



Session 2

Quality public finances, fair and progressive taxation, good governance in tax administration

Introduction to current trends and challenges in the area of taxation systems and policies. Trade union perspectives.

PERC-EPSU meeting on the development of quality public services in Eastern Partnership countries, Russia and Central Asia

19 December 2012



Eastern Europe in a comparative perspective

- The OECD/IFI policy reform package
- Overview of national tax systems
- Focus on personal income tax & on social security contribution
- Post-crisis fiscal consolidation
- Tax evasion & Financial speculation

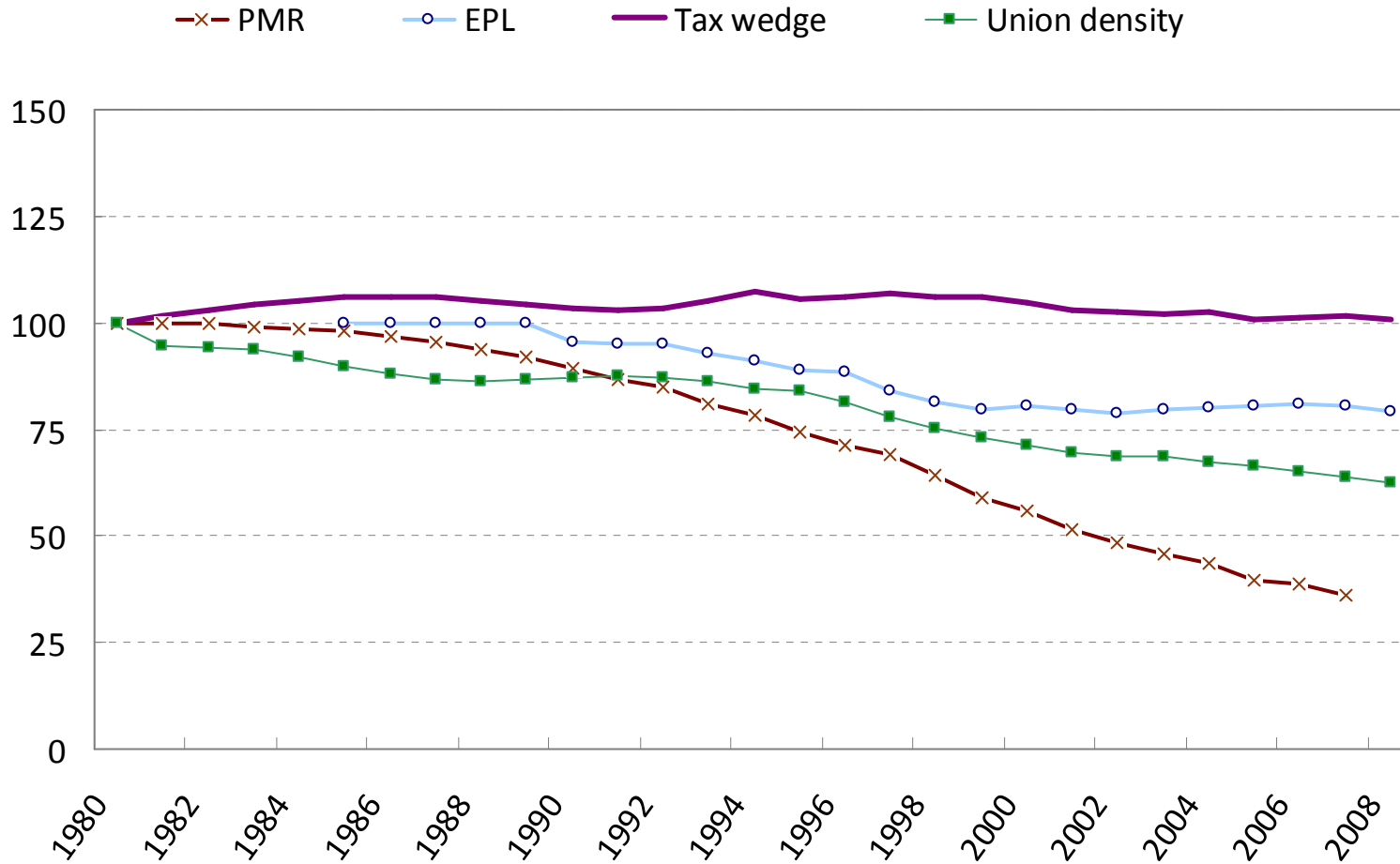
“Redistribution systems were generally effective at slowing trends towards widening income gaps which were due to falling incomes at the bottom.

Tax-benefit systems, however, were less successful at offsetting growing inequality in the upper parts of the distribution, which became a more powerful driver of inequality trends in some countries.”

(Divided We Stand, OECD, 2011)



Developments in product market regulation, employment protection legislation, tax wedges and union density, OECD average, 1980-2008 (1980=100)



Shifting from distributive justice to private sector growth & competitiveness objectives.

- 2009 edition of OECD's flagship publication, 'Going for Growth'
- IMF article IV reports
- WB Doing Business ranking

Avoiding distorting business choices

Shift the tax structure from mobile income taxes:

- Corporate income, high personal income, dividends and capital gains are those most affected by globalisation
- and which taxation must reduce to limit the risk of tax arbitrage

To less mobile taxes:

- lower-skilled workers and consumption
- Property



OECD principles

Key recommendations

- Increasing and broadening VAT and property taxes.
- Reducing (or maintaining) corporate and personal income taxation
- as well as employer social security contributions (hand in hand with public cuts or privatisation)
- Taxing capital income (interest, dividends and capital gains) at lower rates than labour income
- reducing tax expenditures
- Improving tax administration

Impact on inequality

- OECD concedes that its reform package would “reduce progressivity” but offers a solution to deal with the trade-off

OECD country recommendations in 2011

Reduce PIT

- Austria, Australia, Finland, Italy, Norway, Poland, Denmark, Sweden, and the US;

Reduce PIT targeted at lower incomes, lone parents or second earners

- Canada, Netherlands, the UK, Germany, Ireland, Netherlands and the Slovak Republic;

Reduce tax on labour or on low-income earners (financed by public cuts)

- Belgium, the Czech Republic, Greece and Turkey;

Reduce employer social security contributions

- Germany, Hungary, Poland, and the Slovak Republic;

Reduce corporate income tax

- Japan

Reduce capital income taxation

- Canada

Raise property taxes

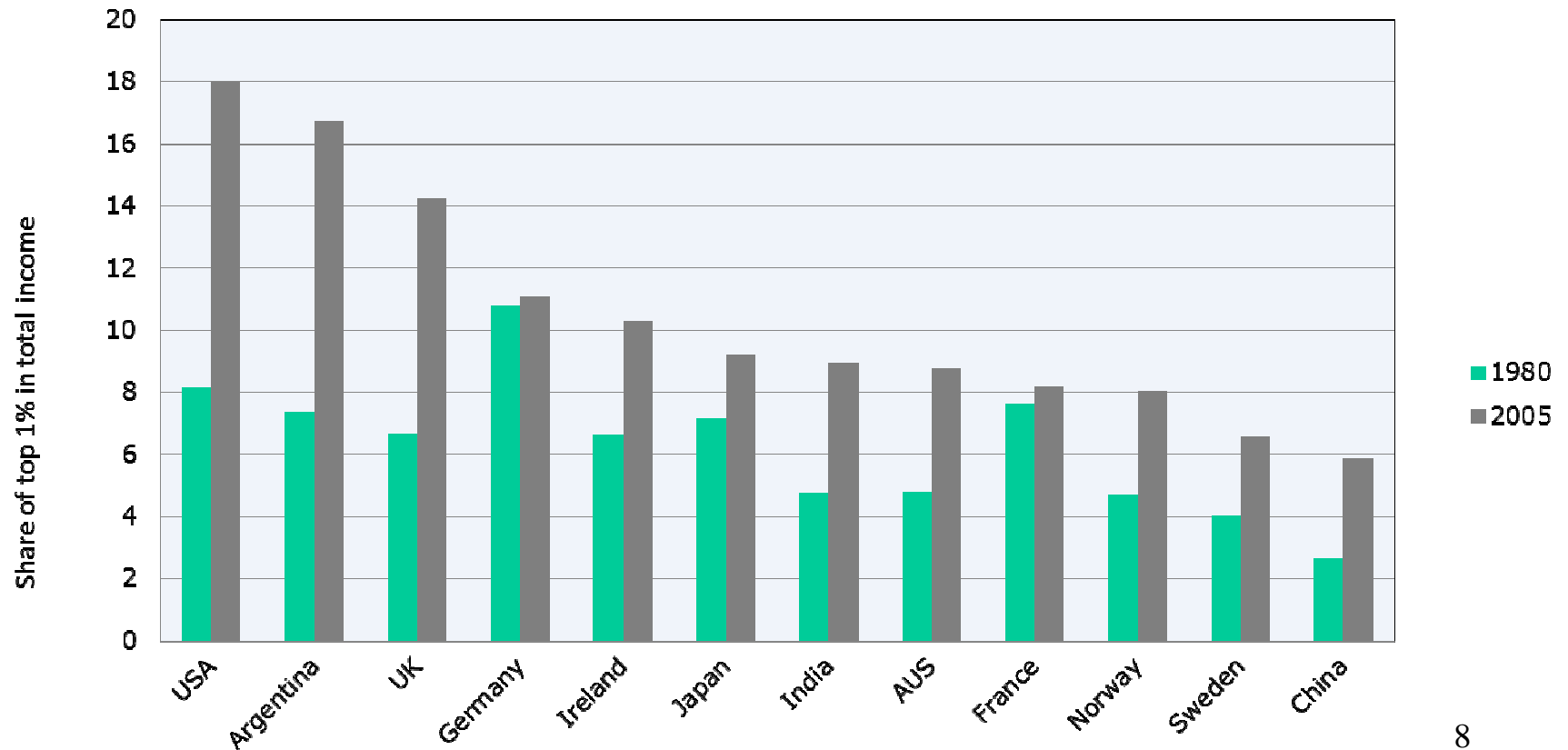
- Denmark, Finland, Japan and Sweden

Raise, introduce or broaden consumption-related taxation, such as VAT

- Mexico, Netherlands and the US.

OECD concedes that its reform package would “reduce progressivity” but offers no solution to deal with the trade-off

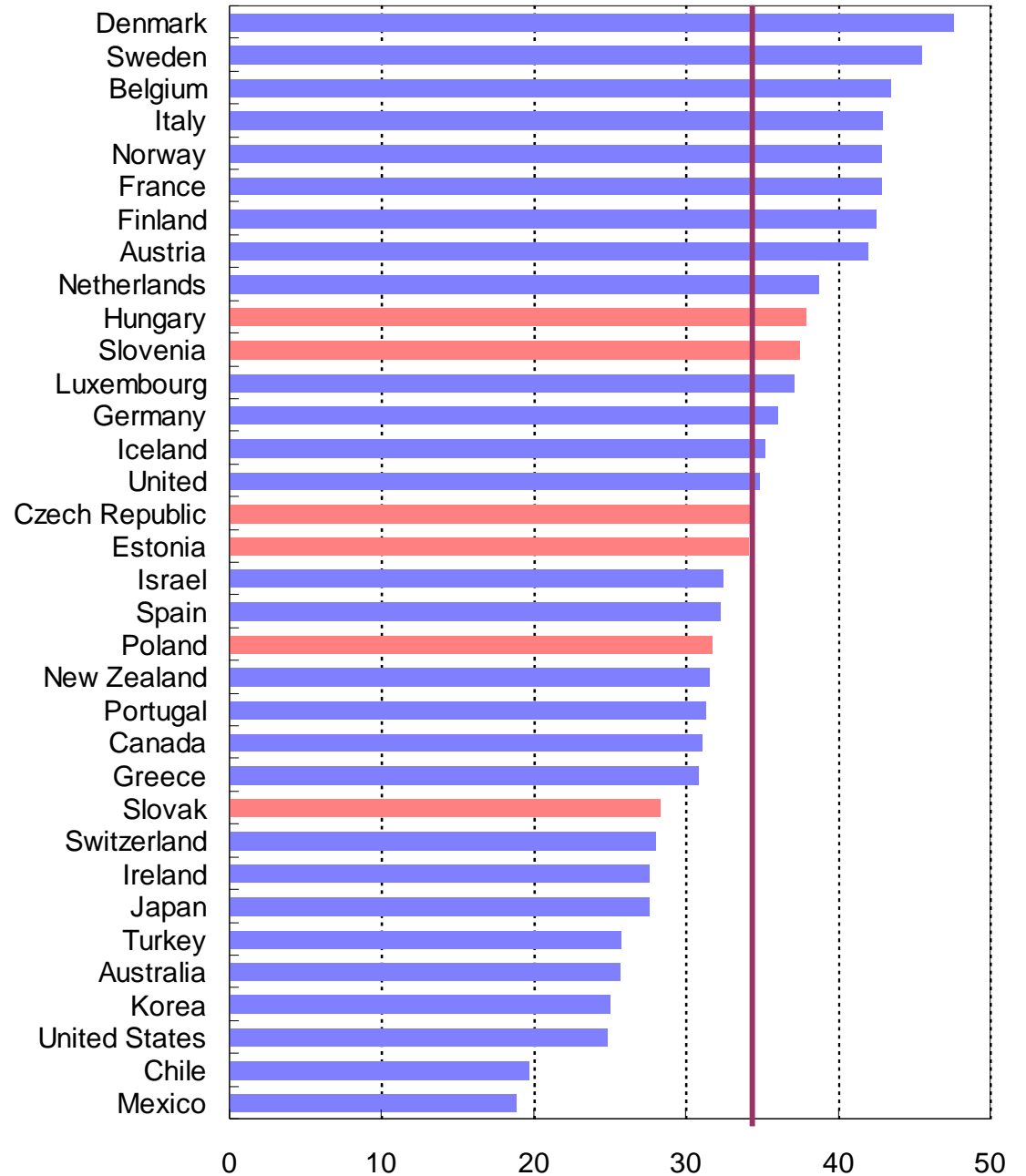
Top 1% income shares (1980, 2005)



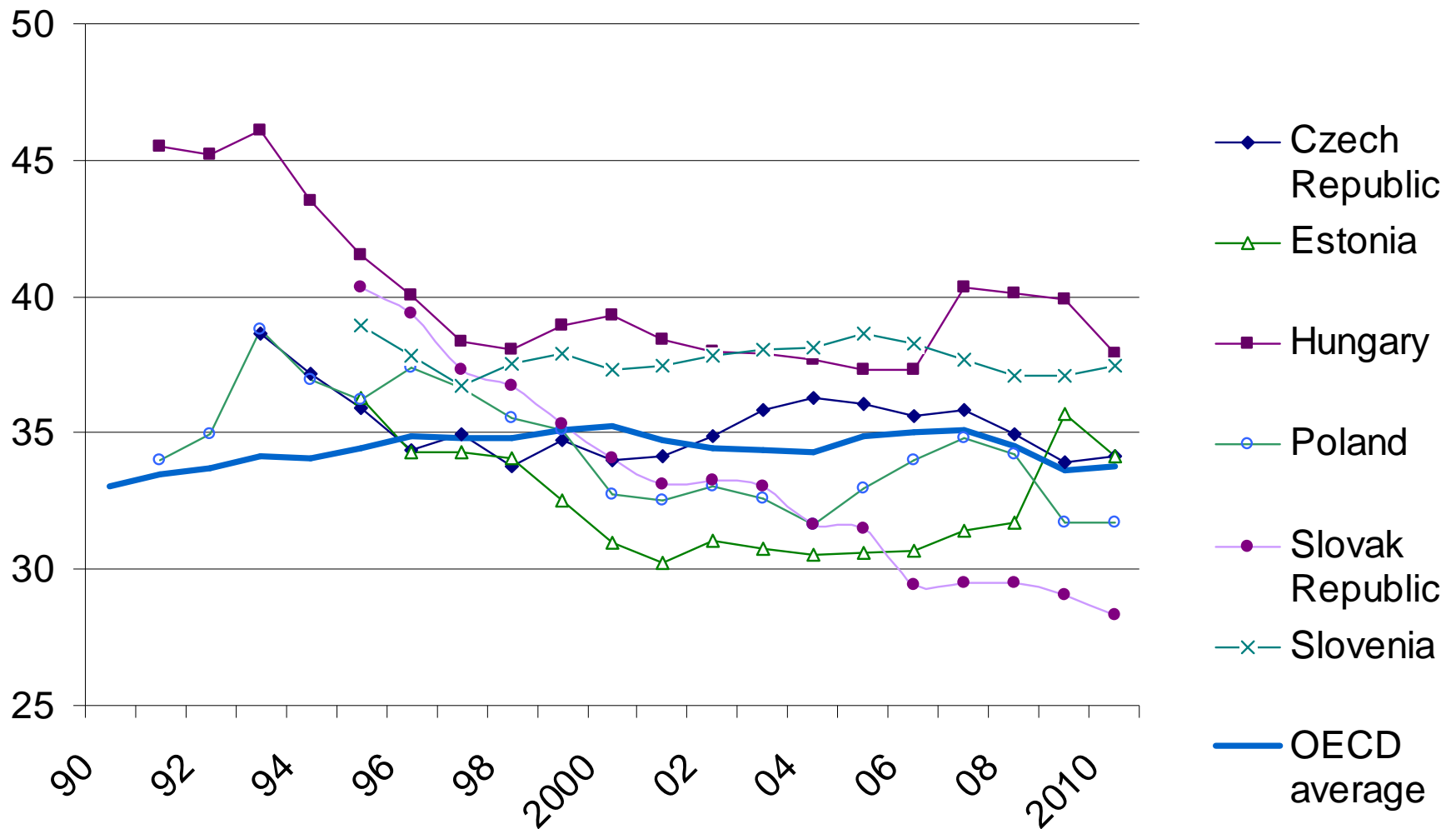
Source: Atkinson and Piketty (2007)



