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The impact of Direct Tax and Indirect Tax on the Economic Growth in Albania

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ABSTRACT:*The major groups of taxes in a country are Direct Taxes and Indirect Taxes. The main objective of our study is to analyze the impact of Direct Taxes (DIR) and Indirect Taxes (IND) on the economic growth in Albania. This topic has been subject for different studies during recent decades. To conduct this study, secondary data were collected on an annual basis for a time span of 10 years. We have used the method of linear regression analysis by identifying the gross domestic product as the dependent variable and the Direct Taxes (DIR) and Indirect Taxes (IND) as the independent variables. The study results indicate that the independent variables have a positive effect on the economic growth of Albania.*

KEYWORDS -*direct taxes, economic growth, gross domestic product, indirect taxes*

I. INTRODUCTION

Taxes are the main source of public revenue collection with which the state completes the public expenditures that are within its competences. For today's contemporary states taxes are permanent, regular and the most important revenues, which are collected from individuals and businesses and serve to finance public revenues. Tax is considered any payment required by law, made in favour of the state budget, by individuals and economic units of a country, based on the income or wealth they have, the consumption of goods and the services they benefit from. They constitute the main source of income in the state budget (over 90%). There are two major groups of taxes: direct and indirect.

Direct taxes include all those types of taxes that are paid from income, meaning from salary or other income gained from private, individual or collective activity. These are massive taxes from the point of view of the extent of the number of taxpayers, they are exposed and they are applied with certain percentages on income or profits. In direct taxes are included the Consumption Tax, Company IncomeTax, Social and Health Insurance Contributions, Wealth Tax, Personal Income Tax etc.

Indirect taxes are those that are essentially paid by the consumers, users of goods or services and apparently to the production entities, i.e. producers. As a rule, they are included in the price of the goods, they are disguised, hidden, social control over them is small and the reaction of the mass of buyers to them is small, because they pay for the goods they buy without realizing that they have paid in favour of the seller of the goods some tax too. In other words Indirect taxes are those taxes that are calculated and collected on the circulation of goods and services. In Indirect taxes are included Value Added Tax, Custom Duties, Excise Tax, Inheritance and Gift Taxes etc.

The classification of taxes into direct and indirect is based on several principles:

- On the basis of the transfer criterion, different theorists such as Milli, Vagner, Moll, etc. have made the tax classification into direct and indirect. According to them, direct taxes are those which are paid by the persons who are expected by law to bear the tax burden. Whereas indirect taxes are those that do not burden the persons who are assigned by law to pay tax, but the other persons to whom the tax has been transferred.

- According to the tax source principle, direct taxes are personal taxes, such as property taxes, income taxes, while indirect taxes are consumption tax, inheritance and gift tax, etc.

-The tax power principle is based on when the tax is paid. According to this criterion, wealth and income are included in direct taxes, while indirect taxes are expressed through consumption.

Table 1. The differences between Direct Taxes and Indirect Taxes

Indicator	**Direct Tax**	**Indirect Tax**
Who pays the tax?	They are paid directly from the owner	The final consumer pays
The comunication system with the state	Direct	Through intermediaries (sellers)

Object of taxation	Movable and immovable property of the taxpayer	The product or service performed
The factors that determine the tax rate	Citizen's income, type of taxable property	The product price
Visibility level	The taxpayer knows in advance the amount of tax and the obligation to pay it	It is hidden and the consumer often does not know that the price of the goods includes tax
Complexity of calculations	Difficult	Easy
Dependence on accompanying factors	Exists	Absent
Transferability	Directtaxisnon-transferable.	Indirecttaxistransferable– usuallytotheendconsumer.
Equity	Direct tax ensures equity asindividual taxpayers payaccordingtotheirincome.	Indirect tax ensures equality astax rates are pre-decided andhavetobepaidbyanyonewhopur chases the product or usestheserviceregardlessoftheir earningcapacity.
Usage of paperwork	Directtaxinvolvespaperworkbefo recollection.	The indirect tax requires nopaperworkandiseasiertobe collected.
Awareness	There is more awareness aboutdirecttaxduetothedesignated taxslabs/brackets.	There is less awareness aboutindirecttaxchargesastheyget hiddeninthetotalcost.

Source: Author's illustrations

The purpose of this study is to analyse the impact of Direct Taxes and Indirect Taxes on the economic growth in Albania. The study main purpose is to show the positive impact and importance of these two group of taxes in order that the state undertakes new fiscal policies to collect as much revenues as possible from these sources.

Regarding the structural composition of taxes in Albania, based on Table 2, VAT and excise with 45.4% represent the main weight. However, if we were to compare them grouped into direct and indirect taxes, we would see that direct taxes have the highest weight in state revenues.

