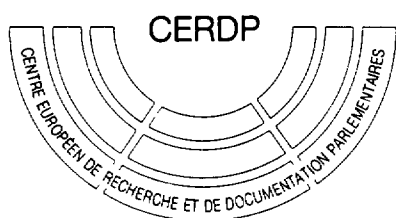


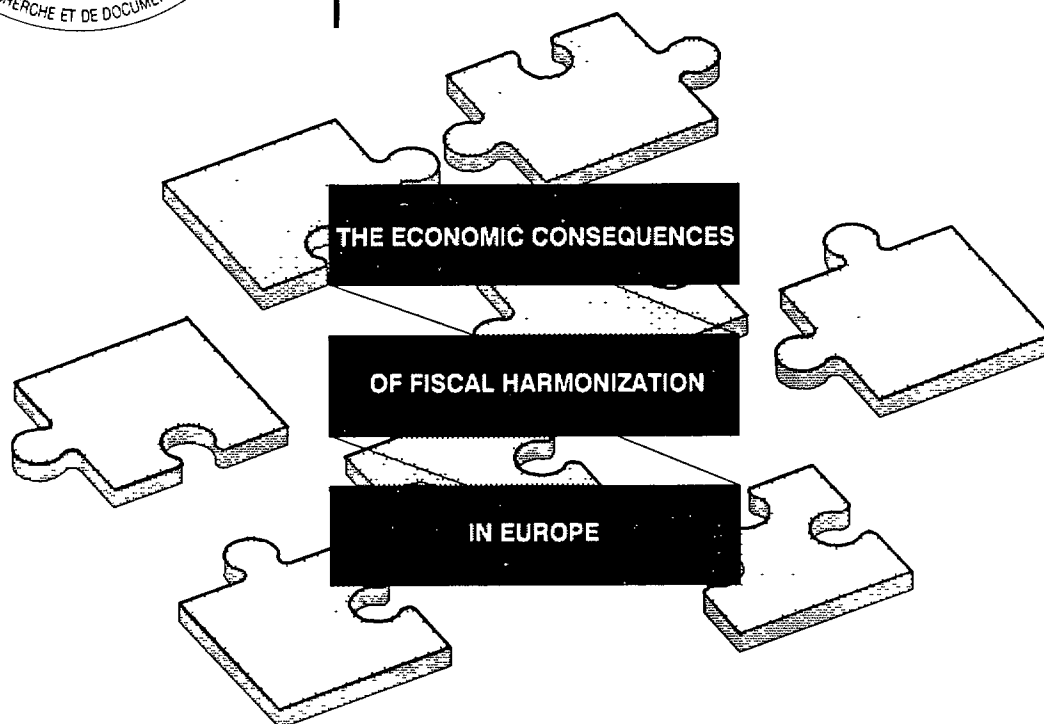


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of fiscal harmonization
in Europe**

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The Economic Consequences of Fiscal Harmonization in Europe

Foreword

This publication is a summary of a four-hundred page report commissioned by the French Sénat for their Committee on Finance in May 1990.

Due to the wide interest that this study has already generated, it was decided to make its conclusions more readily available by preparing a summary which has been translated into English, German, Italian and Spanish.

The original report was prepared by a group of experts from the Centre d'Etudes prospectives et d'informations internationales, the Observatoire français des conjonctures économiques and the Institute for Fiscal Studies, and the summary was written by Georges Chevallier of the Sénat.

The Sénat has kindly given the publication rights for this summary to the European Centre for Parliamentary Research and Documentation and any comments relating to this report should be addressed to:

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BRIEF SYNOPSIS

I. COMPARATIVE ANALYSIS OF NATIONAL COMPULSORY DEDUCTION SYSTEMS

The experts paid particular interest to the economic impact of the disparities in the level and structure of compulsory deductions from one country to another. In this connection, they set out certain 'macroeconomic equivalences' which prompt them to play down the real impact of apparently important differences:

1. From a macroeconomic point of view, employees' social insurance contributions can effectively be equated with an income tax deducted at source.
2. There is no correlation between the volume of employers' contributions and the proportion of the value added by firms accounted for by wages: for example, despite employers' contributions which are double their German counterparts, French firms do not devote a greater proportion of their added value to wage and welfare costs than do German firms; in the case in point, higher contributions are offset by lower wages.
3. The experts show that once the 'surprise effect' has worn off, a rise or fall in VAT rates is passed on to firms roughly one year later: this is the result of the relationships observed between wages and prices.

Comparing worker tax rates in the various countries, taking account of earnings and family situation, the experts show that the wide disparities which emerge if such comparisons are restricted to income tax in the strict sense of the term become much less marked if social insurance contributions based on wages are included.

As regards corporate taxation, the experts calculated the rates of return required before tax in order to secure a 5% return after tax in terms of both the country where the investment is made and the nationality of the firm which makes it. They derive from this 'incentive coefficients' in respect of the export or import of capital in the various countries: for example, the incentive to invest abroad is greatest in Germany; the incentive for investment from abroad is greatest in the United Kingdom and Ireland.

II. RECOMMENDATIONS FOR HARMONIZATION

In general terms, the experts come down in favour of harmonization restricted to the absolute minimum. However, they also suggest adjustments which, without being dictated by the completion of the large internal market, would make tax systems more rational.

As regards the funding of social welfare, the experts take the view that each country may remain free to choose the degree of redistribution they think fit, on condition that they levy from households the extra resources which will be required as a result of the ageing of the population in the coming decades, this being by far the most important problem in their view).

The experts see income tax as the prime example of a tax which should not be harmonized. However, in the name of 'rationality', they advocate various adjustments to this tax, mainly in France.

With regard to VAT, the experts regard the rate approximations proposed by the Commission as adequate. In most countries these approximations should have no major budget impact. However, they are raising serious difficulties in Denmark, where compulsory deductions are very largely based on only two taxes: VAT (the yield from which would be reduced by 30% by harmonization) and income tax. The experts also understand the objections raised by the United Kingdom to the abandonment of the zero rate, which favours products which make up 30% of household consumption; they do not regard its continued application as necessarily incompatible with the abolition of checks at intra-Community frontiers.

With regard to taxes where there is a risk of 'competition to levy the lowest tax rates', the experts go much further in their recommendations: these cover the taxation of the investment income of households (current trends are moving such income outside the tax net, a development which the experts criticize from the point of view of social fairness and economic rationality) and corporation tax, in respect of which the experts propose both a complete standardization (the only means of ensuring that the tax does not vary according to the location of investments throughout the Community) and a reworking of the mechanisms, partly in order to make borrowing less attractive.

In the long term, the experts envisage that the tax on the investment income of households, corporation tax, in full or in part, and taxes on pollution will become Community own resources.

III. SIMULATIONS

Simulations carried out with the aid of the MIMOSA model illustrate the macroeconomic impact of certain tax harmonization measures in Europe:

1. With regard to VAT and the taxation of petroleum products, the experts put forward a scenario which goes beyond their own recommendations, since it simulates complete harmonization with accompanying measures geared to the specific situation of each country; the implication is that tax adjustments which have such a strong impact on prices are dangerous and should be staggered.
2. Another scenario simulates a reduction in employers' social insurance contributions in the three countries where rates are higher than the Community average (Spain, France and Italy) with, by way of compensation, an increase in deductions from households: only Italy benefits clearly from this scenario, which is shown to have an adverse effect on economic growth in the Community as a whole.

