Taxation trends in the European Union

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Statistic

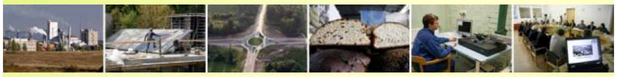
Indicator	Latvia	Hungary
Population	1 989 500	9 855 571
Area, km²	64 589	93 030
Neighbors	Lithuania, Estonia, Russia, Belarus	Austria, Croatia, Romania, Serbia, Slovakia, Slovenia, Ukraine
Currency	EUR	HUF
GDP, $ per 1 inhabitant	25 195 (2015)	23 609 (2014) 26 941 (2016 estimate)
EU accession	On 1 May 2004	On 1 May 2004
The highest mountain, m	Gaiziņkalns 311	Kékes 1 014
Forests	45%	19%

Tax support for agriculture

Tax support for rural tourism

Tax support for investment

Tax support for free ports and special economic zones



Tax support for environmental protection

Tax support for small companies

Tax support for families with children

Tax support for donations

Terms English - Hungarian

tax	adó
taxpayer	adófizető
tax rate	adókulcs
tax relief	adómentesség
tax deduction	adólevonás
tax credit	adó hitel
tax deferral	adóhalasztást
tax annulations	adó annulations
tax burden	adó teher
indirect taxes	közvetett adók
direct taxes	közvetlen adók
value added tax (VAT)	hozzáadottérték-adó, áfa
corporate income tax (CIT)	társasági adó
personal income tax (PIT)	személyi jövedelemadó
social contributions	társadalombiztosítási hozzájárulások
excise duty	jövedéki
natural resource tax	természeti erőforrás adó
property tax	tulajdon adó

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Definition of "Taxes" - an obligatory payment enforced by the government and levied on corporations or individuals to finance government activities.

Tax development (1)

- Taxation - financial ratio component of the country's existence.
- The economic substance – by paying taxes a part of private consumption is given to public consumption.
- Taxes are needed to finance public needs
  - for administration of justice and ensuring the country's defence (not regular);
  - natural fees (taxes in kind) as yield: grain, oil, honey, cattle etc.
  - public administration maintenance (regular)
  - special state tax collection officials (Egypt, India, China, Babylon, etc.)
  - taxes as activities: road and bridge building, construction work, military services etc.

Tax development (2)

At the final stage of the Roman Empire – existed highly developed tax system, about 200 types of taxes

- **Direct taxes**:
  - land, property, slaves, cattle, heritage, etc.
- Later emerged **indirect (consumption) taxes**, such as:
  - trade taxes: 1% of the sales of goods, 4% of the sales value of the slave,
  - for the use of roads and bridges,
  - wine, grain, cucumbers, soap, toilet tax (money does not smell) etc.
  - tax levy on having a donkey (the seal similar to the modern car registration)

Medieval Europe - fragmented, disordered local tax system contributed to the discontent that led to revolutions (XVIII century).

The evolution of tax theories

- The first systematized work of taxes – **W.Petty "A Treatise of Taxes and Contributions"** (1662)
  - Tax systems injustice
  - Stimulating economic activity with sensible tax policy
- In XVIII - XIX centuries **classic tax theory** developed - **A.Smith** (1723-1790), **D.Rikardo** (1772-1823)
  - Taxes are organized systematic shares of the income and property giving for state
  - Taxes is main source of financing public spending
- In XIX - XX century **J.M.Keynes** (1883-1946) theory
  - Taxation is a key element of national economic regulation
  - Taxes are divided into consumption and savings taxes
    - higher taxes should be incurred on savings
- **Supply side economy** - **A.B.Laffer** (1940)
  - High tax rates have a negative impact on business and investment activity (LAFER curve);
  - Rate reduction can be a positive impact on economic development.

Tax science nowadays

- Tax - mandatory, coercive, gratuitous payment with no penalty or compensation character.
- From the economic theory point of view, taxes are the economic allocation of resources, the national income redistribution and macroeconomic stabilization tool
- key functions of tax payments:
  - **fiscal function** - public goods need financing source;
  - **economic regulation function** - affect individuals and legal entities behaviour and the behaviour of a market economy;
  - **social function** (income redistribution)
  - **protection of local market function**
  - **ecological function**, etc..

