

Analysis of Economic Effects of VAT Transformation Reform

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Abstract: With the current changes in the international economic environment and the deepening of domestic economic development and reform, especially after China's accession to the WTO, the systemic flaws of the production-type value-added tax not deducting input tax on fixed assets have also gradually emerged, increasing from production-oriented value-added. The transition from tax to consumption-type VAT has become the internationally and domestically recognized VAT reform direction. The value-added tax reform can be said to affect the whole body. The transformation will inevitably bring significant impacts on society, the economy, and the people's lives on many levels. In this year, China's economy has gone out of the trough and turned into a local overheating and economic structural strategy. Under the special background of the critical period of adjustment, and China is currently in a period in which all tax systems need to be reformed as a whole, the significant impact of VAT reform on all levels of society has forced us to make more thoughts and studies. This article analyzes the economic effects of the VAT transformation and reform.

1. Introduction

VAT can be divided into production-type VAT, income-type VAT, and consumption-type VAT according to the different methods of processing outbound fixed assets. Since China officially introduced VAT in 1994, production-type VAT has been used. At that time, China was facing comprehensive factors such as inflation, overheated investment, and tight financial resources. It is for the above considerations that the input tax included in the purchase of fixed assets is not deductible. The production-type VAT with the widest tax base and the furthest distance from efficiency and fairness goals has been selected. Production value-added tax, in conjunction with other policy measures, has played an active role in effectively suppressing irrational investment, preventing increased inflation, ensuring sufficient fiscal funds, and expanding tax revenue. Today, the economic environment facing China has undergone major changes. The focus of macro-control is to expand domestic demand, continuously improve the overall competitiveness of the economy, and take the path of scientific development for sustainable development. Production value-added tax is no longer adapted to the needs of the development of the market economy, inhibiting the investment enthusiasm of enterprises, hindering the pace of industrial upgrading and the optimization of the industrial structure, causing imbalance in tax burden between different industries and regions, and its disadvantages are exposed. It is becoming more and more obvious that it has caused serious obstacles to economic development. Seriously deviate from the principle of VAT tax neutrality. Therefore, the transition from production-type VAT to consumption-type VAT is a must.

VAT transition is a major measure of China's tax reform in recent years. Since September 2004, the VAT transformation reform has been officially launched in the Northeast region. The consumption-based VAT in China has begun to be promoted from theory to practice and has achieved great results. Experience. The accumulation of years of experience in the reform of the VAT reform, the continuous increase in fiscal revenue, and the economic situation of the financial crisis have accelerated the introduction of a comprehensive VAT reform plan. From January 1, 2009, the full implementation of consumer-type VAT will be implemented nationwide. The transformation and reform of VAT is a systematic project, and the leverage effect is very obvious. As the capital city of Jinan City, Jinan City has a high level of economic development, especially

the secondary industry in Jinan City accounts for a large proportion of the overall economic structure, and the effect of the VAT transition is even more pronounced. It can be seen that since the transition of value-added tax, Jinan's overall economy, fiscal revenue, and corporate tax burden will be affected on many levels.

2. The Concept of VAT

VAT was first developed on the basis of the business tax system. Due to the increasingly detailed division of labor in industrial production, and the full taxation of multiple links of business tax, the more links in product production and circulation, the heavier the tax burden, which seriously hinders the development of socialization of production. After the end of World War I, Yale University professor T.S. Adams and German businessman Dr. Wilhelm von Siemens put forward the concept of value-added tax. Adams believes that gross profit is the sum of wages, rents, interest, and profits from a financial perspective, and it is the value-added portion of national income. Value-added should be used as the tax base for value added tax. It also proposes a simple calculation method for deducting the output tax from the output tax when the enterprise purchases goods. Siemens also proposed to replace the German sales tax at that time with a "smart sales tax" ¹. But their suggestions were not officially endorsed and supported initially. Until 1954, France took the lead in implementing VAT reform, and in 1968 expanded VAT from the industrial sector to agriculture, commerce, transportation, services and other industries, establishing the world's first systematic consumption-based VAT system. In the following decades, the European Economic Community has completed reforms of the value-added tax system. In the late 1970s, value-added tax was introduced in Asian countries, and a system was developed during development. Value-added tax itself is a turnover tax. In theory, value-added tax is a tax levied on the value added realized in the process of producing, selling goods or providing services. In actual calculations, all taxes included in the production materials (including fixed assets) purchased by the taxpayer for the production of taxable products or the provision of taxable services are deducted.