I. LEVEL AND STRUCTURE OF COMPULSORY DEDUCTIONS IN EUROPEAN COUNTRIES

A. Overall tax take

The overall rate of compulsory deductions (income tax and social insurance contributions) is an accounting indicator. The conventions employed in calculating it vary from one country to another. In order to make comparisons possible, the OECD calculates harmonized rates (Table No. 1) which differ by varying degrees from those which appear in the national accounts of each country (Table No. 2): the difference is particularly marked in Germany (41.2% under the national accounting system and 37.6% under the OECD system) and in Spain (30.9% and 33% respectively). One of the main differences between the accounting conventions employed concerns social insurance contributions (Table No. 3) which, in order to be classified by the OECD as compulsory deductions, must be both legally compulsory and paid over to a public body.

In 1987, the most recent year for which OECD statistics are available), compulsory deductions represented, on average, 39.6% of the GDP of the European Community: 33% in Spain, 36.2% in Italy, 37.5% in the United Kingdom, 37.6% in Germany and 44.8% in France.

By comparison with 1965, the average increase was 10% over the Community as a whole (+ 6% in Germany, + 7.1% in the United Kingdom, + 10.3% in France, + 10.6% in Italy and + 18.5% in Spain).

B. Compulsory deductions, public expenditure, the budget deficit and the public debt

The differences between deduction levels from one country to another can no doubt in part be traced back to accounting conventions. In particular, since the total for deductions is not 'consolidated', the taxes and social insurance contributions which administrations pay over to each other give rise to double accounts whose scope is not necessarily the same in each country. State intervention by means of tax allowances reduces the burden of compulsory deductions, but this is not true of intervention by means of subsidy.

However, above and beyond these accounting phenomena, four factors must be taken into account (see Table No. 2): the level of the public sector deficit, the burden of interest charges on the debt accumulated in the past, the extent of the income redistribution carried out by the social security authorities and the level of other public expenditure (administrative and capital expenditure).

1. Public sector deficit and public debt

Given the same level of public expenditure, a country which runs a higher budget deficit than another will enjoy lower income from compulsory deductions. However, this represents a 'temporary trade-off' which, sooner or later, will force the country with the higher deficit to increase its compulsory deductions or greatly reduce its expenditure other than on interest charges in order to cater for the increase in those charges. Table No. 2 shows that this scenario corresponds to the position of Italy.

Conversely, a state (such as Belgium or Denmark) which seeks to reduce the debt accumulated in the past must, given the same level of public expenditure, impose a higher rate of compulsory deductions than a country whose public debt is smaller.

Table No. 4 gives details of the public debt in the various European countries. Working from this, a list can be drawn up of those countries whose past budget policies are now imposing tight constraints on future government action: this applies both to countries where compulsory deductions are currently lower than the Community average (Italy or Greece, for example) and countries where these deductions are already high (Belgium, the Netherlands and Denmark).

Table No. 5 refines this analysis by employing the concept of the 'primary deficit' (or 'primary surplus') which represents the budget deficit minus interest charges (the 'deficit net of interest').

As an initial approximation, it can be stated that when real interest rates are equal to the rate of growth of GDP, the achievement of a budget balance net of interest charges is essential if the ratio between the volume of the public debt and the level of GDP is to be stabilized.

However, this is not enough in the current situation where real interest rates are higher than the rate of growth of GDP. In order to stabilize the public debt/GDP ratio, the budget must show a 'primary surplus' which depends, in each country, on the level of interest rates, the rate of growth of GDP and the volume of the public debt.

In the light of all these factors, the experts calculated the volume of the primary surplus required in each country in order to stabilize the public debt/GDP ratio.

Three groups of countries can be distinguished:

- the United Kingdom and Denmark, where budgetary consolidation has gone beyond the primary surplus required to stabilize the debt ratio (these countries are currently showing a relative fall in their indebtedness);
- Germany, France, Ireland and Belgium, countries where the effective primary surplus and the surplus required roughly coincide;
- the Netherlands and, above all, Italy and Greece, where further efforts are required in order to stabilize the public debt ratio.

Spain is at a halfway house, in that its low public debt and fast rate of growth currently limit the required adjustment to less than one GDP percentage point.

In the case of Italy, Belgium, the Netherlands, Ireland and Greece, a fall in the debt ratio, rather than mere stabilization would be necessary in order to restore some room for manoeuvre in budget policy.

2. Social transfers

The extent of the income redistribution achieved by means of social transfers is a key factor in the differences observed in the level of compulsory

deductions in the various countries: for example, taking France or the Netherlands on one hand and Germany or Spain on the other, a certain correlation emerges between the level of social benefits and the level of compulsory deductions.

However, the 'social benefits' column in Table No. 2 provides only partial clues in this connection. For example, the particularly low level of social benefits in the United Kingdom and Denmark can in part be explained by the fact that health services are paid for from public funds, whereas elsewhere they are funded by private insurance.

Moreover, it is probable that, as far as economic analysis is concerned, the level of expenditure on health services, or the level of pensions, is in itself more important than the method of financing this expenditure. This is why Table No. 6 sets out the results of a calculation made by the OECD concerning expenditure on medical care in the main countries. In 1987, this expenditure represented 6.1% of GDP in the United Kingdom, 7.2% in Italy, 8% in Germany and 8.7% in France, as against 11.1% in the United States. With regard to this last figure, it should be noted that public expenditure on medical care accounts for only 6% of GDP in the United States, i.e. a level comparable with that of the other countries.

By the same token, Table No. 3 shows that a proportion of the social benefits received by households is not paid over to them by the public authorities but by private bodies: this proportion is lower in France (1.7% of GDP) than in Germany, Italy or the United Kingdom (4.5% of GDP).

3. Public expenditure on administration and infrastructure

The third column of Table No. 2 shows that, expressed as a percentage of GDP, total public expenditure in the European countries ranges from 37% in Spain to 53.8% in the Netherlands (via 40.8% in the United Kingdom, 43% in Germany, 46.6% in France and 46.8% in Italy).

Taking only government expenditure on administration and infrastructure, the differences are much less marked and the countries appear in a different order: 17.7% of GDP in Spain, 22.2% in Italy, 22.6% in France, 23.8% in the United Kingdom and 24.2% in Germany.

C. Structure of compulsory deductions

Table No. 7 classifies compulsory deductions according to the economic nature of their assessment basis. It thus distinguishes between taxes on the income of households (income tax itself and social insurance contributions paid by households), corporate income (corporation tax), labour costs (essentially employers' social insurance contributions), other production costs and, finally, product prices (mainly VAT and excise duties).

First and foremost, this table reveals the peculiar nature of the Danish tax system, a good half of whose revenue is generated by income tax and a third by VAT and excise duties.

A comparison restricted to the five main countries of the Community prompts the following conclusions.

Income tax in the narrow sense, the revenue from which corresponds on average in the Community to 9.6% of GDP, is less burdensome in France (5.7% of GDP) and in Spain (7%) than in Italy (9.5%), the United Kingdom (10%) and Germany (10.9%).

If one adds to this tax the social insurance contributions paid by households (essentially employees), it emerges that overall deductions levied on the income of households represent on average 16% of GDP in the Community and that the differences between countries do not exactly correspond to those in respect of income tax in the narrow sense: Spanish households face the lowest tax burden (10.3% of GDP); the deduction rate is 13.3% of GDP in Italy, 13.9% in France and 15.7% in the United Kingdom; it is considerably higher in Germany (18.4% of GDP).

Corporation tax plays a relatively limited role: 1.9% of GDP in Germany, 2.2% in Spain, 2.3% in France, 3.8% in Italy and 4% in the United Kingdom, the Community average being 2.8%.

The contributions which add to labour costs (8.2% of GDP on average in the Community) are particularly high in France (13% of GDP) and particularly low in the United Kingdom (3.5% of GDP), where employers' social benefit contributions are relatively unimportant. They represent 7.2% of GDP in Germany, 8.9% in Italy and 9.1% in Spain.

