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USE OF CORPORATE INCOME TAX IN ACHIEVING ECONOMIC GROWTH OBJECTIVES. THE CASE OF THE REPUBLIC OF MOLDOVA

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Abstract
The paper contains the author's analysis and research on using the corporate income tax for economic recovery after the post-crisis period. The case of the Republic of Moldova, which implemented a tax reform regarding the tax exemption on reinvested profit, is analyzed. The article aims to explore the effects of the reform from the perspective of the impact on economic growth and budget revenues. Following the analysis, solutions are proposed to improve the national tax system to contribute more to economic growth. The solutions aim to implement tax incentives better directed to the intended purpose and have a lower budgetary impact.

Keywords: *tax policy, economic growth, tax revenues, structure of the taxation system, corporate income tax, Accelerated Depreciation*

JEL Classification: *H21, H25 H26*

I. INTRODUCTION

The reduction in the economic growth rate due to the consequences caused by the COVID-19 pandemic and the war in Ukraine has brought to the fore discussions regarding the measures to be taken by Governments to relaunch economic activity. Also, the Government's efforts to mitigate the impact of the economic crisis, especially the increase in public spending on health and social protection components, resulted in increased budget deficits in most countries.

In such circumstances, to achieve the objectives of economic growth and consolidation of public finances, measures are required to make the fiscal policy more efficient on two dimensions:

- public expenses – carrying out the rationalization processes of public expenditures to reduce/reallocate inefficient expenses;
- revenue mobilization – increasing the efficiency of taxes and the tax base;
- the revision of the system of tax exemptions - from the perspective of increasing public revenues, as well as the implementation of well-targeted tax exemptions that stimulate companies to invest in assets and contribute to economic growth.

This article aims to analyze and propose tax solutions in the form of tax incentives that contribute to economic growth. Economic research finds that the corporate income tax is the most used type of tax to contribute to economic growth on the dimension of tax policy because of its capacity to influence investment decisions.

It should be noted that any tax policy instrument has its intervention limits, as economic growth is influenced by several factors other than those of a tax field (labor force, natural resources, location of the country, etc.) and the use of tax policy must be with utmost caution.

Moreover, the lower the level of taxation, the more limited the subsequent interventions will be. For example, a country with a corporate income tax rate of 30% has a much greater margin of intervention in implementing tax policy measures aimed at stimulating economic growth than a country with a tax rate of 5%.

Accordingly, any reduction in the level of taxation diminishes the ability of the Government to intervene in the future through tax policy to achieve the objective of economic growth. The ones presented show the need to study and perform a complex analysis of the opportunity for intervention on the tax policy dimension.

Regarding the use of corporate income tax to achieve economic growth objectives if we refer to Romania, it may differ from several aspects mainly related to the level of corporate income tax, ways of using favorable tax policies to attract foreign investment, offering various tax incentives to stimulate investment and business development. Overall, while the general ideas behind using corporate income tax to spur economic growth are applicable everywhere, Romania may use different tactics and policies depending on its particular economic environment, goals for policy, and regulatory structure. It is evident that, in any event, how these tax laws are enacted and upheld will determine how successful it is to use corporate taxes to achieve economic growth goals (Cazacu et al., 2022). To increase investor confidence and foster a favorable business environment, tax laws must be transparent, stable, and predictable.

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II. LITERATURE REVIEW

Throughout history, various empirical economic studies have been carried out that had as their object of research the existence or non-existence of a causal link between fiscal policy and economic growth. Thus, the neoclassical (exogenous) theory (Solow, 1956; Cass, 1965) predicts that tax policy changes do not affect economic growth in the long term, but only in the short term. Thus, a change in the level of taxation will cause an increase or decrease in economic activity in the short term, but in the long term, the level of economic growth will be the same as if there were no changes in the level of taxation.

On the other hand, endogenous theories (Romer, 1990; Lucas, 1988) predict that a change in fiscal policy also entails a change in the economic growth rate.

