

ARE ABLE THE MEMBER STATES TO PROMOTE THE EUROPEAN FISCAL CO-ORDINATION WITHIN THE EUROPEAN UNION? THE BACKGROUND OF THE TAX STRUCTURES

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Abstract: In planning of this paper we have started from the question whether those 27 states belonging to the European Union are able to promote, due to their fiscal systems, the fiscal co-ordination within the European Union or to accept the fiscal systems, consequently. In this way, the paper provides a breakdown of taxes according to different classifications: by types of taxes (direct taxes, indirect taxes, social contributions) and by levels of government. The breakdown of tax revenue data computed in percentage of GDP provides indicators of the tax burden and of the structure of taxation in the different Member States, as well as developments over time. As the interpretation of the tax-to-GDP ratio as an indicator for the tax burden requires additional information, an economic classification of taxes has been developed and implicit tax rates have been computed for the economic categories identified.

Key words: tax systems, new member states, old member states, differences in tax system

1. Introduction

Taxation, by using three main sources, can make up both developments and wellbeing:

- firstly, the taxation system has to attract income effect in order that public services should be properly financed, as well as social transfer at high standards;
- secondly, taxation persuades ultimately economical judgement and it would have to offer a stimulus for the key personnel to be deeply engaged. Moreover, the natural resources, efficiently used are consequently required;
- thirdly, the taxation system undeniably redistributes gainfulness and this has to be done in such a way that to strengthen the effective request as well as social balance that is the covering of huge misuses from the income distribution.

Regarding European fiscal policy, this one has to contribute towards the accomplishment of the general goal established by the European Union, namely, “by the end of 2010 the European Union economy should become the most competitive and dynamic from the world, capable of a long-lasting economical development, displaying the best places of employment as well as a greater social cohesion” (target established by the European Council, Lisbon, March 2000). This goal demands a drastically diminishing of a fiscality general level from the EU, and, consequently, requires that the taxable basis be extended so that a balance should be achieved among this diminishing financial consolidation supporting through public debts decreasing and proper investments in essential public services.

Starting from this strategic target proposed by the official meeting in Lisbon, it has been concluded that home market should act a sole market. However, a great contradiction is to be noticed: the measures referring to taxation, the ones that develop inequality and halt the demand, are hardly supposed to achieve such an economical area with a dynamic economical growth, mentioned by the Lisbon Strategy.

Undeniably the question, whether the 27 states, members of the EU are able to contribute through their fiscal systems to the fiscal co-ordination within the EU is to be raised; in other words they have to accept the fiscal systems mandatory, systems that proved to be lately more and more distasted because of the inner logic of such fiscal competition.

The question raised is as judicious because the multinational cooperations are able to complete set of strategies of fiscal optimization provided that the capital is a mobile one.

The transfer facilitated for the profits relocation to the areas with a slight level of taxation as well as financial departments creation in so-called tax heavens/tax shelters are being used in order that investments should be financed by credit lines from the group.

2. Tax structures by type of taxes

Bearing in mind the inherent heterogeneity of tax systems, it is perhaps not surprising that there are significant differences between the new and the old Member States tax systems. The structure of tax revenues differs between new and old Member States, as the former raise relatively little revenue from direct taxation (personal and corporate income tax) and proportionately more from indirect taxation (VAT in particular) and social contributions (figure 1).