Taxes affecting product prices are higher in France (12.7% of GDP) and in the United Kingdom (11.1% of GDP) than in Spain (9.7% of GDP), Germany (9.1%) or Italy (9.1%).

In overall terms, Italy and Germany have compulsory deduction structures close to the Community average, whereas France, Greece, Ireland and, above all, Denmark have structures which depart considerably from the norm.

D. Real economic impact of compulsory deductions

The classification of deductions in accordance with the economic nature of their assessment basis which has just been examined must not be confused with their real economic impact because, wherever possible, every economic agent endeavours to pass on to others the fiscal burden imposed on him. For the economist, the important thing is to discover who the tax is ultimately passed on to and the consequences of this. Two questions are central to this:

- is the tax ultimately passed on to households or firms?
- does the tax alter the relative cost of production factors (capital and labour)?

Any analysis of these feed-through phenomena must take into account the time factor.

1. The short term

In the short term, one can say that the economic impact of taxes corresponds to the classification given in the preceding paragraph. If VAT is increased, this immediately reduces the purchasing power of households. If employers' social insurance contributions or corporation tax are increased, company profits will be the first affected.

2. In the medium term

Once the 'surprise effect' has passed, how do economic agents react to tax changes?

The outcome of the chain reactions caused by a tax change which has a direct impact on production costs or consumer prices essentially depends on two factors:

- whether, and how quickly, firms can pass on the increase in their costs to producer prices;
- the sensitivity of nominal wages to the increase in consumer prices.

This second factor deserves attention, because it determines the real economic impact of changes in VAT.

Even if wages are not automatically indexed to prices, this does not mean that the past or anticipated inflation rate is not in fact taken into account in wage negotiations. Generally, a change in the inflation rate is reflected to varying degrees, and more or less rapidly, in wage trends. For example, a recent study by INSEE (National Institute for Statistics and Economic Research) concludes that in France a price change is passed on to nominal wages at a rate of roughly 75% and with an average delay of six months.

Chain reactions of this type show that a reduction in VAT works to the benefit of firms in respect of value-added gain sharing and an increase works to their detriment. This is why, when considering the medium-term consequences of a change in VAT, the economist tends to regard it as a tax on firms rather than on households.

3. The long term

In the European Community, national economies have been interdependent to a considerable degree for the last thirty years. Adjustments in exchange rates, methods of fixing wages and, in general, market mechanisms as a whole have absorbed the differences between the various fiscal and social systems. Thus, in the long term, this type of difference is offset by wage disparities, since competition leads to an approximation of production costs. The chapter devoted to social insurance contributions will demonstrate this.

II. SOCIAL INSURANCE CONTRIBUTIONS

A. Proportion of compulsory deductions made up by social insurance contributions

Tables Nos. 3 and 7, considered above, provide general clues as to the proportion of compulsory deductions made up by social insurance contributions. In 1987, they represented 13.5% of Community GDP, the figure for total compulsory deductions being 39.6%. Practically non-existent in Denmark, they reached 19.2% of GDP in France, 14% in Germany, 12.4% in Italy and 6.8% in the United Kingdom.

However, with regard to economic analysis it is important to draw a distinction between employees' contributions and employers' contributions. The former differ little from income tax, at least as regards their macroeconomic impact. The latter add to labour costs: increasing them in order to finance a rise in social benefits has the same macroeconomic impact as a wage rise.

In most Community countries, the volume of employers' social insurance contributions increased considerably between 1970 and 1980 (Table No. 8): + 4% of GDP in Spain, + 2.6% in France, + 2.5% in Belgium, + 2% in the Netherlands and + 1.9% in Germany. Since then, their volume has stabilized.

With regard to employees' contributions, the increase was less marked between 1970 and 1980, but it continued between 1980 and 1987.

During periods of severe unemployment, the high level of employers' social insurance contributions in certain countries harms economic effectiveness. In France, for example, an employee whose gross earnings are 100 costs his employer 141 on the same scale and himself receives 84 as his net salary. If he were unemployed, he would receive an average benefit of 37. For the state, the cost of his being employed is $84 - 37 = 47$, i.e. one third of the wage and social cost borne by the firm (141). The cost which the firm puts down to the labour factor thus represents three times its cost to the state.

This explains why proposals are often made in France to reduce the burden of social insurance contributions on low wage-earners.

B. Contribution rates and value-added gain sharing

Employers' social insurance contributions are only one component of wage costs, wages themselves clearly being the main component, and it will emerge, from the arguments set out below, that the countries where social insurance contribution rates are highest are not those where value-added gain sharing is least favourable to firms.

Table No. 9 sets out the social insurance contribution rates applicable in the main European countries, whilst Table No. 10 shows how the value added by firms is shared between:

- on the one hand, employees' earnings (gross wages + employers' social insurance contributions);

- on the other, company profits (gross operating surplus)¹.

Putting these two tables side by side reveals just how much caution must be exercised in making international comparisons:

- Italy, the country with the highest employers' social insurance contribution rates, is also the country where wage costs make up the smallest proportion of the added value;
- Conversely, it is in Denmark that wage costs make up the highest proportion of the added value, whereas firms pay no social insurance contributions;
- In France, the proportion of the value added by firms made up by wage costs is comparable, and even slightly lower, to that in Germany, whereas the rate of employers' social insurance contributions is twice as high in France (36.5%) as in Germany (18%);
- In the United Kingdom, the proportion made up by wage costs is higher than in Germany and France despite much lower social insurance contribution rates.

C. Wage costs and compulsory deductions from wages

Table No. 11 sets out the results of a calculation designed to highlight all the compulsory deductions (employers' contributions, employees' contributions and income taxes) levied from the earnings of a worker who receives an average wage, whose wife does not work and who has two children.

A comparison restricted to the five main countries of the Community reveals that the German worker is the most expensive, followed in order by his Italian, French, British and Spanish counterparts.

The rate of compulsory deductions on the average worker's wage is highest in Italy, followed by Germany, France, Spain and the United Kingdom.

In this example, the French worker is alone in not paying income tax.

D. Experts' recommendations

As already noted, the long-standing differences between national compulsory deduction systems have been absorbed by market mechanisms which tend, in the long term, to even out the production costs of competing firms.

There is, therefore, no need to reduce the established differences in respect of social welfare systems or the 'costs borne by firms'.

In the future, the experts take the view that the ageing of the population will result, in all European countries, in an increase in welfare costs which will create a need for new resources.

¹ In order not to complicate the argument, no mention is made here of the third component of the added value, i.e. taxes on production (net of subsidies).

Table No. 12 traces likely changes² in the ratio between the number of persons aged over 65 and the active population. It will certainly lead to an increase in pension costs, but also in health-related expenditure, since a person aged over 65 requires, on average, 2.5 times as much care as a person aged under 65.

In order to determine the orders of magnitude involved, the experts set up a scenario based on the underlying trends in the French social welfare system from which it emerges that employees' social insurance contributions should be increased by 9% over 30 years.

According to the experts, each country may remain free to determine its level of welfare protection on condition that any increase in expenditure should be financed by means of deductions from households (insurance benefits logically being financed from social insurance contributions, whereas supplementary benefits should be financed from income tax).

If any increase in employers' social insurance contributions is to be ruled out, should they be reduced in those countries where they are highest? This would offer those countries a means of pursuing a competitive disinflationary policy, whereas the rules of the European Monetary System preclude 'competitive devaluations'.

Table No. 13 sets out the results of a simulation, conducted with the aid of the MIMOSA model, tracing the impact of a 1% annual reduction in employers' social insurance contributions in France, Italy and Spain. To offset this, an increase in deductions on households was assumed (income tax or social insurance deduction on overall income)³.

