



Small and Medium-Sized Businesses in Albania Prefer Progressive Tax or Flat Tax

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Abstract: A progressive and flat tax system is widely debated not only in public finance but usually as a political issue in Albania. A progressive tax has been applied in Albania in recent years. Many researchers in Albania have studied the effect of the flat and progressive tax on public finances, but what we will bring in this paper is the point of view with which small and medium businesses in Albania consider the effect of the tax on the income of their companies.

Based on the results of the survey of Structural Statistics, for the year 2021, 99.8% of active enterprises are SMEs. This important fact intrigued us to study the effect of taxes on SME income as well as their opinion on each tax. In order to see the effect of the tax system, the analysis of the data collected from 200 SMEs (through questionnaires) for the main indicators such as progressive taxation, and simplified tax on small business was carried out. The descriptive analysis of the data collected as well as the confidence interval estimation for the VAT rate preferred, are going to generate some conclusions and recommendations for policymakers.

1. INTRODUCTION

The debate on the flat or progressive tax has been a political issue that has accompanied the changes of governments in Albania. In 2007, by law no. 9766, from 07.09.2007, a flat tax of 10% was applied for the first time in Albania, while in 2013, with a change of government, a progressive tax was introduced. In fact, it is difficult to show the pure impact of a flat or progressive tax on GDP.

Positive and negative sides of the flat tax. It is easy to understand, has a low cost to implement, businesses are more confident in their decision-making due to the recognition and ease of flat tax abatement, etc. Besides the positive sides, there are also negative sides. The flat tax disproportionately impacts the middle class and those with lower income levels.

Positive and negative sides of a progressive tax. The application of a progressive tax reduces the tax burden on people who are less able to pay. This leaves more money in the pockets of low-income earners, who are likely to spend more money on essential goods and stimulate the economy in the process.

A progressive tax system also tends to collect more tax than a flat tax, since the highest percentage of tax is levied on those with the highest amount of money. It creates a system full of bureaucracy. It creates tax evasion. A progressive tax also results in the largest amount of funds being used to finance public services, such as road maintenance and public safety, so this tax is indirectly returned to citizens.

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Based on the advantages and disadvantages of the flat and progressive tax, it is not easy to determine which type of tax is appropriate at the current level of development in Albania.

Both types of taxes have been implemented in Albania, first the flat tax and finally the progressive tax. Many experts have analyzed their effects and reached different conclusions. In general, these studies start from the perspective of the impact of the tax on GDP.

We think that, in order to give an accurate conclusion on the right type of tax, their effect on the business as the subject that is directly impacted by this tax should be analyzed.

2. FLAT AND PROGRESSIVE TAX IMPACT STUDIES

According to [Elezi \(2014\)](#), the flat tax has had a positive effect on GDP growth only in the first year of implementation, while in the other years, there has been a decrease. The same can be said about the level of employment in the private sector, which increased in the first year of the implementation of the flat tax, while in the following years it decreased.

In the study by [Bardhi \(2017\)](#), a theoretical analysis was made for the implementation of the progressive or flat tax. Based on the economic conditions of the country, the culture of taxpayers, and the transitional period that the country is going through, it was concluded that the flat tax has an advantage over the progressive tax because it taxes all businesses at the same percentage. Even though the percentage is the same, the flat tax itself is progressive, since those who receive more pay more.

[Kraja et al. \(2023\)](#) analyzed the impact of the flat tax (2007-2013) and the impact of the implemented progressive tax (2014-2021) on GDP. They concluded that both taxes have a positive impact on the country's economy, but the progressive tax has a slightly higher positive impact than the flat one. In the first years of implementation, the progressive tax has a smaller impact than the flat one, but afterward, its impact is higher.

Based on the above, we conclude that many analyses have been carried out referring to the impact of the flat or progressive tax on the country's GDP. In general, all studies have looked at the impact of the tax on public revenues. To judge comprehensively, in addition to measuring the impact of the tax on the country's economy, the effect of taxes on business income must first be studied as those directly affected by the tax. What is their opinion on the flat or progressive tax?

More than the tax changes, which are happening more often recently in Albania and which have not brought more income, the fiscal scheme and system must be changed. However, we think that it is time to pay more attention to the implementation regime of the fiscal system than to the type of tax.

3. SME REPRESENTATIVES OPINION ABOUT THE FISCAL SYSTEM IN ALBANIA

As we mentioned above, many studies have been conducted to show the effect of the tax on GDP. In this article, we will show what is the opinion of the SME representatives on the fiscal system and its implementation regime. For this purpose, the opinion of 200 SME representatives was gathered. We have chosen to analyze the opinion of SME representatives since about 76% of businesses in Albania are small and medium ([INSTAT, 2023](#)). Referring to INSTAT data, 505,186 companies were registered as SMEs in 2021, while the total number of enterprises in the same year was 664,217.

4. THE COMPOSITION OF THE SAMPLE

The sample size was 200 small and medium enterprises. From the data processing, we find that 79 interviewees are women, which represents about 39% of the respondents and 121 interviewees are men, or about 61% of the respondents. This fact is obvious since in Albanian companies (enterprises) most of the management positions are held by men.

About 34.5% of the respondents are up to 30 years old, 30.5% are in the age group of 31-40 years old, and about 20.5% belong to the age group of 41-50 years old, about 13.5% of the interviewees are in the age group up to 51-60 years old and 1 % age group 61-65 years. About 52% of the companies participating in the sample carry out their activity in Tirana, 30% in Durrës, and 18% in Fier.