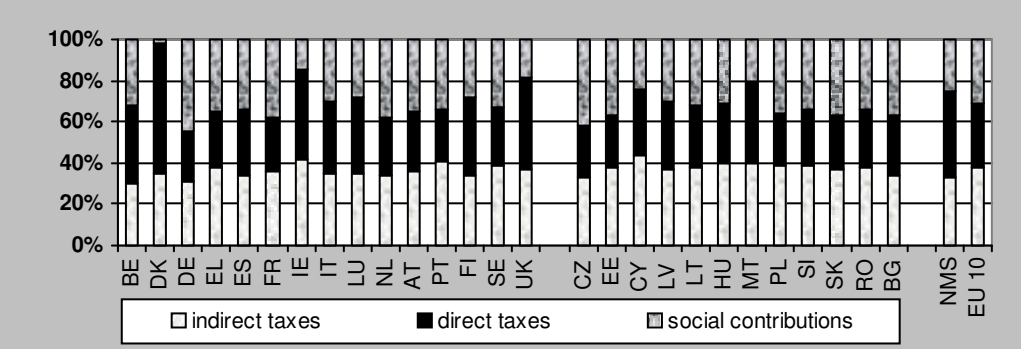


Figure 1. Structure of tax revenues, 2006 (% of total tax burdens)

Source: European Commission (2007)

In 2006, the difference between the EU-15 and the new Member States averages was about 10 percentage points (36.0% vs. 25.7%). With the exception of Malta, all the new Member States are below the EU-15 average. The lowest shares of direct taxes are recorded in Slovenia (19.8%), Poland (24.1%) and Hungary (24.2%). One of the reasons for this difference can be found in the generally lower tax rates applied in the new Member States regarding corporate tax and personal income tax. The following figures 2 and 3 however highlight the limited predictive power of the top rates viewed in isolation as neither Slovenia nor Poland particularly stand out in this respect.

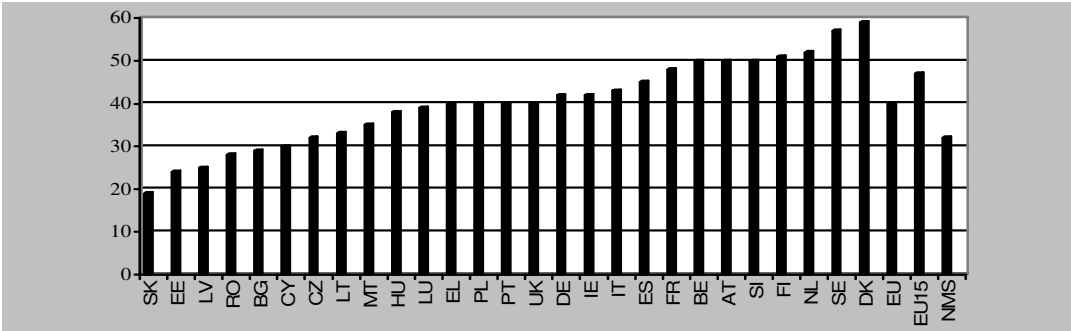


Figure 2. Personal income tax rate, 2006 (% of total tax burdens)

Source: European Commission (2007)

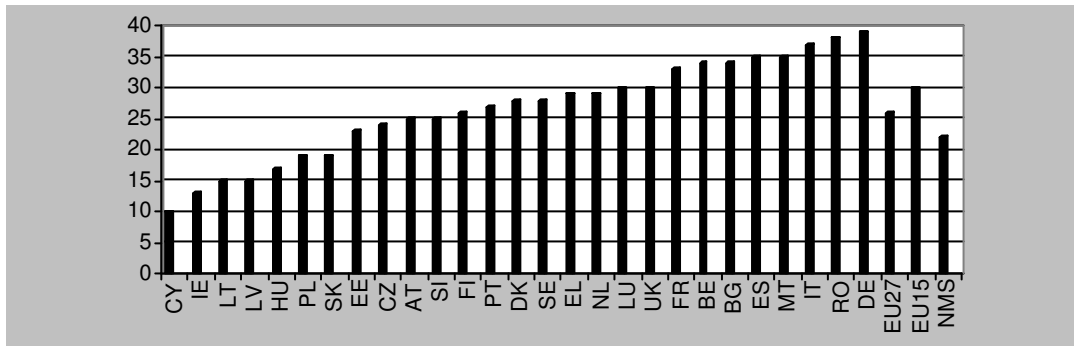


Figure 3. Corporate income tax rate, 2006 (% of total tax burdens)