Only Italy benefits clearly from the simulated measures which have a restrictive overall effect on European growth as a whole.

In fact, the conditions for the success of a policy of 'competitive disinflation' are almost the same as for a 'competitive devaluation':

- Domestic demand must be squeezed in order to increase the exportable surplus (a condition met in the simulation by the rise in income tax);
- Exporters must not benefit so much that they are able to widen their profit margins and the volume of exports must increase more than their value falls (the sensitivity of exports and imports to price competitiveness is particularly marked only in the case of Italy);
- It is vital that several countries do not pursue the same policy at the same time (a condition not met in the simulation).

² The reader is reminded that forecasts of this kind are based on the hypothesis of sustainable control of migratory flows.

³ In the case of France, the simulated measure would correspond, for example, to the progressive assumption by the state of the cost of financing family allowances offset by a social insurance deduction on the overall income of households

III. INCOME TAX

This section will first deal with the general characteristics of the taxation of the income of households in the countries of the Community before moving on to the more specific problem of the taxation of income from investments in securities.

A. General characteristics of income taxation

Table No. 7 shows the revenue from income tax in the countries of Europe expressed as a percentage of GDP. The income tax/Community GDP ratio has risen from 6.1% in 1965 to 11.2% in 1987. The majority of this increase occurred in the 1970s.

The experts' report touches on many topics which cannot be summarized here: allowances by virtue of principal place of residence, allowances in respect of professional expenses, allowances specific to employees, other allowances, taxation of couples and measures to take account of children.

This section will merely compare the average tax rates and summarize the experts' conclusions.

1. Comparison of average rates of taxation of employees

In all the countries of the Community, progressive taxation is applied by means of a sliding scale in which successive income bands are taxed at increasing rates (Table No. 14). Germany has an original system: the marginal tax rate is an increasing monotonous function of the level of income, the number of bands therefore being virtually infinite. Certain countries prefer a very large number of bands; others employ only three or four. The trend is now towards the reduction of maximum rates. They range between 40% in the United Kingdom and 68% in Denmark. The French rate is not particularly high if one takes account of the fact that it must be multiplied by 0.72 for employees earning less than FF 50 000 per month.

The rate applicable to the final band in the scale is not necessarily an accurate indicator of the proportion of the tax burden borne by taxpayers whose incomes are high.

The experts calculated the tax paid in the various countries by typical taxpayers receiving only earned income: Table No. 15 shows the tax paid by an unmarried employee whose wages vary between 70% of the average worker's wage and five times that average wage; Table No. 16 takes the situation of a married couple with two children where, by convention, the woman earns the equivalent of 70% of her husband's wage: the incomes of the couples considered in this table thus vary between 1.2 times and 8.5 times the average worker's wage.

Alongside the income tax rate itself, it seemed interesting to show a tax rate including all social insurance contributions based on wages. These notional tax rates lend themselves much better than the others to international comparisons since they eliminate differences deriving from institutional choices in respect of the financing of social welfare systems.

For a single man (Table No. 15) receiving a low wage, income tax is very low in France, Spain and the Netherlands and very high in Ireland and, in

particular, Denmark. At higher wage levels, the tax rate is low in Italy, Spain and the United Kingdom and high in Denmark and Ireland.

Incorporating social insurance contributions brings the deduction rates very much more closely into line, although Spain and the United Kingdom remain appreciably below the average. The difference between tax brackets is greatly reduced: the deduction rate varies roughly between 40% for low wages and 60% for high wages, i.e. a 20-point difference, whereas for income tax alone the gap is 30 points in Belgium and Germany, 37 in France and 45 in the Netherlands.

For a working couple with two children (Table No. 16), the tax rate in the narrow sense is low in France, Italy and Spain and high in Belgium and Denmark. If the overall rate is taken, the disparity narrows considerably: deductions rise in step with wages in Belgium and Denmark, but lag far behind them elsewhere.

2. Experts' conclusions

Income tax is the prime example of a tax which should not be harmonized and which can remain an instrument for pursuing national economic policy objectives. The same applies to social insurance contributions borne by households.

The risks of workforce displacement, including that of the most skilled workers, on tax grounds are small. Gross wage levels and the cost of living, in particular of housing, are more important factors.

This diagnosis does not prevent the experts from putting forward recommendations to improve the French tax system. They regard a widening of the tax base (at present, roughly half of French households pay no income tax) and collection by deduction at source as desirable.

They also observe that high marginal rates have the drawback of making additional work barely profitable for skilled, well-paid individuals, highlighting the advantages of the British system where the maximum rate is lower than in other countries but the intermediate rates higher.

Finally, the French system of family-related rebates deserves to be taken as a model, in the experts' view.

B. Taxation of household income from investments in securities

With regard to fundamental principles, the experts challenge the validity of arrangements in national tax systems which favour income from investments in securities. However, the fact that these arrangements exist and that capital moves freely leads to a risk of 'competition to impose the lowest tax rate' which may give rise to the displacement of savings.

1. The failure of Community plans

In outline form, two systems can be conceived of with a view to maintaining the taxation of income from investments in securities in the Community:

(a) An identical withholding tax in all the Member States

The failure of the attempt to introduce such a mechanism in Germany led to the abandonment of the Community plan.

(b) Taxation of the holder of the capital invested in his or her country of residence

Certain countries, in particular France, apply this system, but its effectiveness is open to doubt. To be workable in the long-term it would require changes to the banking secrecy rules to which certain Member States, notably Luxembourg, are strongly attached and effective cooperation between national tax authorities. In addition, given the globalization of capital movements, the main countries in the world financial system would have to reach agreement on an international code of banking ethics (the United States seem to be advocating such a move).

2. The drawbacks inherent in the non-taxation of investment income

In the absence of a Community agreement, the short-term trend is likely to be towards the virtual exemption from tax of the majority of investment income in the Community. This trend can be criticized from several points of view:

- **Fairness:** taxation will be concentrated on earned income and property;
- **The financing of pension schemes:** national tax incentive systems designed to encourage the individual to save under private pension schemes will lose their *raison d'être*;
- **Economic effectiveness:** the experts take the view that the taxation of all income (earned and unearned) is preferable to the taxation of earned income alone.

In the longer term, if a code of banking ethics can be introduced at world level the experts propose, with a view to expanding the Community's own resources, the levying of a Community tax on unearned income.

IV. CORPORATION TAX

A. Main characteristics of the tax systems

As revealed by the comments on Table No. 7, corporate taxation accounts for only a fairly small proportion of tax revenue. It is important only in Luxembourg (because of the proliferation of financial institutions) and, to a lesser degree, in the United Kingdom (particularly by virtue of the size of the profits generated by oil companies) and in Italy.

1. Tax scale (Table No. 17)

Tax rates are generally high. They apply to gross profits net of interest and minus tax write-offs. In all the countries other than Denmark, write-offs are calculated according to the purchase price of the materials. In order to prevent this calculation method penalizing firms during periods of inflation, the tax write-off is more rapid than the economic depreciation, particularly by virtue of the declining balance depreciation system.

Nine countries operate the tax credit system with a view to preventing or limiting the double taxation of shareholders.

In overall terms, the methods of calculating this tax differ very greatly from one country to another and, for a modest yield, the tax gives rise to many administrative difficulties which hamper the free movement of capital in Europe.

2. The experts' criticisms

The group of experts voice many criticisms of the corporation systems currently in operation. In particular, they accuse them of treating interest, distributed profits and retained profits in a different way and thus of encouraging firms to borrow as much as possible. The irrational nature of the system is exacerbated during periods of inflation.

