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TAX EXPENDITURES: SPENDING THROUGH THE POLISH TAX SYSTEM

Summary: The subject of this article is the presentation of tax expenditures as a type of public spending recognized as the off budget expenditures, as well as indicating their influence on Polish budget. This aim was proved in the way of comparative studies of theoretical concepts of tax expenditures and solutions applied in the countries reporting them. Tax expenditures strictly related to particular economic and social policy goals, are special tax provisions which partly or absolutely reduce tax burden of some groups of taxpayers, and in the result – diminish the tax revenue appropriately. The focus on these privileges arisen on the base of tax code is highly important in the current budgetary conditions while the huge part of countries is struggling with imbalances of public finance, and increasing public debts. The overall value of estimated tax expenditures in Poland amounted to 81.6 billion PLN in 2012. Comparing this value to the general government deficit in 2012 of 62.7 billion PLN, the scope of public spending realized out of budget procedure is clearly evident. In 2009-2012 the share of tax expenditures in total public spending amounted on average by 18.3%, and the adequate loss of government revenues was estimated at 26.1% of total tax revenue. Unfortunately this not always transparent part of public spending is out of public control and effectively limits the ability of proper and responsible fiscal policy.

Keywords: fiscal imbalance, fiscal policy, Polish tax system, tax expenditures, transparent fiscal policy.

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1. Introduction

The deepening public debt, and its serious budget consequences, is one of the key issues of modern public finances. The tendency for excessive deficits, and thus the rise of the public debt, increases with the number of politicians using the same common resources as an implementation of the policies of each of their departments requires expenditures which exceed the optimal level for society as a whole. However, this spending is not always apparent or transparent, because it is not realized in the form of “traditional” direct budget expenditure. The policymakers eagerly use the indirect

spending taking advantage of the lack of procedure appropriate direct expenditures, allowing them in the “back-door” way, outside of the budget process, and out of any other control.

Depending on the specific budgets of individual countries, an expenditure classified as off-budget includes a variety of financial transactions. They can be broadly defined as transfers of public resources which do not result directly from the provisions of the budget act. It is assumed that a common feature of off-budget expenditures is that they are in contradiction to the principle of transparency and unity of the budget. Indirect spending, effectively avoiding reporting and control, can be also realized by special tax provisions resulting in lower tax burden. In the literature they are classified as tax expenditures.

Tax expenditures like direct expenditures are an equivalent form of public funds spent by the government on individuals. They are, however, more selective since they could be directed to narrow groups of taxpayers. At the same time, by reducing the fiscal burden of selected entities, tax expenditures decrease tax revenues of the budget. Unfortunately, this may in consequence result in the need to reduce the pool of public goods provided by the government, or increase the tax burden on society as a whole.

While examining current tax systems it can be noted that the use of tax expenditures is becoming more popular, both in terms of quantity and value. This applies to all taxes, although income taxes in particular. The share of tax expenditures in GDP in different countries is very diverse, ranging e.g. from 12.5% of GDP in the United Kingdom (2008) to 0.64% of GDP in Germany (2008) [OECD 2010]. Given these values, it is clear that the use of tax expenditures in the tax system can be costly. At the same time, this often implicit part of public spending seems to be getting out of control and increasing the fiscal imbalance. This is of particular importance in times of crisis, under conditions of limited ability to raise government revenue and rising public debt.

The aim of this paper is to present the nature of tax expenditures as a form of hidden public spending, and to show the budgetary consequences of their use in Poland. Detailed statistical analyses are based on reports of Polish Ministry of Finance, budget execution reports, and OECD data. This article has been written under the project financed by National Science Centre, research grant no. DEC-2011/01/B/HS4/02878¹.

2. Tax expenditures versus direct expenditures

The Organisation for Economic Co-operation and Development (OECD) and the World Bank both define tax expenditures as a part of the tax structure which is

¹ The article was prepared on the basis of the paper presented at The Congress on Economy, Finance and Business, Bangkok, 6-8 November 2013.

divergent from general tax code provisions or benchmark, resulting in benefits for the limited group of activities or individual taxpayers. In other words, a tax expenditure is variously understood as a departure from “the norm”, where a given country’s tax system is universally accepted as the basis for defining benchmark tax. Because of the diversity of particular national tax systems, tax expenditures definitions differ from one jurisdiction to another, which hampers their cross-country comparisons.

Tax expenditures may take the form of various tax constructions. Usually such standard tax constructions, as: allowances, exemptions (as well as exclusions) and rate reliefs are related to tax expenditures. If we consider what tax measures should be exactly classified as tax expenditures, there is no simple answer. In practice, regarding wide diversity of tax systems, there are a lot of different tax constructions falling within the one broad definition in particular jurisdictions, and therefore constituting tax expenditures.

