

Analysis of the historical development of the main general government revenues

In this assessment, the **National Council of Public Finances ("CNFP") analyses the historical development (1995-2021) of general government revenues**, in particular tax revenues, i.e. direct and indirect taxes, which on average account for 34% and 28% of total general government revenues respectively.

Total revenues increased over the entire period, even during the economic and financial crisis of 2008-2009 and the sovereign debt crisis that followed in its wake. The year 2020 is a notable exception, with the COVID-19 crisis leading to an unprecedented revenue decline of 0.8% despite nominal GDP growth of 2.4%. One explanation is that the COVID-19 crisis affected both demand and supply in the economy, and did so abruptly in view of the confinements and bans or restrictions on whole sectors of the economy. As a result, both indirect and direct taxes were affected, especially as the payment of some taxes could be postponed as part of the measures decided. In contrast, in 2008-2009, the economic downturn was initiated by a financial crisis (or liquidity crisis), which in a second stage turned into an economic crisis affecting more sectors. The negative effects on supply and demand were therefore rather sequential and, in the first instance affected the demand side in particular (mainly affecting indirect taxes). Thus, revenues still rose by +0.4% in 2009 despite a decline in nominal GDP of 2.4%.

The average annual growth rate of total revenues coincides almost perfectly with that of nominal GDP (6.1% and 6.2% respectively). However, the CNFP notes a general deceleration (of about 2 percentage points) in the average annual growth rates of total revenues between the pre- and post-financial crisis period. Moreover, the average annual growth rate for nominal GDP is higher (+0.5 percentage points) than that for revenues before the crisis; a situation which has been reversed (-0.1 percentage points) in the post-crisis period.

As regards **tax revenues**, on average over the period under consideration, the relative share of direct taxes (54%) is greater than that of indirect taxes (45%). The CNFP finds that the evolution of indirect taxes (with an average annual growth rate of 6.2%) is above that of nominal GDP until 2015, while the evolution of direct taxes (with an average annual growth rate of 6.3%) is below that of nominal GDP until 2018. The explanation of these changes in the trajectory can be found in the following paragraphs.

Concerning **indirect taxes**, the three main sub-categories are VAT-type taxes, excise duties and the subscription tax on company shares ("TABO"). While the evolution of excise duties shows a less dynamic evolution from 2005 onwards (which results in particular from a slight reduction in oil sales on the territory after years of strong growth: -4% for petrol and -2% for diesel on average over the period from 2005 to 2020), VAT-type taxes and the TABO show a dynamic evolution that is largely above that of nominal GDP. However, their dynamic evolution is interrupted by several drops and jolts, notably induced by the change in tax regulations concerning VAT applicable to e-commerce in 2015, which led to a sharp drop in VAT-type taxes and which therefore explains the change in the trajectory of indirect taxes in relation to nominal GDP in 2015.

Regarding **direct taxes**, of which income taxes are the main source of revenue (average weight of 94%), they are composed of taxes on individual or household income ("IRPP") (average weight of 60%) and taxes on the income or profits of cooperation ("IRBS") (average weight of 40%). The CNFP notes, however, that the separation between IRPP and IRBS is not always clear and precise between individuals and "companies". Thus, part of the IRPP comes from the activity of individual entrepreneurs and partnerships (SNC, SCS, etc.), an activity that is not subject to corporate income tax, whereas this activity is comparable, economically speaking, to that of legal entities with limited liability (SA, SARL) which in turn pay IRBS. Moreover, the TABO is considered as a tax on production and income (indirect

tax) and not as an IRBS, whereas it is a tax that capital companies (e.g. funds) pay on their issue of negotiable securities. **On the IRBS side**, since about 2003, revenues have generally been evolving below nominal GDP. It is only from 2015-2016 onwards that IRBS recovered and evolved closer to GDP growth before deviating again in 2020. **As for the IRPP (RTS, assiette, solidarité** – as defined in the assessment), its growth has been stronger than that of nominal GDP since 2003 (8.6% against 5.9%, on average over the period 2003-2021) with a widening gap since 2013 in relation to the evolution of nominal GDP and employees' remuneration. The non-indexation of tax scales to inflation is a key explanation for this development. An increase in wages (e.g. due to regular indexation) increases the average tax rate, as a household is likely to move with a proportion of its income into tax brackets with higher marginal rates.