From the point of view of the effectiveness of the European economy as a whole, the existence of twelve national corporation tax systems gives rise to a situation whereby comparisons of the return on investments in accordance with their location produce differing results in respect of the return before tax and the return after tax.

A rational taxation system should meet two conditions of neutrality in connection with the location of the investment:

- neutrality in respect of the export of capital: a firm must be subject to the same taxation regardless of the country in which it invests; in this way, the choice of where to establish a subsidiary abroad is not influenced by taxation;
- Neutrality in respect of the import of capital: the tax rate must be the same for all firms established in a given country whatever the nationality of the parent company.

Table No. 18 takes the example of multinational companies planning investments on which they wish to secure a 5% return after tax. The table shows the pre-

tax return required according to the country of origin of the firm and the country in which the investment is made.

It emerges, for example, that in respect of investments in France, Danish, German and French firms are subject to the lowest tax rates, whereas Italian and Irish firms are the highest-taxed. Conversely, French firms are best advised to invest in Ireland, then in France; they are very highly taxed when they invest in Germany.

Table No. 19 shows, for each country, the pre-tax return required if a firm wishes to secure a 5% profit after tax. The following scenarios are covered:

- a firm from the country in question investing in that country (first column);
- a foreign firm investing in the country in question (second column);
- a firm from the country in question investing abroad (third column).

On the basis of these results, a 'capital import incentive ratio' (fourth column) and a 'capital export incentive ratio' (fifth column) can be calculated.

Consideration of the capital import incentive ratio shows that in most countries foreign firms are more highly-taxed than domestic firms, particularly in Greece. However, Portugal and, in particular, Ireland favour foreign firms. In Germany, domestic and foreign firms are treated in the same fashion.

Conversely, the capital export incentive ratio is particularly high in Germany and, to a lesser degree, in Denmark. There are fiscal disincentives to the export of capital in Ireland, Italy and Greece.

B. Experts' recommendations

The harmonization of corporate tax profits is desirable, not with a view to making conditions of competition between firms in the Community more equal⁴, but in order to ensure that rational choices can be made regarding the location of investments.

The only means of achieving 'double neutrality' (in respect of the export and import of capital) would be to standardize the rules governing the taxation of corporate profits throughout the Community.

With this in mind, the experts advocate that corporate taxation should ultimately become, either in full or in part, a Community tax. They also suggest, on the grounds of economic rationality, either incorporating interest

⁴ The reasoning here is similar to that put forward in connection with employers' social insurance contributions. The characteristics of corporation tax must not be considered in isolation when judging the comparative return on investments: in the long term, higher corporation tax must be reflected in lower labour costs and, therefore, a greater pre-tax return on investment. However, it still holds true that a country which lowers its tax rates temporarily offers its firms a competitive advantage (on condition that several countries do not take the same decision).

charges into the taxable profit or basing the tax on the total volume of capital used by firms.

However, the complete standardization of corporation tax in the Community would deprive Member States of the option of altering that tax other than through the application of a Community decision. This would perhaps be going too far, since many economic activities fall within what is known as the sheltered sector which is protected from foreign competition. The behaviour of firms in this sector would not be affected by international disparities in taxation systems which concern only transnational economic activities.

A less ambitious objective than the complete standardization of tax systems would be that of making taxation more neutral in respect of the location of investment. In this regard, it would be desirable for any firm operating in a country, whether as a domestic firm or the subsidiary of a foreign firm, should be taxed fully and exclusively in accordance with the tax system of the country in question, and that only its profits generated in that country should be so taxed.

V. VAT AND EXCISE DUTIES

A. Current situation

VAT plays an important role in the tax systems of all the European countries (Table No. 20), particularly in France, where in 1987 the proceeds from VAT reached 8.7% of GDP (i.e. 42% of state revenue). VAT is least important in Italy (5.3% of GDP and 23% of state revenue).

Excise duties are also a substantial source of revenue: 4.1% of GDP (and almost 20% of state revenue, almost as much as VAT) in the United Kingdom; 2.9% of GDP (and almost 20% of state revenue) in France; 2.6% of GDP in Italy, 2.4% in Germany and 2% in Spain.

1. VAT

The first difference which emerges from a comparison of national VAT systems concerns the rates (Table No. 21). The standard rate ranges from 12% in Spain and Luxembourg to 23% in Ireland (14% in Germany, 15% in the United Kingdom, 18.6% in France and 19% in Italy).

Denmark is unique in applying only a single VAT rate of 22%.

The reduced rates (certain countries apply several) are set at zero in the United Kingdom, 5.5% in France, 6% in Spain and 7% in Germany.

Six countries operate an increased rate applicable to certain luxury products and, in most cases, cars. This increased rate is 25% in France, 33% in Spain and 38% in Italy. However, it must be added that cars are often subject, in addition to VAT, to a specific tax which, in the United Kingdom for example, raises the total volume of taxes on car purchases to the same level as in France.

In addition to these VAT rate disparities, there are differences in the distribution of products among the rates, particularly in respect of petroleum products: Table No. 22 gives a number of examples.

Although the VAT assessment basis is already 90% harmonized, sizeable disparities remain in certain sectors such as telecommunications and passenger transport.

Finally, certain countries are less restrictive than others in respect of rights to deduct, for example for private cars, fuel, entertainment expenses and business travel.

2. Excise duties

The structure of excise duties varies considerably from one country to another.

As regards the taxation of petroleum products (Table No. 23)⁵, on the one hand there are countries such as Germany and the United Kingdom which levy relatively modest taxes on petrol and make diesel only slightly more attractive and, on the other hand, countries such as France and, above all, Italy which tax petrol heavily and apply reduced rates to diesel.

As regards alcoholic beverages, the tax disparities divide Europe into three areas: the north of Europe, in particular the United Kingdom, applies very high rates of duty to alcoholic beverages; the centre, in particular Germany and France, apply moderate rates; the south applies very low rates or no duty at all. Rate structures tend systematically to favour local production (wine or beer as appropriate).

The taxation of tobacco products is more uniform in overall terms. The proportion of the final price of cigarettes made up by duty varies relatively little between countries: it generally amounts to between 70 and 75%. However, the structure of the duties creates a distinction between producer countries and importing countries. As producers of dark tobacco, whose production costs are low, France and the southern European countries apply a system of ad valorem taxation which favours national products. Conversely, tobacco-importing countries place greater reliance on fixed duties, which favours light tobaccos, whose production costs are higher.

B. Budgetary impact of the approximation of indirect taxation

In December 1989, the Commission abandoned its initial plan of standardizing excise duties around Community averages. It is now proposing to fix minimum rates, applicable as of 1 January 1993, and to secure 'target rates' in the longer term, but without setting firm dates. The impact of these proposals on the tax revenue of the main Member States should ultimately be very small, at least in the foreseeable future.

The harmonization of national VAT systems raises more problems.

Once the Member States agreed, despite the reservations expressed by the Commission, that the disappearance of fiscal frontiers on 1 January 1993 did not require the transition, on the same date, from the system of taxation in the country of destination to that of taxation in the country of origin, the fixing of a new date for this switch became a key negotiating issue. However, this matter does not bear very closely on that of the approximation of VAT rates, which will now be examined.

⁵ In addition to the duty rates applied in the main countries of the Community, this table sets out the minimum rates which the Commission proposes to accept as of 1 January 1990 and the target rates which it plans to aim at in the long term.

1. The planned approximations of VAT rates

The Commission has proposed that national VAT systems should in principle operate only two rates: a standard rate, between 14 and 20%, and a reduced rate, between 4 and 9%⁶.

Exemptions may be granted, in particular for cars which, as they are subject to registration formalities, may have specific taxes applied to them equivalent to an increased rate of VAT.