Stanley S. Surrey [Surrey 1973] is considered to be the progenitor of the tax expenditures concept. He was a professor of law at Harvard University and served as Assistant Secretary of the Treasury for Tax Policy under President Kennedy (from 1961 to 1969). Surrey prepared a list of special deductions and exemptions in the U.S. income tax, and was the first to use the phrase “tax expenditure” to describe them². The use of term was not accidental. His intention was to emphasize the similarity of certain deductions, exemptions or exclusions to direct expenditures, because they are both targeted on achieving the same particular spending goals – social, economic or political ones. Furthermore he noticed that the majority of tax reliefs and exemptions is a permanent part of the tax system – they are of general nature, depend on a taxpayer’s personal or economic situation (e.g. number of children, level of income, health condition, etc.) and do not serve any specific purpose. At the same time the nature of tax expenditures is entirely different. Tax expenditures “(...) often called tax incentives or tax subsidies, are departures from the normal tax structure and are designed to favor a particular industry, activity, or class of persons. They take many forms, such as permanent exclusions of income, deductions, deferrals of tax liabilities, credits against tax, or special rates. Whatever their form, these departures from the normative tax structure represent government spending for favored activities or groups, effected through the tax system rather than through direct grants, loans, or other forms of government assistance” [Surrey, McDaniel 1985, p. 3]. Surrey asserts that tax expenditures only occur in specific circumstances and apply exclusively to particular groups of taxpayers, supporting their specific activities, so they take the form of financial aid.

Surrey strongly emphasized, however, that not all preferential tax constructions like tax reliefs or exemptions could be classified as tax expenditures. Some of them

² Surrey presented his idea in public in 1967, although he had probably dealt with this issue earlier. In 1953, he published an article titled “Our Schizophrenic Income Tax”, which criticizes the “technical” way to escape from the income tax, enabling a reduction in the tax burden of the wealthiest taxpayers, but also diminishing tax revenue.

comprise the normal tax structure and realize general purposes, so that cannot be treated as indirect spending targeted at achieving particular economic and social goals of certain taxpayer groups [Dziemianowicz, Wyszowski, Budlewska 2014].

Tax expenditures are unquestionably related to tax construction. The other side of the coin is their relation with budget. They are a functional equivalent of direct public spending, and furthermore, they can replace them. One cannot forget that using particular tax mechanism – in fact, recognized as tax expenditures – results in lower revenues of government. Therefore, already in the 1960s Surrey stressed the need of controlling them.

Current tax systems are believed to face the challenge of the growing use of tax expenditures, both in terms of number and value. This tendency is observed in all taxes, although income taxes are a category of tax with the most significant growth of tax expenditures. Politicians take advantage of the opportunity of tax expenditures eagerly, which raises a query: Why are tax expenditures an object of such interest to policymakers?

The tax expenditure concept is entirely based on the simple assumption that from the taxpayer's point of view there is no significant difference between direct expenditures and spending through particular tax reliefs system (which basically results in foregone tax revenue). Tax expenditures are the various instruments resulting in a reduction of the tax burden and enabling informal subsidizing of certain taxable objects or entities. Particular social and economic objectives can be therefore achieved either through government programs financed directly by tax revenues or through the implementation of special preferences into a tax system (see Tab. 1).

Table 1. Public expenditure classification

Type of expenditure	Definition	Transparency
Direct expenditure	Traditional way of public spending, which is a direct transfer of public resources to beneficiaries	Value of transfers is the integral part of the budget act; spending is realized in the scrutiny of rigorous law provisions
Tax expenditure	Special preferential tax structures which reduce tax liability of selected taxpayers to pursue certain social and economic policy objectives	Special provisions in a tax law, usually disclosed in annual reports (only in several countries), generally there is no legal obligation of reporting

Source: own study.

Despite the above-mentioned issues, it cannot be simply assumed that the use of tax expenditures as an alternative to direct expenditures is undesirable. In certain circumstances, tax expenditures can be as effective as the less expensive mechanism of public spending programs. One must bear in mind, however, that they could unfavorably affect such areas as:

- Integrity and simplicity of the tax system (tax expenditures may make the tax system more difficult).
- Income redistribution through taxes (taxpayers who produce relatively high income have the greatest benefits from tax expenditures, apart from those taxpayers who do not have a taxable income and do not gain any advantages from tax expenditures).
- Effectiveness of public spending (tax expenditures are frequently introduced into the tax code as a result of pressure from particular groups of interest, so in the result policymakers do not take into account real costs of these spending compared to direct expenditures).
- Transparency and accountability of fiscal policy.

If it is assumed that tax expenditures and direct expenditures are equivalent forms of public spending, which means that both categories should be the subject of a common budget process. Moreover, they should be put under scrutiny and evaluation so as to decide which way of spending is more effective, and, what is particularly relevant, which can contribute to the better achievement of specific social and economic objectives. In order to make a well-founded review of tax expenditures, they should be first identified and made public.

