LABOUR TAXATION IN THE EUROPEAN UNION

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This article proposes an analysis, which we consider extremely useful in the current economic context, of the evolution of labour income fiscality, more precisely, the effect of the public debt growth on the tax wedge for the labour income.
The share of fiscal revenues from direct taxes, indirect taxes and social contributions is relatively close in the old member states of the European Union in comparison with the new member states, which register a lower level of income from direct taxes. The low level of income from direct taxes is compensated by more significant shares of the social contributions or indirect taxes.
The main motivations of cross-border migration are: a successful career in a multinational corporation, high variations of the tax rate, of the salary income between states and, last but not least, the level of the net salary. To this day, there are no plans to harmonize across the European Union the legislation regarding the taxes wages and the social security contributions. Still, the European Union had in view the coordination of the national tax systems to make sure that the employees and the employers do not pay several times the social contributions in their movement across the community space.
Despite the fact that some states tax the labour income at a low level, the labour fiscality remains high in the European Union in comparison with other industrialized economies, probably also due to the fact that the majority of the member states have social market economies. The increase of the fiscality level for the labour income determines the decrease of the employment rate and the raise of the unemployement rate.
The solution to guarantee a higher employment rate, which is a target of the European Union Strategy „Europe 2020" could be the relaxation of the labour income fiscality by transferring the tax wedge on the labour income towards property or energy taxation.

Keywords: labour income, social contributions, tax quotas, taxes

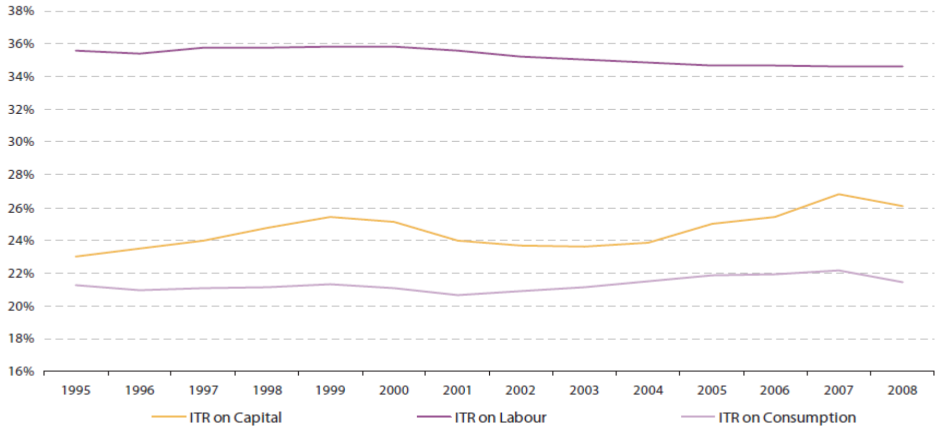
JEL Codes: F22, G28, H2

1. Introduction

The mechanism of the Single European Market is based on the four freedoms acknowledged by the European Community legislation: the free movement of goods, people, services and capital. The main motivations of cross-border migration are: a successful career in a multinational corporation, high variations of the tax rate, of the salary income between states and, last but not least, the level of the net salary. According to some research realized in Switzerland (Kirchgassner, Pommerehne, 2001) and (Feld, Kirchgassner, 2001) we can notice that the level of payroll tax and the level of social contributions have an important influence on the dispersion of the labour force with high income (Peter Egger and Doina Maria Radulescu 2008: 2).
To this day there are no plans to harmonize across the European Union the legislation regarding the social security contributions. Still, the European Union had in view the coordination of the national tax systems to make sure that the employees and the employers do not pay several times the social contributions in their movement across the community space.

If we analyze the structure of budgetary income collected by the European Union, according to the economic classification, the labour taxation and the compulsory social contributions are the most important source of revenue, representing an average of 50% of the budgetary income collected in the European Union. Thus, the labour taxes collected by ten member states: Hungary, Slovenia, Czech Republic, Holland, France, Belgium, Finland, Denmark, Greece and Italy represent between 50-55% of the total income; the labour taxes collected by four states: Sweden, Austria, Germany and Estonia exceed 55% of the total income.
Concerning the rates of labour taxation, the following figure proves that these are the highest of the European Union, amounting to 34%-36% in comparison with the lower rates of capital gain tax and consumption tax.