Moreover, since the approximation of rates is only required for 'transferable' products, it is quite possible that electricity supply and telephone services, for example, might be taxed at differing rates according to the country concerned.

At all events, the strict harmonization of VAT rates is not necessary. It must be borne in mind that almost all transfrontier trade is carried out between firms subject to VAT which, since they recover the tax on their purchases, take into consideration only the prices net of tax. Moreover, mail order sales and purchases carried out by non-taxable major institutions (banks, hospitals, public authorities) could be subject to specific arrangements.

2. Budgetary impact of approximations of VAT rates

The approximations of VAT rates proposed by the Commission would raise the most serious budgetary problems in Denmark. The transition from the current system (single rate of 22%) to one comprising a standard rate of 18% and a reduced rate of 9% would cut 30% from the proceeds from VAT, i.e. roughly 9% of state revenue.

If, as the experts suggest, France merely implemented a strict minimum of harmonization measures, the cost could be limited to 2.5 billion ECU. In this case, cars would still have to be taxed at a higher rate, possibly through the application of a registration tax, and electricity and domestic fuel, intended in principle to be taxed at the reduced rate under the Commission proposals, would have to remain at the standard rate, since trade in these products is protected from international competition.

The cost of a broader harmonization could reach 4.5 bn ECU.

In Germany, whose VAT system comprises two rates, 14% and 7%, the changes would entail a slight widening of the assessment basis and the application of the reduced rate to products currently subject to the standard rate; this would lead to a loss in revenue totalling 1.0 bn ECU. However, if, at a later stage of negotiations, the Member States agreed to narrow the range for

⁶ The Member States have expressed their intention of laying down a narrower range for the standard rate (Council meeting of 18 December 1989). However, given the lack of precise details, the calculations referred to below are based on the Commission proposals. The Council wishes to lay down, by the end of 1991, the list of products subject to the reduced rate. A zero-rate would continue to apply to a limited range of items.

the standard rate (14% to 20%), this rate would have to be increased in Germany.

In Italy, the transition from the current four-rate system (ranging between 4 and 38%) to a two-rate system could be achieved without affecting the budget by applying a standard rate of 16% and a reduced rate of 4%.

As regards the United Kingdom, budgetary problems do not arise, since it is the continued application of a zero rate which is at issue. Products benefiting from this rate account for almost 30% of household expenditure. Their taxation at a rate of 4% would be inflationary and would generate a tax take of 4.6 bn ECU. However, it is perhaps not essential to abandon the zero rate, since the goods to which it applies are not likely to be traded internationally in any volume.

In Spain, the standard rate should be increased from 12% to 14% and the increased rate (33%) should be abandoned. These two measures would lead to a slight increase in tax revenue.

OTHER SUBJECTS DEALT WITH IN THE EXPERTS' REPORT

Several chapters in the experts' report have not been dealt with in the above summary.

They cover:

- local taxation;
- the taxation of households' financial assets;
- Community taxation;
- tax reforms implemented in the major OECD countries;
- the macroeconomic consequences of the complete standardization of indirect taxation.

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TABLES

B Belgium
 DK Denmark
 D Germany
 GR Greece
 ESP Spain
 F France
 IRL Ireland
 ITA Italy

LUX Luxembourg
 NL Netherlands
 POR Portugal
 UK United Kingdom
 EUR European average
 USA United States
 JAP Japan

Table No. 1

**Level of and trends in compulsory deduction rates
 - OECD definitions -**

(% of GDP)

	Level in 1965	Variations			Level in 1987
		from 1965 to 1973	from 1973 to 1979	from 1979 to 1987	
B	30.8	6.6	7.1	1.6	46.1
DK	29.9	12.5	2.1	7.5	52.0
D	31.6	4.7	1.4	-0.1	37.6
GR	20.6	2.6	6.9	7.3	37.4
ESP.....	14.5	4.3	4.6	9.6	33.0
F	34.5	0.5	5.2	4.6	44.8
IRL	26.0	5.2	0	8.7	39.9
ITA	25.5	-1.1	2.2	9.6	36.2
LUX	30.4	2.7	7.1	3.6	43.8
NL	33.2	8.6	3.2	3.0	48.0
POR	18.4	3.5	4.1	5.4	31.4
UK	30.4	1.0	1.4	4.7	37.5
EUR	29.5	2.6	2.9	4.6	39.6
USA	25.9	2.8	0.3	1.0	30.0
JAP	18.3	4.2	1.9	5.8	30.2

Source: OECD

Table No. 2

Compulsory deductions and public expenditure
- National definitions -

(% of GDP)

	Compulsory deductions (A)	Public sector deficit (B)	TOTAL A + B = D + E + F (C)	Social benefits (D)	Net interest payments (E)	Other net expendi- ture (F)
B (1)	45.7	7.2	52.9	21.4	10.5	21.0
DK (1)	52.3	-2.0	50.3	16.4	4.5	29.4
D (1)	41.2	1.8	43.0	16.0	2.8	4.2
GR (1)	35.2	12.00	47.2	13.8	7.2	26.2
ESP (2) ...	30.9	6.1	37.0	16.2	3.1	17.7
F (1)	44.6	2.0	46.6	21.9	2.1	22.6
IRL (2)....	41.0	11.8	52.8	17.0	9.5	26.3
ITA (1) ...	35.6	11.2	46.8	17.3	7.3	22.2
LUX (2) ...	41.6	- 2.7	38.9	19.5	1.1	18.3
NL (1)	47.3	6.5	53.8	26.4	5.2	22.2
POR (2) ...	34.5	6.4	40.9	11.6	8.8	20.5
UK (2)	38.4	2.4	40.8	14.0	3.0	23.8
USA (1) ...	30.2	2.6	32.8	10.8	3.6	18.4
JAP (1) ...	30.0	-0.6	29.4	11.8	4.4	13.2

(1) 1987 (2) 1986

Source: OECD

(3) Minus sign signifies surplus

Table No. 3

Role of general government in social transfers

(% of GDP)

	Social insurance contributions			Social benefits		
	Included in compulsory deductions	Others	Total	Paid over by govern- ments	Others (3)	Total
D (1)	14.0	5.00	19.0	16.0	4.4	20.4
ESP (2) ...	11.9	3.0	14.9	16.2	2.3	18.5
F (1)	19.2	3.3	22.5	21.9	1.7	23.6
ITA (1)	12.5	4.4	16.9	17.3	4.4	21.7
UK (2)	6.9	3.6	10.5	14.0	4.5	18.5
USA (1) ...	8.7	6.0	14.7	10.8	6.8	17.

(1) 1987 (2) 1986

Source: OECD

(3) Mutual associations, employers' schemes, other private funds

Table No. 4

Net public debt

(% of GDP)

	1980	1988
B ¹	69.3	124.5
DK ¹	33.5	56.1
D ¹	14.3	23.5
GR ¹	27.7	71.5
ESP	7.8	31.1
F	14.3	25.5
IRL	78.0	137.6
ITA	53.6	92.4
NL	24.9	55.4
UK	47.5	38.4
EUR	27.8	43.2

1 Gross debt

Source: OECD

Table No. 5

Primary deficit and primary surplus
required to control the debt

(% of GDP)

	Primary deficit in 1988	Primary surplus required ¹ minimum/maximum
B	2.4	1.9/2.5
DK	4.3	0.9/1.2
D	0.3	0.2/0.3
GR	-7.2	0.7/1.1
ESP	-0.4	0.3/0.5
F	0.7	0.4/0.5
IRL	2.8	1.4/2.1
ITA	-2.5	1.6/2.0
NL	-0.4	0.9/1.2
UK	3.3	0.6/0.8

- 1 The results are presented in the form of a target range reflecting the various hypotheses concerning the rate of growth of GDP and the level of interest rates