Total tax revenue, GDP % 2010



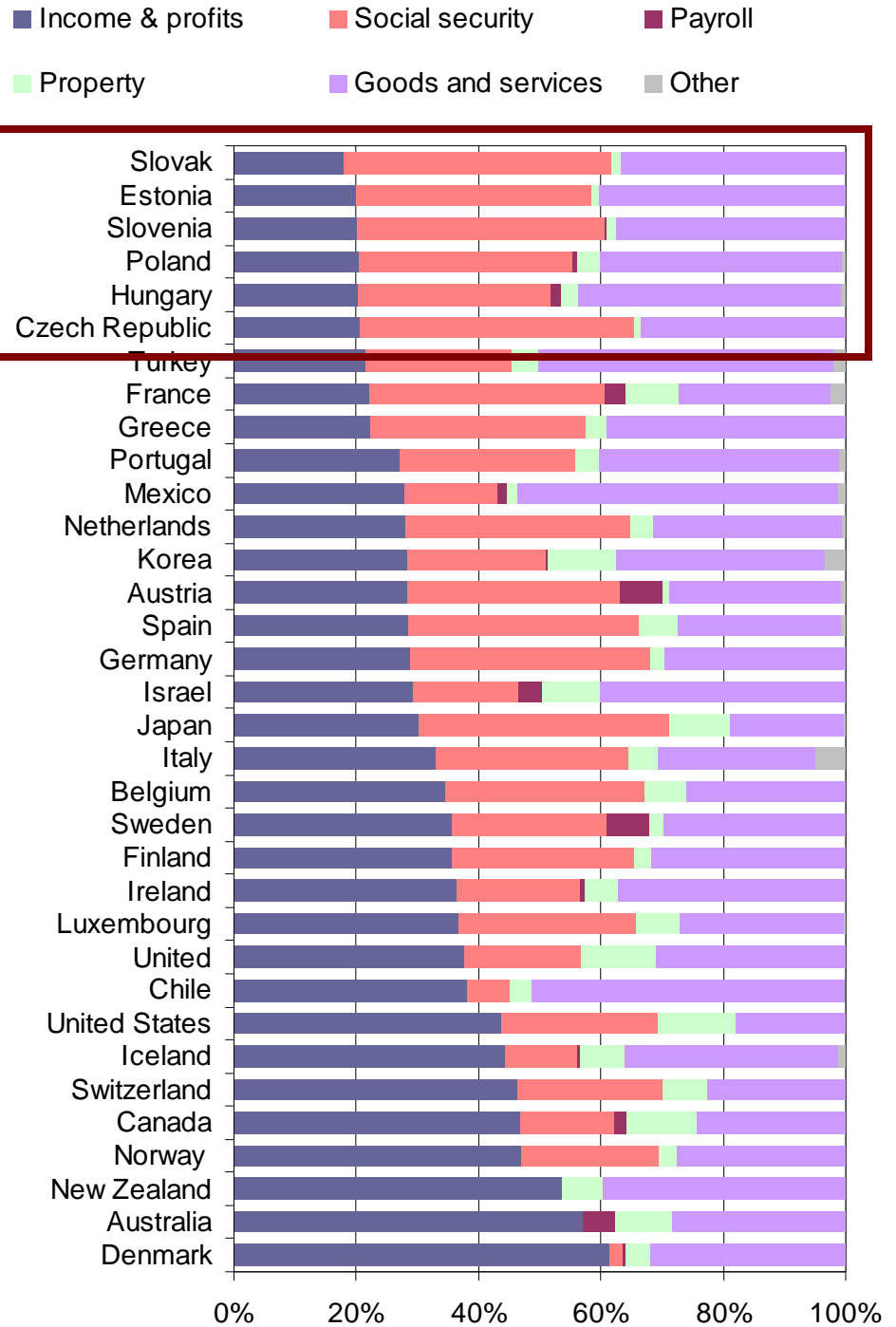
Total tax revenue, GDP % 1990 - 2010



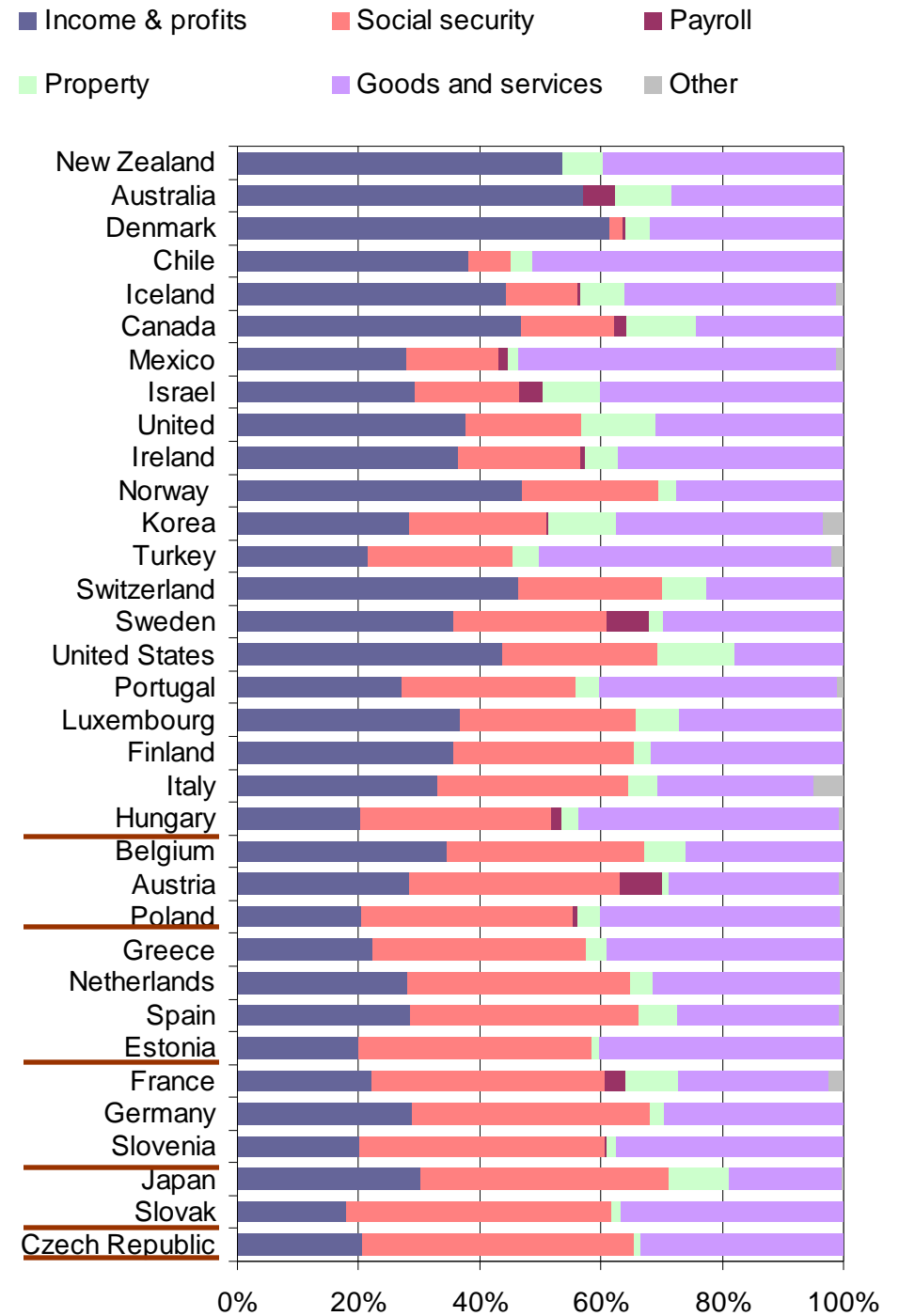


Tax revenue of main headings as percentage of total tax revenue

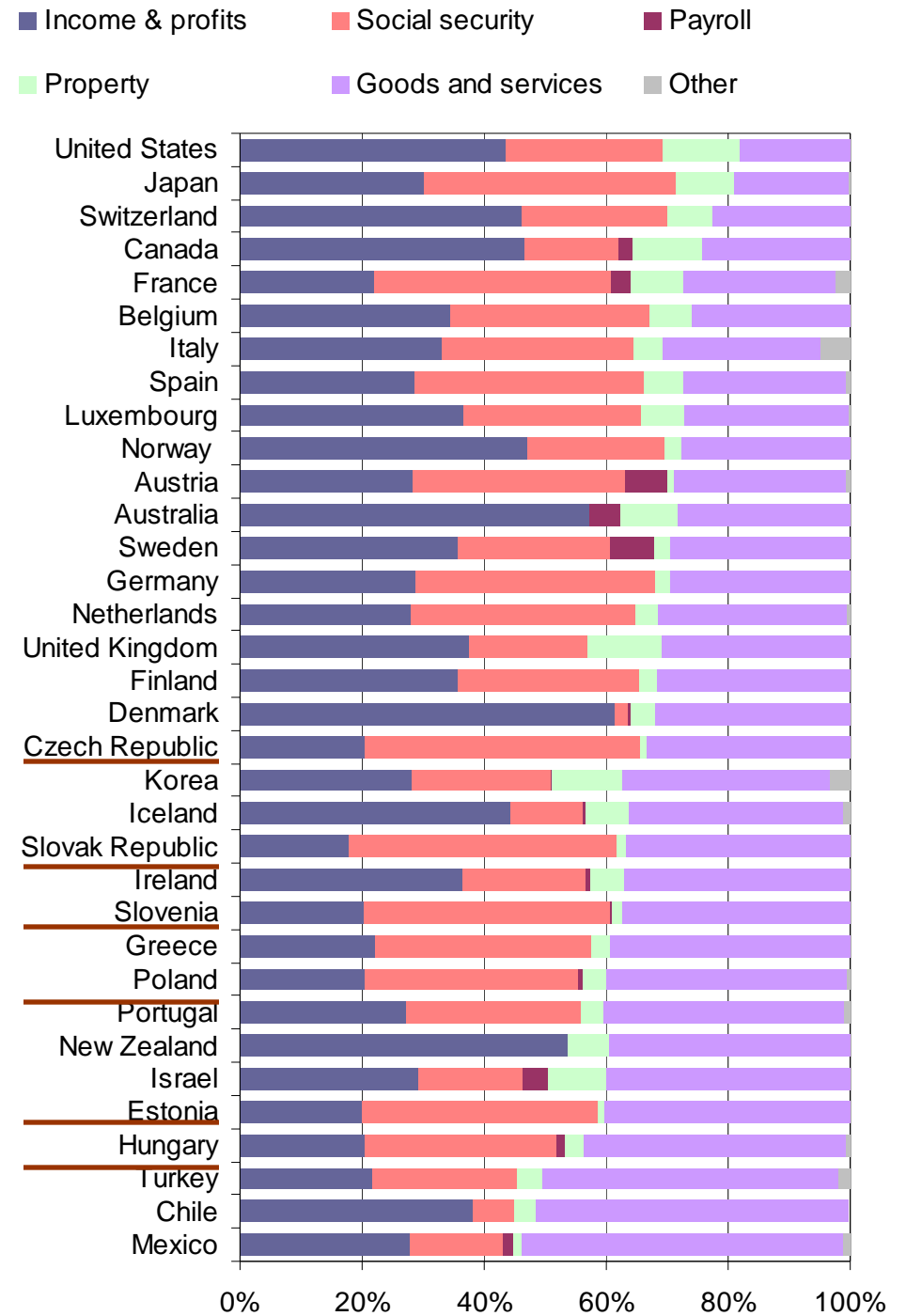
Ranking per income & profits



Ranking per social security

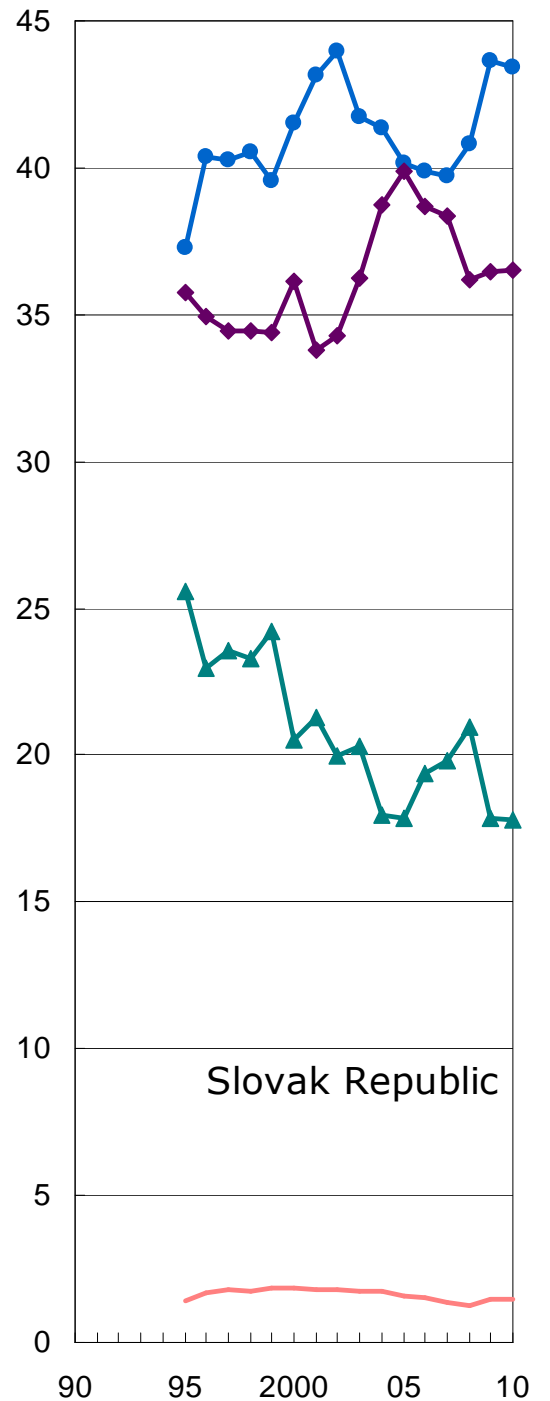
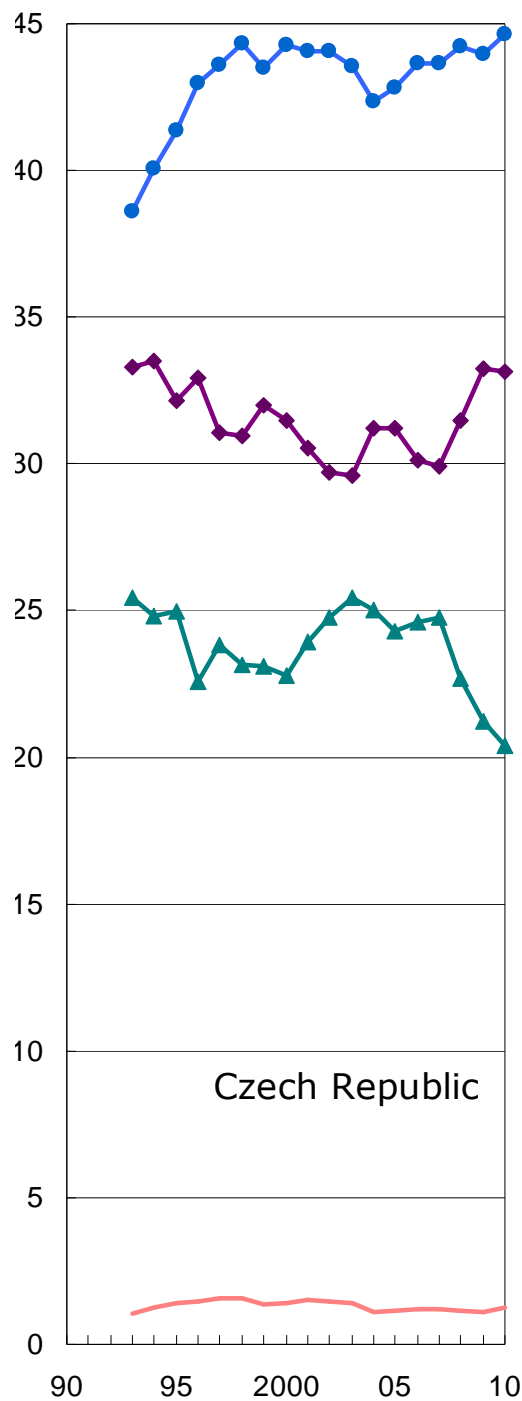
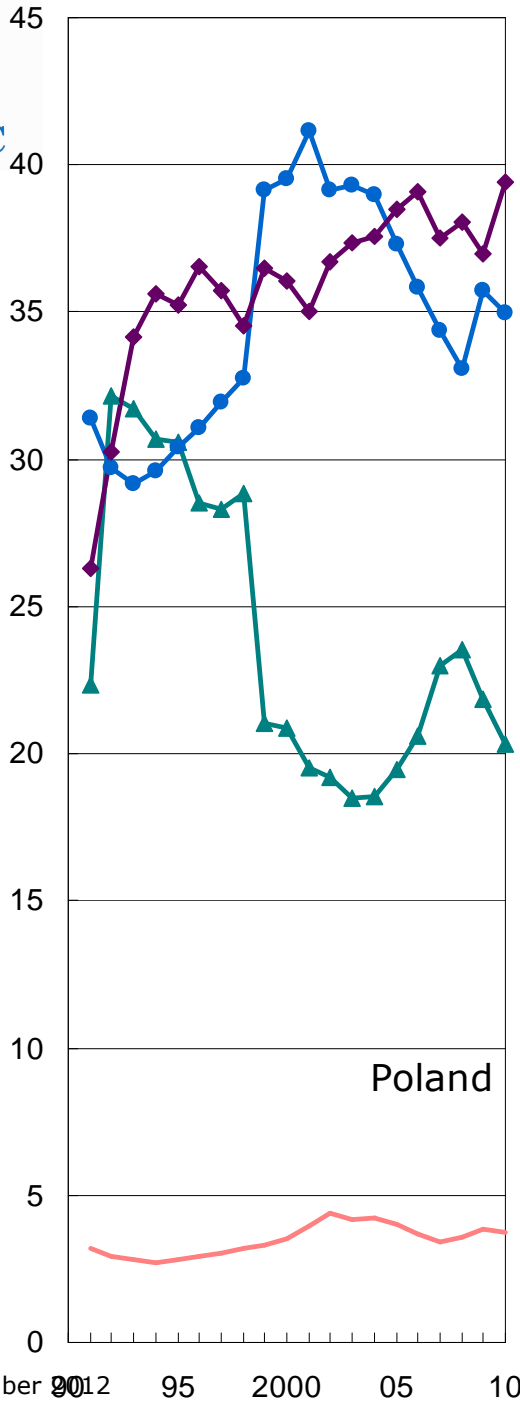