Under the conditions of budgetary imbalances and limited ability to raise public revenues (e.g. by increasing taxes), monitoring of all public expenditures, including indirect spending realized outside the regular budget process, is particularly relevant. The budget as an annual plan of intended revenues and expenditures of the government should recognize all public expenditures regardless of their form. Only on this condition is it possible to ensure the identification, monitoring and control which facilitate the analysis of the state of public finances and the assessment of fiscal policy. Among the first steps taken in this regard are reports enclosed to the Budget Act or other budgetary documentation issued by particular governments. The need of public disclosure and tax expenditures monitoring in the budgetary process was emphasized by the International Monetary Fund (IMF) in a report from 1998: “Code of Good Practices on Fiscal Transparency”³ [IMF 2007]. The monitoring of public expenditure, including indirect spending, such as tax expenditures, will not only make it possible to better control them, but will also help compare spending programs and select the most effective ones. In this way it will be possible to answer the question whether direct expenditures are a more effective way of achieving the goals of social and economic policies than spending through the system of special tax exemptions, allowances and deductions. Obviously, the opposite could be the case.

³ The Code is a specific list of rules for a transparent fiscal policy. It reflects the practices applied by many countries, and aims to encourage public debate on fiscal policy and public accountability of the government in this area. The revised version of the Code was published in 2007. The IMF is not the only institution which draw attention to fiscal transparency. In 2001 the OECD published the document “Best Practices for Budget Transparency” [OECD 2002], which states that transparency of fiscal policy is a fundamental element in the management of public finances.

Table 2. Size and fiscal effects of tax expenditures in selected OECD countries

Country	Fiscal year	Share of tax expenditures according to category (%):				
		GDP	total government tax and non-tax revenue	relevant tax revenue		
				income taxes	capital income taxation	VAT or sales tax
Canada	2004	6.94	44.37	52.97	6.32	52.38
Germany	2006	0.74	8.48	7.71	1.10	1.54
Netherlands	2006	2.00	5.15	9.60	0.00	9.74
Spain	2008	4.55	12.48	17.21	1.97	59.69
United Kingdom	2006	12.79	35.17	22.86	14.35	54.66
United States	2008	5.97	33.65	51.10	6.86	-

Source: [OECD 2010, pp. 224-227].

Unfortunately, in practice, budget statements of many countries fail to reflect a substantial part of indirect expenditures, as do other budget-related documents published by governments. From the politicians' point of view tax expenditures are a very comfortable solution which, in a sense, enables creative accounting, frequently misrepresenting the actual state of public finances. It must not be forgotten that taxes are the major source of revenues to governments, whereas tax expenditures mean lost budget revenue (see Tab. 2)⁴.

3. Tax expenditures in Polish tax system

In 2010 the Republic of Poland joined the group of countries which identify and estimate the value of tax expenditures⁵. In the first Polish report titled "Tax preferences in Poland", the Ministry of Finance has not adopted one comprehensive definition of special tax structures envisaged in the Polish tax system. Instead, it uses a set of certain characteristics. According to them tax expenditures (so-called "tax preferences") usually take different forms of tax deductions, exemptions, rate reliefs, deferrals or joint taxation of spouses, which result in a reduction of tax liability, and, consequently, are a substitute for direct spending. The process of tax expenditures identification by Polish Ministry of Finance follows the rules of the benchmark tax, based on several tax principles like the universality of taxation principle as well as the completeness and equity of taxation [Ministerstwo Finansów 2010].

⁴ While comparing tax expenditures values across the countries, one should remember that the estimates are quite approximate, and it is caused mainly by the lack of one comprehensive method of estimating. See: [OECD 2010; LeBlanc 2013].

⁵ The analysis of the Polish Ministry of Finance are based on the assumption regarding own definition of tax expenditures, which has been called "tax preferences".

If we compare this definition with other countries experience, it seems to be clear that the definition implemented in Poland is very wide. Hence, there are significantly more identified tax expenditures in Polish tax system (489 in 2010) than in the jurisdiction of other states (for example 391 in the United Kingdom, 140 in Spain, 98 in the Netherlands, and only 86 in Germany) [OECD 2010]. Of course, it is difficult to conclude whether the data are comparable, unless a detailed analysis of the benchmark tax system and tax structures of particular taxes used in those countries is performed. Nevertheless, the large number of tax expenditures in Poland clearly demonstrates the complexity of Polish tax code. Not only is this situation detrimental to the fiscal efficiency of taxes, but it also affects future state revenue.

The total of tax expenditures identified in the Polish tax system includes tax expenditures in state taxes (416 in 2010), and in local taxes (73 in the same year). The number of preferences in income taxes was 205 and the majority of them, i.e. 145, was the part of personal income tax. For value-added tax and excise duties these figures were 195 and 16 respectively.

The Polish Ministry of Finance has estimated tax expenditures on the base of most frequently used method, i.e. revenue forgone method. The value of tax expenditures was estimated with no regard for behavioral changes caused by the abolition of certain tax structures. The calculations were mainly based on data from tax returns and other tax forms available in the Ministry of Finance, as well as on data collected by the Main Statistical Office, and, in some cases, on information provided by other institutions. For example, in 2011, the value of 89 tax expenditures was not estimated (it means that 18% of all identified tax preferences was excluded from estimation). The scarcity of current data also prevented a microsimulation model that could help determine the value of all tax expenditures identified in the Polish tax system.

