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THE PORTUGUESE 2017 BUDGET: TREAT-OR-TRICK?

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The Portuguese Parliament discussions on the draft 2017 budget presented by the Government are on the way.

The draft forecasts a budget deficit of 1.6% of the GDP which, if achieved, would be the lowest Portuguese budget deficit in 40 years. A 0.8% deficit cut should make EU Commission happy and the Government expects to reach it despite of the €10 increase in all lower pensions imposed by the far-left parties to approve the budget, the entire removal of all cuts in public officers' salaries and pension made from 2010 to 2015 and the phase-out of the 3.5% personal income tax surcharge.

Considering the increase in public spending and the reduction in income tax revenues, it does not come as a surprise that, despite the "treats" offered by the Government, fiscal policy will have to do its "tricks" and taxes overall will have to increase further.

The Government had already announced in November 2015 that it would stop the corporate income tax reform, which contemplated a reduction of the general rate from 21% to 20% in 2016 and from 20% to 19% in 2017. The draft 2017 budget confirms that the general rate will remain unchanged.

The removal in 2017 of the personal income tax 3.5% surcharge, approved by the Government in December 2015, will now only apply in full to those earning less than €20,261 euros a year. Taxpayers earning up to €80,640 will only benefit from a gradual phase-out in 2017 and those earning more than €80,640 will have to wait until December.

In addition, the Government decided to resort to an increase of indirect taxation. Not only to the recurrent increase of taxes over vehicles, alcohol, oil products and tobacco, but also to a new tax on sugary and low alcoholic drinks ("fat tax"), an extra 0.3% tax on real estate above €600,000 (which will be levied on top of the current real estate tax) and even a special tax on gun shells.

Notwithstanding the 2016 figures on the budget implementation disclosed last week showing that indirect tax revenues, including VAT, are expected to fall below the forecasts made in the 2016 budget, the Government seems convinced that there is still room to increase indirect taxation. And the fact is it may well be right.

As an example, the new fat tax on sugary and low alcoholic drinks should raise a mere €80 million in 2017. But what prevents the Government from increasing it in the next years, as it was done in respect of all other excite taxes in the last years? And why leaving other sugary products out of this tax? After all, aren't these products associated with weight and obesity problems?

The room to increase indirect taxes seems endless and new taxes are very likely to appear in the next years, such as the inheritance tax over high-net-worth estates - which was included in the Government's programme and is waiting for the right moment - and the financial transactions tax - which is waiting for EU approval.

The 2017 budget shows a clear trend to give preference to indirect taxes, which already represent more than 50% of the whole tax revenues. One of the arguments used by the Government is that this is the only way to reduce personal income tax.

A more pragmatic perspective would argue that indirect taxes are efficient, raise less controversy and could even be more popular, if you have the right arguments - in reality, many times the end consumer will not even notice them, especially if they have a marginal impact on prices.

The downsides are known: unlike direct taxes, indirect taxes are regressive and will treat taxpayers equally irrespectively of their income, which may increase inequality and affect those with low income; on the other hand, some indirect taxes may harm competitiveness of the economy as a whole and/or of some products produced locally, especially if they entail an increase of production costs (*e.g*. taxes on oil products/power).

For now, the Government seems to have accomplished what some considered the impossible mission of squaring the circle: increase taxes and keep everyone happy! However, if inflation, interest rates or oil prices increase in the near future, the Government and taxpayers may be faced with a new dilemma: trick-or-trick?