Ranking per goods & services



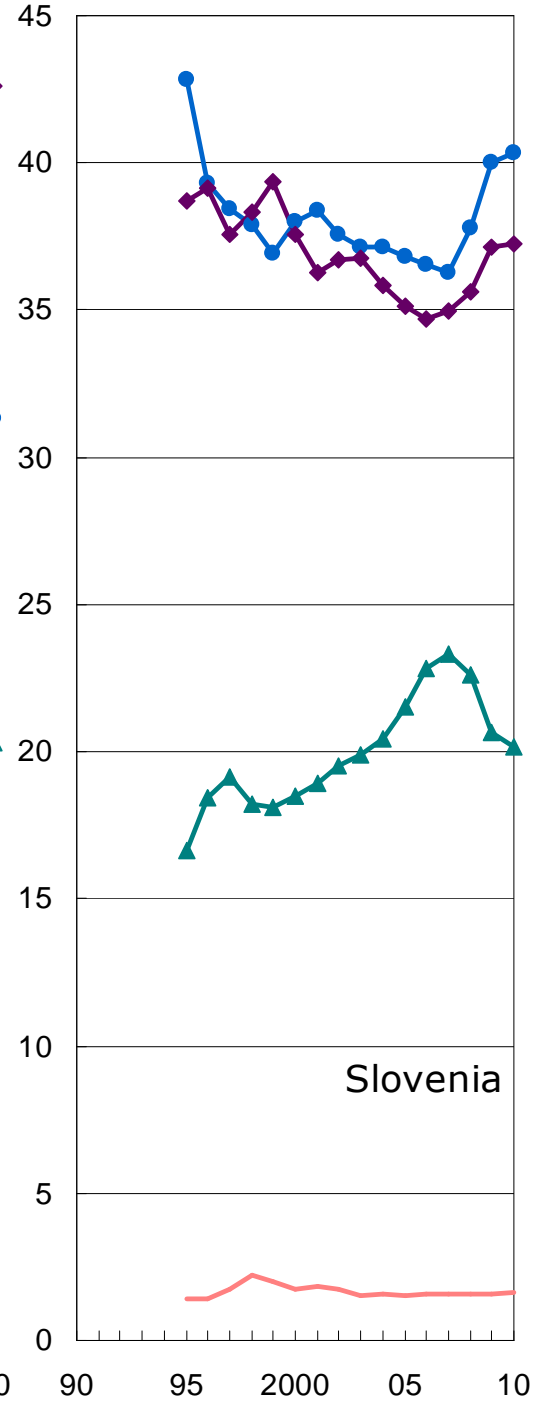
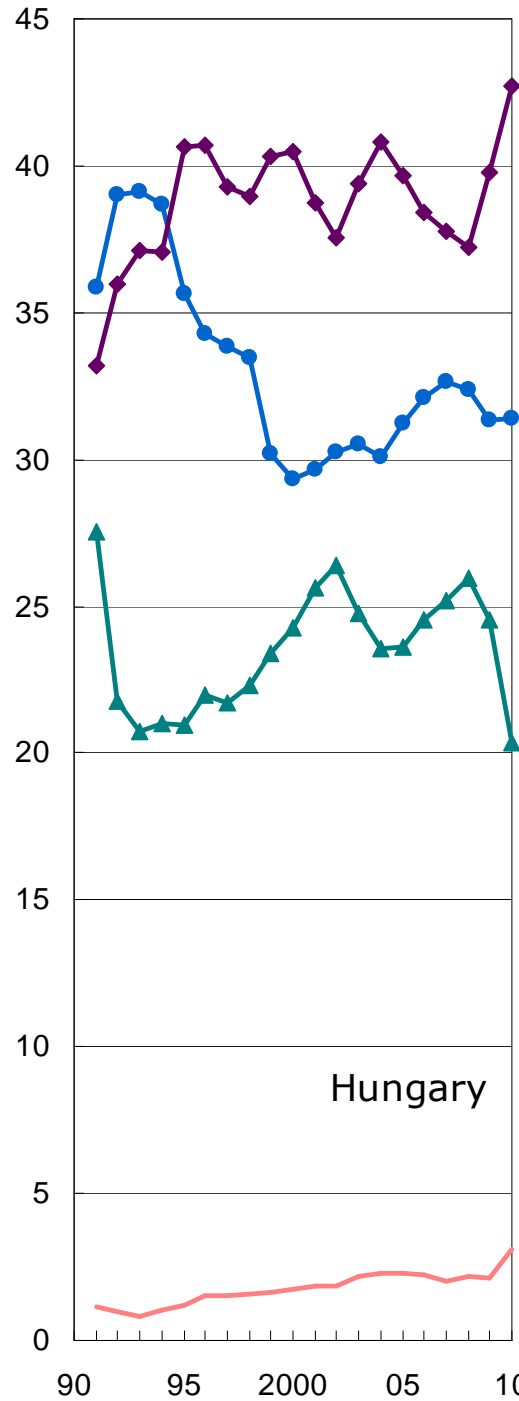
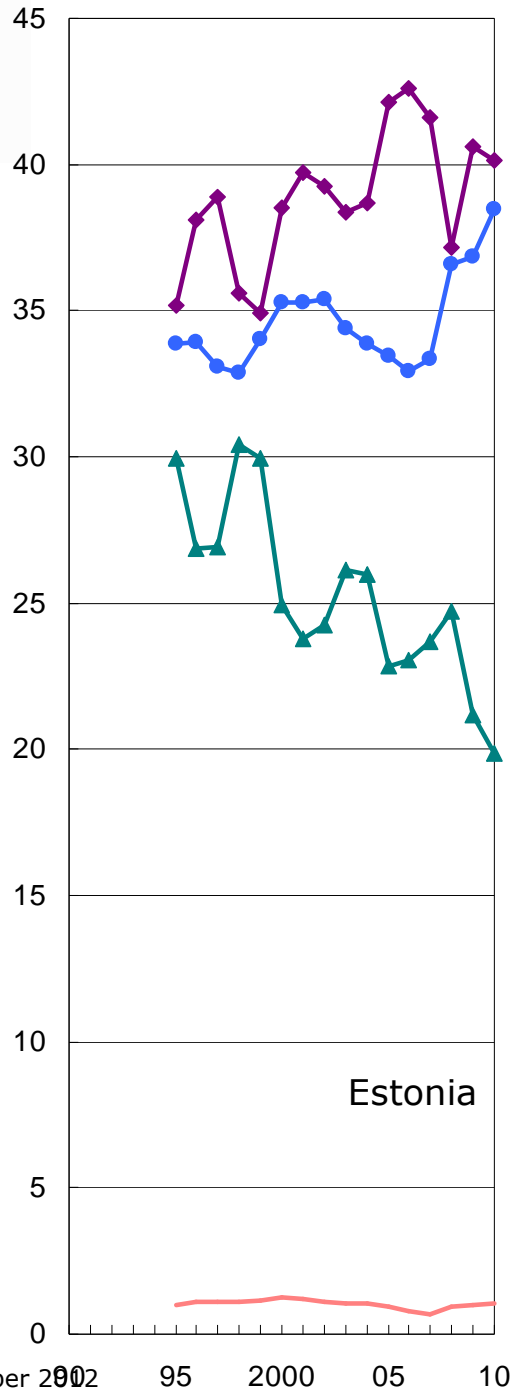


- Income & profits
- Social security
- Property
- Goods & services





- Income & profits
- Social security
- Property
- Goods & services



Over the last decade, reductions in

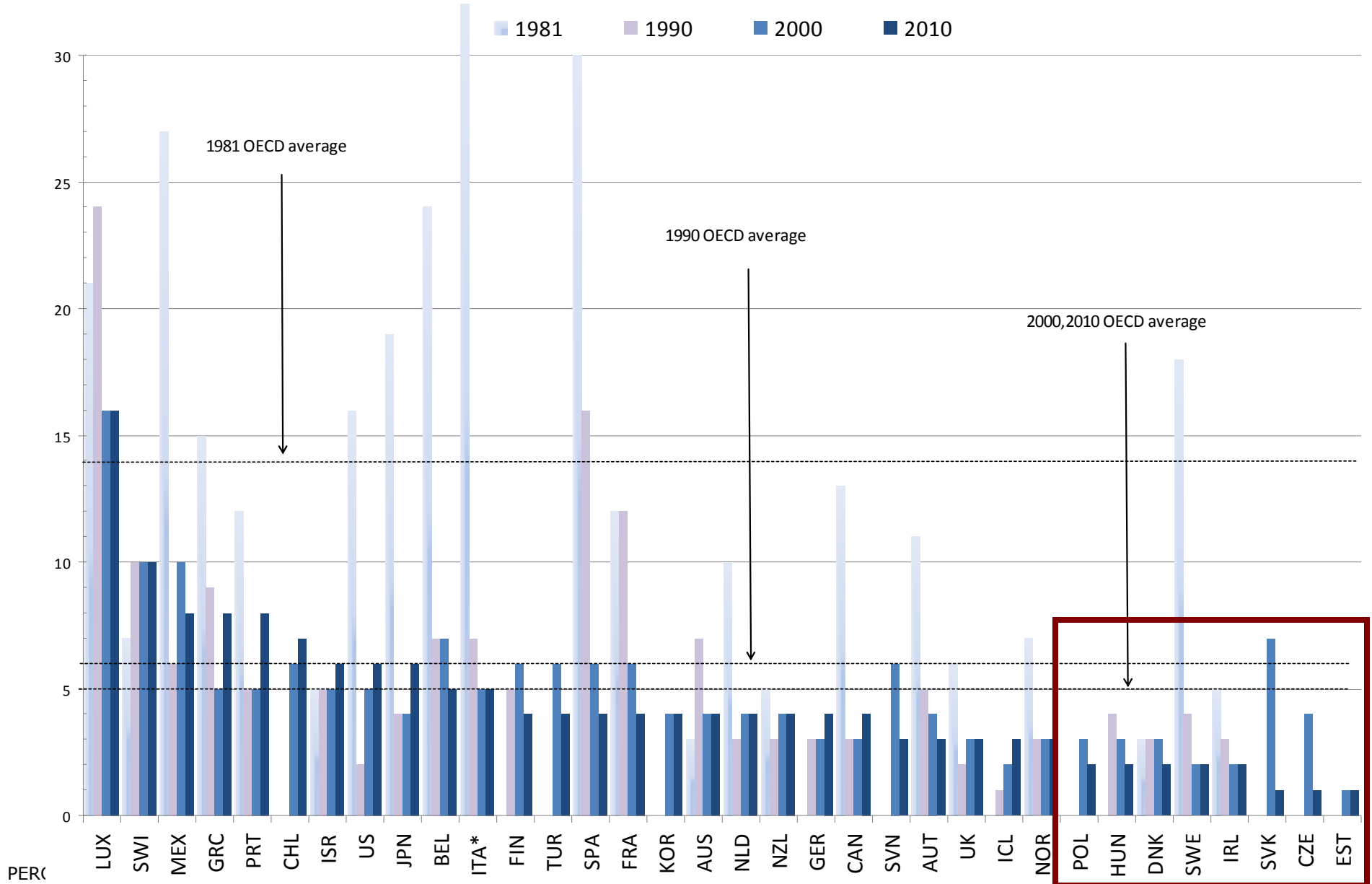
- the number of tax brackets
- the top statutory PIT rate
- the threshold at which the top rate applies.

No clear trend regarding

- the bottom statutory rate
- the level of earnings at which taxpayers start paying

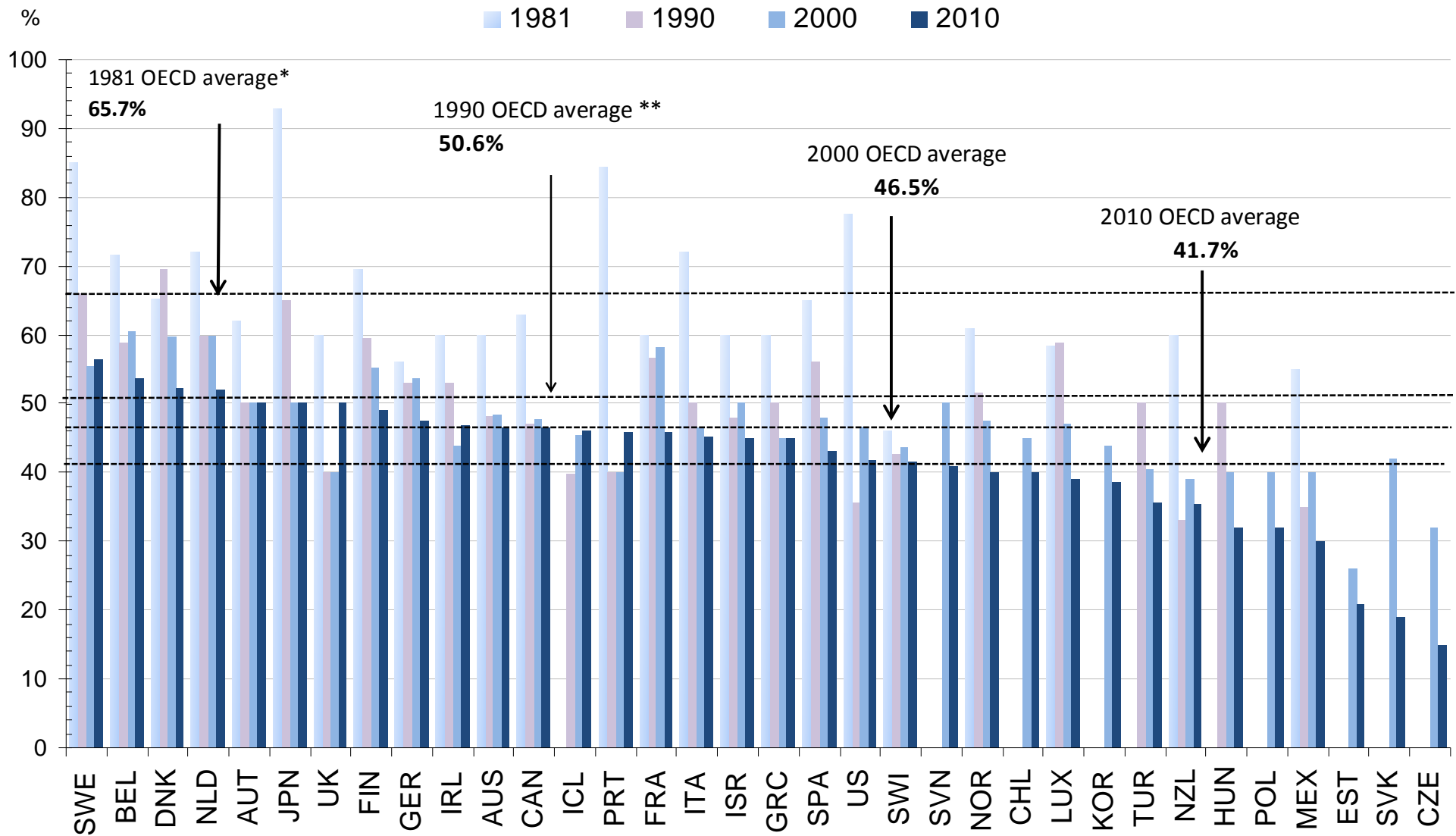
But all OECD countries exempt an initial portion of earnings

