RECENT DEVELOPMENTS IN THE EU TAXATION

Assoc. Prof. Flavia Barna Ph.D
West University from Timişoara
Faculty of Economics and Business Administration
Timişoara, Romania
Assist. Petru-Ovidiu Mura Ph. D Student
West University from Timişoara
Faculty of Economics and Business Administration
Timişoara, Romania

Abstract: Anticipating the economic and social change, European Union member states have decided to restructure their aspirations and fiscal priorities. European Union fiscal policy aims to achieve important goals, such as free movement of capital, competitiveness, economic growth and employment, avoiding, at the same time, harmful tax competition between Member States. In this paper we undertook a structural - quantitative analysis of the EU taxation in order to highlight the degree to which fiscal policy objectives proposed by European decision makers are fulfilled and the existent disparities among the member states, resulting in frustration of the taxpayers.

JEL classification: E62, E63.

Key words: fiscal policy, labor taxation, tax burden, implicite rate of taxation, fiscal revenues structure.

1. Introduction

In a general sense, the fiscal policy means "the volume and source of the means of financing the public funds, the assessment methods to be used, the objectives and means of achieving them". (Manolescu, G., 1997) Another approach argues that fiscal policy reffers to "all the measures, practical actions - based on an economic conception– the types of taxes used, their place throughout the budgetary revenues, the dynamic relations between them, as well as how to use them as leverage to stimulate economic development, solving social and political problems in the country". (Dobrotă, N., 1997, p. 468)

Seen as a support of complex decision making, fiscal policy means "all fiscal decisions taken by public decision-makers, in order to ensure the financial resources to finance public needs and achieving the socio-economic goals, while the real economy is affected by objective factors, annd their trend is not exclusively cyclical". (Corduneanu Carmen, 1998, p. 379) Fiscal policy is determined directly related to the state's options on taxes, meaning that it must require conscious use of the full set of fiscal tools and methods for determining the level, structure and fiscal incentives regime in the distribution of social product, so as to ensure political, economic and social objectives. (Condor I., Stancu R., 2002)

The European desire is to create a favorable tax area that may influence the economic growth and competitiveness in Europe, leading to the creation of a European welfare state, modern, innovative and sustainable. The fiscal policy adopted in the EU proposes to achieve important goals, such as free movement of capital and employment, avoiding, at the same time, harmful tax competition between Member States. In this context, we show that European fiscal system affects different categories of taxpayers due to structural differences that appear in terms of income, consumption, degrees of regulation, different ways of administering the tax system branches and the possibility of avoiding tax liabilities.

2. Objectives

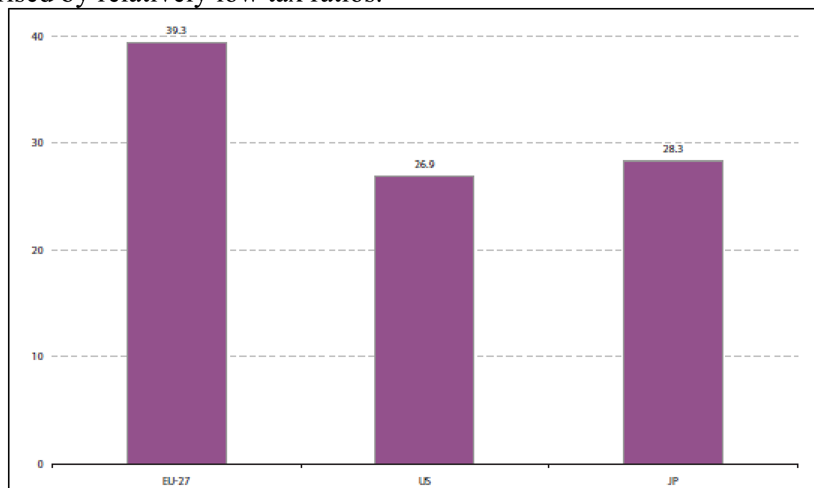
The objectives of this article can be summarized as:

1. to illustrate the evolution of fiscal pressure in EU.
2. to highlight the evolution of tax burden related to labor taxation, the implicite rates of labor taxation and the composition of labor taxation rates.
3. to offer a detailed description of the structure of tax revenues by country and cathegory of taxes.