Figure 1. The tax rates of capital, labour and consumption



Source: Eurostat

During the period before the crisis, in the European Union, generally speaking, the tax wedge increased especially concerning the labour taxes and the social contributions as a result of the need to finance the government expenditures.
During the period after the crisis, the fiscal measures to support the employment offer adopted in the majority of the European Union states visible in the reduction of the fiscality for labour income led to a decrease of the share of the direct fiscal incomes. The tax wedge on the salary income, especially for the low incomes decreased in almost all member states. Instead, the level of social contributions, which increased during the period 2008-2009 registered an asymmetrical evolution. (European Commission, Taxation Papers, 2010: 18).

2. Aspects regarding the taxes wages in the European Union

The labour tax rates in the EU increased continually from 28% in 1970 to approximately 42% in 1997. The continual growth of labour fiscality was due to the tendency of excessive increase of the unemployment rate at the beginning of the 1990s, as a result of the recession. Thus, at the end of the 90s the concerns aiming to decrease the excessive employment costs in order to stimulate the employment rate became more important. While some measures could be generally applied like: the decrease of labour tax rates or of the social contributions rate, others aimed at certain target groups: the decrease of the contribution rates for the unskilled workers.
Regarding the fiscal reforms adopted by the member states, the national governments preferred measures in order to narrow the taxable base or to grant allowances for the low income households rather than to reduce the tax rate. Thus, measures meant to increase the labour tax rate

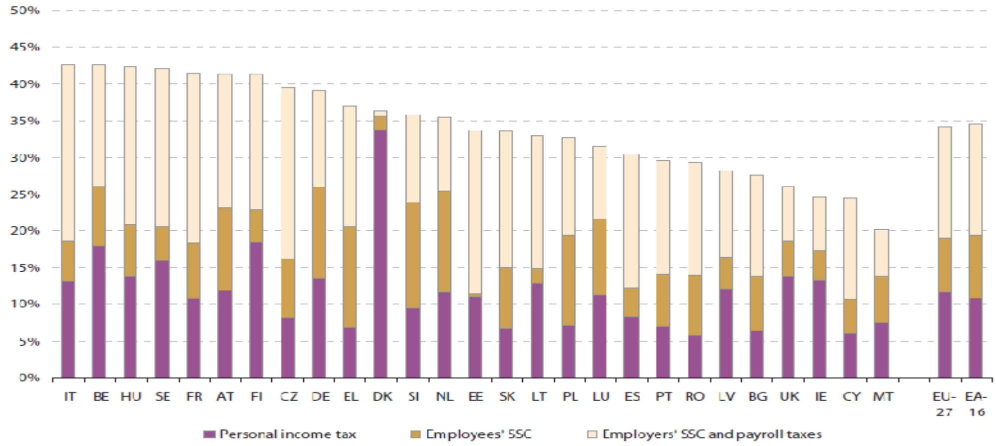
were adopted by Greece, France, Latvia, Portugal, Slovenia, Great Britain, Ireland; measures meant to decrease the labour tax rates were adopted by Austria, Germany, Denmark, France, Finland, Hungary, Latvia, Lithuania, Romania. Measures meant to increase the taxable base were adopted by states such as Denmark, Greece, Estonia, Spain, Ireland, Hungary, Portugal; measures meant to decrease the taxable base were adopted by Austria, Belgium, Bulgaria, Germany, Denmark, Finland, Hungary, Luxembourg, Holland, Poland, Portugal, Romania, Sweden. Fewer fiscal measures were adopted regarding the social contributions. The states which chose to apply measures meant to increase the social contributions rates were: Cyprus, Estonia, Portugal, Slovakia, Finland; the states which chose to decrease them were: Bulgaria, Czech Republic, Sweden. The enlargement of the taxable base was adopted by the following states: Bulgaria, Czech Republic, Estonia, Latvia, Lithuania and the narrowing of the taxable base was adopted by Finland.

The series of changes occurred during the period 2000-2008 had a very different effect upon the labour fiscality in the member states. The states of Central and Eastern Europe which joined the European Union in 2004 and 2007 faced a decline stronger than 4.4% of the labour tax rates, a decrease of 4.4%, while the average decrease of tax rates in the European Union was of 1.7%. The strongest diminution of these rates, of 11.1% was registered in Bulgaria and an increase of the rates was registered in Portugal (2.4%, Greece (2.5%), Spain (1,9%), Luxembourg (1.6%), Cyprus (2.9). During the period 2000-2008, in Romania, the labour tax rates decreased by 4%. (European Commission, Taxation trends in European Union, 2010: 107).