Source: European Commission (2007)

The low share of direct taxes in the new Member States is counterbalanced by higher shares of social contributions (+4.2% respect to the EU-15) and indirect taxes (+5.7%) on total tax revenues; the gap between the EU-15 and the NMS-12 in the shares of social contributions had been shrinking in the last few years but increased in 2006. The highest shares of social contribution among the NMS-12 are found in the Romania, Czech Republic, Poland and Slovakia. Cyprus and Malta have the highest share of indirect taxes. Also among the EU-15 countries there are some noticeable differences, as illustrated by figure 1. The Nordic countries (Sweden, Denmark and Finland) have relatively high shares of direct taxes in total tax revenues, whereas some southern countries (in particular, Portugal and Greece) have relatively high shares of indirect taxes compared to the EU-15 average. In Denmark and, to a lesser extent, also in the United Kingdom and Ireland the shares of social contributions to total tax revenues are relatively low compared to the EU-15 average. In Denmark, most welfare spending is financed out of general taxation. The share of direct taxation to total tax revenues in Denmark is in fact the highest in the Union. Germany has the highest share of social contributions in the total tax revenues. Germany's share of direct tax revenues, on the other hand, is the lowest in the EU-15. France also has a relatively high share of social contributions and a corresponding relatively low share of direct tax revenues, compared to the EU-15 average.

3. Tax structures by levels of government

In the new ESA95 framework of national accounts, taxes are usually classified according to four different units of government that may operate within a country and to the Institutions of the European Union. The combination of the different government levels operating within a Member State is called the general government, and may include:

- Central (or federal or national) government, including all administrative departments and central agencies of the State whose competence extends normally over the whole economic territory, except for the administration of the social security funds;
- State (or regional) government, when relevant within a Member State, which are separate institutional units exercising some of the functions of government at a level below that of central government and above that at local level, except for the administration of social security funds;
- Local (or municipal) government, whose competence extends to only a local part of the economic territory, apart from local agencies or social security funds;
- Social security funds, including all central, state and local institutional units whose principal activity is to provide social benefits.

Figure 4 displays a classification of aggregate tax revenue (including social contributions) by receiving level of government.

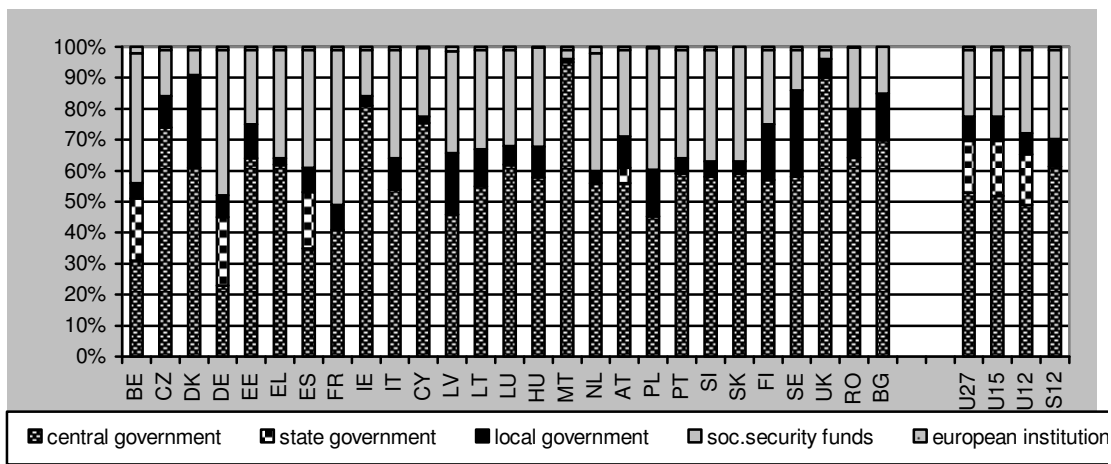


Figure 4. Classification of tax revenues, 2006, (% of total tax burdens)

Source: European Commission (2007)

The figure 4 represent “ultimately received” tax revenues. This means that the shares displayed under State and local governments do not only include 'own' taxes of government sub-sectors, but mostly also the relevant part of the tax revenue that is actually “shared” between the different levels of the general government, even in cases where a government sub-sector has practically no power to vary the rate or the base of those particular taxes.