3. Structural - quantitative analysis of taxation in the European Union

3.1. Fiscal pressure in the European Union

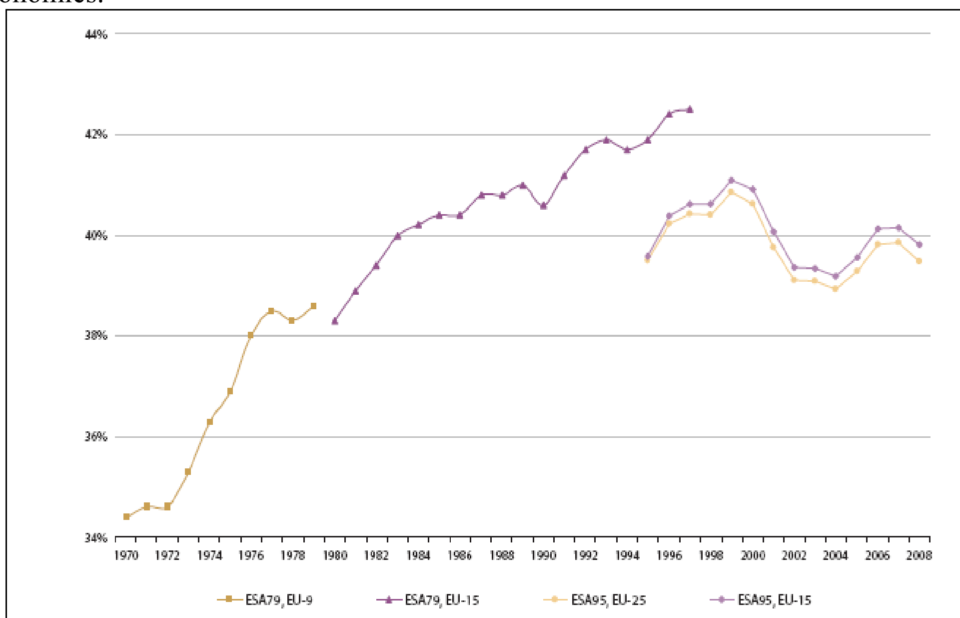
The European Union is, taken as a whole, a high tax area. In 2008, the overall tax ratio, i.e. the sum of taxes and social security contributions in the 27 Member States (EU-27) amounted to 39.3 % in the GDP-weighted average, more than one third above the levels recorded in the United States and Japan. The tax level in the EU is high not only compared to those two countries but also compared to other economies in general; among the major non-European OECD members, only New Zealand has a tax ratio that exceeds 34.5 % of GDP(2). As for less developed countries, they are typically characterised by relatively low tax ratios.



Source: Commission Services for the EU, OECD for the US and Japan

Figure no. 1 Overall tax-to-GDP ratio (incl. SSC) in the EU, US and Japan 2008, in %

At the end of the 1990-2000 decade, a number of countries have benefited from dynamic tax revenues to reduce tax burden, applying reductions for income tax, social security or income tax. A clear decline in the tax burden is evident between the years 2001-2002 (see Figure 2); however, successive increases in the years following 2004 show that in most countries there is a limited appetite regarding a drastic reduction in overall tax burden. The most aggressive tax cuts were recorded in the Member States of Central and Eastern Europe (in the 90s), due to the urgent need of restructuring their economies.