3. Background of the VAT Transition

As a system design, the VAT transformation reform is a long-term arrangement of systems and laws. It is global, strategic, and stable. Its fundamental purpose is to further optimize the tax system, create a good external institutional environment for market players, and promote a faster economy Better development. However, any degree design is carried out under certain socio-economic conditions. In order to fully implement the VAT transition, we must first examine China's social environment, macroeconomic development status, political system, fiscal and taxation system, and other reform measures during the VAT transition period in order to coordinate macroeconomic policies and provide reference for transition decisions.

The 1994 tax reform faced an urgent task of controlling inflation, which inevitably required the choice of production-type VAT. However, since the Asian financial crisis in 1997, domestic market demand has continued to be sluggish, and international market competition has become increasingly fierce. The Chinese government is faced with the problem of expanding demand and needs to work hard on investment, consumption and exports. Production value-added tax cannot deduct input tax on capital goods purchased by enterprises. The production cost is relatively high, and the final price of products or services is also high, which increases the tax burden on end consumers, further exacerbating shrinking market consumption and sluggish demand. However, during this period, China did not adopt such tax-cutting measures as switching from production-type value-added tax to consumption-type to stimulate domestic demand, because we are not only restricted by the permit of fiscal capacity, the lack of management methods, but also considering To VAT as an indirect tax, the transition may induce further declines in commodity prices and exacerbate deflation. At present, China's economy is in the rising stage of the economic cycle, and the tax reform has a relatively loose macroeconomic environment. At the same time, it is also an important period for the strategic adjustment of China's economic structure. Market competition is becoming increasingly fierce, and

enterprises have a very strong desire to update equipment, technological progress, and product upgrades. The choice of VAT transformation can well meet the above requirements.

However, as the national economy enters the fast lane, investment in urban infrastructure, real estate, metallurgy, non-ferrous metals and other industries is heating up, and private investment is growing rapidly. Especially in the second half of 2003, over-investment in some industries has occurred to some extent. In the face of the current macroeconomic situation of structural investment inflation, many scholars worry that if a comprehensive value-added tax transformation is implemented now, it will likely form a stimulating effect on inflation, exacerbate the excessive expansion of fixed asset investment, and affect the stability of the national economy. Sustainable development. Moreover, the tax reduction effect of pushing forward the reform of the value-added tax reform nationwide has been greater. With the same fiscal expenditure, it may cause an increase in the fiscal deficit, which is inconsistent with the goal of a sound fiscal policy.

However, we believe that the Chinese economy still belongs to the "dual economic development model of urban and rural areas" under the condition of "unlimited labor supply", and regional development is still very unbalanced. Consumer demand, especially rural residents, is still not strong, and economic development remains an investment-pull stage. The so-called overheating of the economy is also only a partial overheating of certain industries in certain regions, which is no longer comparable to the overheating of the overall economy in the early 1990s. Further analysis of the specific reasons for the current overheating of investment in China, real estate, steel, coal, machinery, and chemical industries are industries with a large increase in investment. Among these industries, the real estate industry does not levy VAT, and the VAT transition has no direct impact on it. Iron and steel, coal, machinery, chemical and other industries are bottleneck industries in the operation of the national economy, and are also industries that the country urgently needs to support and develop. Moreover, regardless of whether VAT is transformed, the price guidance and economies of scale generated by bottleneck industries are the main factors that determine the scale of investment. The VAT transition has limited incentives for investment in these industries.