Tax is a mandatory periodic or one-off payment prescribed by law for ensuring the revenues of the State budget or local government budgets and the funding of the functions of the state and local governments. The payment of taxes does not imply any compensation to the taxpayer directly *(LR Law: On Taxes and Duties)*

Tax elements

1. **Taxpayer** (subject) - a person who is liable to pay the tax in question
2. **Taxable object** - economic phenomenon to which the tax applies (income, property, expenses, consumption of certain transactions)
3. **Tax base** - tax object quantitative indicator, which is taxed according to the rate
4. **Tax rate** - a specific amount of tax on a single base size (in absolute terms or as a percentage)
5. **Tax relief** - tax cuts (tax exemption, tax deduction, tax credit, tax deferral, tax annulations)
6. **Organisation of tax collection** - determination of tax liability: term frequency, payment arrangements (advances), etc.

Breakdown of taxes

- **By tax items**: property, revenue, transactions
- **By collection type**:
  - **direct taxes**
    - property (real estate, vehicles, capital, wealth, property registration);
    - income (PIT, CIT, gift and inheritance, capital gains, dividends, etc.).
  - **indirect taxes**
    - universal consumption taxes (VAT)
    - specific consumption taxes (excise)
    - customs duties
  - **social taxes**
  - **special tax regimes** (agricultural tax, patent fees or constant payment for any sector etc.).

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Taxation (policy)

Taxation is a set of state measures directed to the stimulation of economic growth, while ensuring public goods and public funding needs, taking into account taxpayers' interests and rights.

- Government instrument:
  - to increase the state’s competitiveness
  - taxes serve for support for innovation and economic growth (in economic sectors, territories).
- **The main indicator of fiscal policy - tax burden.**
- Today, the tax policy is directed towards:
  - reducing the tax burden, or at least ensuring stability,
  - reducing the number of taxes and the amount or simplifying fiscal procedures (reducing tax administration costs).

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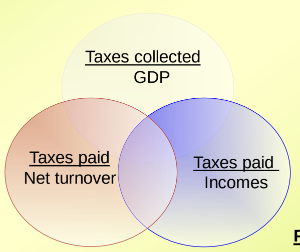
Tax burden

For a country



For a company

For a person

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The tax policy in the EU

Indirect taxation - harmonisation of Member States' rules, because indirect taxes may create an immediate obstacle to the free movement of goods and the free supply of services within an Internal Market. They may also create distortions of competition.

- VAT - determination of taxable persons, taxable transactions, requirements of VAT rates: standard rate ≥ 15%, 1-2 reduced rate ≥ 5%, still lower rates apply as an exception.
- Excise Duties - determination of the minimum rate, taxable goods, the movement of goods and the payment procedure. EU is governed by 3 excise goods groups: alcohol, tobacco, energy (fuel, gas, coal, etc.).

Other taxes - only some recommendations and legislation have been adopted in the personal tax, company tax and capital duty areas to avoid creating barriers to the single market and ensuring the free movement of goods, services, capital and persons.

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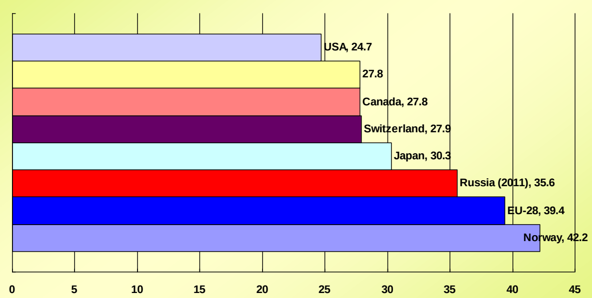
Definition of “Tax burden” - the amount of tax paid by a person, company, or country in a specified period considered as a proportion of total income in that period.

- Gross Domestic Product (GDP) per capita (1 inhabitant) in 2013 (EU-28 100%)
  - Luxembourg 264%, Austria 129%, Netherlands 127%, Sweden 127%
  - Bulgaria 46%, Romania 54%, Croatia 61% (Latvia 67%)

Tax burden in the EU and selected countries, 2012



Source: *Taxation trends in the European Union (eurostat)*

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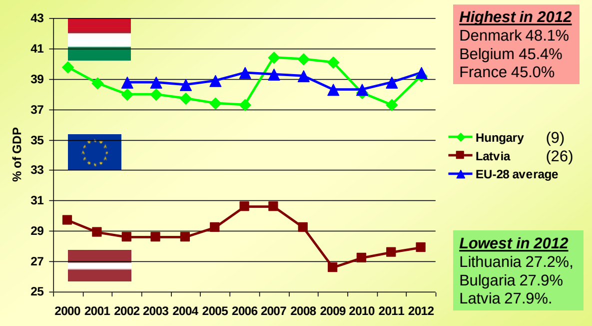
Total Taxes as % of Gross Domestic Product (GDP)