Source: Commission Services

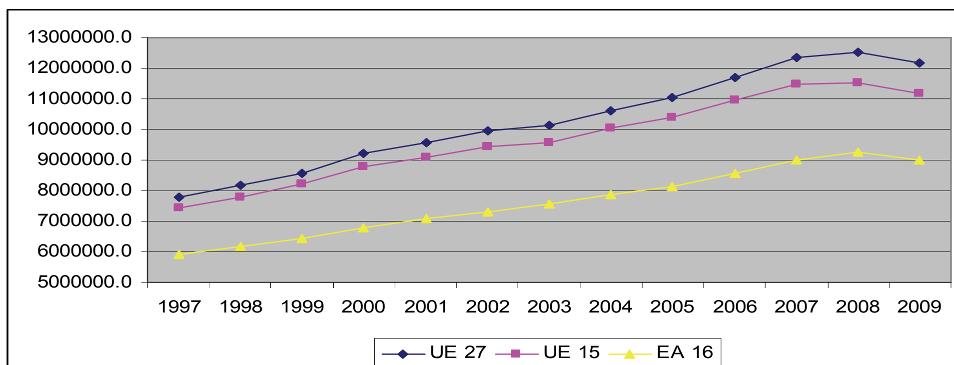
Figure no. 2 Long-term trend of tax burden (including social contributions) - 1970-2008 (% of GDP)

Today, in response to the global financial crisis, European countries have resorted to carrying out extraordinary public programs and the designing of growing budget deficits, which will complicate in the future the reducing of the tax burden and also the budgetary stability.

Tax burden has declined since 2000, but only for a few years. The reducing of the tax rate was quite steep in 2001, but decreased in intensity in the years that followed and stopped in 2005. Between 2005-2007, there was an increase, followed by a further decline in 2008 (see Figure 2). Cyclical factors were those who contributed to this development: economic growth has slowed immediately after 2000, reducing the fiscal revenues, and since 2004 the growth accelerated (see Figure 3).

In addition, some countries' need to reduce the general government deficit made it more difficult to fiscal relaxation. The high general level of taxation does not mean that each Member State shall impose higher rates. The geographically peripheral countries (except the Nordic countries and Cyprus) tend to apply lower tax rates, especially in Eastern Europe. There are two groups of countries with a high tax burden, ie the Nordic countries (Denmark, Sweden, Finland) and four Member States of Central Europe (Belgium, France, Italy and Austria), which recorded values of the tax burden

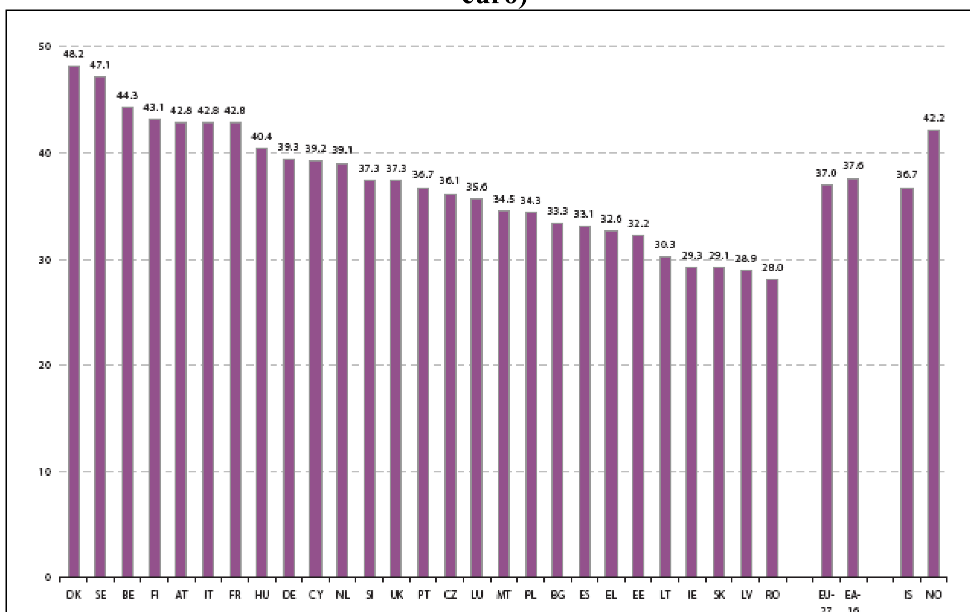
over 40% in 2008. Overall, differences in tax levels within the EU are significant, eaching over 20% of GDP: from 27.9% in Romania to 48% in Denmark.