Therefore, the focus of current macro-control is still to expand domestic demand, stimulate investment, and continuously improve the overall competitiveness of the economy; the goal of the tax reform is to further optimize the tax system, create a good external institutional environment for market players, enhance the vitality of economic players, and promote The economy develops faster and better. Therefore, how to implement the VAT transformation step by step to achieve the purpose of improving the investment structure and coordinating economic development is still of global and strategic significance.

4. The Impact of VAT Transition on National Fiscal Revenue

The starting point of the research on VAT transition is the assumption of tax policies for VAT transition. Based on the previous discussion of tax policies for VAT transformation and the experience of foreign countries, this paper proposes the following tax policy assumptions for incremental deductions of fixed assets: 1. Calculate the input tax amount at the applicable tax rate of 17%; 2. Scope of fixed asset deduction: The newly added fixed assets of the year are deductible for equipment, tools, and appliances, and the details are explained by the detailed rules. At the same time, the imported tax-free equipment and foreign-funded enterprises purchase domestic equipment and enjoy tax rebates for machinery and equipment. Production, unused, and unused machinery and equipment and obsolete used machinery and equipment are not deductible; 3. Fixed assets can be deducted only after they have been inspected and delivered for use. Considering that in the practice of fixed asset investment, the form of abnormal loss of fixed asset investment of enterprises is very complicated. If it is handled after deduction, a large amount of tax evasion will exist and it will not be easy to improve the efficiency of tax collection and management. Therefore, the provision of fixed assets can only be deducted after acceptance and delivery.

At the same time, setting up this clause is also conducive to promoting the construction process of fixed assets. In order to obtain the benefits of capital flow brought by the VAT deduction, enterprises will inevitably speed up the pace of production and construction and shorten the

construction cycle. In addition, the total deduction in the initial stage of the VAT transition is an important factor in the introduction of the VAT transition. The provision of a “fixed asset that must be deducted after acceptance and delivery for use can reduce the total deduction in the initial stage of the VAT transition.

Fixed assets include productive and non-productive equipment investment, non-productive equipment investment is not deducted according to regulations, and investment in equipment, tools, and appliances for small-scale VAT taxpayers and non-VAT taxpayers is not deducted, which will cause Reduction of VAT deduction tax base.

After the implementation of consumption-based value-added tax, the current reductions and exemptions for machinery and equipment (such as reductions on imported equipment) and reductions and exemptions for some intermediate products will be cancelled. In the above-mentioned calculation of the basic tax deduction process, the investment in such equipment has not been deducted, resulting in a reduction in the VAT deduction tax base. In addition, the transformation of VAT will promote corporate investment and bring economic growth, which will be conducive to the increase of government revenue.

Therefore, the impact of the VAT transition on fiscal revenue will actually be less than the data derived from the calculations above. Correctly treating the temporary reduction of income caused by the transition of VAT is the key to the smooth implementation of the VAT reform. We believe that the reduction of fiscal revenue brought by the transition is the price that must be paid to improve the tax system and promote the transition from government-led investment to enterprise-led investment. And there is still a lot of room for this cost. For the government, the VAT transition means a temporary reduction in tax revenue; for enterprises, the reduction in tax revenue is also the reduction of the corporate tax burden. The economic incentive effect brought by the transition dynamically brings the state's fiscal revenue. Rapid growth, offsetting the impact on fiscal revenue. The value-added tax transition should be viewed from a sustainable perspective. Rather than temporarily reduce fiscal revenue, we must also provide a powerful booster for the technological progress of our enterprises and enlarge the entire economic cake. Naturally, fiscal revenue will increase.