Based on available data, the overall value of Polish tax expenditures in 2012 amounted to 81.6 billion PLN, which constituted – similarly to 2011– 5.1% of GDP. Value of tax expenditures in the Polish tax system rose by 15.7 billion PLN since the first report of 2009. Estimated tax expenditures in state taxes amounted to 73.8 billion PLN, i.e. 4.6% of GDP, that is 29.7% of overall tax revenue in 2012. Preferences in value-added tax were the tax expenditures with the highest estimated value. The preferences accounted for 35.4% of the relevant tax revenue, whereas the figure for 43.0% of corporate income tax (see Fig. 1). As regards PIT, the indicator was 25.6% of total tax expenditures in 2012. This value was almost half the tax revenues from this category of tax (i.e. 47.5%). The share of tax expenditures for excise duties was the lowest and accounted for 2.1%. Relative to 2011, the total value of tax preferences rose by 3% (2.4 billion PLN). The greatest increase, by 3.4%, was recorded for value-added tax and amounted to 1.4 billion PLN, and for excise duties it grew by ca. 60% relative to 2011 (0.6 billion PLN). The nominal value of tax expenditures decreased slightly only in case of personal income tax, and it amounted to 0.3 billion PLN less than in 2011.

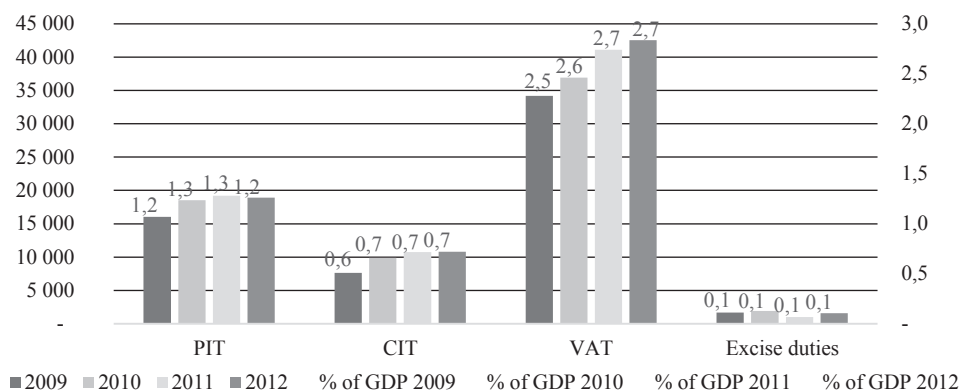


Figure 1. Tax expenditures in state taxes in Poland (million PLN, GDP %)

Source: own study based on the reports of the Polish Ministry of Finance.

The report distinguishes nine areas⁶ of tax support. In 2012, and similarly in previous years, the largest share of aid was extended in the form of family and social benefits – ca. 44.5% of all identified tax expenditures in the Polish tax system (accordingly 45.2% in 2011). In this field, tax aid amounted to ca. 36.3 billion PLN (i.e. 2.3% GDP). Most tax breaks in this group related to personal income tax (ca. 11.8 billion PLN). They principally included child tax allowances, joint assessment of spouses and social benefits exemption (Tab. 4). Most of these indirect transfers could easily be replaced with direct public programs, which should be more targeted and income related and thus available to the less well-off taxpayers. Unfortunately, tax expenditures in Poland are not the subject of comprehensive public control assessing their effectiveness or efficiency. However, such measures would definitely reduce the so-called “leaky bucket” effect, resulting from non-market redistribution. They would also increase the efficiency of public spending. In the research studies there is explicitly pointed out that the child allowance introduced in 2007, as the biggest tax expenditure in the personal income tax (Tab. 3) which has improved the financial situation of many families, has not made any significant difference to the welfare of the most disadvantaged social groups, as they are often unlikely to benefit from this kind of assistance [Horacio et al. 2009, pp. 91-114]. This is because the child allowance is non-refundable, which means that it cannot bring total payable tax below zero, and as a result cannot be used to obtain a refund. Thus it does not improve the situation of those persons whose income is so low that they do not have

⁶ 1) economy, 2) agriculture, 3) employment, 4) education, science, culture, sport, 5) public benefit organizations, churches, social and civic organizations, 6) health, 7) family and social assistance, 8) transport and environment protection, 9) others (this category includes such expenditures which cannot be attributed to other categories).

an income tax liability or pay very little tax. Other taxpayers are not able to use the full amount of relief, which in turn leads to the exclusion from the tax subsidization of low-income people who pay relatively low taxes, and to whom the child allowance was primarily directed.

