different rules concerning the revenue/tax expenses generation point: accrual basis versus cash basis accounting;
4) adoption of diversified rules of calculation of tax base (e.g. definition of tax-deductible expenses, scope of exclusions, transfer pricing adjustments, deductions).

Due to the above-mentioned reasons, bare comparison of tax systems in the form of juxtaposition of selected structural elements of tax, such as tax rates, lists of revenues or tax expenses, cannot produce reliable conclusions. Whether the direct taxation system had been subject to a convergence process was established in a comprehensive manner, based on, among others, data clustering algorithms, time series similarity measures using hidden Markov models, and most of all expert analysis of data available for each country covered by the study. A key part of statistical analyses was based on the relation of tax revenue from some types of tax to GDP, or total tax revenue.

Convergence research indicates that in times of crisis countries become similar to each other in respect of direct taxes as a percentage of GDP or corporate income tax as a percentage of GDP or as a percentage of total tax revenue. The only exception are personal income taxes, which differentiate the analysed countries compared to the reference country (Latvia), thereby generating processes of group divergence.

Despite numerous differences in taxation policies of CEE countries, reflected by our original method of classification of countries, a range of regularities can be observed. First of all, taxation systems in place are far from theoretically effective models. Major pillars of the taxation systems of the analysed countries are, apart from turnover tax, corporate income tax and personal income tax. However, they do not prevail in the tax revenue structures of the CEE countries. A positive feature was the fact that most of these countries reduced tax burden of income tax. The process of tax burden reduction should however be perceived in the context of not only stimulation of global tax competition, but also exploration of taxation rate adjusted to long-term economic growth. We should also mention some tax incentives that could

FIGURE 1. Pace of convergence for CEE countries covered by the research



Direct tax as % of GDP.

Personal income tax or household income tax, including tax on gains on property as % of GDP.

Corporate income tax as % of GDP.

Corporate income tax as % of tax revenue.

Source: own study by SGH Warsaw School of Economics support R&D activities. For the innovation imperative as a condition of economic growth is so obvious that it is perceived almost as a tenet of contemporary economics.

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TAXES AND COVID-19 (I)

CEE countries introduced some changes in their income taxation systems due to the coronavirus pandemic. Let us list solutions applied in Poland that affect the volume of tax base. A possibility of back-settlement of a tax loss was introduced. Under some conditions entrepreneurs will be able to deduct tax loss incurred in 2020 from their revenue earned in 2019. They can also use tax allowance for donations granted for counteracting COVID-19, deduct from their income R&D expenses aimed at developing products necessary to control the coronavirus epidemic. Enterprises manufacturing goods connected with combating COVID-19 can include one-off depreciation expense in tax expenses. Other solutions include: a possibility to resign from simplified advance tax payments in 2020 for small taxpayers, resignation from charging extension fee, resignation from penalties for delay in filing PIT declaration for 2019.