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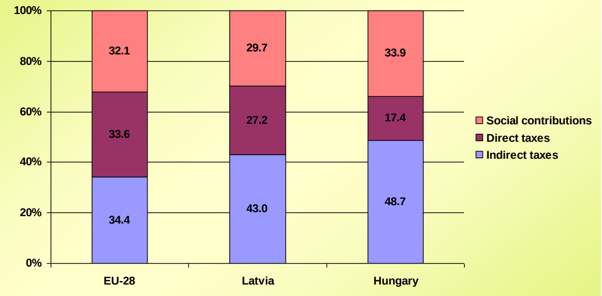
Tax revenues by main taxes 2013, %



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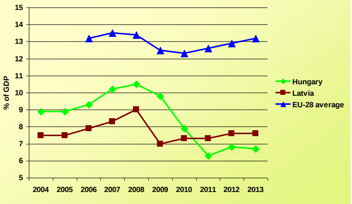
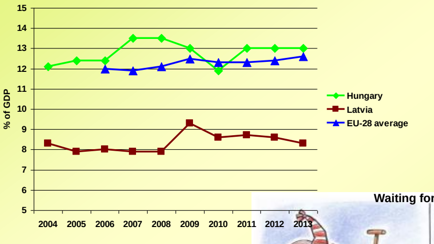
Indirect Taxes as % of GDP

Direct Taxes as % of GDP



Social contributions as % of GDP



Waiting for the pension ☺

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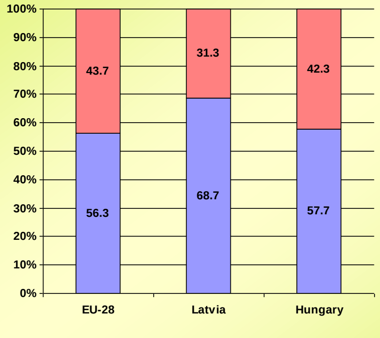
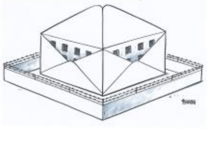
Social Contributions by payers 2013, %

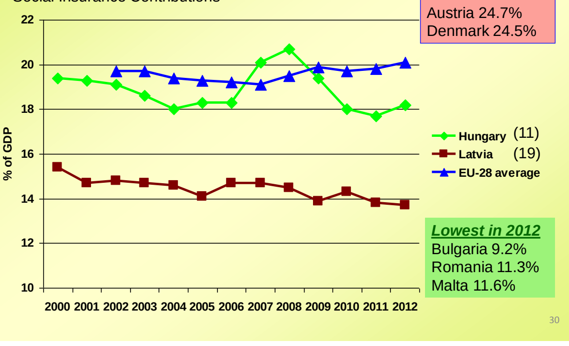


“Envelope” wages



Taxes on Labour as % of GDP

Paid by employers and employees:
- Personal income tax
- Social Insurance Contributions



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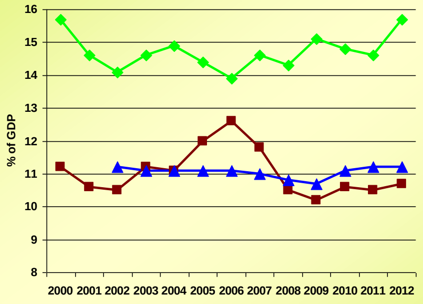
Taxes on Consumption as % of GDP

- Value added tax (VAT)
- Excise duties and other taxes on consumption



Highest in 2012
Croatia 17.5%
Hungary 15.7%
Denmark 14.9%

Lowest in 2012
Spain 8.6%
Slovakia 9.5%
Ireland 10.0%

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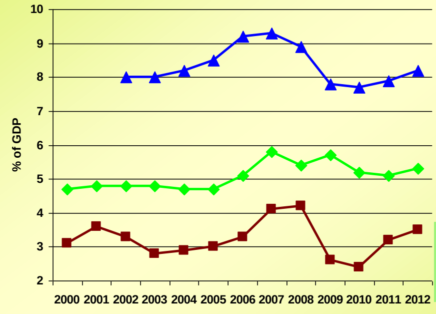
Taxes on Capital as % of GDP

- From capital and business income



Highest in 2012
Luxembourg 10.8%
Italy 10.6%
France 10.6%

Lowest in 2012
Estonia 2.3%
Latvia 3.5%
Croatia 3.7%

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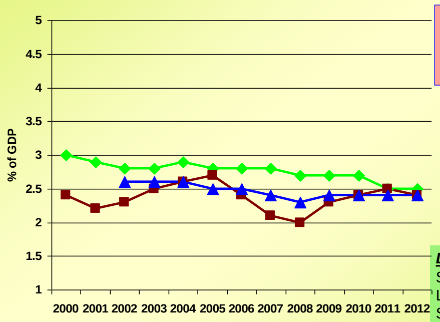
Environmental Taxes as % of GDP