Table 3. The value of selected tax expenditures in Polish personal income tax (2009-2012)

Tax expenditure	Value of tax expenditures (million PLN)				Share of tax expenditures within given tax (%)			
	2009	2010	2011	2012	2009	2010	2011	2012
Child allowance	5,633	5,684	5,740	5,699	35.2	30.6	29.9	30.1
Joint taxation of couples	2,693	2,880	2,979	3,067	16.8	15.5	15.5	16.2
Agricultural subsidies	1,947	2,008	2,334	1,715	12.2	10.8	12.1	9.1
Exemption of family benefits	1,478	1,557	1,625	1,582	9.2	8.4	8.5	8.4
Social benefits	*	820	813	871	–	4.4	4.2	4.6

Tax expenditure	Share of tax income (%)				GDP (%)			
	2009	2010	2011	2012	2009	2010	2011	2012
Child allowance	8.98	9.10	8.50	8.07	0.42	0.40	0.38	0.36
Joint taxation of couples	4.29	4.61	4.41	4.34	0.20	0.20	0.20	0.19
Agricultural subsidies	3.10	3.21	3.46	2.43	0.14	0.14	0.15	0.11
Exemption of family benefits	2.36	2.49	2.41	2.24	0.11	0.11	0.11	0.10
Social benefits	-	1.31	1.20	1.23	–	0.06	0.05	0.05

* data is not available.

Source: reports of the Polish Ministry of Finance.

According to data published by the Polish Ministry of Finance also economy and agriculture strongly benefited from tax preferences in 2012: ca. 13.5 billion PLN and ca. 6.1 billion PLN respectively. Regrettably, the report fails to address the question whether the expenses incurred within the above-mentioned areas were efficient and effective. It should also be noted that tax expenditure support for the agricultural sector is probably much higher than the report indicates. Due to unavailability of relevant data, the report has ignored the fact that income from agricultural activity is tax-exempt.

Among tax expenditures in corporate income tax, the most numerous are those which affect the financial condition of economic entities. In the reported years, the largest tax expenditure was related to the deductions for losses sustained in previous taxable years (2.6 billion PLN, i.e. 0.16% GDP). Despite the crisis the value of this preference significantly increased in 2009-2010 unlike in 2011-2012 when the financial condition of enterprises increased (reflected by the significant increase of public revenues collected via the corporate income tax). In 2012, the costly

preferential policy of tax exemption for special economic zones generated 1,596 million PLN revenue forgone for the Polish budget.

However, it is the consumption tax expenditures that constitute the largest part of revenue foregone by the Polish state. This includes the value-added tax. In 2012, the total value of given preferences was 42.5 billion PLN (2.66% of GDP), in comparison with 41.1 billion PLN in 2011 (2.76% of GDP). This kind of expenditure was related to preferential VAT tax rates (lower than the standard 23% rate). The largest amount of revenue was lost due to preferential tax rates for housing development services (e.g. construction, renovation or maintenance). The Ministry of Finance estimates that in 2012 those expenditures were 11.2 billion PLN, which accounted for around 15.2% of total tax expenditures in Poland. If we take into consideration preferential tax treatment of, among others, medicinal products (4.9 billion PLN in 2012), meat and dairy products (2.9 billion PLN), the overall amount of expenditure is as high as 19.0 billion PLN, i.e. a half of total identified expenditures in VAT. As a result, the state budget loses 1.18% of the annual GDP.

The other consumption tax, excise duties, generated far less tax expenditure: respectively 1.0-1.9 billion PLN in 2009-2012. The tax preferences applied mainly to reduced excise duty for biofuels, and – to a lesser extent – to support renewable energy and cogeneration. Due to the unsatisfactory effects of environmental tax incentives on the behavior of consumers and producers, the excise tax expenditures will probably be abolished.

Apart from central government tax expenditures, the report also discusses tax expenditures in local taxes (property tax, transport vehicles tax). In this case, preferential rates, exemptions or reliefs can be introduced by local self-government entities, which enjoy a degree of autonomy in terms of tax policy. In 2012, the overall value of local tax expenditures amounted to 7.8 billion PLN (0.49% GDP), whereas the year before it stood at 7.1 billion PLN. Following the decision by local authorities to introduce object exemptions, the 2012 tax revenue was reduced by 1.8 billion PLN. The budgets of territorial governments were principally affected by property tax expenditures (0.23% of GDP in 2012). The most substantial expenditures included, among other things: farm buildings exemption (0.93 billion PLN) and vacant and wooded land exemptions (1.25 billion PLN), which jointly added up to one third of local tax expenditure in 2012.

4. Fiscal consequences of tax expenditures in Poland

The economic and financial crisis had generated sharp increase in the general government deficit and debt in many countries, including the European Union Member States. In 2007-2013 in the euro area the average public debt increased from 66.3% to 92.6% in terms of GDP, whereas in the EU-27 from 59.0% to 87.1% respectively [Eurostat 2014]. The reasons were undoubtedly related with too expansionary fiscal policy, especially a strong bias of policymakers towards excessive deficits. Although

the average general government deficit in the EU-27 in 2013 fell to 3.3% of GDP (4.4% in 2011, and 6.5% in 2010) and in the euro area to 3.0% of GDP respectively (4.2% in 2011, and 6.2% in 2010), still in many European Union Member States it was higher than the reference value of 3%. The increase of the general government deficit and public debt did not spare Poland. In 2007-2013 the public debt in terms of GDP increased from 45% to 57.1% and approached dangerously the limit of 60% of GDP (this limit is the fiscal rule specified in the Polish Constitution), whereas the general government deficit in 2013 amounted to 4.3% of GDP (Fig. 2).