The international economic and financial crisis did not determine a decrease of the labour fiscality. If we analyze the situation in the member states, we can notice that the most significant decrease of the labour tax rates was registered in Denmark, Estonia, Romania, Ireland, Sweden, Bulgaria, Latvia and Lithuania. We can also notice that the taxation level in the three northern states is closet o the European Union average. The labour tax rates increased significantly in Cyprus, Portugal, Greece, below the European average in the case of the first two. The lowest labour tax rates are registered in Malta (20.2%), Cyprus (24.5%), Ireland (24.6%) and the highest labour tax rates are Italy (42.8%), Belgium (42.6%) and Hungary (42.4%).

If we analyze the salary tax evolution, we can notice that the decline of the tax wedge on the labour income is due to the decrease of the social contribution rates, as well as of the tax rates of the natural persons' income. The tax wedge is calculated by dividing the payroll tax, the social contributions paid by the employee and by the employer and other taxes to the total labour cost. The tax wedge supported by the employee and bt the employer for the labour force is quite high in the European Union and this represents one of the main causes for the poor performance concerning employment in the European Union.

Figure 2. The structure of the tax wedge – the level of labour taxation in 2008
(Implicit tax rate on Labour)(%)



Source: European Commission, Taxation trends in European Union, " Data for the EU member states, Iceland and Norway", 2010, p. 110

If we analyze the structure of labour taxation in the European Union, we can notice that its largest share is represented by the employer's compulsory social contributions, closely followed by the payroll taxes and the employee's social contributions.

Thus, in Denmark, Ireland and Great Britain, the largest share of the tax wedge on the labour income is represented by the payroll taxes and in states like Romania, Slovakia, Greece, the largest share is represented by the social contributions, the payroll tax representing less than 20%. The labour tax and the social contributions attenuate the economic fluctuations by decreasing the available income volatility. In many member states, the progressive character of the payroll taxes is often compensated by the regressive system of compulsory social contributions. The diminution of the tax wedge for the low wages increased the progressiveness of the tax wedge in the member states. The majority of the member states collect taxes on the natural persons progressive income. Seven member states apply progressive tax rates on the natural persons' income: Czech Republic, Bulgaria, Estonia, Latvia, Lithuania, Romania, Slovakia.

Table 1. The tax wedge on labour income – single worker with average income (% of the labour cost) in 2009

Country	Tax wedge	Income tax	Employee SSC	Employer SSC	Tax wedge	Income tax	Employee SSC	Employer SSC
	(1)	(2)	(3)	(4)	(1)	(2)	(3)	(4)
Belgium	55.2	21.1	10.7	23.3	-0.54	-0.50	0.00	-0.04
Hungary	53.4	15.9	12.8	24.6	-0.72	0.11	0.17	-1.00
Germany	50.9	17.3	17.3	16.3	-0.57	-0.52	-0.03	-0.03
France	49.2	9.9	9.6	29.7	-0.05	-0.05	0.00	0.00
Austria	47.9	12.1	14.8	17.8	-0.91	-1.05	-0.02	0.10
Italy	46.5	15.0	7.2	24.3	-0.03	-0.03	0.00	0.00
Sweden	43.2	13.9	5.3	23.9	-1.65	-1.11	0.04	-0.57
Slovenia	42.9	9.3	18.9	14.7	-0.52	-0.20	0.00	0.30
Finland	42.4	18.6	5.1	18.7	-1.39	-0.88	0.14	-0.66
Czech Republic	41.9	8.3	8.2	25.4	-1.55	0.05	-1.05	-0.55
Romania	41.7	8.8	12.3	20.6	-1.65	0.31	-1.03	-0.93
Lithuania	41.7	15.6	2.3	23.8	-1.30	-1.30	0.00	0.00
Latvia	41.6	14.9	7.3	19.4	-0.81	-0.81	0.00	0.00
Greece	41.5	7.1	12.5	21.9	-0.06	-0.06	0.00	0.00
Estonia	39.5	12.6	2.0	25.0	-0.56	-0.56	0.00	0.00
Denmark	39.4	29.1	10.3	0.0	-1.20	-1.25	-0.03	0.00
Spain	38.2	10.3	4.9	23.0	0.19	0.33	0.01	-0.15
Netherlands	38.0	15.1	13.8	9.1	-0.96	1.18	-1.06	-0.29
Slovak Republic	37.6	6.3	10.6	20.8	-1.17	-1.17	0.00	0.00
Portugal	37.2	9.1	8.9	19.2	-0.07	-0.07	0.00	0.00
Bulgaria	35.1	7.2	10.8	17.1	-1.37	0.27	0.78	-2.42
Poland	34.0	5.6	15.5	12.9	-0.52	-0.52	0.00	0.00
Luxembourg	34.0	12.7	10.9	10.3	-1.16	-1.59	0.08	0.35
United Kingdom	32.5	14.6	8.3	9.6	-0.34	-0.21	-0.06	-0.07
Ireland	28.6	12.9	6.0	9.7	1.54	0.35	1.18	0.00
Malta	22.8	8.7	7.0	7.0	-0.81	-0.07	-0.74	0.00
Cyprus	13.9	2.1	5.9	5.9	-0.21	-0.21	0.00	0.00
EU27	39.7	12.4	9.6	17.6	-0.69	-0.36	-0.09	-0.22