Number of Personal Income Tax Brackets

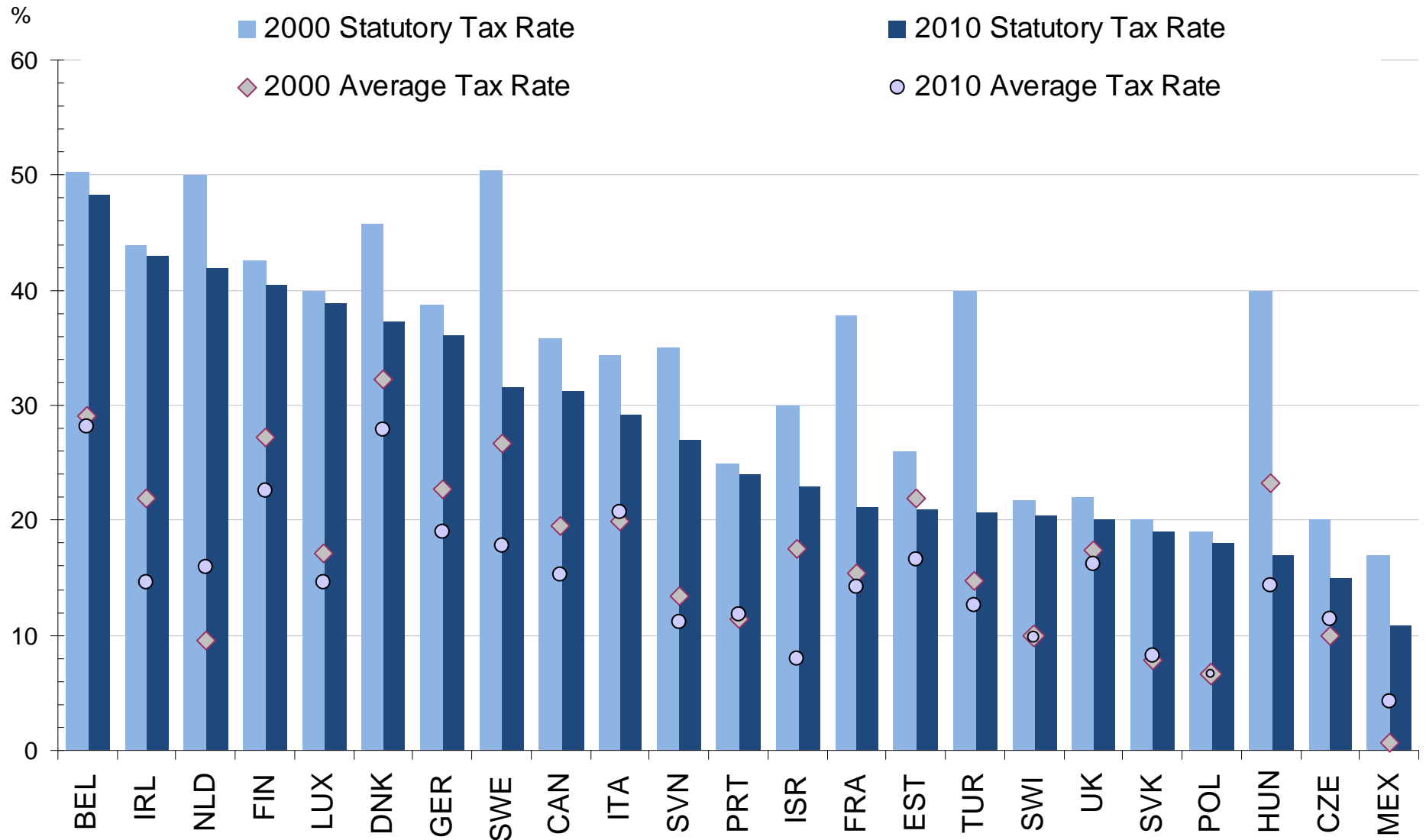




Top combined statutory personal income tax rate



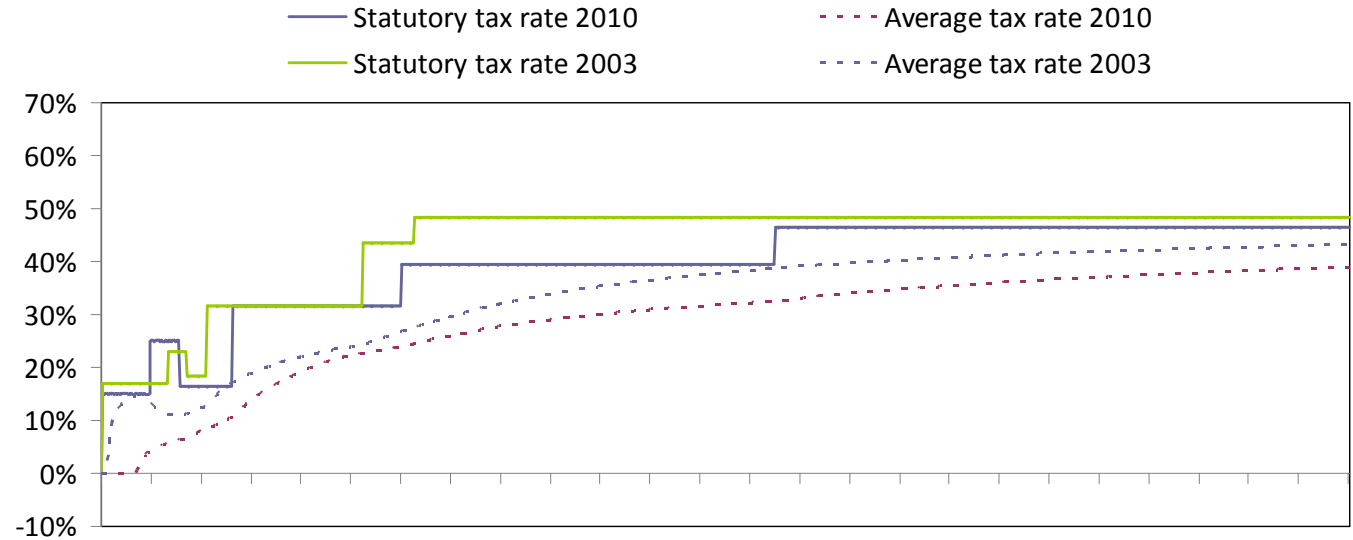
Personal Income Tax Rates, statutory vs average (single childless individual)





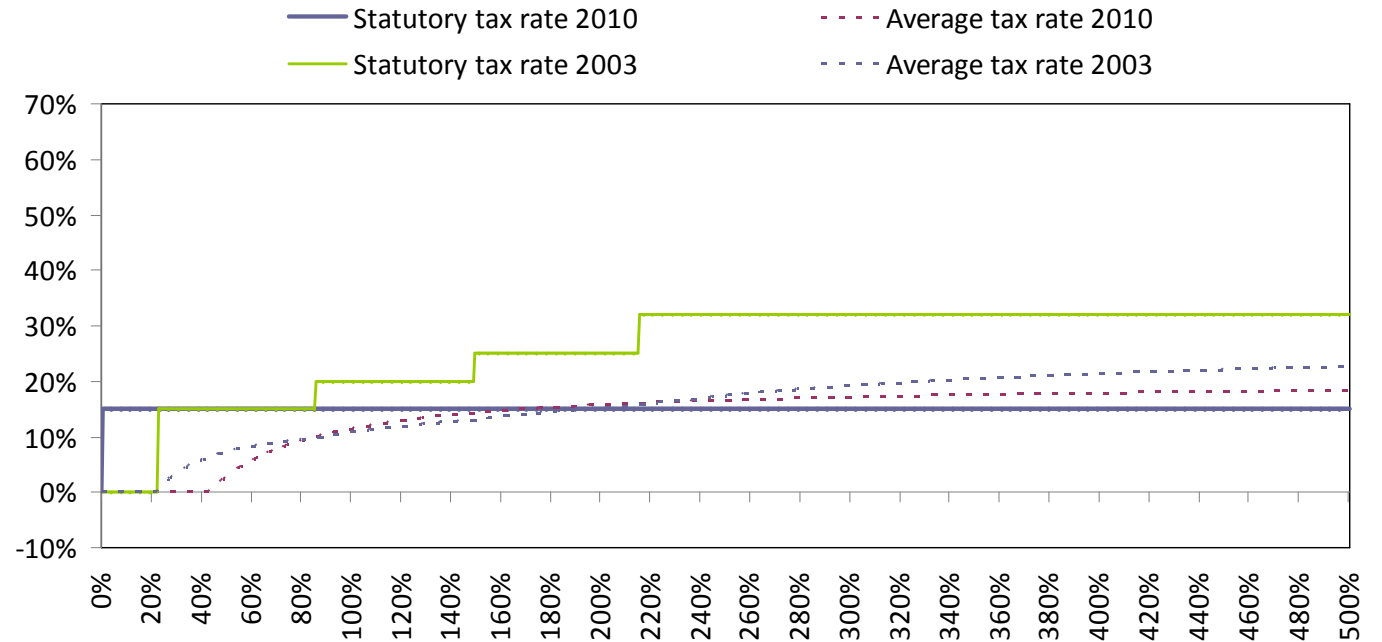
Australia: 2003, 2010

Income tax rates by level of gross earnings expressed as a % of the average wage



Czech Republic: 2003, 2010

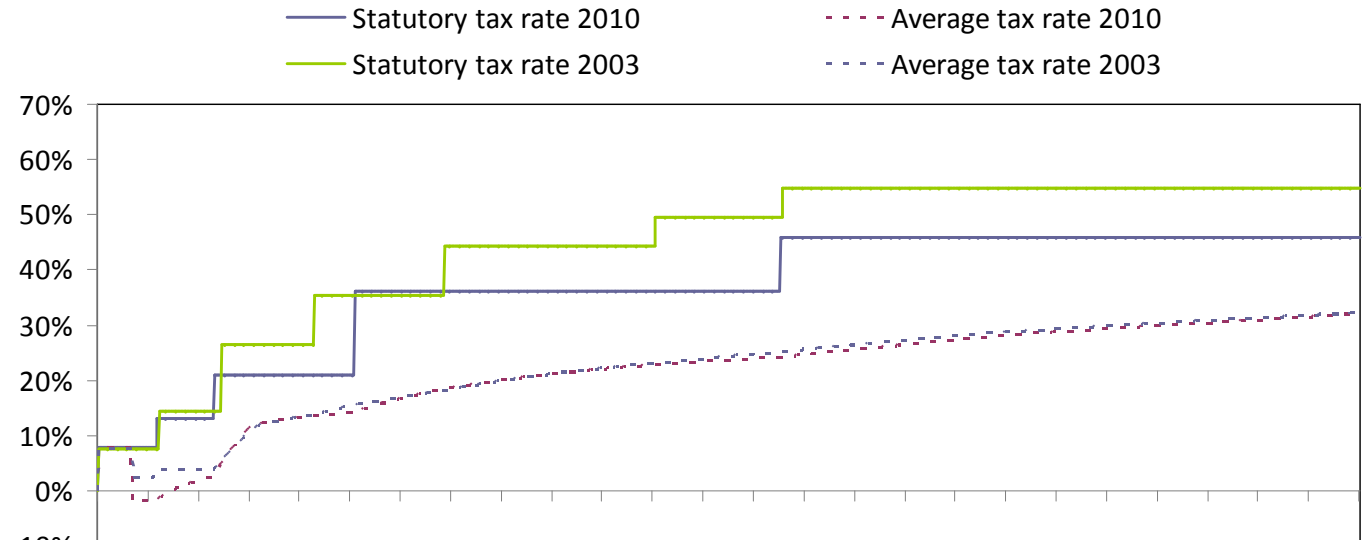
Income tax rates by level of gross earnings expressed as a % of the average wage