Table 2. The structural composition of taxes in Albania (% of revenues)

Personal Income Tax	9.2
Company Income Tax	7.4
VAT & Excise	45.4
Social and Health Insurance Contributions	22
Other Taxes	16

Source: INSTAT

II. LITERATURE REVIEW

In neo-classical economic growth models, taxation only affects the level of income, but not the growth rate, while endogenous growth models suggest that taxes can affect the long-term growth rate.

Plosser (1992) finds a significant negative correlation between the level of taxes on income and profits (as a percentage of GDP) and the growth of real GDP per capital. It is analysed by Odusola (2006), that government revenue, at some time is motivated by the changes in tax base, tax policies and tax rates .

Solow (1956) presents, an open up study, about taxes and growth association. It is inspected in his new classical growth model, that taxes have no effect on steady state growth, while income tax has a negative impact on economic allocation.

Arisoy and Unlukaplan (2010) examine the effect of direct-indirect tax composition on economic growth. For this purpose, they take time series data, from 1968-2006 for Turkish economy, by applying Feeder Model. To check the importance, in-between direct and indirect taxes they find that indirect taxes are

significantly positively correlated with economic growth. They finally conclude, that share of indirect taxes should be more than that of direct taxes, if there is planning to augment economic growth

Babatunde, Ibukun and Oyeyemi (2017) concluded that tax revenue has a significant positive relationship with Gross Domestic Product. The study investigated the impact of taxation on economic growth in Africa from 2004 to 2013. The study carried out various preliminary tests including descriptive statistics, and stationary tests using Augmented Dickey Fuller (ADF) test, Levin et al. test, Im, Pesaran and Shin W-stat tests. The study Therefore, high and weak levels of taxation are favorable to economic growth as upheld by the economic effect of IbnKhaldun's theory on taxation, which approves the positive impact that lower tax rate have on work, output and economic performance.

According to Anastassiou and Dritsaki (2005) there exists causal relationship between tax revenues and economic growth in Greece. This study examines the relationship between tax revenues and the rate of economic growth for Greece using annual data from 1965 until 2002 and causality analysis.

III. METHODOLOGY

This section provides the methodology used for analyzing the impact of direct taxes and indirect taxes on economic growth in Albania. We have conducted the study by using a linear regression model analysis. The data we are using in this study are annually time series data in the period of 2012-2021. The data for the study variables (DIR, IND and GDP) was collected from the Institute of Statistics in Albania. The statistical computer software used to run the analysis is The Statistics Package for Social Sciences (SPSS) 20.

The regression equation used to study the relationship between DIR, IND and GDP is:

$GDP = \beta 0 + \beta 1\ (DIR) + \beta 2\ (IND) + e$

Where

GDP= Gross Domestic Product, the dependent variable DIR= Direct Taxes, first independent variable
CIT= Indirect Taxes, second independent variable
$\beta 0$= is the constant term
$\beta 1$, $\beta 2$, = are the coefficients of the independent variables
e = is the error term of the equation

In Table 3.are presented the data collected for the study for all the variables during the period taken into study 2012-2021.

Table 3: Aggregate annual value of GDP, Direct Taxes and Indirect Taxes for the period 2012-2021 in billions of Albanian Lek

Year	GDP	Indirect Taxes		Direct Taxes					
		VAT	Excise	Consumption Tax	CIT	Personal Income Tax	Tax on Labor & Capital	Social & Health Insurance Contributions	Other Taxes
2012	1332.8	115.95	35.98	151.94	17.33	27.99	55.98	57.31	41.32
2013	1350.1	112.06	37.80	149.86	14.85	29.70	47.25	59.40	44.55
2014	1395.3	124.18	40.46	165.65	20.93	29.30	55.81	69.77	48.84
2015	1434.3	126.22	38.72	164.94	24.38	30.12	65.98	71.72	45.89

2016	1472.48	131.05	41.23	172.28	29.45	30.92	69.21	79.51	53.01
2017	1550.65	139.56	44.97	184.53	31.01	32.56	72.88	86.84	58.93
2018	1636.73	144.03	44.19	188.22	34.37	36.01	80.20	93.29	62.19
2019	1691.9	131.97	47.37	179.34	37.22	45.68	116.74	98.13	49.06
2020	1617.5	131.02	45.29	176.31	22.32	33.97	66.31	97.05	63.41
2021	1769.3	161.01	51.31	212.31	35.39	38.92	74.31	111.47	77.85

Source: INSTAT

FINDINGS AND DISCUSSIONS

In this study we have analyzed the impact of Direct Taxes and Indirect Taxes on GDP using a linear regression model ran on The Statistics Package for Social Sciences (SPSS) 20.