Source: Data processed using the Eurostat statistical series

Note: the value of GDP used to express the tax rate, also includes estimates of production made by the informal sector ("gray" or "black" economics). So a low tax burden may reflect not only lower taxes but a higher tax evasion.

Figure no. 3 Evolution of GDP (at market prices) during 1997-2009 (millions of euro)

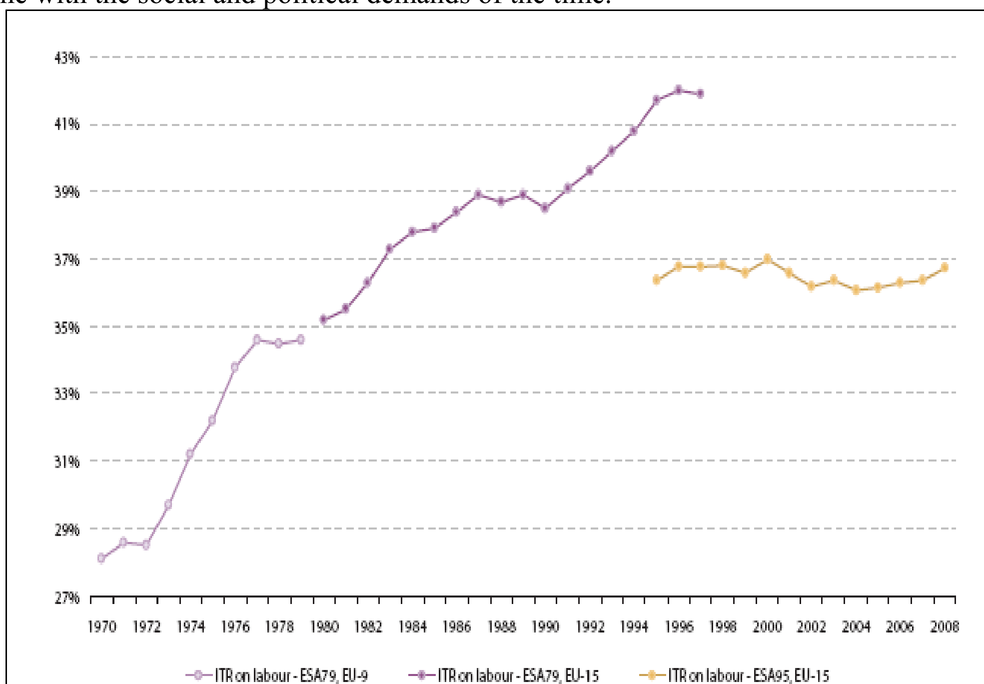


Source: Eurostat for EU countries and Norway, OECD for U.S. and Japan

Figure no. 4 Tax burden in EU, U.S., Japan and Norway in 2008,% of GDP

In general, the taxes / GDP report tends to be significantly larger in the EU-15 than in the 12 new countries: the first seven items (after tax burden) are occupied, indeed, by the old member countries (see Figure 4). There are exceptions: for example, Ireland and Greece have among the lowest tax rates in the European Union. Euroland shows a slightly higher tax burden than the EU-27, this being explained by the fact that euro area contains mostly old Member States.

Regarding the tax burden related to labor taxation, it started growing strongly in the early 1970s. The increase was very marked in the 1970, decelerating only slightly in the 1980s and the first half of the 1990s. The weighted EU-15 average implicit tax rate on labour employed (ITR on labour) increased from about 28% (1970) to almost 42 % (1997). Now, only five countries in the EU have ITRs (implicit tax rate) below the 30 % mark. Labour taxes rose so forcefully because they were the only ones that could provide the volume of funds necessary to finance the additional government expenditure and because unlike consumption taxes, they could be made progressive in line with the social and political demands of the time.