The existence of different points of view of the theories mentioned above is explained by the following:

1. different periods. Neoclassical researchers' empirical studies were carried out in more distant periods when economic developments were largely influenced by parameters other than fiscal or economic ones.

2. different economic systems. The results of the studies are determined by the economic situation and specifics of the analyzed countries. Some countries have a decisive human and/or capital factor for economic growth, while others rely mainly on natural resources.

3. analysis tools used/types of variables used. Along with scientific progress, research is characterized by a higher degree of precision, making it possible to delimit the influencing factors of economic growth (Noroc, 2022).

To analyze the influence of taxes on economic growth, it is necessary first to distinguish between distorted taxes that affect economic growth and non-distorting taxes that are characterized by a neutral impact. The main conclusion from the research is that the pace of economic growth is primarily influenced by the changes made in the system of distorted taxes and not by the non-distorted ones. Kneller et al. (1999) counted income and property taxes among the distorted taxes and consumption taxes in the non-distorted category.

Also, Schwellnus and Arnold (2008) demonstrates a negative relationship between corporate tax and economic growth. According to this research, lower corporate tax rates can promote economic activity while higher tax rates typically impede economic growth. The relationship between corporate taxes and business investment, innovation, and overall productivity within an economy provides the justification for this relationship. Businesses may devote a sizeable amount of their revenue to paying taxes when corporate tax rates are high, which reduces the amount of money available for capital expenditures, R&D, or expansion plans. As a result, the prospects for economic growth may be hampered by this decreased investment, which may also limit productivity gains and innovation.

An important aspect in determining the optimal structure of the taxation system is the characteristics of the taxes and their impact on the various micro- and macroeconomic variables.

According to the results of the analyses carried out in work by Acosta-Ormaechea et al. (2019), it was found that the change in the taxation structure, by moving from consumption and property taxation to income taxes, is negatively associated with economic growth in the long term. Likewise, higher rates of social and medical insurance contributions and personal income tax negatively affect economic growth to a greater extent than possible increases in corporate tax rates. At the same time, the shift from income tax to property taxes has a more substantial positive influence on economic growth than the shift to consumption taxes.

Arnold (2008) analyzes 21 OECD member countries and suggests in his paper that income taxes are associated with lower economic growth compared to consumption and property taxes. Likewise, the author finds that property taxes, mainly recurring taxes on real property, appear to be the most growth-promoting, followed closely by consumption taxes. Personal income taxes seem significantly lower, and corporate income taxes have the most negative effects on GDP per capita. There is also evidence of a negative relationship between the progressivity of personal income taxes and growth.

III. MATERIALS AND METHODS

Corporate income tax is very complex and is applied in various forms, which can differ even within the same country depending on the nature of the companies (size, activities carried out, etc.). Recently, to simplify the taxation of company profits, especially small and medium ones, new forms of taxation based on the gross income of companies have been implemented in national legislation, replacing the classic taxable base—the profit tax.

Analyzing the international practice, we could mainly distinguish the following forms:

- profit tax;
- tax on dividends;
- gross income tax;

In this sense, depending on the political options, the goals and objectives set by the government, etc., the application of corporate income tax can be done in the following ways:

1. Taxation of the total profit before its distribution, followed by taxation of the distributed profit in the form of dividends. This method of taxation is currently applied in the Republic of Moldova. The income tax rate

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for legal entities (except for small and medium-sized enterprises) is 12%, and a tax of 6% is withheld when distributing dividends.

2. Taxation of only the profit distributed for dividends, in which case the retention of the profit for taxation is encouraged. The Republic of Moldova had such an experience when, between 2008 and 2011, the "0" tax rate on the income of economic agents related to the income reinvested in the company's activity was established.

3. Taxation of only the profit retained by economic agents for self-financing, in which case the distribution of profit in the form of dividends is encouraged, a less common practice.

4. Taxation applied to gross income aims to simplify the process of calculating company tax. It has been widely used recently for small and medium-sized enterprises.