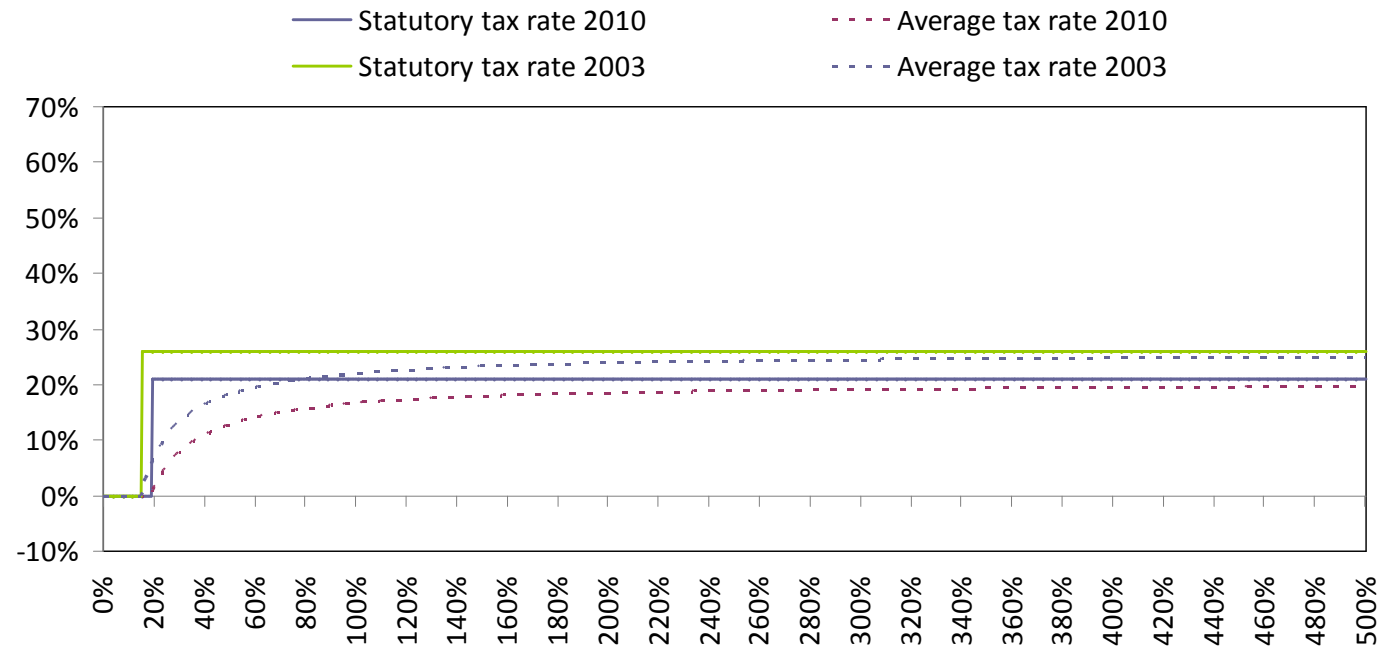
France: 2003, 2010

Income tax rates by level of gross earnings expressed as a % of the average wage



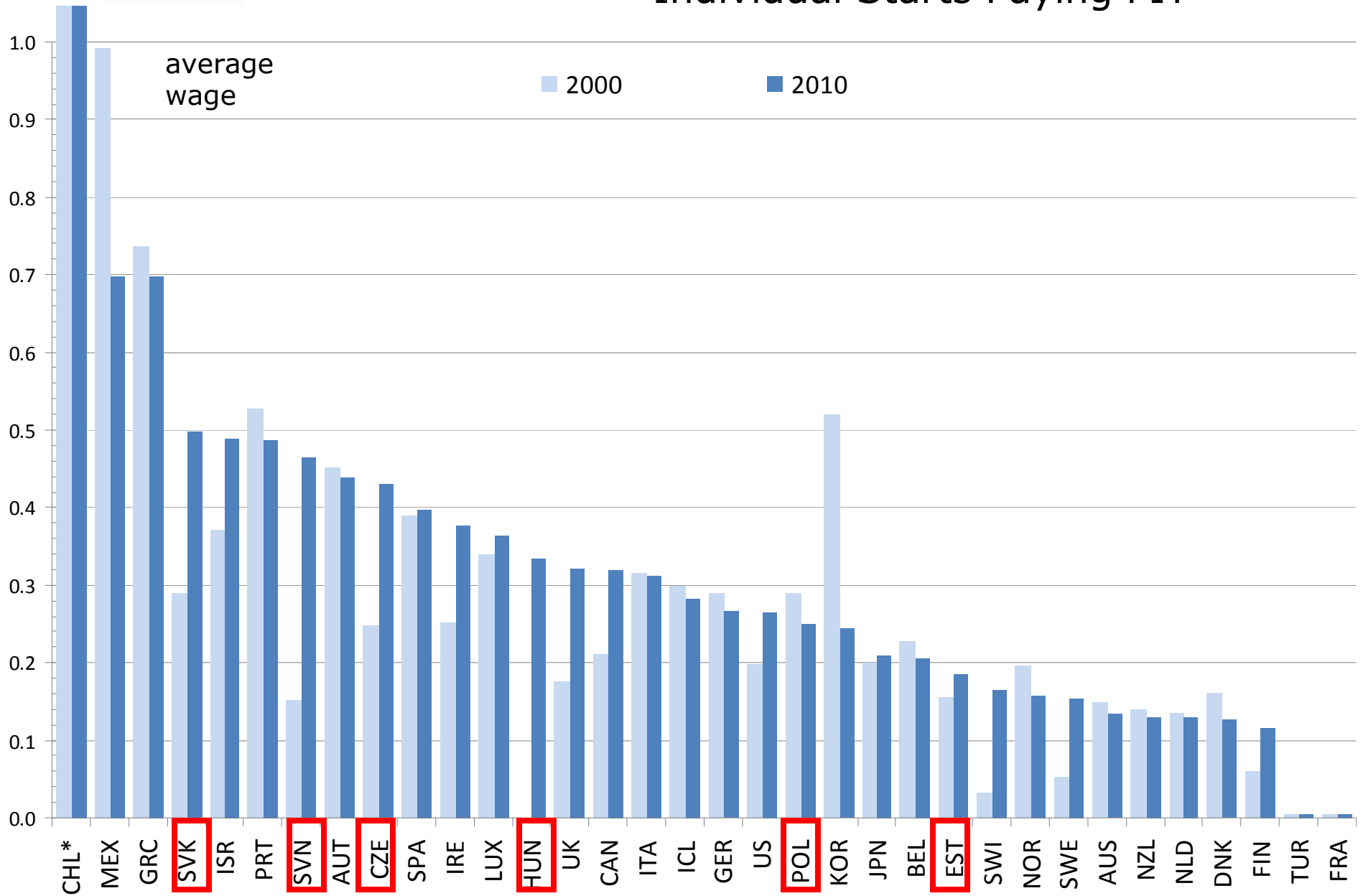
Estonia: 2003, 2010

Income tax rates by level of gross earnings expressed as a % of the average wage





Income threshold where a Single Individual Starts Paying PIT



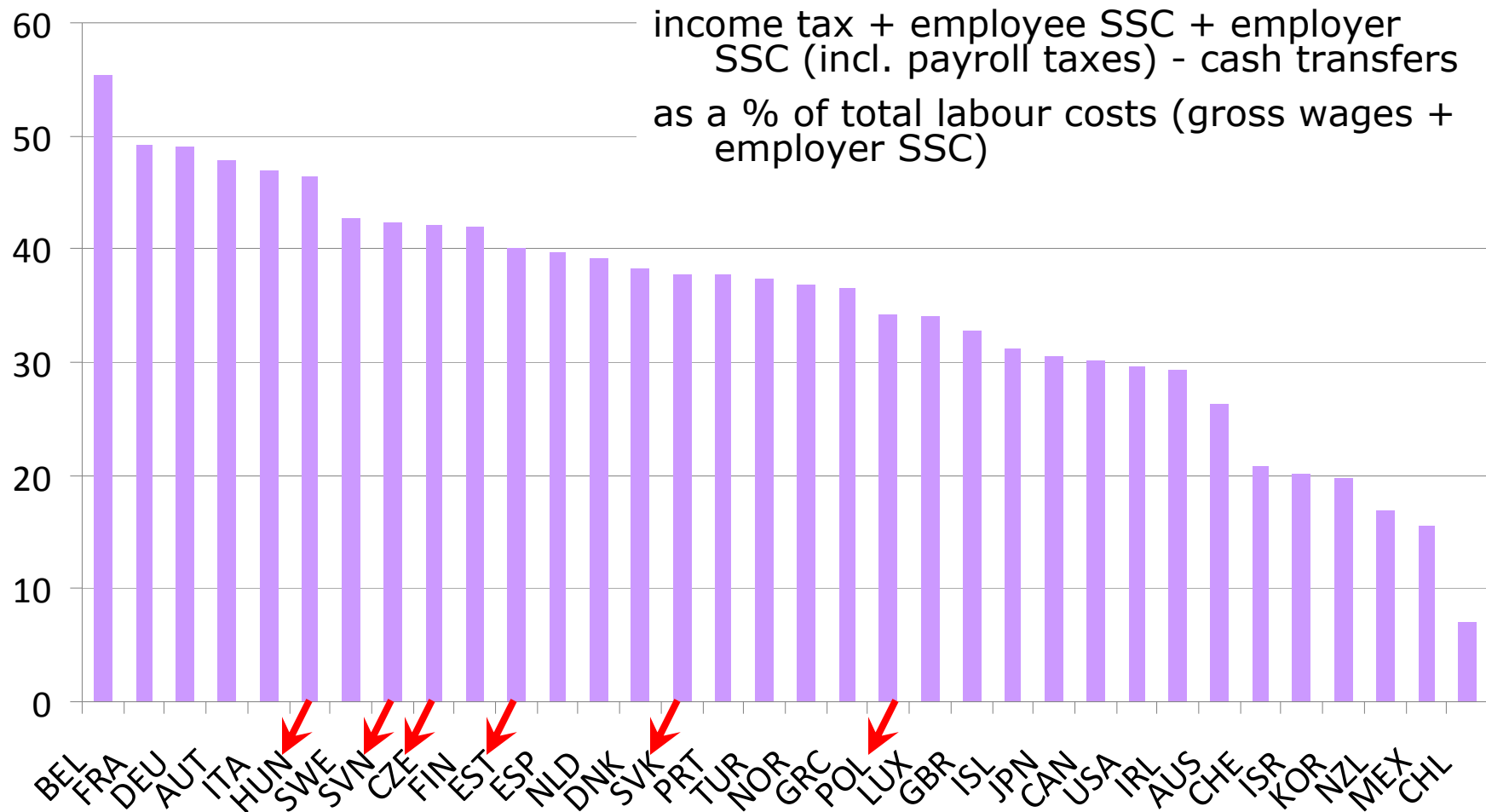
Long-term impact of cuts in employer social security contributions on employment levels are limited

- Employers have either reported an increase in profits resulting from the tax cuts or
- (where trade unions are effective) an increase in wages for the existing workforce
- Case of low-income workers & of workers close to retirement
- Shocking the sources of social security financing

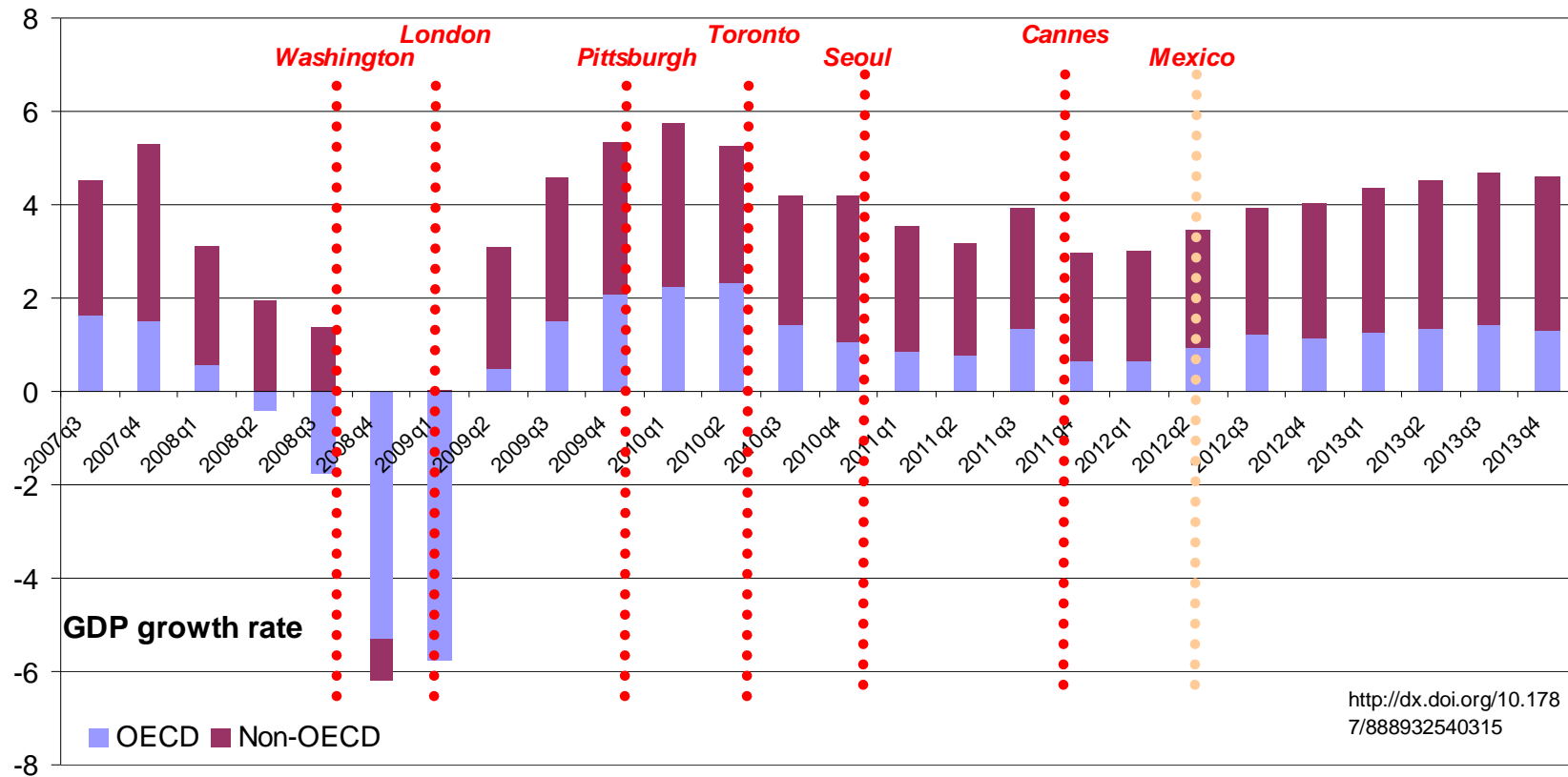
Employee social security contributions are payable on the first unit of earnings in most OECD countries

- Few countries apply minimum income thresholds
- Capped when income exceeds a certain level in 14 countries
- Contributions are deductible from PIT base in 20 OECD countries

Average tax wedge for single individual earning 100% of the average wage: 2010



Fiscal consolidation - The context



Category A, countries under IMF/EU/ECB programmes

- Greece, Ireland and Portugal
- Average cumulative fiscal consolidation equivalent to 6.6% GDP for 2012-2015

Category B, countries under “distinct market pressure”

- Belgium, Hungary, Italy, Poland, the Slovak Republic, Slovenia and Spain
- 3-5%GDP equivalent for 2012-2015 .

Category C, countries with substantial deficits and/or debt, “but less market pressure”

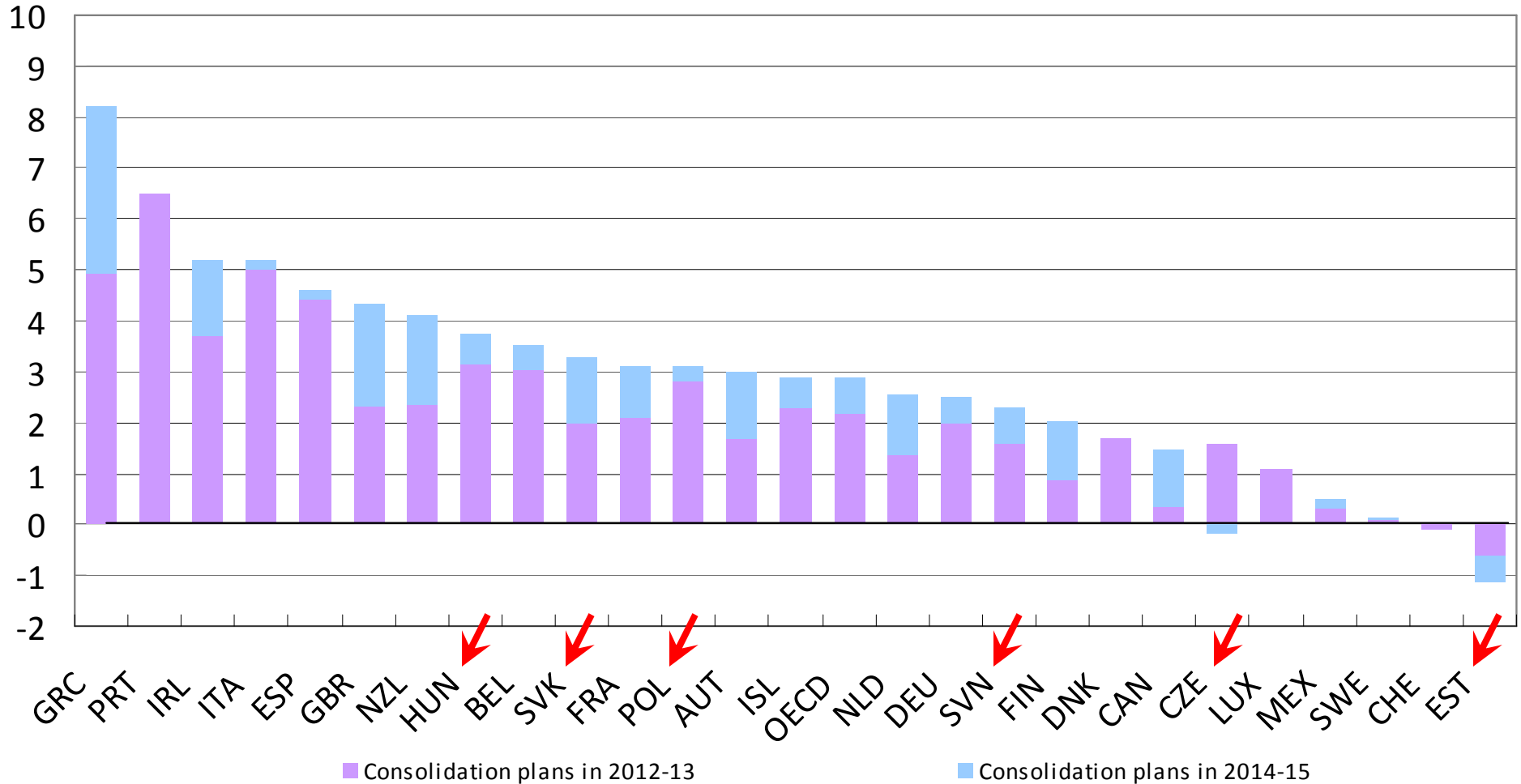
- Austria, Canada, the Czech Republic, Denmark, Finland, France, Germany, Iceland, Israel, Japan, Mexico, the Netherlands, New Zealand, the United Kingdom and the United States
- 2.5-3.7% GDP equivalent.

Category D, countries with no or marginal consolidation needs

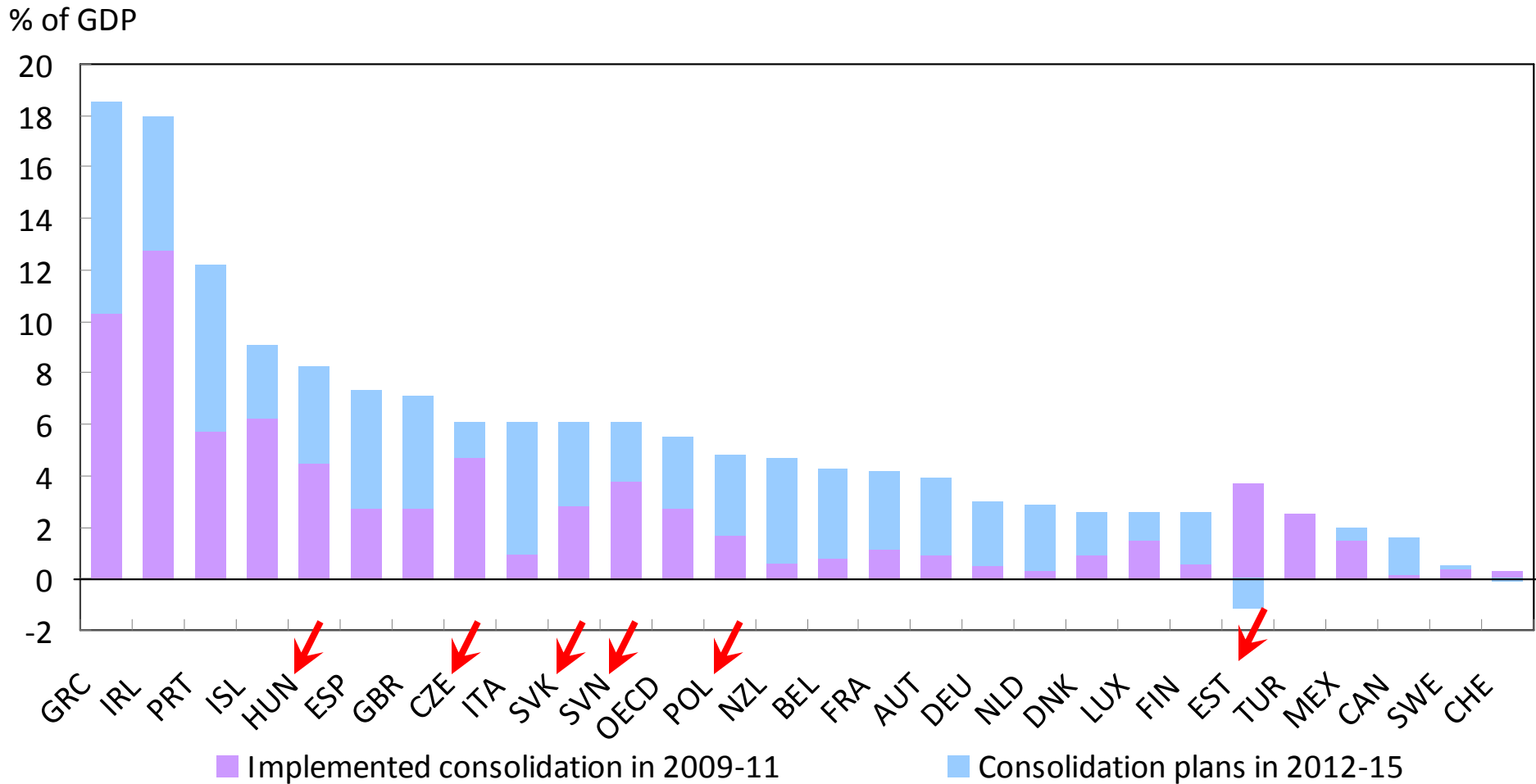
- Australia, Chile, Estonia, Korea, Luxembourg, Norway, Sweden, Switzerland and Turkey.