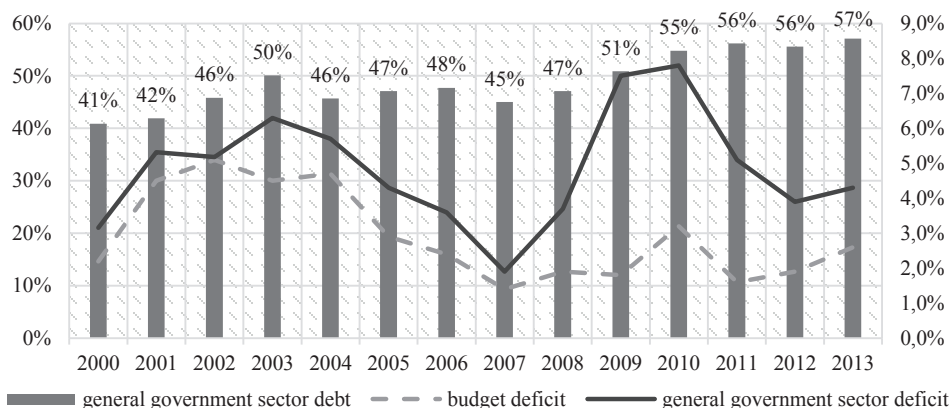


Figure 2. Budget deficit, general government sector deficit and general government sector debt in Poland in 2000-2013 (as % of GDP, current prices)

Source: own study based on Eurostat and the Polish Ministry of Finance data.

It should be noted that whereas the increase in deficit during the crisis is rather a natural phenomenon, it is also high in the years preceding a crisis. It indicates that the imbalance of Polish public finances is rather structural. The development of the general government balance ratio in history showed systematically excessive deficit. Moreover, in a period of very strong economic growth, general government deficit amounted to about 2% of GDP. However, since the mid-90s deficit stood at an average of 4.7% of GDP, i.e. 3.7% over the Poland's medium-term objective (MTO) fixed at 1% of GDP [Ministerstwo Finansów 2012, p. 13]. At the same time, public expenditure significantly exceeded the value of public revenue in Poland. It raises a necessity for a detailed analysis of public spending, especially with regard to spending realized through the tax system, which subsidizes selected taxpayers and in the result diminishes tax revenues.

The share of tax expenditures in total public expenditure in Poland (both direct and indirect spending through the tax system) is significant (Fig. 3). In 2009-2012 it was from 16.65 to 18.84%. This means that almost one fifth of the expenditure was not visible in the state budget. This is not always an explicit part of public

spending and it is unfortunately getting out of public control, and hence increases the fiscal imbalance. At the same time, the Ministry of Finance does not provide detailed information on the beneficiaries of using these structures and does not know whether the goals of socio-economic policy in this case has actually been achieved. However, the cheaper and more effective solution for the realization of such objectives could be replacing tax expenditures with the direct ones. Unfortunately, there is no comprehensive analysis of the effectiveness and legitimacy of individual tax expenditures in the Polish tax system, so far. Furthermore, tax expenditure reports do not encourage politicians to take any decisions to reform or simplify the tax system.

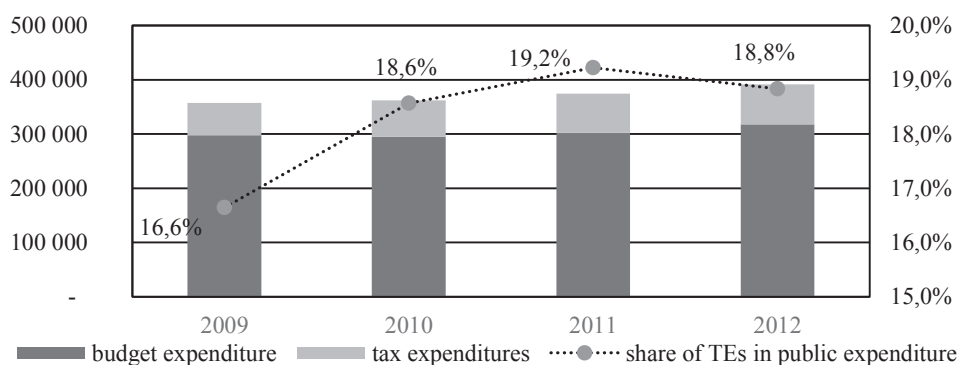


Figure 3. The share of tax expenditures in the total budget expenditure in Poland (million PLN)

Source: own study based on the Polish Ministry of Finance data.