In the Republic of Moldova, the income tax rate from entrepreneurial activity has undergone a series of changes, always having a downward trend. Thus, if in 1998 it constituted 32%, then in 2008 it reached the level of 0%, and starting from 2012 it constituted 12%.

In the following, we will analyze the effects of the tax exemption reform on reinvested profit from 2008 from the perspective of its impact on public finances and companies. However, the overlap of the international financial crisis of 2009 limits the possibility of studying the impact of the tax reform on economic growth.

The revision of the profit taxation mechanism of economic agents by subjecting to taxation only the profit to be distributed among shareholders or associates in the form of dividends by applying the "0" rate to the reinvested profit had a rather radical character influencing the budget revenues and in a to a lesser extent the desired behavior of economic agents.

Several premises related to the informal economy and the stimulation of economic development were invoked to implement reform, including stimulating companies to reinvest the profits obtained from entrepreneurial activity.

A first economic assessment of the tax reform of 2008 is that it has a general character, being granted to all companies, regardless of their size and the type of activity carried out (production, trade, etc.); it did not target specific activities or certain changes in the behavior of economic agencies (for example, to invest in fixed assets and not circulating ones, etc.).

This characteristic determined that the reform was costly from the perspective of public finances, negatively affecting a significant decrease in revenues to the national public budget from the corporate income tax. From Figure1. we observed a drastic reduction in the revenues from the corporate income tax, from 1,388.4 million lei in 2007 to 443 million lei in 2009. Thus, in the conditions of the estimation of similar budget revenues from 2007, the tax reform determined the failure of potential budget expenditures in the amount of 3.3 billion lei during four years of implementation.

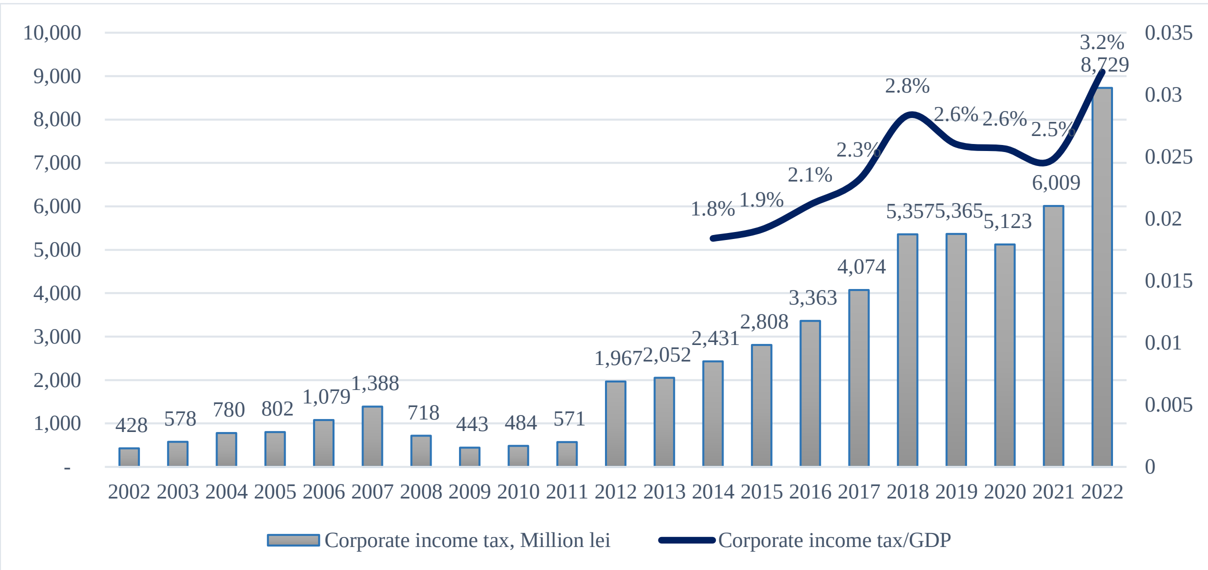

Figure 1. The evolution of revenues from the corporate income tax at the national public budget and the share in GDP, million lei, %, 2002 - 2022

Source: Prepared by the author based on the data of the Government Portal of Open Data and the National Bureau of Statistics of Moldova

The expected effect of increasing investments was not achieved in terms of achieving the economic growth objective following the introduction of the zero rate on reinvested income. The growth rate of private investments

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in the first year of the reform's implementation was similar to previous years. In the following years, private investments collapsed due to the global economic-financial crisis (Figure 2).