Consolidation plans in 2012-2015

% of GDP

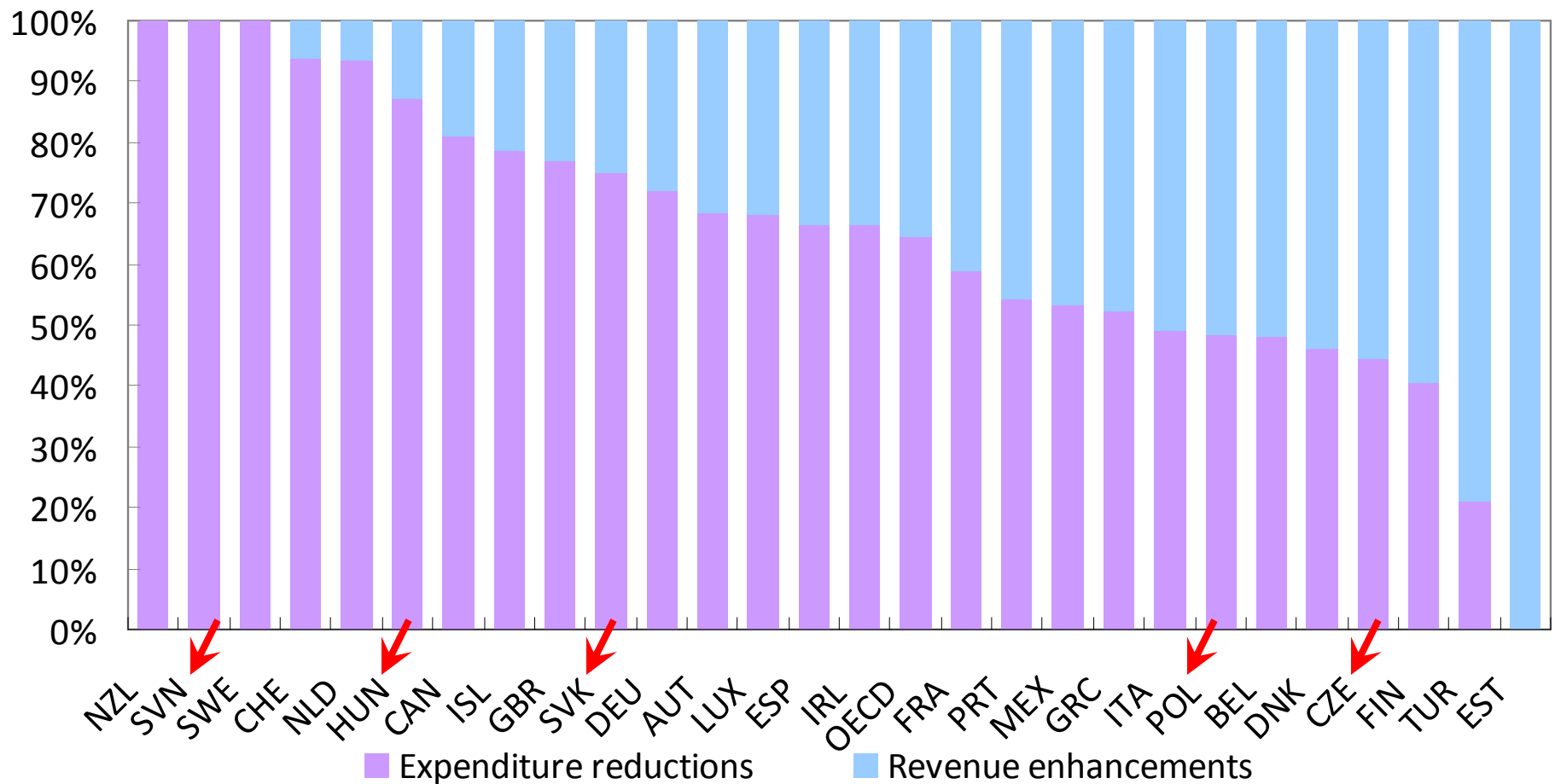


Most OECD countries have increased the total consolidation "volume" between the early post-crisis period 2009-11 and the current one 2012-15



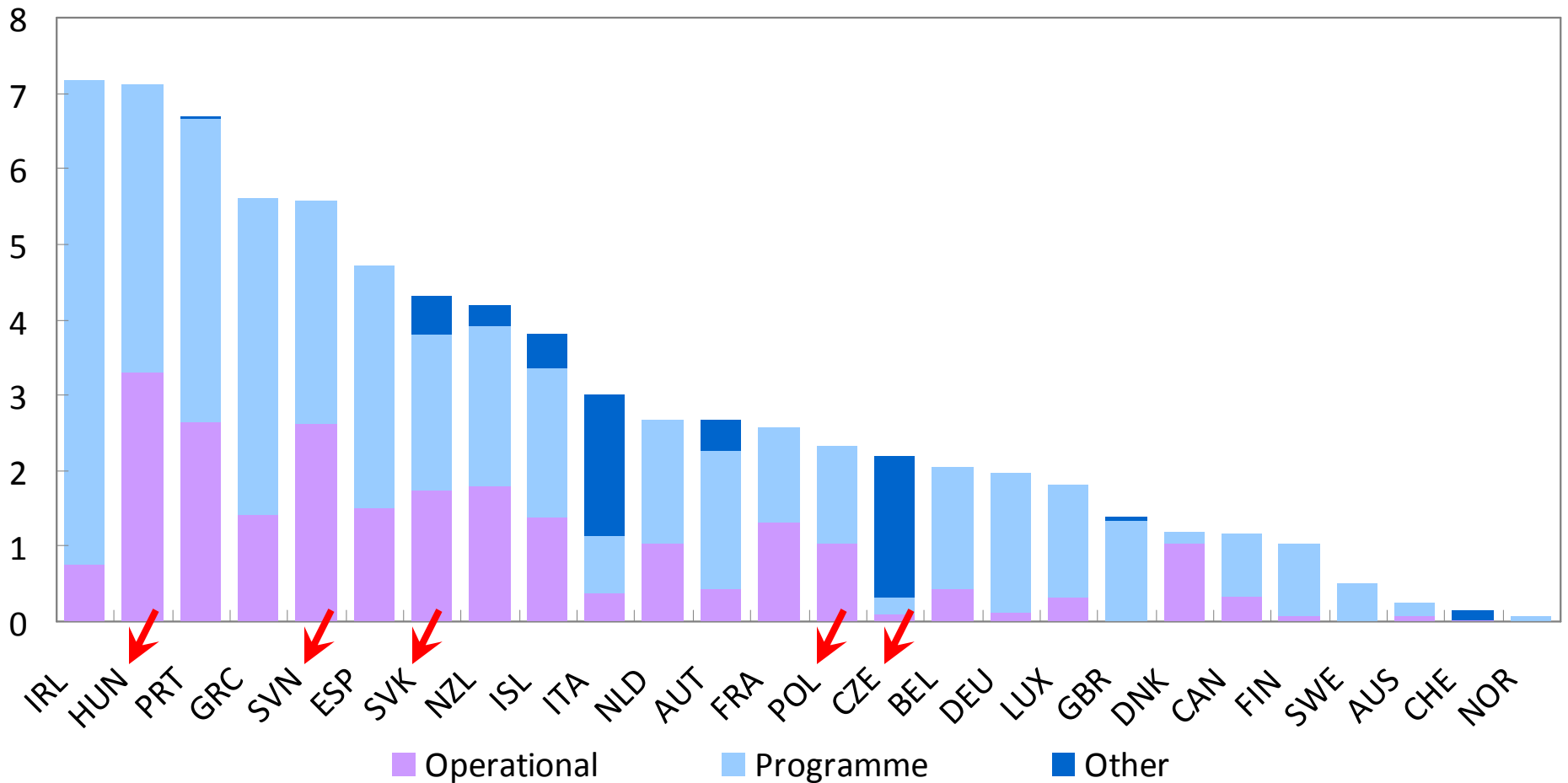
The composition of the consolidation programmes (2009-15) tilts in favour of expenditures cuts, by opposition to tax revenue enhancing measures.

This imbalance is more pronounced for countries under market pressure

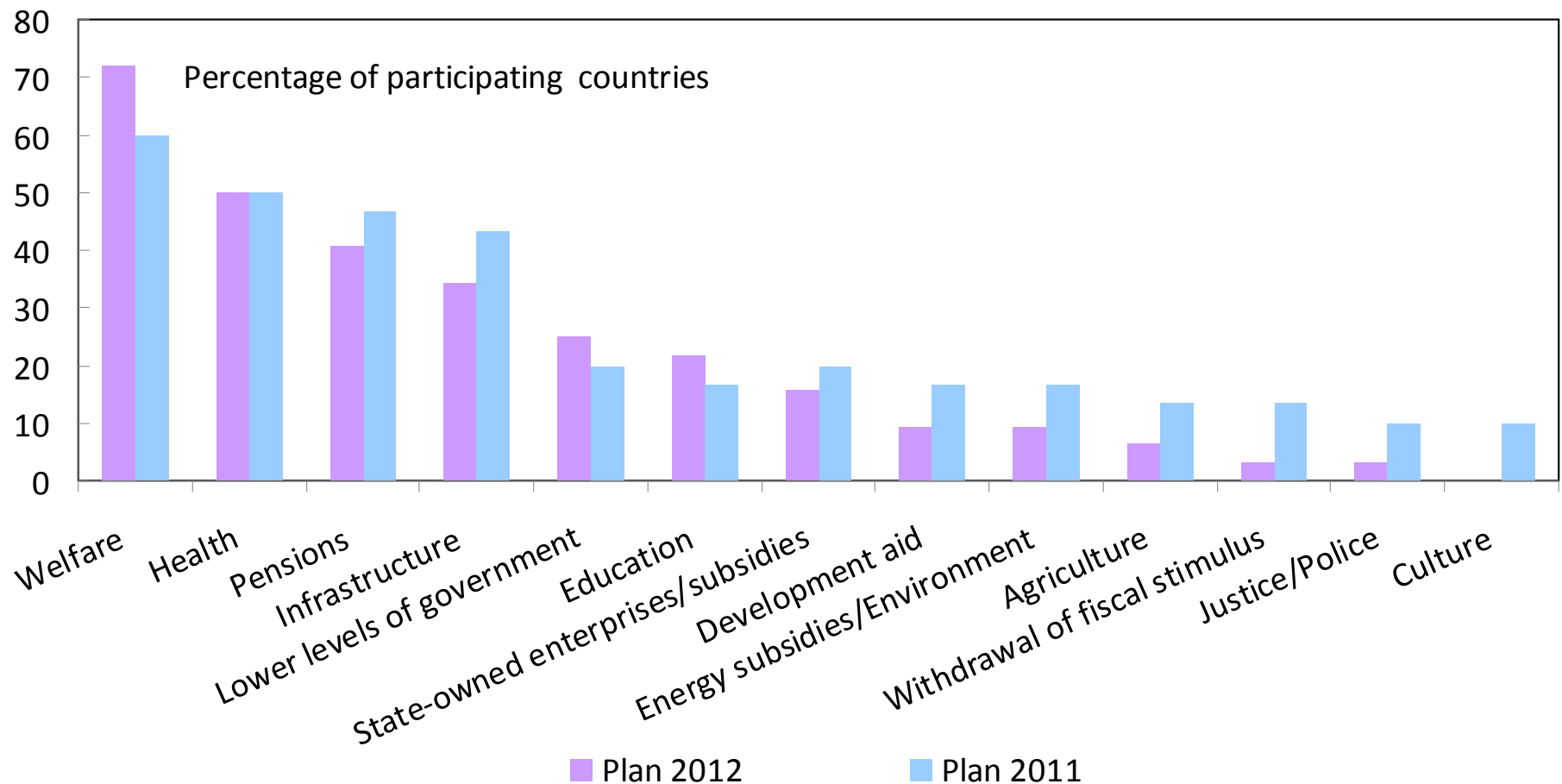


Entitlements (health care, pensions, other social benefits), public infrastructure, ODA & transfer to local government are more likely to be hit than Operational expenditures (government running costs, wages and staff in public sector)

% of GDP

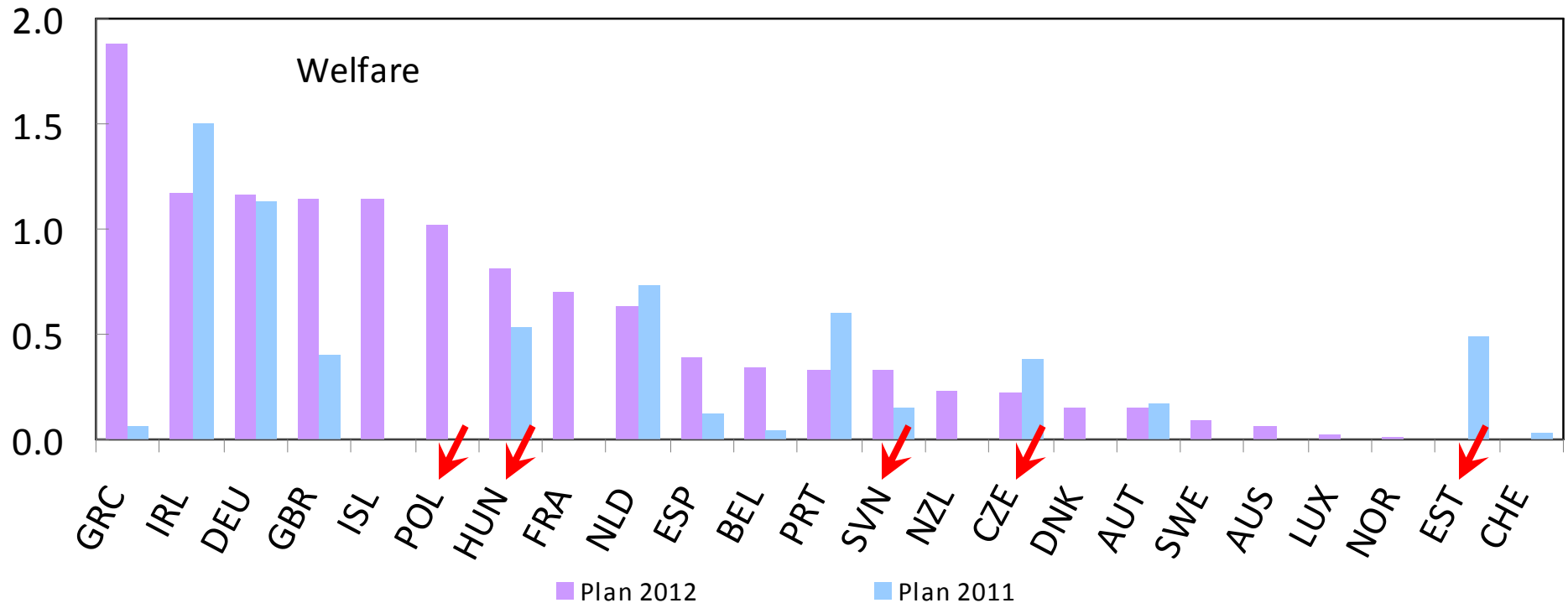


The most frequent cuts in “programme” expenditures are in welfare and social protection, followed by health and pensions