5. DATA ANALYSIS AND THE RESEARCH QUESTIONS

Through the questionnaire, data related to income, expenses, number of employees, investments, hospital expenses, cultural expenses and other important data were collected in response to some research questions. In addition to the above, data on their opinion regarding the following has been collected and processed:

- a) How much are businesses involved in the preparation of fiscal legislation?
- b) Which tax model do you prefer?
- c) Which of the alternatives is more suitable for improving the tax system?
 - (i) Changing the income tax method
 - (ii) Changing the level of income tax
 - (iii) Improving the tax administration.
- d) In your opinion, what percentage rate do you believe is appropriate for VAT?

6. RESULTS OF DATA ANALYSIS

Question (a): *Do you think that the tax revenues deposited in the state budget by SMEs are used to improve the general economic conditions of SMEs (business climate)?"*

The summarized results of the responses are presented below in Table 1. All the interviewees answered this question.

Table 1. Do you think that the tax revenues deposited in the state budget by SMEs are used to improve the general economic conditions of SMEs (business climate)?"

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	No	125	62.5	62.5	62.5
	Don't know	51	25.5	25.5	88.0
	Yes	24	12.0	12.0	100.0
	Total	200	100.0	100.0	

Source: Authors

Analyzing the data, it becomes evident that a significant proportion of business representatives believe that the taxes they pay are not utilized to enhance the overall business environment.

Question (b): *Which kind of taxation do you prefer?*

During the interview, we were interested in business preferences regarding the flat and progressive tax. There were three answer alternatives:

- a) Flat tax,
- b) Progressive tax,
- c) Indifferent.

We added the “indifferent” option as an alternative since during the piloting of the questionnaire there were business representatives who were not interested in the type of tax. The results after data processing show that 31% of businesses prefer the progressive tax, 55% prefer the flat tax, and 14% are indifferent to the type of tax.

Question (c): *Which option among the alternatives is better suited for enhancing the tax system?*

Through this question, we sought to indirectly understand in which part of the fiscal system there are gaps.

Table 2. Which option among the alternatives is better suited for enhancing the tax system?

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Changing the income tax rate	40	19.5	19.5	19.5
	Changing the income tax method	61	30.0	30.0	50.5
	I don't know	22	11.0	11.0	61.5
	Improvement of tax administration	77	38.5	38.5	100.0
	Total	200	100.0	100.0	

Source: Authors

Referring to the data in Table 2, we notice that business dissatisfaction is mainly towards the tax administration, approximately 38.5%, followed by the alternative “Changing the income tax method” with 30%.

Question (d). *In your opinion, what percentage rate do you believe is appropriate for VAT?*

One of the aspects discussed by SME representatives is the percentage of VAT. In Albania, VAT is applied at the rate of 20% (Law no. 92/2014 “On tax on value added in the Republic of Albania”, p. 19). This level of VAT is considered high by SME representatives.

At the beginning of 2018, small and medium businesses were also included in the VAT declaration scheme. According to Albanian tax legislation, all businesses (regardless of size or legal status), that register a taxable income of at least 2 million lek, are included in the VAT scheme. This change caused many debates and dissatisfaction in the business environment, not only for the introduction of the business in the VAT declaration scheme but also for other issues such as the percentage rate of the simplified tax on small businesses, etc.

Based on this fact, the opinion of the SME representatives was drawn in the questionnaire as to what is the tax rate (%) of VAT that they are willing to pay.

From the data in Table 3, we notice that the average percentage for which the businesses expressed their willingness to pay is 10.1735 % (mean) and the standard deviation is 3.39% (McGraw-Hill, 1989, p. 13). Median is equal to 10%.

Table 3. Descriptive results for the response of the interviewees regarding the VAT rate

		Statistic	Std. Error	
What do you think should be the percentage rate of VAT?	Mean	10.1735	.33901	
	95% Confidence Interval for Mean	Lower Bound	9.5050	
		Upper Bound	10.8420	
	5% Trimmed Mean	10.2372		
	Median	10.0000		
	Variance	22.985		
	Std. Deviation	4.79431		
	Minimum	.00		
	Maximum	19.00		
	Range	19.00		
	Interquartile Range	5.38		

Source: Authors (SPSS Processing of data collected through the questionnaire)

The confidence interval for the average value of VAT declared by the SME representatives is calculated. With 95% certainty, we have enough evidence to believe that the VAT rate acceptable to businesses ranges from 9.505 % to 10.8420%.

7. CONCLUSION

The implementation of a tax, no matter how simple it is, will affect the whole or a significant part of society directly or indirectly. Therefore, at any time, initiatives must be accompanied by in-depth analysis and studies for the effect that the implementation of this tax has. Policymakers before approving fiscal changes must be clear about all the accompanying socioeconomic effects and use it during the preparation of the fiscal package in such a way that the fiscal package has as few negative socioeconomic effects as possible.

Different researchers have shown that both the flat tax and the progressive tax have a positive effect on GDP, regardless of whether the progressive tax has a greater effect. Both taxes have been implemented in Albania, but none of the studies clearly show which of the taxes is more successful. Referring to the analysis of the data collected from businesses according to which the VAT rate accepted by businesses is lower than what is applied, this makes us think that in the current conditions, it is more important for the government to focus on the regime of tax implementation than in the type of tax.

Approximately 39% of the SME representatives think that one of the factors that would improve the fiscal system in Albania is the improvement of the tax administration. So, their trust in the tax administration has decreased. Based on this fact, the government should strengthen the transparency of the tax authorities by adopting the highest standards of transparency.

Cross-referenced and repeated studies related to the effect on the budget of the fiscal system with studies on the effect of the fiscal system on business performance will ensure accuracy, transparency and safe implementation.

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