Table 1. The evolution of economic indicators of Moldovan companies (billions of lei**)**

Economic indicators	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Sales revenue	98	117	149	175	146	178	208	212	233	263	282	301	331	357	398	382	488
The financial result	4	5	11	16	4	13	14	5	4	4	3	15	25	23	26	19	40
Profit/Sales Revenue, %	3.9 %	4.2%	7.3%	8.9%	2.5%	7.4%	6.9%	2.2%	1.8%	1.4%	1.2%	5.0%	7.4%	6.5%	6.6%	4.9%	8.3%

Source: Prepared by the author based on the data of the National Bureau of Statistics of Moldova

However, this reform also had some positive aspects regarding company tax compliance. Thus, in the first year of implementation of the tax reform, the highest level of declared profit was recorded in relation to sales revenue, representing 8.9%, the highest value during the years 2005 – 2021 (see Table 1).

The data are irrelevant for the following years of tax reform implementation (especially 2009), considering that the respective microeconomic indicators were affected by the global crisis.

Likewise, starting in 2012, the reintroduction of the 12% profit tax deteriorated tax compliance, and the declared profit indicator relative to sales revenue dropped significantly from 6.9% in 2011 to only 2.2% in 2012.

Analyzing the effect of the reform on categories of companies, according to the size of the activity, we conclude that the most significant increase in the declared profit indicator related to sales revenue in the year of implementation of the reform compared to the previous year was recorded by micro and small companies. Similarly, in 2012, with the reintroduction of the income tax, the most significant decrease in the analyzed indicator was recorded in the case of micro-enterprises (Figure 2.).