Source: Eurostat

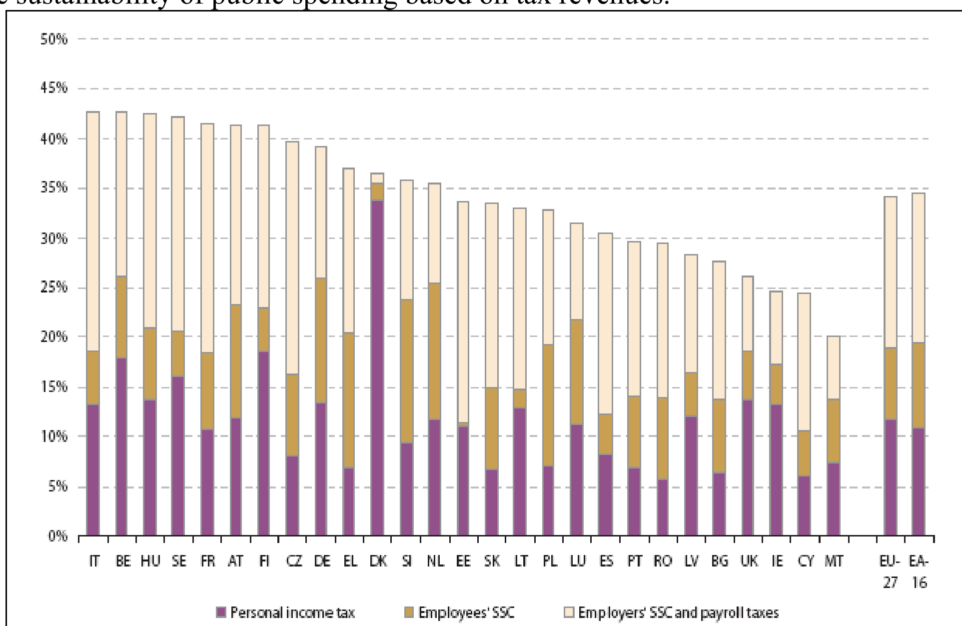
Figure no. 5 Long-term trend of ITR on labour - 1970-2008 (% of GDP)

Starting from the late 1990s, concerns about excessive labour costs prompted initiatives to lower the tax burden on labour income, in order to boost the demand for labour and foster work incentives. Some Member States opted for cutting taxes or social contributions across the board while others focused on targeted reductions in social contributions for low wage and low-qualified workers. These cuts in social contributions were mostly aimed at granting relief to employers, although some countries have also implemented substantial cuts in employees' social contributions. The EU-27 arithmetic average has slightly decreased from 36.0 % in 1999 to 34.2 % in 2008. Eight Member States have ITRs on labour below the 30 % mark and seven are above the 40 % threshold.

There are large differences in the level of labour taxation among the Member States. At one extreme, Malta (20.2 %) and Cyprus (24.5 %) stand out with the lowest ITR on labour in the Union. This might be linked with their historical ties to Britain, as the United Kingdom and Ireland are the only other two countries whose ITR on labour is more than eight percentage points below the EU-27 average. Other countries, too, have low taxes on labour. Bulgaria has a below 30 % ITR, while the rate in Portugal

and Romania is very close to the 30 % mark. In contrast to these geographically more peripheral Member States, most 'continental' European Member States (Italy, Belgium, Czech Republic, France, Hungary, Austria, Germany, Slovenia) exhibit above average ITRs.

The same applies to the Nordic countries. Within these two groups of countries Italy, Sweden, Belgium, Finland, Czech Republic France, Hungary and Austria stand out for reporting an ITR on labour which exceeds 40%. When comparing the ITR on labour with the overall tax-to-GDP ratio, it is noticeable that those Member States that exhibit a high ITR on labour in most cases also have a high tax-to-GDP ratio. The same applies to low-tax countries. This result is in line with the high share of labour taxes in overall tax revenues. The reason is that the fiscal policy implemented in the EU aims the sustainability of public spending based on tax revenues.