In 2006, in the EU-15 about 56% of the “ultimately received” aggregate tax revenue (including social contributions) was claimed by the central or federal government, roughly 29% accrued to the social security funds, and around 11% to local government. Around 1% of this tax revenue is paid to the Institutions of the European Union. There are however considerable differences from one Member State to another. For instance, a few Member States have a State government level. The share of regions and municipalities varies from less than 1 % in Greece to 35% in Denmark. Not only Denmark, but also Sweden (33%), Belgium (29%), Spain (29%) and Germany (28%) show relatively high shares of total taxes received by government sub-sectors. The share is around the EU average in Austria (18%) and Italy (16%). The share is noticeably small in Greece (1%), Ireland (2%), the Netherlands (4%) and the United Kingdom (5%). Concerning social security funds, the highest shares in the EU are reported by France and Germany.

In the new Member States the State government level does not exist. Concerning local government taxation the figures vary between Malta, which does not apply local taxes, to Latvia with a share of 18%. Relatively high shares of local taxes can be seen also in Estonia (13%), Hungary (12%), Poland (13%) and Lithuania (10%). Concerning social security funds, high shares appear in Poland (40%), Slovakia (39%), Slovenia and Lithuania (37%).

Conclusions

The competition extension among the member states made them exceed themselves in order to attract a large number of economic operations. As it has already been shown “taxation” is one of the implements used. From this point of view, there is a sharp competition among these states, an issue which, inevitably, may cause disturbances in the assurance of the best level. Moreover, according to W. Koko, this type of conduct may lead to “such an extreme race” for taxes or income (W.Kok, 2003).

In the latest years, especially in the states from Eastern Europe, an increasing amplification has been registered regarding preferential fiscal systems promoting various investments, some of them even displaying high efficiency in attracting foreign investments.

This happens according to a well known opinion suggesting that preferential fiscal systems, the reduced taxation being included, may represent premises of an attractive location for foreign investments (G.Nicodeme, 2003).

In present, 27 taxation systems coexist in the EU, afferent to the 15 member states, plus those taxation systems belonging to the 10 new states which joined on May 1st 2004, besides Romania and Bulgaria entered the EU at the beginning of 2007.

There are noticeable differences among all these states according to their fiscal policies regulations because the national fiscal policies signify a consistent of the member states sovereignty.

The tax system inherent heterogeneity being taken into account, the significant differences between the former member states do not make anybody feel surprised at such diversity in tax systems.

The structure of tax revenues differs between new and old Member States, as the former raise relatively little revenue from direct taxation (personal and corporate income tax) and proportionately more from indirect taxation and social contributions. While direct tax revenues represent more than one third on average in total revenues in EU-15, these are closer to 20% in the new Member States.

The new Member States collect less tax from the corporate sector than the old and corporate tax revenues are less important both in terms of its share of GDP and relative to other tax sources. *Corporate tax rates* are generally lower in the new Member States. While the average corporate tax rate in EU-15 is around 30%, it averages nearly 10 percentage points lower in the new Member States.

However, corporate tax rates in the new Member States vary widely, and the differences fall comfortably within the range of Ireland's 12.5% and Germany's rate just below the 40% mark.

Finally, while EU-15 Member States have reduced rates and have broadened tax bases since the 1980s the new Member States have cut rates more aggressively, especially since the late 1990s.

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