Source: European Commission, Taxation Papers, Monitoring tax revenues and tax reforms in EU Member States 2010," Tax policy after the crisis", Working Paper nr. 24, 2010, pp. 84

A research conducted by the World Bank in eight member states: Czech Republic, Estonia, Latvia, Lithuania, Poland, Slovakia and Slovenia concerning the relationship between the tax wedge on labour income and the employment level revealed that there is an inverse relationship between the tax wedge and employment. Is was also revealed that the labour force structure – with many unskilled workers, compulsory minimum wages, high level of labour taxation and progressive fiscal systems have worse effects on employment than in the rest of the European Union member states. (World Bank, EU-8 Quarterly Economic Report, 2005:12).

In the case of low-wages category, it is important to analyze the stimulants offered by the employees. In this respect, two indicators were developed: *the effective marginal tax rate* and *the effective average tax rate*, in order to study the effect of wage modifications. If the first rate takes into account the marginal modification of salary income, the second takes into account the salary changes implicit to the transition from unemployed to employed. The effective average tax rate is a specific concept of unemployment or inactivity; it is used to monitor the labour market distortions, especially regarding financial constraints in order to gain access to a job.

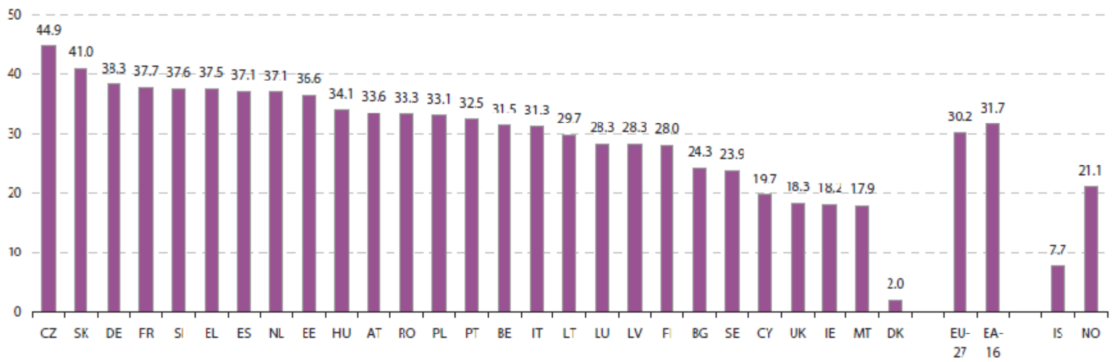
It is also obvious that an increase of the tax wedge has a stronger negative effect on the employment level in the case of workers with a lower qualification level. A research conducted in Belgium, Holland and France confirms this observation since a decrease of fiscality for the low-income workers led to a considerable increase of the employment level.

3. Aspects regarding the importance of compulsory social contributions to the formation of public income in the EU

The share of fiscal revenues from direct taxes, indirect taxes and social contributions is relatively close in the old member states of the European Union in comparison with the new member states, which register a lower level of income from direct taxes. The low level of income from direct taxes is compensated by more significant shares of the social contributions or indirect taxes. While in some states such as Bulgaria, Romania, Malta and Cyprus the most significant share of the budgetary income is represented by the income from indirect taxes, in other states like Czech Republic, Slovakia, Germany and France, the income from social contributions is high. At the opposite side are Denmark, Ireland and Great Britain, states which collect relatively low income from social contributions. The motivation for the very low level of social contributions in Denmark is the fact that its social expenditures are not financed by the social insurance budgets, but by income from general taxes. This explains the very high level of direct taxes, one of the highest in the European Union.

If we analyze the evolution of the budgetary income, we can notice that in time most of the states changed the structure of he budgetary income. For example, in case of Latvia and Slovenia, the increase of the share of the direct taxes was compensated by a decrease of the social contributions and of indirect taxes. In Sweden, the increase of the share of indirect taxes meant a decrease of the share of direct taxes and social contributions in the total income. In Greece, the decline of direct and indirect taxes was completed by an increase of the social contributions rates.