Moreover, the use of preferential tax structures in tax system affects the value of tax revenue in Poland, reducing it considerably (Fig. 4). Tax expenditures in 2012 constituted 29.7% of tax revenue of state taxes, which is the major source of budget revenue in Poland, whereas this indicator accounted for 13.0% of local taxes accordingly. The share of tax expenditures in individual taxes is presented in Table 4. The preferences in the personal income taxes generated the highest losses as the consequence of tax expenditures and accounted for ca. 50% of revenue from the given tax. For corporate income tax it was the indicator of over 43% and 35% for value-added tax respectively. Basing on above-mentioned analysis it can be concluded that the loss of tax revenue as the result of implementing special tax structures in particular taxes in Poland is very significant. However, the introduction of tax expenditures should be the result of comparative studies on different tools of public intervention. If tax expenditure realizes the policy objective better than other instruments, it should be introduced. Otherwise, it is reasonable to overview the catalogue of existing tax reliefs in order to assess the necessity of losing this huge part of public revenue, affecting significantly the fiscal imbalance in Poland.

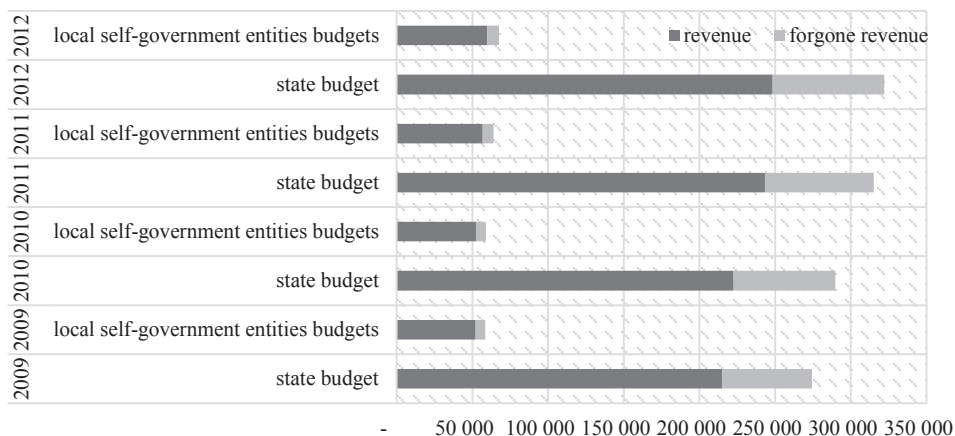


Figure 4. Theshare of tax expenditures in tax revenue in Poland (million PLN)

Source: own study based on the Polish Ministry of Finance data.

Table 4. The share of tax expenditures in relevant state taxes revenue in Poland (million PLN)

Tax	Category	2009	2010	2011	2012
PIT	Tax revenue	35,764	35,593	38,075	39,809
	Tax expenditures	16,015	18,552	19,213	18,904
	Share in state tax revenue	44,78%	52,12%	50,46%	47,49%
CIT	Tax revenue	24,157	21,770	24,862	25,146
	Tax expenditures	7,620	9,886	10,730	10,806
	Share in state tax revenue	31,54%	45,41%	43,16%	42,97%
VAT	Tax revenue	99,455	107,880	120,832	120,001
	Tax expenditures	34,192	36,902	41,112	42,512
	Share in state tax revenue	34,38%	34,21%	34,02%	35,43%
Exciseduties	Tax revenue	53,927	55,684	57,964	60,450
	Tax expenditures	1,690	1,901	986	1,573
	Share in state tax revenue	3,13%	3,41%	1,70%	2,60%

Source: own study based on the Polish Ministry of Finance data.

Tax expenditures estimated by the Polish Ministry of Finance greatly exceeded the value of state budget deficit in 2009-2012 (Fig. 5). In the last two years, the value of forgone revenue was almost three times higher than the budget deficit. However, it should be noted that these estimates could not be explained straightforward in

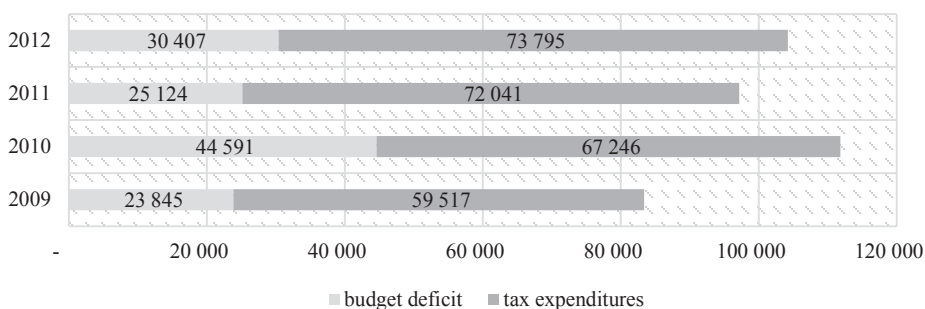


Figure 5. Deficit and tax expenditures in Poland in 2009-2012 (million PLN)