Source: OFCE - CEPII

Table No. 6

Expenditure on medical care

(% of GDP)

	1970			1987		
	Public expenditure	Other expenditure	Total	Public expenditure	Other expenditure	Total
D	4.2	1.4	5.6	6.3	1.7	8.0
F.....	4.3	1.8	6.1	6.7	2.0	8.7
ITA	4.8	0.7	5.5	5.7	1.5	7.2
UK	3.9	0.6	4.5	5.3	0.8	6.1
USA.....	2.8	4.8	7.6	6.0	5.1	11.1
JAP.....	3.0	1.6	4.6	5.0	1.9	6.9

Source: OECD

Table No. 7

Classification of compulsory deductions according to the
economic nature of their assessment basis
(1987)

(% of GDP)

	B	DK	D	GR	ESP	F	ITA	NL	UK	EUR
HOUSEHOLD INCOME	22.0	27.5	18.4	10.8	10.3	13.9	13.3	22.6	15.7	16.0
including:										
- Income tax	15.1	25.6	10.9	4.6	7.0	5.7	9.5	9.5	10.0	9.6
- Employees' social insurance contributions	5.1	1.0	6.1	5.3	2.0	5.5	2.4	9.0	3.1	4.5
CORPORATE INCOME										
(corporation tax)	3.0	2.3	1.9	1.7	2.2	2.3	3.8	3.7	4.0	2.8
LABOUR COSTS	9.4	1.3	7.2	5.7	9.1	13.0	8.9	8.2	3.5	8.2
Other production costs ..	0.2	1.5	0.8	0.2	0.1	2.1	0	0.6	2.6	1.1
PRODUCT PRICES	10.5	17.0	9.1	16.7	9.7	12.7	9.1	11.4	11.1	10.7
including:										
- VAT	7.2	9.8	5.9	10.0	5.6	8.7	5.3	7.9	6.0	6.7
- Excise duties	2.1	6.7	2.4	4.8	2.0	2.9	2.6	2.7	4.4	3.0
OTHERS	1.0	2.4	0.2	2.3	1.6	0.8	1.1	1.6	0.6	0.8
TOTAL.....	46.1	52.0	37.6	37.4	33.0	44.8	36.2	48.0	37.5	39.6

Table No. 8

Trends in social insurance contributions from 1970 to 1987

(% of GDP)

	Employers' contributions				Employees' contributions			
	Level in 1970	Variation		Level in 1987	Level in 1970	Variation		Level in 1987
		from 1970 to 1980	from 1980 to 1987			from 1970 to 1980	from 1980 to 1987	
B	5.9	+ 2.5	+ 1.0	9.4	3.2	+ 0.6	+ 1.3	5.1
D	5.3	+ 1.9	0	7.2	4.5	+ 1.3	+ 0.3	6.1
GR	3.7	+ 0.7	+ 0.9	5.3	3.3	+ 1.0	+ 1.0	5.3
ESP	5.1	+ 4.0	0	9.1	1.3	+ 1.3	- 0.6	2.0
F	9.3	+ 2.6	+ 0.3	12.2	2.4	+ 2.2	+ 0.9	5.5
IRL	1.4	+ 1.8	+ 0.3	3.5	1.2	+ 0.4	+ 0.4	2.0
ITA	7.9	+ 0.7	+ 0.1	8.7	2.0	+ 0.1	+ 0.3	2.4
NL	6.2	+ 0.2	0	8.2	5.8	+ 1.4	+ 1.8	9.0
UK	2.7	+ 0.9	0	3.6	2.3	0	+ 0.8	3.1

Table No. 9

Social insurance contribution rates

(%)

	Employers' contributions	Employees' contributions	Ceiling (% of average worker's salary)
B	27.7	12.0	-
D	18.0	18.0	130/170
GR	22.2	13.3	180
ESP	30.6	6.0	220
F	36.5	16.4	130 (a)
IRL	12.4	7.8	170
ITA	48.1	8.2	-
NL	24.5	34.1	120/160/170
POR	24.5	11.0	-
UK	10.5 (b)	9.0 (b)	150 (c)

(a) Solely for old-age pension contributions under basic scheme.

(b) Reduced rates for very low wage-earners.

(c) Solely for employers' contributions.

Table No. 10

Value-added gain sharing
(1987)

(% of value added)

	Wage and social costs	Gross operating surplus
B	52.9	36.5
DK	56.5	27.1
D	53.6	36.3
ESP	45.8	45.6
F	53.0	34.5
ITA	45.2	47.8
NL	53.6	36.9
UK	54.9	31.0

Source: CEPII

Table No. 11

Wage costs and disposable income after tax
for a worker receiving an average wage
(Annual earnings in ECU)

(% of GDP

	Cost to firm (A)	Gross wage (B)	Net wage (C)	Disposable income after tax (D)	Deduction rate in %	
					A-C A	A-D A
B	22 360	15 650	13 860	11 600	38	48
DK	24 280	23 800	23 300	14 640	4	40
D	23 670	20 100	16 600	14 840	30	37
GR	8 400	6 550	5 540	5 340	34	36
ESP	13 750	10 600	9 900	9 210	28	33
F	18 880	13 200	10 940	10 940	42	42
IRL	13 770	12 250	11 600	918	16	34
ITA	19 740	13 200	12 250	10 040	38	49
LUX	19 110	16 630	14 710	14 570	33	34
NL	22 280	17 800	13 400	11 820	40	46
POR	4 550	3 650	3 250	3 030	29	33
UK	18 820	16 450	15 000	12 170	18	32

(1) Income tax has been calculated for a single-income couple with two children.

Source: OECD, OFCE calculations

Table No. 12

Ratio between the number of persons over 65
and the active population (16-65)

(%)

	1980	1990	2000	2010
B	21.9	21.2	21.9	23.6
DK	22.2	22.5	21.5	24.3
D	23.4	22.3	25.4	30.5
GR	20.5	18.3	22.7	25.8
ESP	17.2	19.4	21.9	22.9
F	21.9	20.9	23.4	24.5
IRL	18.2	18.5	16.9	16.4
ITA	20.7	20.2	22.6	25.7
NL	17.4	18.4	19.8	22.0
POR	16.2	17.9	20.7	21.3
UK	23.3	23.0	22.3	22.7

Source: OECD

Table No. 13

Macroeconomic impact of a 1% annual reduction in employers' social insurance contributions offset by a rise in deductions from household incomes in France, Italy and Spain

(% disparities by comparison with constant rates)

	Germany		France		Italy		Other EEC	
	1st year	4th year	1st year	4th year	1st year	4th year	1st year	4th year
GDP (Volume).....	- 0.0	- 0.4	- 0.1	- 0.3	0.0	0.4	- 0.1	- 0.2
Exports (Volume)	- 0.1	- 0.7	- 0.1	- 0.1	0.0	0.4	- 0.1	- 0.3
Imports (Volume)	- 0.1	- 0.3	- 0.3	- 0.8	- 0.3	- 0.7	- 0.1	- 0.7
Consumer prices	0.0	- 0.1	- 0.3	- 0.2	- 0.4	- 2.4	- 1.2	- 1.2
Purchasing power of households	- 0.0	- 0.2	- 0.3	- 0.1	- 0.1	- 0.5	-	-
Current foreign balance (% of GDP)	- 0.0	- 0.0	0.1	0.1	0.0	0.1	0.0	0.1

N.B. This table does not include results for the United Kingdom, since the majority do not differ significantly from zero. Spain is included in 'Other EEC'.