Highest in 2012
Denmark 3.9%
Slovenia 3.8%
Netherlands 3.6%

Lowest in 2012
Spain 1.6%
Lithuania 1.7%
Slovakia 1.8%

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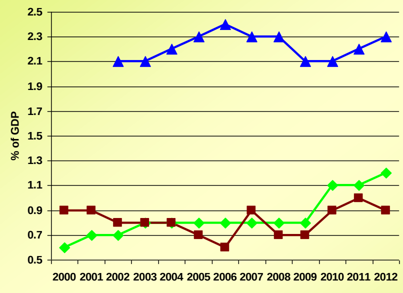
Property Taxes as % of GDP



Highest in 2012
United Kingdom 4.1%
France 3.6%
Belgium 3.4%

Lowest in 2012
Croatia 0.3%
Estonia 0.3%
Lithuania 0.5%

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Basics of tax system in Latvia

- 16 taxes
  - 12 taxes paid into the state budget
    - **Corporate income tax 15%**
    - **Value added tax 21%**
      12% books, medicine, newspapers, hotels, passenger transport etc.
    - **Social Insurance Contributions 34.09%**
    - **Excise duties** depending on the tax object, etc.
  - 2 divided between the state and municipal budgets:
    - **Personal income tax 23%**
    - **Natural resource tax** depending on the tax object
  - 1 paid into the local government budget
    - **Property tax 1.5%** on property cadastral value
- State and local government fees

Taxes on salary in Latvia

Personal income tax (PIT)
State Social Insurance Compulsory Payment (SSICP)

The **minimum salary** per month: EUR 370 (2016)

Calculation of salary and taxes
Gross salary
- 10.5% **employee's SSICP**
- EUR 75 non-taxable income
- EUR 175 allowance for 1 dependant (not working children, student)
= Taxable income x 23%
= **PIT**

Net salary = Gross salary - Total taxes (Employee's SSICP + PIT)

Employer's SSICP 23.59% x gross salary

Taxes on salaries depending of tax relief in Latvia in 2016, EUR

Indicator	Without tax relief	Tax relief	1 child	2 children
Gross salary	1000.00	1000.00	1000.00	1000.00
Employee's SSICP	105.00	105.00	105.00	105.00
Non-taxable income	0.00	75.00	75.00	75.00
Allowance for dependants	0.00	0.00	175.00	350.00
Taxable income	895.00	820.00	645.00	470.00
Personal income tax 23%	205.85	188.60	148.35	108.10
Total taxes	**310.85**	**293.60**	**253.35**	**213.10**
Net salary	**689.15**	**706.40**	**746.65**	**786.90**
Employer's SSICP	235.90	235.90	235.90	235.90
Staff costs	**1235.90**	**1235.90**	**1235.90**	**1235.90**
Tax payments in the budget	546.75	529.50	489.25	449.00

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Taxes on salaries in Latvia, CR, Hungary without tax relief in 2016, EUR

Indicator	Latvia	Czech Republic	Hungary
Gross salary	1000	1000	1000
Employee's SSICP	10.5% -105	11% - 110	9% - 90
Employer's SSICP	23.6% - 236	34% - 340	30.98% - 310
Taxable income	895	1340	910
Personal income tax	23% - 206	15% - 201	137
Total taxes from employee	**311**	**311**	**227**
Net salary	**689**	**689**	**773**
Staff costs	**1236**	**1340**	**1310**
Tax payments in the budget	547	651	536

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Taxes on salaries in Latvia, CR, Hungary for parent with 2 children in 2016, EUR

Indicator	Latvia	CR	Hungary
Gross salary	1000	1000	1000
Employee's SSICP	10.5% -105	11% - 110	9% - 90
Employer's SSICP	23.6% - 236	34% - 340	30.98% - 310
Non-taxable income	**75**	0	0
Allowance for children	**175 x2 = 350**	0	0
Taxable income	470	1340	910
Personal income tax	23% - 108	15% - 201	15% - 137
Tax relief for tax payer	0	**77**	0
Tax relief for children	0	**42+48 = 90**	**32**
Total taxes from employee	**213**	**144**	**195**
Net salary	**787**	**856**	**805**
Staff costs	**1236**	**1340**	**1310**
Tax payments in the budget	449	484	505

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Tax relief in Latvia – for small business

Micro-enterprise tax – one payment replaces several taxes:
- taxes on employees (social insurance contributions, personal income tax)
- taxes on corporate income (corporate income tax)

Micro-enterprise criteria:
1. the annual turnover ≤ EUR 100 000
2. the number of employees ≤ 5, including the owners
3. the income (salary) of an employee ≤ EUR 720 per month

Tax rate: 9% from company's turnover (sold goods and services).