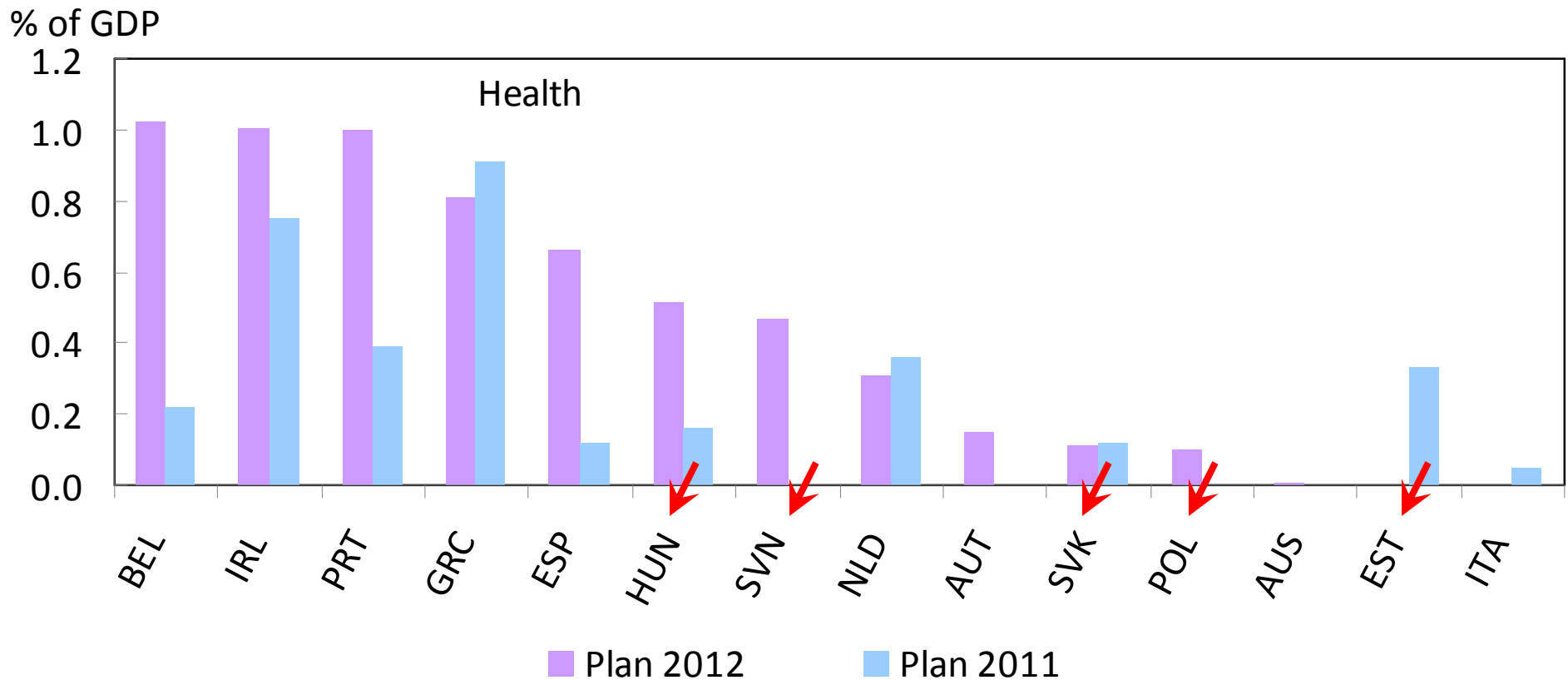


Largest cuts in welfare / social protection schemes

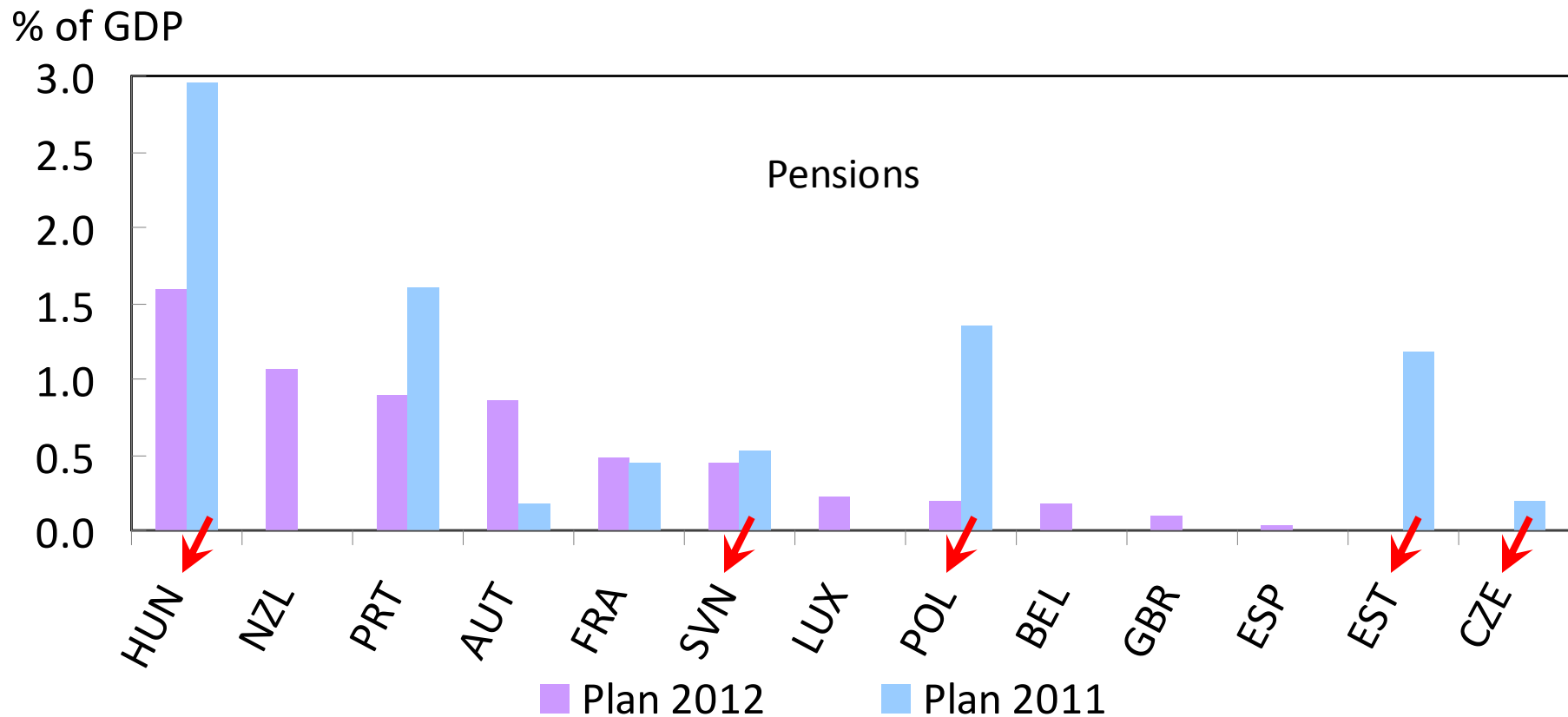
% of GDP



The largest health-related cuts



Pension cuts are less pronounced, but they are also more difficult to quantify given their very long term nature

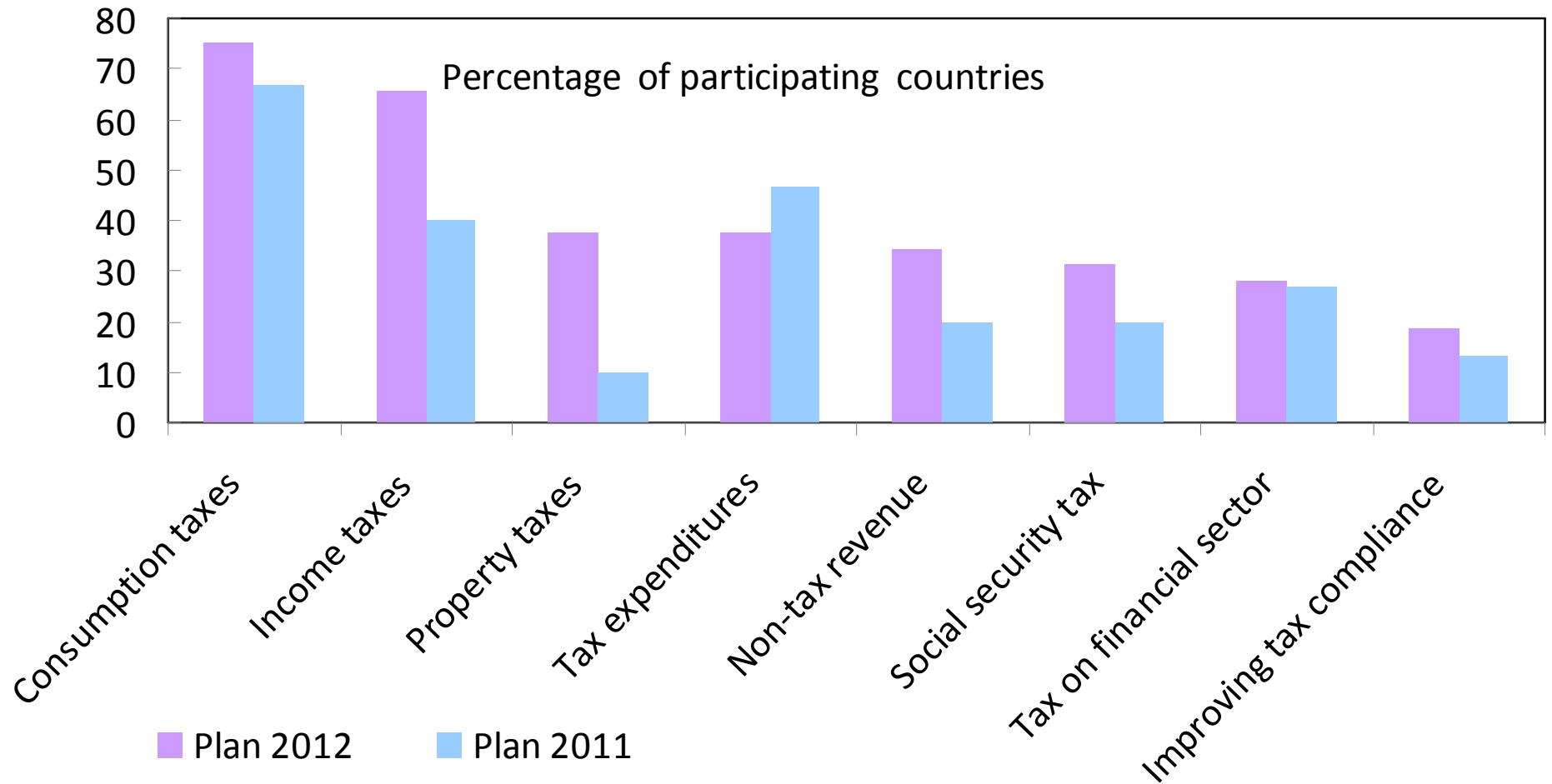


Expenditures cuts: wage and staff reductions in the public sector

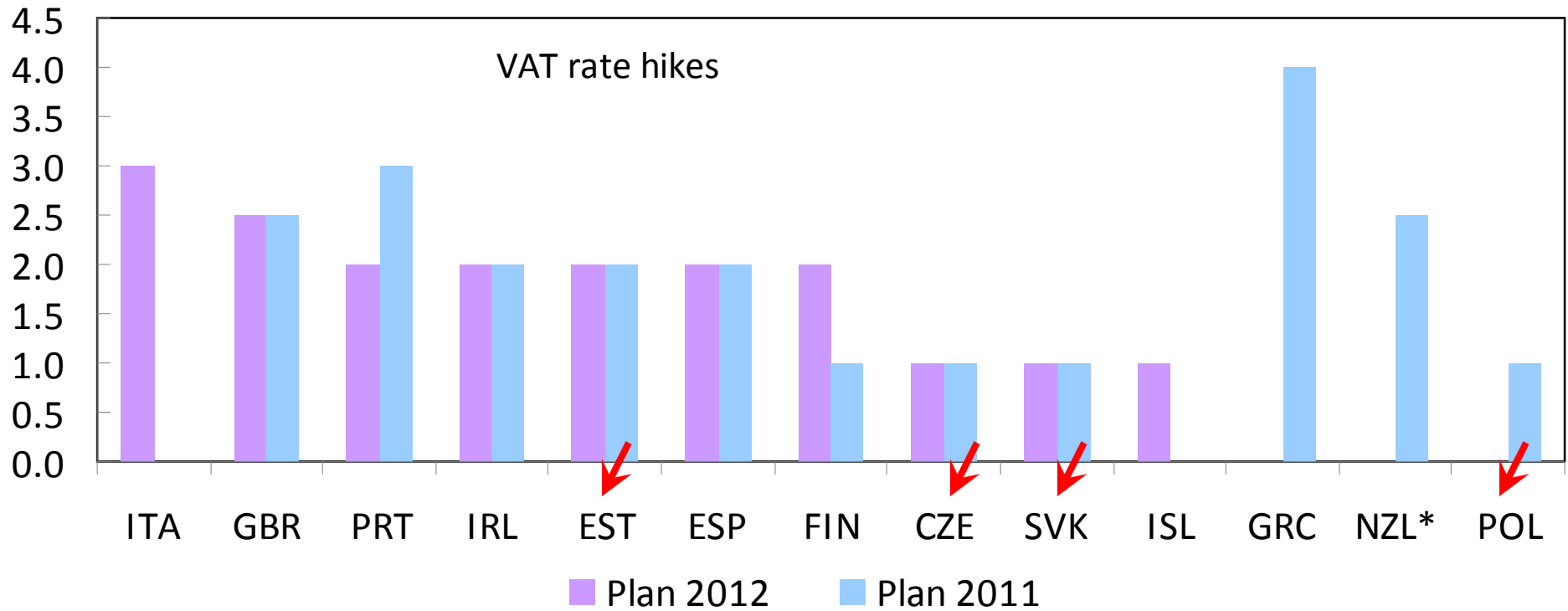
% of GDP



3/4 of OECD countries plan to raise consumption tax revenue – more than was the case last year

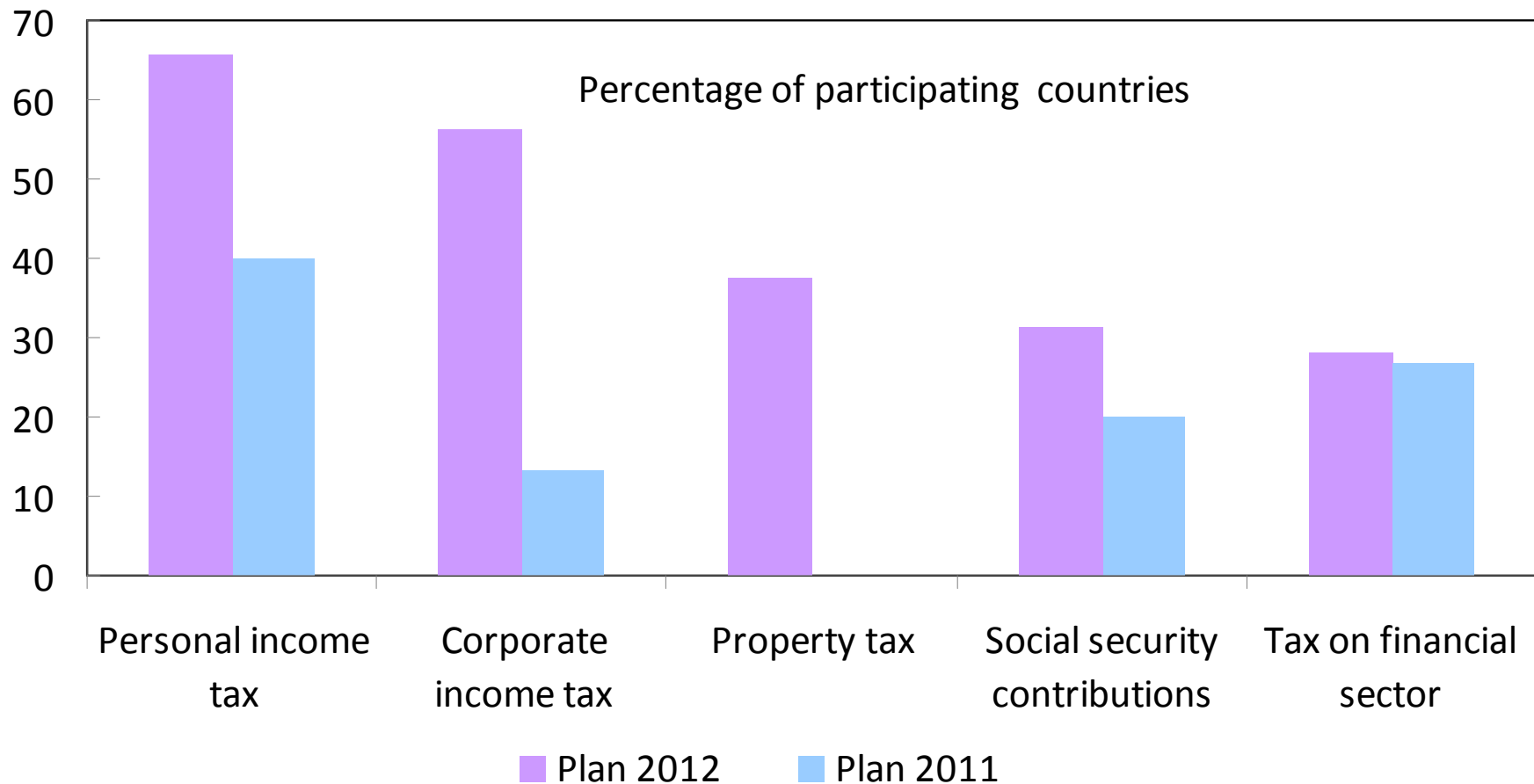


Percentage

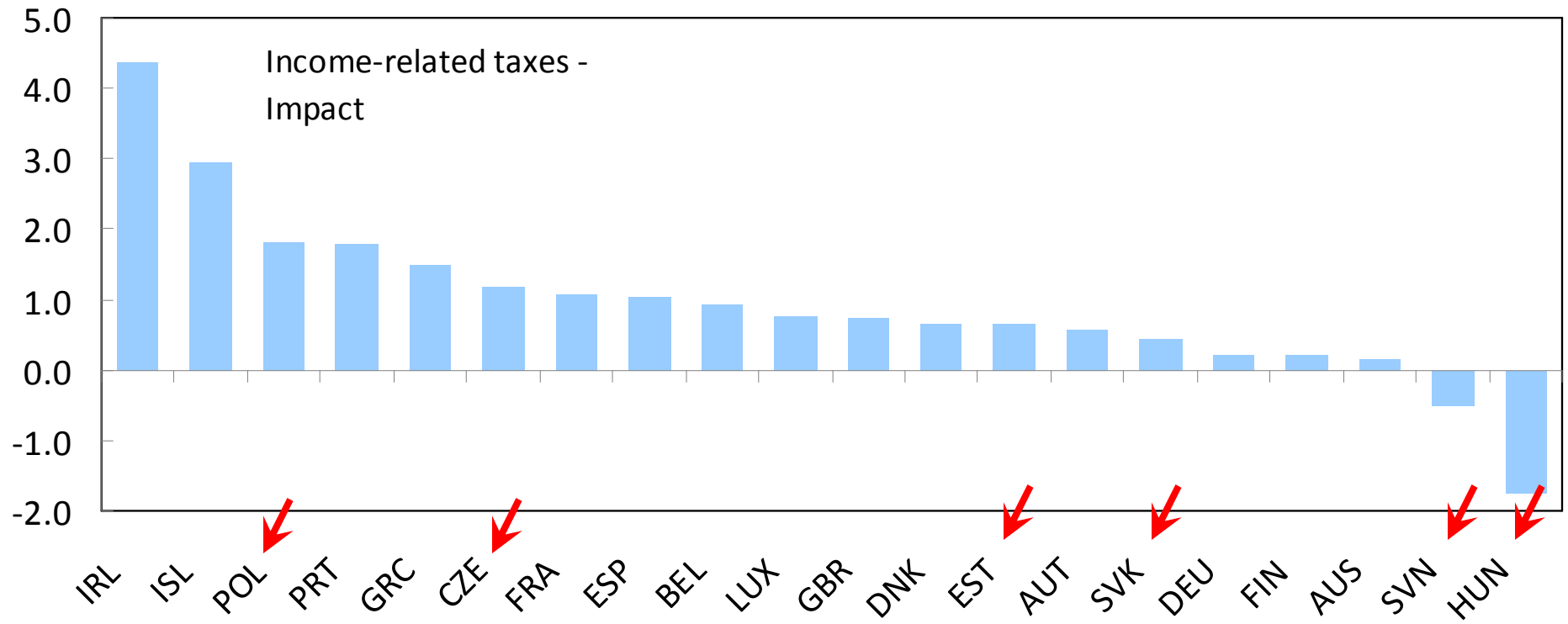


Increases in income taxes come second and mainly affect personal income taxes, although corporate income tax measures are on the rise