Source: Eurostat

Figure no. 6 Composition of labor taxation rates (2008)

3.2. Income structure by tax types

Within the European Union, the structure of tax revenue (total tax) includes:

- taxes on production and imports (d2) *(3)*,
- current taxes on income and wealth (d5),
- capital taxes (d91),
- actual compulsory social contributions (d61111 + d61121 + d61131).

"Indirect taxes" are defined as taxes linked to production and imports (code d2 in the ESA95 system), i.e. as compulsory levies on producer units in respect of the production or importation of goods and services or the use of factors of production. They include VAT, import duties, excise duties and other specific taxes on services (transport, insurance etc.) and on financial and capital transactions. They also include taxes on production (d29) defined as 'taxes that enterprises incur as a result of engaging in production', such as professional licences, taxes on land and building and payroll taxes.

Indirect taxes are defined as the sum of the following ESA95 tax categories:

• VAT: value added type taxes (d211).

• Excise duties and consumption taxes: excise and consumption taxes (d214a) + excise duties (d2122c).

• Other taxes on products (incl. import duties): taxes and duties on imports excluding VAT (d212), excluding excise duties (d2122c), taxes on products, except VAT and import duties (d214), excluding excise duties (d214a).

• Other taxes on production (d29).

"Direct taxes" are defined as current taxes on income and wealth (d5) plus capital taxes including taxes such as inheritance or gift taxes (d91). Income tax (d51) is a subcategory, which includes personal income tax (PIT) and corporate income tax (CIT) as well as capital gains taxes.

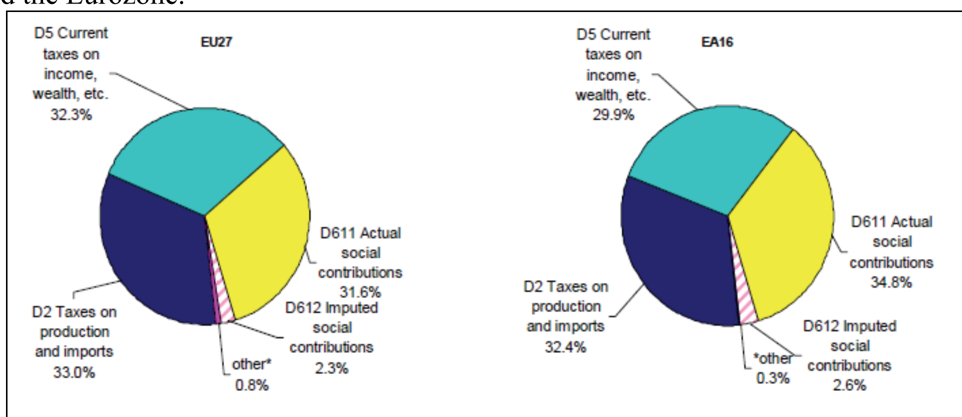
Direct taxes are defined as the sum of the following ESA categories:

- personal income tax: taxes on individual or households income including holding gains (d51a + d51c1);
- corporate income tax: taxes on the income or profits of corporations including holding gains (d51b + d51c2);
- other income and capital taxes: other taxes on income corresponding to other taxes on holding gains (d51c3), taxes on winnings from lottery or gambling (d51d) and other taxes on income n.e.c. (d51e); taxes on capital defined as other current taxes (d59) and capital taxes (d91).

Actual compulsory social contributions are paid by employers and employees on the basis of a work contract, or by self- and non-employed persons. They include three subcategories:

- compulsory employers' actual social contributions (d61111);
- compulsory employees' social contributions (d61121);
- compulsory social contributions by self- and non-employed persons (d61131).

Figure 7 presents an overview of the structure of tax revenues, both the EU27 and the Eurozone.