Source: MIMOSA model (CEPII-CFCE)

Table No. 14

Characteristics of income tax scales

	Number of bands	Maximum rate (%)	Maximum rate threshold ⁽¹⁾ as multiple of average worker's salary
B	13	70.8	7.3
DK	3	68	1.1
D	00	56	3.1
ESP	17	56	5.5
F	13	56.8	2.5
IRL	4	58	1.0
ITA	8	50	15.0
LUX	25	56	1.7
NL	10	72	5.5
UK	3	40	1.9

⁽¹⁾ For a single man.

Table No. 15

Average rates of tax paid by a single male worker:

(a) income tax rate¹(b) overall deduction rate²

(%)

Wage as multiple of average worker's wage	0.7		1		2		3		5	
	(a)	(b)	(a)	(b)	(a)	(b)	(a)	(b)	(a)	(b)
B	18	43	25	48	38	57	40	58	48	64
DK	40	42	45	46	56	57	60	60	63	63
D	16	42	20	45	31	48	40	50	46	51
ESP	6	33	12	37	20	42	24	41	31	41
F	3	42	8	45	16	50	21	53	40	57
IRL	27	40	34	46	46	54	50	55	53	57
ITA	14	45	18	48	24	52	27	54	32	57
NL	7	44	12	48	26	53	39	55	52	59
UK	18	31	21	35	24	35	29	39	33	41

¹ Tax paid
Net wage

² Income tax + employers' and employees' social insurance contributions
Gross wage + employers' social insurance contributions

Table No. 16

Average rates of tax paid by double-income couple with two children:

(a) income tax rate¹(b) overall deduction rate²

(%)

Two wages as multiple of average worker's wage	0.7 + 0.5		1 + 0.7		2 + 1.4		3 + 2.1		5 + 3.5	
	(a)	(b)	(a)	(b)	(a)	(b)	(a)	(b)	(a)	(b)
B	14	40	23	46	37	56	44	55	53	67
DK	38	41	43	44	54	55	59	59	62	63
D	12	39	16	41	26	46	34	47	53	50
ESP	2	29	8	34	18	41	22	41	29	41
F	0	40	4	42	10	46	16	49	22	53
IRL	22	36	27	40	41	51	47	53	51	54
ITA	10	35	13	37	21	43	25	46	30	50
NL	6	41	10	46	23	51	35	53	48	57
UK	16	29	20	33	23	36	27	38	32	40

¹ Tax paid
Net wage

² Income tax + employers' and employees' social insurance contributions
Gross wage + employers' social insurance contributions

Table No. 17

Rate of corporation tax
(1990)

(%)

	Tax rate	Tax credit rate (1)
B	43	73
DK	50	40
D	36(a)/50(b)	100
GR	40 (c)/46	100
ESP	35	26
F	37(b)/42(a)	69
IRL	10(c)/43	83
ITA	36	100
LUX	34	0
NL	35	0
UK	35	71

(1) Proportion of tax on distributed profits regarded as part-payment of shareholders' income tax

(a) Distributed profits (b) Retained profits

(c) Reduced rate applicable to manufacturing firms

Table No. 18

Rate of pre-tax return required to obtain a 5% return after tax

(%)

Country of origin	Country in which the investment is made									
	B	DK	D	GR	F	IRL	ITA	NL	POR	UK
B	5.83	6.34	6.36	6.36	6.53	7.17	7.24	6.71	6.71	6.61
DK	8.35	7.02	7.64	9.36	7.24	7.84	9.42	7.38	8.01	7.28
D	9.07	8.63	8.86	8.66	8.92	9.23	10.30	9.12	8.21	8.51
GR	6.69	7.51	6.46	5.55	7.73	8.52	7.27	7.41	7.95	7.82
F	6.26	5.67	5.69	6.75	5.75	6.81	7.09	6.17	6.59	6.08
IRL	4.68	4.53	4.54	4.57	4.64	5.08	4.53	4.77	4.85	4.71
ITA	6.30	6.07	6.92	6.52	6.24	6.87	5.60	5.91	6.42	5.97
NL	6.28	7.03	6.27	6.47	6.73	6.52	6.74	6.11	7.58	6.25
POR	6.36	6.00	6.11	6.13	6.28	6.87	7.04	6.43	6.59	6.25
UK	5.71	7.24	5.91	6.64	6.11	6.60	6.93	5.75	7.02	6.12

Source: Institute for Fiscal Studies

Table No. 19

Capital import and export incentive ratios

	Pre-tax return required (%) for a 5% profit after tax			Incentive ratios	
	Domestic investment (A)	Investment from abroad (B)	Investment abroad (C)	Import of capital (A)/(B)	Export of capital (A)/(C)
B	5.83	6.67	6.78	0.88	0.86
DK	7.02	7.96	6.61	0.88	1.06
D	8.86	8.83	6.35	1.00	1.40
GR	5.55	7.59	6.97	0.73	0.80
ESP	6.10	6.90	6.91	0.88	0.88
F	5.75	6.33	6.70	0.91	0.86
IRL	5.08	4.68	7.41	1.09	0.69
ITA	5.60	6.32	7.54	0.89	0.74
LUX	6.19	6.74	6.69	0.92	0.93
NL	6.11	6.63	6.68	0.92	0.92
POR	6.59	6.37	7.22	1.03	0.91
UK	6.12	6.46	6.65	0.95	0.92
USA	5.93	6.67	6.76	0.89	0.88
JAP	8.24	8.22	7.07	1.00	1.17
Average	6.35	6.88	6.88	0.92	0.92

Source: Institute for Fiscal Studies

Table No. 20

**VAT and excise duties as proportion of state revenue
(1987)**

	VAT		Excise duties	
	% of GDP	% of state revenue	% of GDP	% of state revenue
B	7.2	25.8	2.1	11.7
DK	9.8	27.8	6.7	20.3
D	5.9	29.3 (a)	2.4	16.0
GR	10.0	40.7	4.8	27.0
ESP	5.6	25.4 (b)	2.0	19.5
F	8.7	41.8	2.9	19.8
IRL	8.1	24.4	6.9	24.1
ITA	5.3	22.9	2.6	16.2
LUX	5.9	21.8	4.0	16.6
NL	7.9	30.5	2.7	13.8
POR	6.6	31.8		
UK	6.1	23.0	4.4	21.1

(a) Federal Republic + Länder

(b) State + regions

Table No. 21

VAT rates in Europe

(%)

	Reduced rates	Standard rate	Increased rates
B	0-6-17	19	25-33
DK	-	22	-
D	7	14	-
GR	6	18	36
ESP	6	12	33
F	5.5	18.6	25
IRL	0-5-10	23	-
ITA	4-9	19	38
LUX	3-6	12	-
NL	6	18.5	-
POR	0-8	16	30
UK	0	15	-

Table No. 22

VAT rates applicable to certain specific products

(%)

	Food products	Petroleum products	Books	Newspapers
B	6	17	6	6
DK	22	22	22	22
D	7	14	7	7
ESP	6	6-12	6	12
F	5.5	18.6	5.5	2.1
IRL	0	10	0	10
ITA	4-9	9-19	4	9
LUX	6	6	0	12
NL	6	20	6	6
UK	0	0	0	0

Table No. 23

Main tax rates for petroleum products

(ECU for 1000 litres)

	Super	Diesel	Domestic fuel
B	260.94	122.31	0
DK	472.50	236.25	236.25
D	255.77	213.29	8.11
GR	367.30	138.91	95.37
ESP	188.69	30.91	38.42
F	388.50	190.49	53.21
IRL	361.50	279.08	48.04
ITA	552.69	177.62	177.62
LUX	208.75	100.18	0
NL	340.33	108.83	43.86
POR	357.75	161.77	23.24
UK	270.69	228.92	16.36
Commission proposals:			
- Minimum rate	337	195-205	47-53
- Target rate	340	200	50

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