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RED TAPE? THE REVENUE IMPACT OF THE VAT FILING THRESHOLDS*



Jan Luksic†
European Commission

Shekhar Mittal‡
University of California

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Abstract

Value-added tax systems across the world are afflicted with size-dependent regulations.The benefit of such regulations to the tax authority is unclear. In this paper, we use an administrative dataset from the state of Delhi in India to first show that a policy which mandated different frequencies of filing based on self-reported turnover resulted in bunching of firms below the thresholds at all levels. Using the subsequent change in these reporting policies, we provide evidence that such sharp bunching indeed occurs due to the VAT reporting frequency thresholds. We document that such bunching partly occurs due to turnover shifting and underreporting, provide evidence that the observed bunching has no growth consequences for the bunching firms - and find that bunching occurs to similar degree across industries. Second, we calculate the VAT revenue losses due to such bunching. Third, the subsequent withdrawal of the policy allows us to show that in a regime with size-dependent reporting requirements, more frequent reporting is not associated with greater VAT collection. Finally, according to our back of the envelope welfare analysis, the sized-based filing policy is welfare improving if a welfare-maximizing government's objective function assigns important weights to small- and medium-sized enterprises.

JEL codes: H26, H32, O38.

Keywords: Value-added tax, size-based regulation, reporting rules, notches, bunching.

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†European Commission. jan.luksic@ec.europa.eu

‡University of California, Los Angeles. shekhar.mittal.1@anderson.ucla.edu

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