Only 6-9 countries use special taxes on the financial sector and improving tax compliance



% of GDP



Major consolidation measures: Czech Republic

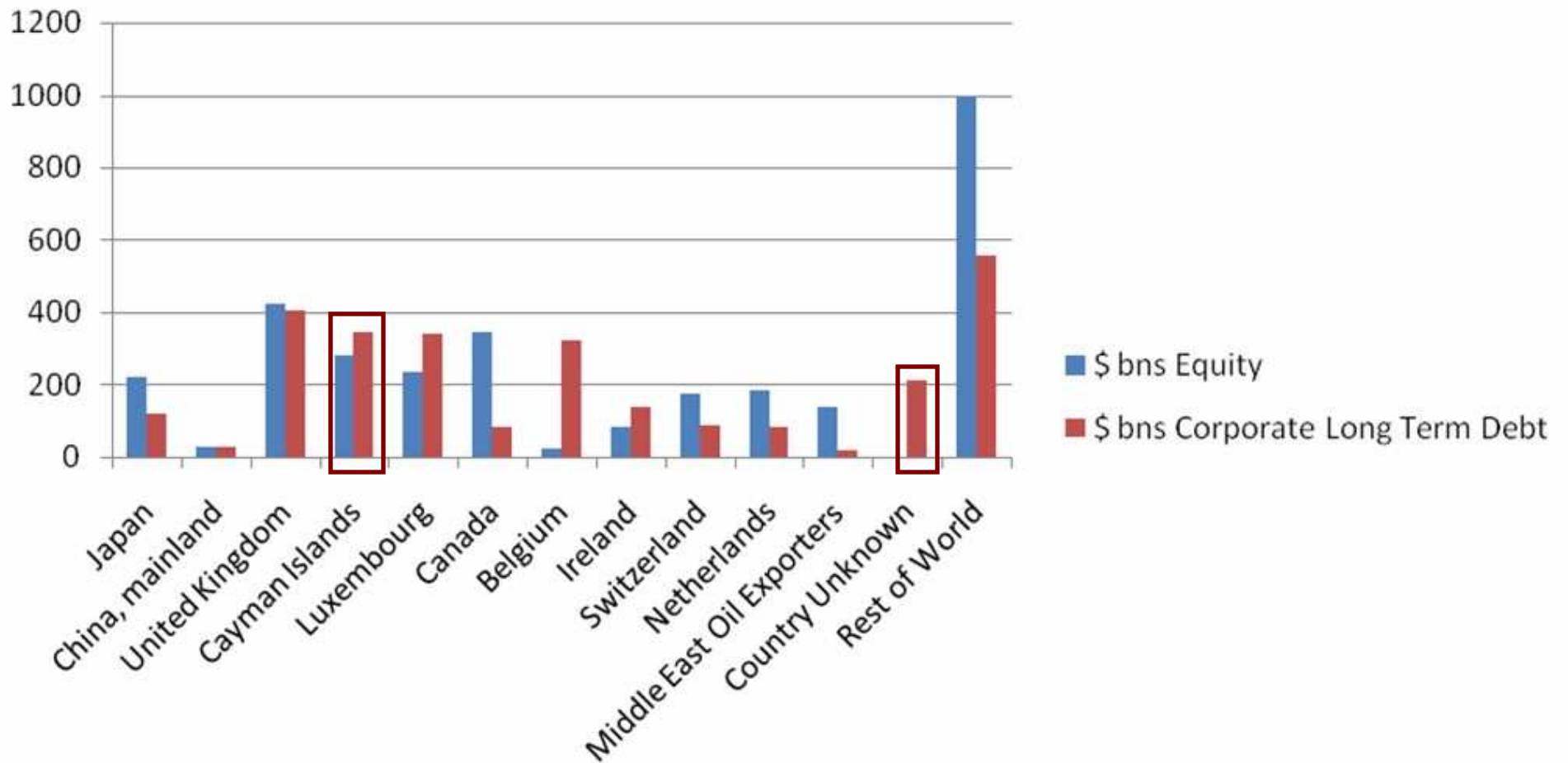
in CzKBn	2010	2011	2012	2013	2014
Public expenditure cuts	37.7	89.3	71.4	93.8	91.7
<i>in % GDP</i>	1%	2.3%	1.8%	2.3%	2.2%
Decrease in public sector pay by at least 10% (excluding teachers).	2.0	13.2	7.4	5.9	4.4
Temporary decrease of sickness benefits; reductions in social benefits and unemployment support.	2.2	<u>14.8</u>	<u>11.4</u>	<u>9.4</u>	<u>9.1</u>
No increase in pensions (contrary to the original budget draft).	6.9				
Expenditure freeze and other cost savings	26.6	<u>44.9</u>	<u>49.6</u>	<u>70.4</u>	<u>69.4</u>
Revenue increases	65.8	68.5	119	121	115
<i>in % GDP</i>	1.7%	1.8%	3.0%	3.0%	2.8%
Individual income tax adjustment.	1.5	3.8	0.4	0.4	<u>-18.8</u>
Taxation of gambling activities and lotteries (20%).			8.7	8.7	7.2
Increase in VAT rates to 20% beginning January 2010.	17.8	18.0	<u>45.0</u>	<u>45.8</u>	<u>50.5</u>
Increase in excise taxes.	11.1		13.2	13.2	13.2
Social security contributions.	<u>32.6</u>	<u>45.5</u>	<u>44.7</u>	<u>50.2</u>	<u>60.7</u>
Doubling real estate tax rates (except for agricultural land).	2.8				
Increase of toll rate 25% increase.		1.2	2.6	2.6	2.6
Inheritance and gift tax Tax on capital transfers.			4.4	0.0	0.0

Major consolidation measures: Hungary

In HuFBn	2010	2011	2012	2013	2014	2015
Public expenditures cuts	942	1 346	2 053	2 338	2 360	2 408
	3.5%	4.7%	7.1%	7.7%	7.3%	7.1%
Public sector pay	141	213	<u>256</u>	<u>256</u>	<u>256</u>	<u>256</u>
Budgetary savings	101	354	600	695	695	695
Health-care expenditure	46	47	141	172	172	173
Pensions	300	338	<u>409</u>	<u>464</u>	<u>496</u>	<u>534</u>
Family allowances	52	74	134	155	155	155
Unemployment benefits	0	0	118	118	118	118
Revenue increases	155	-73	161	154	287	359
	0.6%	-0.3%	0.6%	0.5%	0.9%	1.1%
Social security contribution	-251	29	234	246	327	346
PIT	-205	-690	<u>-1 005</u>	<u>-1 177</u>	<u>-1 147</u>	<u>-1 118</u>
Capital taxes	240	202	202	40	39	36
VAT	412	421	<u>681</u>	<u>844</u>	<u>870</u>	<u>898</u>
Taxes on wealth & duties	-41	-35	-36	-37	-39	-40
FTT				130	130	130
Telecom & energy			85	107	107	107

Tax evasion

Geographic distribution of bond- and shareholders in the US



Under-taxation of the financial sector

- Exempted from VAT
- Government guarantees

Debt-bias, rules encourage excessive risk-taking and/or leverage

- “innovation” in the shadow banking system (debt securitisation) beyond the economic justification of spreading the risks

Private capital

- Disguising income into capital gains (carried interests)
- hybrid capital “Double-Dip” deduction of interest expenses in 2 juris.

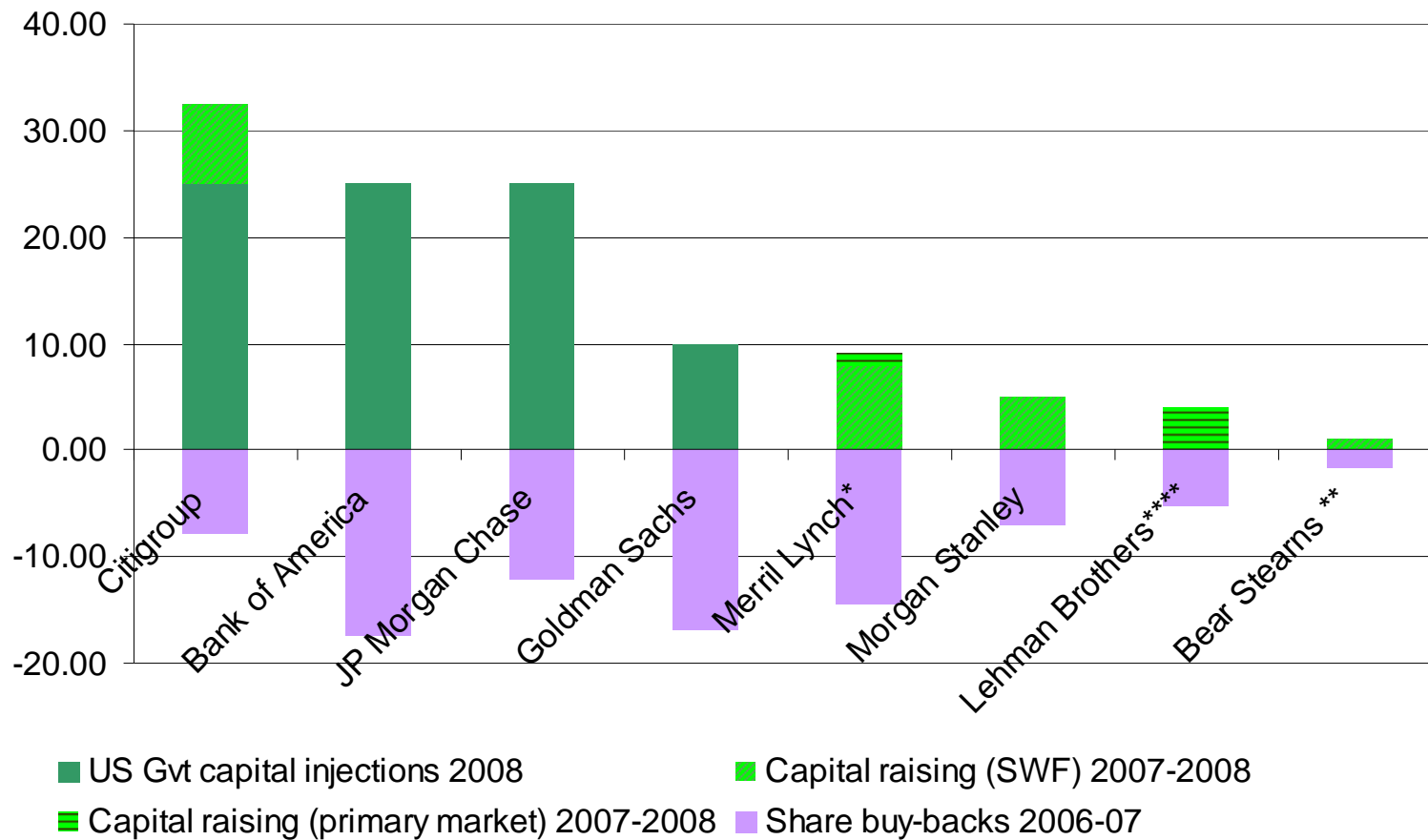
Stock-based remuneration

Impact

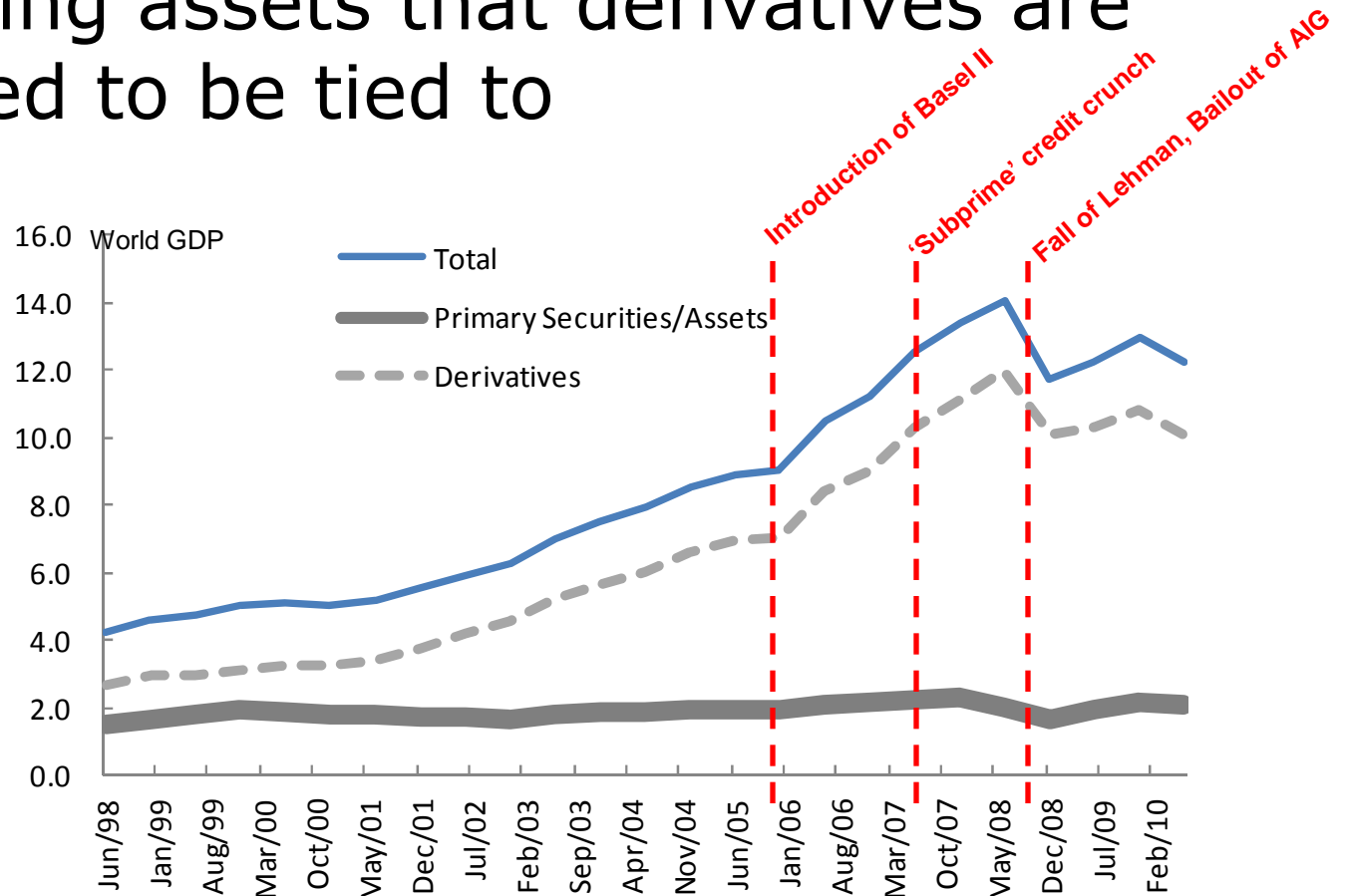
- drain on tax revenues
- Mispricing of assets and risks, and hence diversion of capital away from productive investments

Dividends and share buybacks

Capital injections post-crisis vs Share buy-backs pre-crisis



Growing disconnect between trading flows in derivatives and flows in the underlying assets that derivatives are supposed to be tied to



Blundell-Wignall & Atkinson 2011 "Global SIFIs, Derivatives and Financial Stability", Adrian Blundell-Wignall & Paul Atkinson, OECD Journal - Financial Market Trends, Volume 2011 issue 1, OECD, January 2011 <http://www.oecd.org/dataoecd/62/10/48299884.pdf>



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