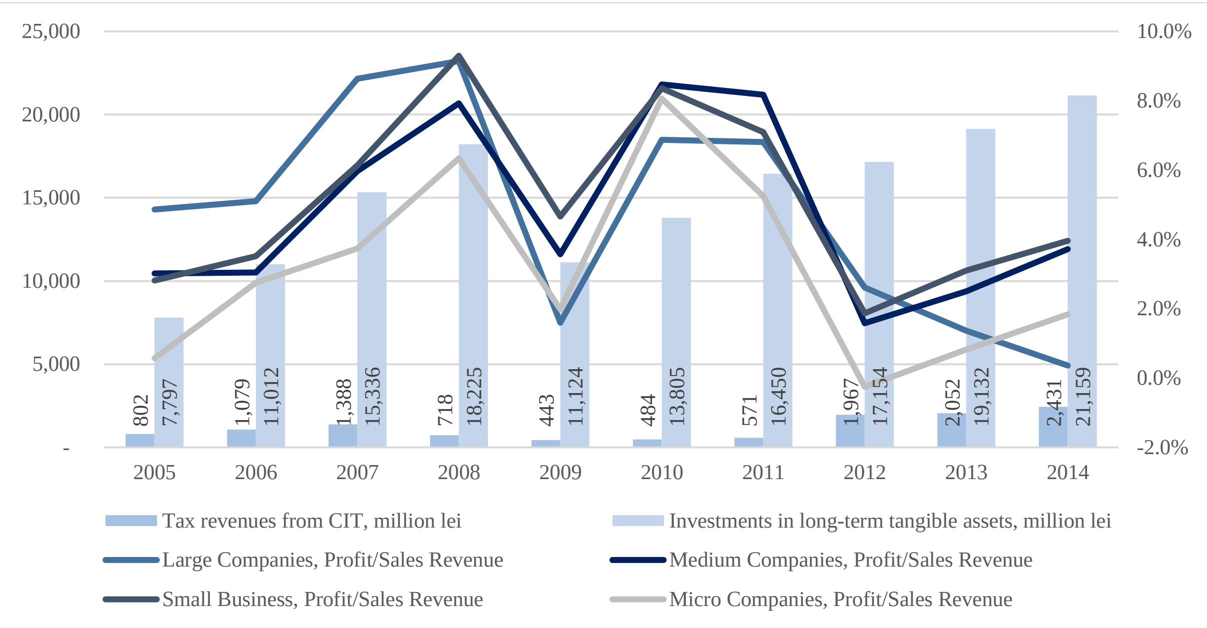

Figure 2. The evolution of tax revenues from corporate income tax to the national public budget, investments in long-term tangible assets, and the share of profit in sales revenue, million lei, %, 2005 – 2014
Source: Prepared by the author based on the data of the Government Portal of Open Data and the National Bureau of Statistics of Moldova

This evolution shows that the private sector in the Republic of Moldova, especially that of small and medium-sized enterprises, is very flexible to changes in the dimension of tax policy in terms of tax compliance, which is also determined by a lower level of tax administration efficiency.

Another conceptual change related to tax policy is the introduction of a single simplified tax of 3% of the income obtained from operational activity by small business agents starting on January 1, 2012. Subjects of taxation are economic agents that are not registered as VAT payers, except farmers and individual entrepreneurs.

The measure aims to simplify taxation, accounting records, administration, and tax reporting by introducing a single simplified tax on income obtained from entrepreneurial activity by small business agents. Such a fiscal

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concept is also applied in Romania. According to the tax code of Romania, micro-enterprises are taxed at the following tax rates:

a) 1% for micro-enterprises with revenues that do not exceed 60,000 euros inclusive;

b) 3% for micro-enterprises that:

- earns more than 60,000 euros; or
- carry out certain activities (computer game editing activities, other software product editing activities, custom software creation activities (customer-oriented software), etc.).

This type of tax goes against the principle of tax equity. In this context, the given system does not take into account the taxpayer's contributory capacity, as there may be situations when the economic agent obtains losses but is obliged to pay income tax.

The respective taxation system favors economic agents that generate income with very low costs, i.e., high profitability, and disadvantages those who obtain income with high costs, i.e., low profitability. In this sense, the size of the tax to be paid largely depends on the field of activity carried out by the economic agent because the profitability obtained also depends on it.

However, SMEs facing more significant difficulties in terms of administrative complexity must be supported. Compliance costs are usually much higher for small companies than for large ones. In addition, multiple changes to tax legislation cause a general increased complexity of the national tax system, which creates not only loopholes favorable for committing tax abuses but also uncertainty for honest taxpayers.

The introduction of a simplified general income tax system using digital solutions will help reduce compliance costs, especially for SMEs. Taxpayers' tax reporting must be as efficient as possible, simple, and data-limited to a minimum. The above could take the form of a tax applied to sales revenue. Reporting sales through online checkout and control equipment would allow the exclusion of SMEs' tax declaration obligation, the latter being notified by the tax administration regarding the amount of income tax.

In many cases, the development of a business ends with the existence of an idea, the latter not being put into practice due to a lack of tax or accounting knowledge. This is why it is important that the tax system for SMEs ensures the maximum exclusion of any barriers to starting a business.

Taxation on turnover/sales income is also supported by IMF economists who mention that this instrument is a relatively simple one and serves to simplify the tax calculations and payment obligations of SMEs while allowing the tax administration to concentrate resources on larger firms, which contribute significantly more to government revenues. The appropriate threshold and rate of turnover tax depend on country-specific factors, including the prevalence of informal sector activities, the capabilities of taxpayers, the quality of tax administration, the use of digital technology for declaring and paying taxes, the average size of profit margins, statutory rates of corporate and natural persons and whether the threshold is familiar with the VAT registration threshold (Wen, 2023). The Republic of Moldova went even further by introducing a single tax encompassing several taxes (IT Parks Tax Regime). A similar taxation is worth considering when applying to SMEs.