5. Economic Effects of VAT Transformation and Reform

5.1 Theoretical Analysis of the Economic Effects of VAT Transition on the Overall Economy

As production-type VAT is not allowed to deduct the taxes contained in fixed assets, the actual tax burden levels in different industries are different, which violates the principle of tax neutrality and is not conducive to the optimization and upgrading of industries and balanced development. The actual tax burden of industries with a high organic capital structure is greater than that of industries with a low organic capital structure, which inhibits enterprises from investing in high and new technology, making the development of originally lagging basic industries more lagging, and the overall level of development is low. Optimization is contradictory. The level of social development must make the industrial structure rise from a low level to a high level, which is embodied by the gradual evolution of the dominant proportion of labor-intensive industries of production factors towards the dominant proportion of capital-intensive and technology-intensive industries. The consumption-type value-added tax allows deduction of the input tax included in the current purchase of fixed assets. There is no double taxation problem, which is conducive to fair tax burdens, lower investment costs, increase investment profitability, shorten investment recovery periods, and objectively stimulate high and new technology. Industrial capital investment to achieve equipment and technology upgrades. It is of great significance to deal with the problems of irrational industrial structure, backward production technology, excess low-end products and lack of high-end products. Inflation has demand-driven, cost-driven, and structural inflation. From the perspective of economic activities that expand the scope of VAT deductions, price increases are mainly driven by costs rather than demand. By expanding the scope of deductions, corporate tax burdens have been reduced, and the ability to absorb the cost of raw material prices has been

increased accordingly. At the same time, promoting enterprises to speed up the upgrading of equipment will help reduce production costs, not only will not promote price increases, but will also ease the contradiction of rising prices. The pilot operation in the Northeast and Central regions shows that expanding the scope of the VAT deduction does not promote price increases, and reduces production costs, which is conducive to lowering the factory price of products. The impact of different VAT policies on import and export trade is different. In the import stage, if the foreign country adopts a complete tax refund policy, the imported products will not include any foreign turnover tax, and the full value tax on imported products is exactly equivalent to income-based value-added tax. If domestic consumption-based value-added tax is adopted, the tax burden on domestic products is lower than imported products, which is conducive to restricting imports and protecting domestic products. And if domestic production-type value-added tax is adopted, the tax burden on domestic goods will exceed that of imported goods, which is not conducive to protecting national industries. In the export sector, only consumer-type VAT can achieve a full tax refund, thereby enhancing the international competitiveness of domestic products. Production-type VAT cannot be fully refunded due to repeated taxation in multiple links, which weakens its competitiveness in the international market and is not conducive to exports. Therefore, the transition of value-added tax will increase the net export value, which is conducive to economic growth. This reform, while fully implementing consumer-type VAT, has eliminated the VAT exemption policy for imported equipment and the VAT refund policy for foreign-invested enterprises purchasing domestic equipment. Enjoy equal treatment in terms of reductions and exemptions, providing a platform for fair competition for Chinese and foreign companies. In the long run, with the optimization and adjustment of the industrial structure, it will inevitably play an important role in technological innovation, core competence improvement, and the high-end, brand and internationalization of products.

5.2 Theoretical Analysis of the Economic Effects of VAT Transition on Fiscal Revenue

It is an indisputable fact that the transformation of VAT will bring about a reduction in tax revenue and a reduction in corporate VAT burden. Urban maintenance and construction tax and education surcharge are based on VAT, so the reduction of VAT will inevitably lead to a reduction in urban maintenance and construction tax and education surcharge. Consumption value-added tax allows one-time deduction of input tax on fixed assets, so the original value of machinery and equipment no longer includes this part of value-added tax, annual depreciation will decrease, the corporate income tax base will increase, and corporate income tax will increase. However, the increase in corporate income tax is much smaller than the decrease in the first three taxes.

First of all, the input tax on fixed assets for equipment and industrial appliances is allowed to be deducted at one time, so that enterprises will no longer have to worry about double taxation when equipment is renewed, resulting in increased tax burdens. The marginal rate of return required for investment will be reduced, which will increase the enterprise Investable projects. The increase in investment brings about the absolute expansion of the production scale of the enterprise, thereby enabling the enterprise to obtain more income, which will lead to an increase in corporate income tax.