Table 4: Descriptive Statistics

	Minimum	Maximum	Mean	Std.Deviation	N
GDP	1332.8	1769.3	1525.106	150.76602	10
DIR	345.63	550.25	442.103	70.09626	10
IND	149.86	212.32	174.44	18.4241	10

Source: Windows SPSS 20

Table 4 displays the descriptive statistics of the research variables. The minimum Gross Domestic Product within the period of the study was 1,332.8 billion ALL, the maximum was about 1,769.3 billion ALL and the mean 1,525.106. While the standard deviation of 150.76602 billion ALL indicated the observations in the GDP for the period under review are not highly spread out. The minimum Direct Taxes in the period of the study were 345.63 billion ALL and the maximum about 550.25 billion ALL with a mean of 442.103. In the other hand, Indirect Taxes have a minimum value of 149.86 billion ALL, with a maximum value of 212.32 billion ALL and a mean of 174.44 ALL. The standard deviation for both independent variables (70.09626 for Direct Taxes and 18.4241 for Indirect Taxes) shows that the data are clustered closely around the mean, especially for Indirect Taxes, which makes them more reliable.

Table 5: The log-run relationship

Variable	Coefficient	Std.Error	t-statistics	Prob
Constant	584.196	121.212	4.820	0.002
DIR	2.094	0.403	5.195	0.001
IND	0.088	1.533	0.057	0.056

Source: Windows SPSS 20

According to the results shown in Table 3, by substituting the computed coefficient values of the variables in the equation, we have:

GDP=584.196 + 2.094 DIR + 0.088 IND + e

From the substituted equation Direct Taxes and Indirect Taxes have positive coefficients and can result in a positive change in Gross Domestic Product whenever its value increases. In other words we can say that an increase in Direct Taxes in 1 unit, will result in an increase in the Gross Domestic Product by 2.094. On the other hand an increase in Indirect Taxes in 1 unit, will result in an increase in the Gross Domestic Product by 0.088.

If we take a look at the results shown in Table 6 the degree of correlation between Direct Taxes, Indirect Taxes and GDP is high (R=0.983) and 96.7% of the total variation in the dependent variable can be explained by the independent variables. The calculated Durbin-Watson value is 1.650, less than 2.0, which means that there is no autocorrelation between the independent variables. The results of the study analysis have

shown that both independent variables, Direct Taxes and Indirect Taxes, have a positive impact on the economic growth. The impact of Direct Taxes in GDP is more positive than the Indirect Taxes one ($\beta 1 - \beta 2 > 0$) . The results in Table 6 also indicates the constant P-value <0.001, which means that the regression model statistically significantly predicts the outcome variable.

Table 6: Regression results

R	0.983
R-Square	0.967
AdjustedR-Square	0.958
Durbin-WatsonStat	1.650
Sig.(P)	<0.001[b]

Source: Windows SPSS 20

IV. CONCLUSIONS AND RECOMMENDATIONS

This study analyzed the impact of Direct Taxes and Indirect Taxes on economic growth in Albania. We determined the Gross Domestic Product as the dependent variable and Direct Taxes and Indirect Taxes as the independent variables. The data used to fulfill the objective of this study was collected from the Institute of Statistics in Albania for the period from 2012 to 2021. The analyze was performed by using a linear regression model ran on The Statistics Package for Social Sciences (SPSS) 20. The results from the statistical analysis from the data indicate that Direct Taxes and Indirect Taxes both have a positive significant impact on the economic growth of Albania but the impact of Direct Taxes is more positive than the Indirect Taxes impact. Consumption Taxes and Social and Health Insurances Contributions occupy a considerable weight in the total of Direct Taxes while indirect taxes mainly consist of Value Added Tax and excise tax.

The limitation of this study is that we have not taken in consideration the changes in time of the rates of different types of direct and indirect taxes such as: Value Added Tax, Company Income Tax, Excise Tax etc. There are also other types of taxes that take part on Direct and Indirect Taxes that can be taken into study in future researches.Another limitation is the fact that our study period includes the period affected by the COVID-19 pandemic, which means that the data collected for thisperiod are influenced by external factors that may have led to out-of-trend results.

Based on this research we recommend an expanding in the taxable base and reforming tax administration. Considering that one of the main revenue for the state are the Social and Health Insurances Contributions paid for every individual registered as employed, and that one of the main problems in Albania is the illegal work without registration. We think that more controls should be made and more strict measures should be taken in order to reduce the level of illegal work. In this way the revenues from the Social and Health Insurances Contributions will increase. Finally, considering that Value Added Tax has an important impact in state's revenues, we recommend using differential VAT rates.

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