Source: Tax revenue in the European Union (Lupi, 2010)

Figure no. 7 Composition of tax revenue in EU-27 and EA -16 (2008)

Tax revenue in the EU-27 were relatively equally distributed between social contributions (33.9%), taxes on production and imports (33.0%), and current taxes on income, wealth, etc. (32.3%). A less balanced distribution of tax revenue was recorded

for the euro area, with social contributions accounting for 37.4% in 2008, while current taxes on income, wealth, etc. accounted for the lowest share, at 29.9%. The EA-16 results highlight the relative importance of social contributions in Germany and France. In fact, these two countries together accounted for 53.4% of the EA-16 aggregate in this category. In addition, in 2008 a difference in the residual component "other" was observed in the EU-27 (0.8%) compared to the euro-area (0.3%) due to the jump for capital taxes in the United Kingdom (+1.2 percentage points in terms of GDP compared to 2007).

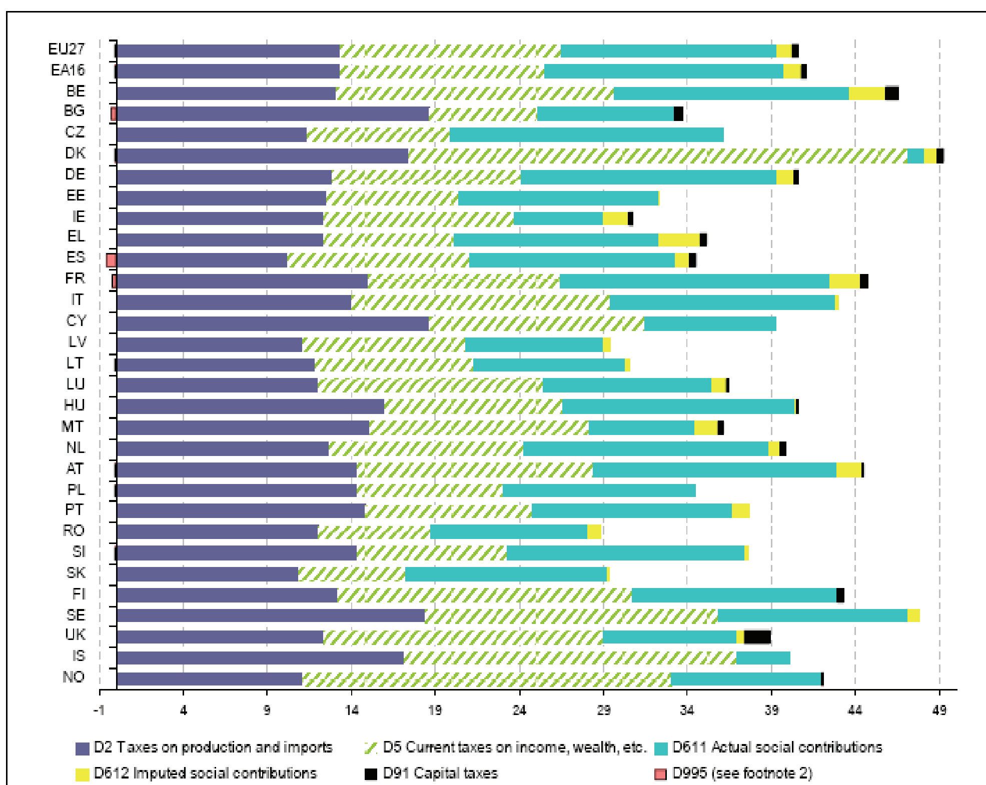
In general, new Member States have a different structure from the old Member States; while the old Member States have recorded tax revenue, in roughly equal share of indirect taxes, direct and social contributions, new Member States often show a smaller proportion of direct taxes in total taxes. The lowest share of direct taxes is recorded in Bulgaria (only 21.0 % of the total), Slovakia (22.1 %), and the Czech Republic (23.8 %); in Poland the share of direct taxes shrank by one third between 1995 and 2004 but has increased again since then and currently stands at 25.2 %. One cause of the low level of direct tax revenues is the moderate tax rates, applied to income and profit tax. Several of these countries have adopted stationary rate systems, which usually induce a greater reduction in the rates of direct taxes than the indirect taxes.