Figure 3. The share of social contributions in the total tax wedge (%) in 2008



Source: European Commission, Taxation trends in European Union, " Data for the EU member states, Iceland and Norway", 2010, p. 68

In Austria, the most important share of the tax wedge is represented by the social contributions. The social contributions rate supported by the employees is approximately 18%, the social contributions rate supported by the employer is 21.5%, and in case of income earned out of independent activities, the social contribution rate is 25%.

In 2010, the total social contributions collected in Bulgaria reached almost 28.5% of the income, out of which the most important part was represented by the contributions to social insurances – pensions – which decreased in 2010 from 18% to 16%, decrease compensated by an increase of the direct tax rates.

In Czech Republic, the most important source of budgetary income is represented by the social contributions (44.9% of the total collected income). The level of income from social contributions is the highest of the European Union, followed by Slovakia and Germany. Taking into account this aspect, the income from direct and indirect taxes is under the European Union average. The social contribution rate owed by the employees is 11%, out of which 6.5% for the social insurances – pensions and 6.5% for social health insurances. The social contributions rate owed by the employer is 34% of the gross income. In Finland, the social contributions level owed by the employer is 28%.

The level of social contributions owed by the employer registered in France in 2008 was the second in the European Union after Czech Republic. The social contribution rate owed by the employer is high in France, amounting to 35%-45% of the income in comparison with the contributions owed by the employees which amounts to 14% (European Commission, Taxation trends in European Union, 2010: p. 160-272).

In Sweden, the social contributions have the lowest share in the total budgetary income. In Sweden, most of the social contributions is paid by the employers (31.42%). The employees pay an additional rate of 7% for the social insurances. In order to facilitate youth employment, the employers benefit from a reduced rate of social insurance for people under 26.

In Ireland, the share of social contributions to the total income is not significant – only 18.2% because of the very low level of labour taxation in comparison to the European Union average. The increase of labour tax rate starting with 2000 was balanced by the decrease of the social contributions level. The contribution paid by the employers is 10.75%, with a reduced rate of 8.5% for those with low income (lower than 352 euros per week) and the contribution supported by the employees is 4% of the gross income. Given the very low level of social contributions rate in Great Britain, the income from this source represents a small share of the total budgetary income.

In Malta, the level of social contributions os very low, much under the European Union average. The income from this source had a declining evolution during the period 2000-2008, registering the lowest level of all the member states. The workers of Malta, the employers and the government contribute equally to the social security fund with 10% of the basic salary.

In Holland, the three important sources in the income formation have equal shares. The social security system is composed of the public insurance and the employees' insurance. The first category is financed by all the members of the society, while the second category is supported by the employers according to the economic sector in which they work. The employees' social contributions rates are identical to those of the employers.

Romania is the fourth country in terms of the importance of income from direct taxes to the total budgetary income after Bulgaria, Cyprus, Malta. In 2008, the level of budgetary income increased with almost 29% in comparison with 2007. This increase of public income came from the increase of income from: income tax -23.6%, natural persons' income tax – 27.8%, VAT – 30.8%, excizes – 8.7% and social contributions – 24.7% (Mara Eugenia Ramona, Inceu Adrian, Cuceu Ionuț, Achim Monica Violeta, 2009: 3). This confirms the importance of social contributions to the formation of public income. The obligation to pay the rate of social insurance belongs to the employer (20.8%) and to the employee (10.5%) in normal working conditions. If the employee develops his activity in higher risk conditions, the contribution rate paid by the employer increases by 5%; for particular working conditions the total contributions rate is 36.3% and for special working conditions, the total contributions rate is 41.3%.

Examining in general the main sources of budgetary income formation in the European Union in 2008, we can notice a quite balanced situation, the social contributions having the smallest share in the total income (12.6% of GDP), in comparison with the direct taxes (13.5% of GDP) and the indirect taxes (31.4% of GDP).

4. Conclusions

In the current context of the financial crisis it is absolutely necessary to compare the evolution of labour fiscality and the effect of the growth of public debts on the tax wedge on labour income. In a research conducted by the European Central Bank, it was revealed that in the majority of the states which registered an increased of the public debt, the labour taxation increased - Greece, Italy and France being relevant examples in this respect.

Despite the fact that some states have low labour taxes, the labour fiscality remains high in the European Union in comparison with other industrialized economies. The increase of the fiscality level for the labour income determines the decrease of the employment rate and the raise of the unemployment rate. The solution to guarantee a higher employment rate could be the relaxation of the labour fiscality. Some specialists consider that fiscal neutrality in the field of labour fiscality could be realized by transferring the tax wedge on the labour income towards property or energy taxation.

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