Source: own study based on reports of the Polish Ministry of Finance.

this way. The revenue of the state budget or local budgets increased approximately by the amount of forgone revenue in the situation the tax structures constituting tax expenditures had been abolished. As noted previously, the method of estimation based on revenue forgone does not take into account changes in the taxpayers' behavior and therefore it could be deceptive. However, the extent of tax expenditures identified in the Polish tax system, means that an in-depth analysis that will answer the question: whether direct spending would be more effective than spending realized through the special system of tax allowances, exclusions and deductions, should be immediately started. Furthermore, it is particularly necessary to immediately begin reforming and simplifying the tax system, which can lead to a reduction in individual tax rates for all taxpayers, not just selected beneficiaries of the tax privileges.

5. Conclusions

Tax expenditures should be considered as a specific substitute of budget expenditures. Their identification and analysis are therefore an essential element of shaping a transparent fiscal policy, enabling not only the in-depth scrutiny and control of all public expenditures and hence improving the efficiency of public finances. The following studies prove that the estimation and evaluation has not been so far part of the budget procedure in Poland. Taking into account the requirements of the Code of Good Practices on Fiscal Transparency, as well as the OECD recommendations for the transparent budget proceeding, however, it is worth considering whether the Polish procedures should not be changed. In an ideal fiscal system, all tax preferences should be properly "balanced" in the process of preparing the budget so as compared with alternative ways of financing them. Full integration of tax expenditures with the budget will undoubtedly enhance fiscal discipline and enable seeking for more effective programs, which is of particular importance in terms of limited public funds.

The first step to ensure improvement in transparency of fiscal policy in this area, are reports which have been prepared by the Polish Ministry of Finance for four years. The reports include quite detailed information about the scope of tax expenditures in the Polish tax system, and therefore show the extent of the problem. It has been confirmed clearly that the use of tax expenditures in Poland is very costly. The total value of tax expenditures in Poland in 2012 amounted to 81.6 billion PLN, about 26.1% of overall tax revenues (state and local taxes) and 5.1% of GDP. At the same time, tax expenditures made up ca. 19% of total public spending – this means spending which refers to “hidden” side of the budget expenditure which successfully avoid public control. It should be clear that the reports are just the first step to ensure compliance with the transparency standards and hence it is necessary to enhance fiscal discipline. It indeed provides the possibility to observe the hidden side of public spending. Apart from that other tools that contribute to the greater efficiency of public expenditures should be improved.

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TAX EXPENDITURES: WYDATKI POPRZEZ POLSKI SYSTEM PODATKOWY

Streszczenie: Przedmiotem artykułu jest problematyka wydatków dokonywanych przez system podatkowy, tzw. *tax expenditures*. Celem pracy jest analiza konsekwencji fiskalnych realizacji tej kategorii wydatków poza procedurą budżetową, w tym wskazanie ich wpływu na polski budżet państwa. *Tax expenditures* są wydatkami, które wynikają z zastosowania specyficznych ulg podatkowych, dzięki którym obciążenia podatkowe określonej grupy podatników są niższe niż według ogólnych zasad. W rezultacie *tax expenditures* powodują zmniejszenie dochodów budżetu państwa. *Tax expenditures* są dokonywane poza budżetem (tzw. *off-budget expenditures*), co skutecznie uniemożliwia jakąkolwiek kontrolę. Problem ten jest szczególnie istotny z punktu widzenia bieżącej kondycji sektora finansów publicznych, gdyż wiele państw boryka się z nierównowagą fiskalną, przejawiającą się m.in. ciągle rosnącym zadłużeniem. Przeprowadzone badania potwierdziły, że zakres *tax expenditures* w polskim systemie podatkowym jest niezwykle istotny z punktu widzenia stanu finansów publicznych w Polsce. Autorzy dokonali przeglądu doświadczeń międzynarodowych w państwach i instytucjach publikujących raporty *tax expenditures*, a następnie, czerpiąc z dobrych praktyk, przeprowadzili analizę wartości tej kategorii wydatków z punktu widzenia konsekwencji budżetowych. W rezultacie określono łączną wartość *tax expenditures* w Polsce (2012 roku), która wyniosła 81,6 mld zł, co znacznie przekracza wysokość deficytu polskiego sektora finansów publicznych w 2012 roku (62,7 mld zł). Utracone dochody budżetowe tytułem funkcjonujących *tax expenditures*, niepodlegające publicznej kontroli i procesowi budżetowemu, wyniosły blisko 26,5% (2012 rok), co potwierdza, że brak przejrzystości tej kategorii wydatków publicznych skutecznie ogranicza możliwość prowadzenia odpowiedzialnej polityki fiskalnej.

Słowa kluczowe: nierównowaga fiskalna, polityka fiskalna, polski system podatkowy, *tax expenditures*, transparentna polityka fiskalna.