An effective alternative to the reinvested income tax exemption measure is accelerated depreciation, which is the granting of the right to companies to deduct in the first years of the use of long-term assets, a more significant amount of depreciation, for example, the RM practice - 50% deduction in the first year of use. Through this measure, there is a postponement of the payment of income tax, the size of which is directly proportional to the amount of investments in long-term assets. Considering that this measure is only a postponement of income tax, to increase the intensity of this incentive and, respectively, to stimulate the propensity of companies for investment to a greater extent, the option of granting an additional deduction related to the expenses of depreciation of long-term tangible assets. For example, when making investments of 1 million lei, the company will have the right to deduct the amount of depreciation for 1 million lei and an additional 50% of its value as a tax incentive.
In this sense, at a tax rate of 12%, the state, through this fiscal facility, co-participates with 6% of the investment value. Exactly on the same principles, with an additional tax deduction, the given option can be applied to some types of expenses that are associated with increasing companies' competitiveness (for example, expenses for research and development).

Table 2 presents the main advantages and disadvantages of the 2 forms of fiscal facilities.

Table 2. Comparison of the main tax expenditures related to corporate income tax

Comparison parameters	Additional/Accelerated Depreciation	Reinvested profit exemption
Cost	Income tax on capital investments is exempt. The size of the budget cost depends on the amount of the investment made.	More expensive. All reinvested profits, usually profits that were not distributed as dividends, are exempt. The size of the budget cost depends on the size of the realized profit.

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The behavior of companies	Capital investments are encouraged.	The maintenance of profit within the company is stimulated, regardless of their further destination.
The degree of complexity	More complex	More simple

Source: Prepared by the author

Analyzing the two types of tax facilities, we believe that the accelerated/additional depreciation instrument should be strengthened more than the tax exemption on reinvested profits. Also, it has been noted that additional/accelerated depreciation promotes capital investment, but the exemption for reinvested earnings encourages profits to be retained by the business, regardless of how they are used later. The reinvested earnings exemption has simpler procedures, but additional/accelerated depreciation requires more work to implement.

IV. CONCLUSION

The analysis carried out allowed us to formulate the following conclusions:

In Moldova, the profit tax has a significant contribution to the formation of budget revenues, being characterized by an increase in the efficiency of tax collections in recent years, reaching 2022 a share in GDP of 3.2%, surpassing several European countries in this chapter

The general exemption from profit tax on reinvested income represents a costly measure from the perspective of public finances; being applied to all economic agents, it generated a significant reduction in budget revenues;

The widespread use of the reinvested income tax exemption did not ensure the achievement of the objective of contributing to a more pronounced economic growth for the first year of implementation. However, the overlap of the international financial crisis of 2009 limits the possibility of studying the impact of the tax reform on economic growth.

The tax reform had a positive effect on increasing the degree of tax compliance through the declaration of income, especially by small companies, but this decreased with the reintroduction of the profit tax.

Following the analysis, it is found that Moldovan companies' behavior is very sensitive to changes in the field of profit tax. This sensitivity suggests that these companies' behavior and decision-making processes are greatly impacted by changes in profit tax rates or regulations (Covali et al., 2020). For instance, businesses may be more likely to invest, grow, or hire more when profit tax rates are lowered in an effort to maximize the tax savings and boost profitability. On the other hand, in the event that profit tax rates are increased, businesses might reduce their expenditures, postpone plans for growth, or even think about moving their operations to countries with more advantageous tax structures. Therefore, in order to promote a favorable business climate and accelerate economic growth in Moldova, policymakers must carefully consider the implications of profit tax reforms.

The scope of increasing the efficiency of the profit tax can be achieved with the following improvement directions from the perspective of public finance consolidation and economic growth:

1. More pronounced use of accelerated/additional depreciation to change the investment propensity of companies;
2. Development of a simplified tax regime for SMEs similar to the tax regime applied to IT parks.

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