The low share of direct taxes in the new Member States is counterbalanced by higher values of the share of indirect taxes, and also of social contributions. The highest value is found in Bulgaria and Cyprus, where indirect taxes weigh more than half of the total tax burden. Malta and Romania, too, show relatively high indirect tax shares. Regarding the social security contributions, the Czech Republic stands out with a share of 44.9%; high share of social contributions are found in Slovakia, Germany and France.

We encounter significant differences in the countries of the EU-15. Nordic countries, but also Great Britain and Ireland, have a high share of direct taxes in total tax revenue. In Denmark, and in a lesser extent in Ireland, Malta and the UK, the share of social contributions in total tax revenue is low. There is a specific explanation for the low level of social security contributions in Denmark: most of the "public welfare" spending are financed from general taxation. This requires greater levels of direct taxation and, indeed, the share of direct taxes in total tax revenue in Denmark is by far the largest in the European Union. Among the old Member States, the German system is the opposite of Denmark: Germany has the largest share of social contributions, while the share of direct taxes in total tax revenue is among the lowest in the EU-15 (see Figure 8).

4. Conclusions

Faced with the effects of rapid changes resulting from liberalization of trade and capital flows, increased competition in the global context, European Union Member States have become aware of the importance of continuing efforts to increase competitiveness and eliminate disparities existing among the integrated regions of the European space, to cope with the challenges of economic and financial globalization. In this context, fiscal policy can become a vector of competitiveness, in order to ensure sustainable economic growth and higher life standards for European citizens.



Source: Tax revenue in the European Union (Lupi, 2010)

Figure no. 8 Structure of tax revenues by country and cathegory of taxes in 2008 (% of GDP)

Quantitative structural analysis of taxation in the European Union indicate that currently (year 2009) the European tax system affects differentiated many cathegories of taxpayers due to structural differences that occur in terms of income, consumption, varying degrees of regulatory, different ways of tax system management branches and the possibility of avoiding tax liabilities. In general, the tax burden falls on taxpayers who have a higher consumption and achieve significant revenues. New Member States have a different structure from the old Member States, focusing on a lower share of direct taxes in total taxes, while the old Member States have raised fiscal revenues in approximately equal shares of indirect taxes, direct ones and social contributions.

In this context, European policymakers must step up efforts to transform structurally and functionally the fiscal area within EU, to ensure improved quality and performance of human capital, capital efficiency of the firms and their openness to innovation in order to create non-pollutant technologies.

References

1. Condor, I., Stancu, R. — Drept financiar şi fiscal român, Ed. Fundaţiei România de mâine, Bucureşti, 2002.
2. Corduneanu, C. — Sistemul fiscal în ştiinţa finanţelor, Ed. Codecs, Bucureşti, 1998.
3. Dobrotă, N. — Economie politică, Editura Economică, Bucureşti 1997.
4. European — Taxation trends in the European Union. Data for the EU Member

	Commission – Taxation and customs union	States, Iceland and Norway, 2010 Edition, available at http://ec.europa.eu/taxation_customs/resources/documents/taxation/gen_info/economic_analysis/tax_structures/2010/2010_full_text_en.pdf
5.	Lupi, A.	Tax revenue in the European Union, 2010, available at http://epp.eurostat.ec.europa.eu/cache/ITY_OFFPUB/KS-SF-10-023/EN/KS-SF-10-023-EN.PDF
6.	Manolescu, G.	Buget – abordare economică şi financiară, Editura Economică, Bucureşti, 1997.
7.	* * *	www.europa.eu
8.	* * *	http://epp.eurostat.ec.europa.eu/portal/page/portal/statistics/search_database
9.	* * *	Eurostat Yearbook 2010 – Economy, available at http://epp.eurostat.ec.europa.eu/cache/ITY_OFFPUB/CH_01_2010/EN/CH_01_2010-EN.PDF