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Tax comparison to small business in Latvia 2016

The company's:
- turnover EUR 100 000 per year,
- 5 employees,
- expenses 20% from turnover, excluding labour expenses

Indicator	Micro-enterprise tax, €	In general, €
Gross monthly income for 1 employee	720	893
Net monthly income for 1 employee	**720**	**720**
Labour taxes per year	x	22 585
Other expenses - 20% of turnover	20 000	20 000
Profit	36 800	14 215
Corporate income tax - 15% on profit	x	2 132
Micro-enterprise tax on turnover	9 000	x
Taxes total	**9 000**	**24 717**

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Tax reliefs for agricultural company in Latvia 2016, EUR

Indicator	In agriculture	In general
Revenue from sales of products (goods)	1 000 000	1 000 000
Revenue from subsidies (grants)	**50 000**	**0**
Owner's social insurance contribution	1 320	1 320
Other expenses	800 000	800 000
Profit	248 680	198 680
Non-taxable grants	**50 000**	**0**
Taxable income	198 680	198 680
Corporate income tax - 15% on profit	29 802	29 802
Tax discount - EUR 14.23 per hectare	29 802*	0
Corporate income tax after discount	**0**	**29 802**
Net profit	**248 680**	**168 878**

* If the farm has more than 2 095 hectares of agricultural land, the tax is 0

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Tax reliefs <u>for small agricultural company</u> in Latvia 2016, EUR

Indicator	In agriculture	In general
Revenue from sales of products (goods)	30 000	30 000
Revenue from subsidies (grants)	**4 000**	**0**
Owner's social insurance contribution	1 320	1 320
Other expenses	20 000	20 000
Profit	12 680	8 680
Non-taxable income from agriculture per year	**3 000**	**0**
Non-taxable grants	**4 000**	**0**
Taxable income	5 680	8 680
Personal income tax - 23% on taxable income	1 306	1 996
Net profit	**11 374**	**6 683**

Tax reliefs in Latvia – for environmental protection

Natural resource tax is to:
- promote economically efficient use of natural resources,
- limit environmental pollution,
- reduce polluting production and marketing,
- promote new, environmentally friendly technologies,
- support sustainable economic development,
- ensure financially environmental protection measures.

Tax is not paid for packaging (including agricultural farms), if the company provides recovery of packaging waste, i.e. applies the used packaging management system.

Tax reliefs in Latvia – for investments in business development

Companies receive a corporate income tax reliefs for:

1. investments in new production technological equipment *For example farmer on a new grain harvester.*
2. large-scale long-term investments

   In this case tax is reduced by:
   1) 25% of long-term investments amount to 50 million euro;
   2) 15% of the long-term contribution to the sum of 50 million to 100 million euro.

Conclusions (1)

1. Taxes are necessary to provide each country with budget revenues to make state and local functions. On average in the EU Member States in 2000 – 2012 taxes are 36-37% of GDP, but there are significant differences between countries: countries with stronger economies taxes charged more, but less developed countries – less.
2. In comparison, higher taxes are collected from labour, in 2012 the average in the EU Member States 17% of GDP, on consumption 12%, on capital 7%.
3. In each country the tax system is different. The highest overall tax burden is in Denmark, Belgium and France, but labour taxes are highest in Sweden, consumption taxes in Croatia, capital taxes in Luxembourg.
4. In Hungary (2000 – 2012) tax burden is 37-40% of GDP is on EU average level (39%).

   Hungary is relatively high taxes on consumption (14-16%, EU 11%), taxes on labour is on the EU average level (18-20%, EU 20%), but lower taxes on capital (5%, EU 8-9%).

Conclusions (2)

5. In Latvia (2000 – 2012) tax burden is 27-31% of GDP, it is significantly lower than in Hungary. However, in Latvia relatively high taxes on labour. In recent years, the government reduced taxes on labour to promote the income increase to families with children and low-paid workers.
6. Tax credits are used for various purposes, such as to stimulate investment in the economy, to support specific areas of activity, in order to reduce income differences between individuals etc. In Latvia most relevant tax relief received agricultural companies. Micro-enterprises have the opportunity to simplify tax calculations and pay less. With regard to natural persons, in Latvia less income tax paid by families with children.

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3. https://www.youtube.com/watch?v=WD80RF8ozcM – LV
4. https://www.youtube.com/watch?v=xMgLFyJONjU - LV


THANK YOU FOR ATTENTION ☺
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