Secondly, the transformation and reform of value-added tax is conducive to promoting technological progress and promoting the transformation of economic growth models. Relying on the advantage of low labor prices, China has developed many labor-intensive industries and achieved a competitive advantage internationally. But as China's economy continues to grow, rising labor costs are inevitable, and some relatively developed regions are already facing the challenge of transforming their growth models. After the implementation of consumer-type value-added tax, the value of fixed assets such as purchased equipment and industrial appliances can be deducted. Enterprises can use this saved capital to improve production technology and labor productivity, bringing technological innovation and relative efficiency. Improve, promote the development of labor-intensive industries to technology-intensive industries, thereby urging the entire society to embark on the road of connotation and expansion of reproduction, and improve the organic

composition of capital in the entire society. This optimized transformation of the economic growth model can bring more fiscal revenue to the country. Thirdly, at present, the consumption demand of Chinese residents, especially rural residents, is still not strong. The increase in investment will stimulate the growth of domestic demand to a certain extent, start the "deflation" market, and thus promote the economic growth to a certain extent. Both taxes and income taxes increase.

Finally, due to the increase of enterprises' own investment, the national fiscal investment in social economy has been reduced, and naturally the financial expenditure for economic construction has been reduced, which is to increase net fiscal revenue from the negative side.

5.3 Theoretical Analysis of Economic Effects of VAT Transformation on Enterprises

Consumption, investment, and exports are the troika driving economic growth, so in the long run, production-type VAT is not conducive to economic development. This effect comes from the different tax deduction policies for fixed assets. Production-type VAT does not allow the deduction of input tax on fixed assets, which makes the investment cost relatively high, and the more the investment, the heavier the actual tax burden, which obviously inhibits investment and increases production costs, and consumption and exports are also indirectly affected. Negative Effects. This suppression is most pronounced in capital-intensive companies. Consumption-type VAT allows a one-time deduction of the input tax included in the current purchase of fixed assets. On the one hand, the company reduces cash payments in the short term, and the value-added tax paid by the company is reduced, saving more funds for the company to apply to other investments. On the other hand, the reduction in the cost of updating fixed assets can stimulate the capital investment of enterprises, improve the technical content of enterprise products, and improve the quality of company operations. But in the long run, in terms of investment entities, it actually increases the rate of return on investment, which will stimulate the expansion of investment to a certain extent, which is conducive to the formation of capital and stimulates economic growth. This is the direction of market economic system reform. Wang Honghai (2003) analyzed the cash flow of the VAT transition and concluded that the consumption-based VAT is larger than the NPV and IRR indicators under the production-based VAT, indicating that the consumption-based VAT is larger. The conclusion that investment VAT is more favorable than production.

The increase in corporate investment caused by the transformation may worsen the company's related financial indicators, such as asset-liability ratio, cash flow, etc., but in the coming years, with the gradual manifestation of investment effects, financial indicators may improve and give companies a competitive advantage. This issue can be recognized through the changes of the following financial indicators after the transformation.

In short, at a macro level, the VAT transition will bring about an expansion of aggregate social supply and an increase in aggregate demand to achieve economic development. From a meso-level perspective, the VAT transition will increase the input tax deduction in the short term, so that Fiscal revenue has decreased, but in the long run, the VAT transition will bring long-term economic growth, increase the tax base, and thus achieve long-term growth in fiscal revenue; from a micro perspective, the VAT transition will stimulate corporate fixed The growth of asset investment, guiding the optimization of the investment structure of enterprises, increasing the enthusiasm for investment, so that enterprises reduce the burden of taxation and the burden of raising funds, and then improve the quality and efficiency of business operations; in the end, these will have long-term and beneficial effects on economic and social development.

6. Conclusion

Correctly treating the temporary reduction of income caused by the transition of VAT is the key to the smooth implementation of the VAT reform. We believe that the reduction of fiscal revenue brought by the transition is the price that must be paid to improve the tax system and promote the transition from government-led investment to enterprise-led investment. Regarding this cost, both in theory and in the practice of the pilot project in Northeast China, there is still a lot of room for finance. For the government, the VAT transition means a temporary reduction in tax revenue: for

enterprises, it means a long-term reduction in tax burden, and the economic incentive effect brought by the transition offsets the impact on fiscal revenue in the long run. The value-added tax transition should be viewed from a sustainable perspective. Instead of temporarily reducing fiscal revenue, we must also provide a powerful booster for the technological progress of our enterprises and enlarge the entire economy. Naturally, fiscal revenue will increase.

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