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VAT incentives in European countries and main reasons for their application

Section: Macroeconomic and regional problems of industrial development

Ekon. promisl. 2016, 76(4): 41-52

<https://doi.org/10.15407/econindustry2016.01.041>

Language: Russian

Abstract: The article examines the reasons for applying the reduced VAT rates; we defined two such motives, notably distributional considerations and presence of public and/or merit goods. We also determined that there are some factors influencing on efficiency of reduced VAT rates, notably passing through the lower rate in sales prices, elasticity of demand, which could be considered as main ones. Also these factors include the size of price reduction, signaling effects, product life cycles, level of price reduction, marketing, etc. The indirect influence of reduced VAT rates on economic efficiency appears principally due to cross-border transactions and opportunities to avoid and/or to evade VAT, arising as a result of use of appropriate incentives. Among other factors are rebound effect, innovation and market transformation, free-rider problem, and effects on state budget. We also briefly analyzed both administrative and compliance costs related to the application of reduced VAT rates and main reasons of their occurrence, such as existence of “mixed products”, etc. We examined the data on 28 European countries concerning both standard and reduced VAT rates in 2016. As a result we defined that currently the most common goods and services, covered by VAT incentives in EU countries, are basic foodstuffs; pharmaceutical products; medical equipment for disabled persons; books, newspapers, periodicals; hotel accommodation, restaurants; and public transport, admission to cultural and/or sport events, water supplies.

Keywords: VAT, tax incentives, tax rates, European Union.

| [Full text \(PDF\)](#)

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