



EU Member States Tax Policy Responses to the global financial crisis

Jean-Pierre De Laet

Head of Unit “Economic Analysis, Evaluation
and Impact Assessment Support”
DG Taxation and Customs Union
European Commission

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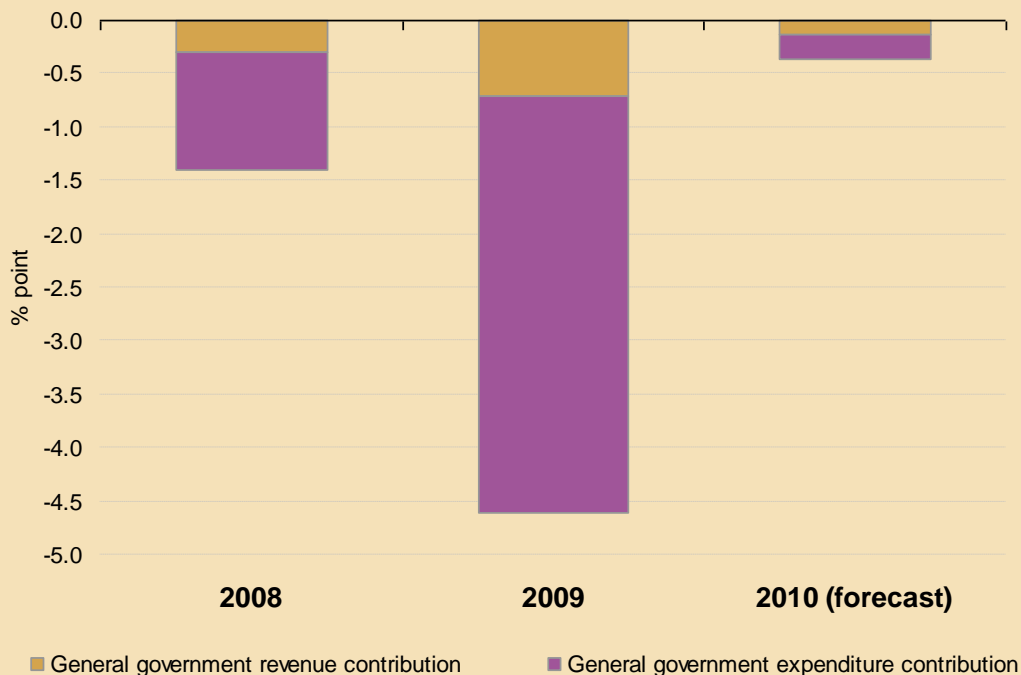
Outline

1. What happened to tax revenue during the crisis?
2. Taxation in « critical » countries: was it responsible – or was it the expenditure side?
3. What measures were taken by Member States ?
4. What are the tax rates now and how do they compare with pre-crisis levels?
5. Assessing the tax reforms made in the last two years



What happened to tax revenue during the crisis?

Change in gov't balance, EU-27, % GDP

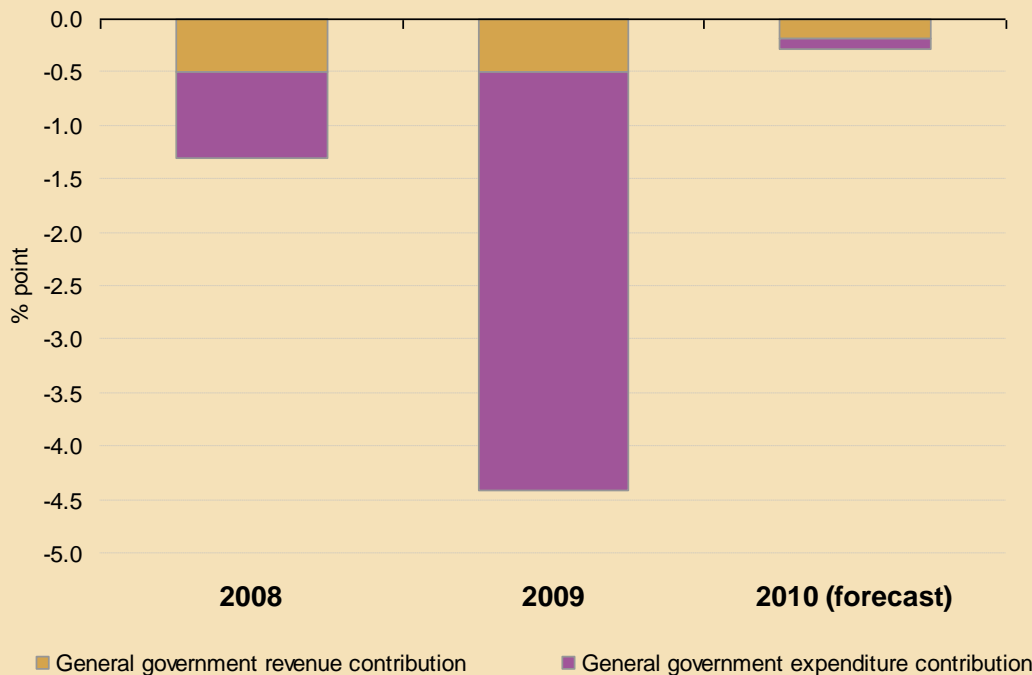


- 2008 : both revenue and expenditure contributed to worsen the government balance, but especially expenditure: - 1.1 % of GDP compared to - 0.3 %
- 2009: similar pattern: revenue -0.7 %, expenditure -3.9 % of GDP
- 2010 forecast: stabilisation – but tax revenue ratios to remain below 2007 level for years...



What happened to tax revenue during the crisis?

Change in gov't balance, euro area, % GDP

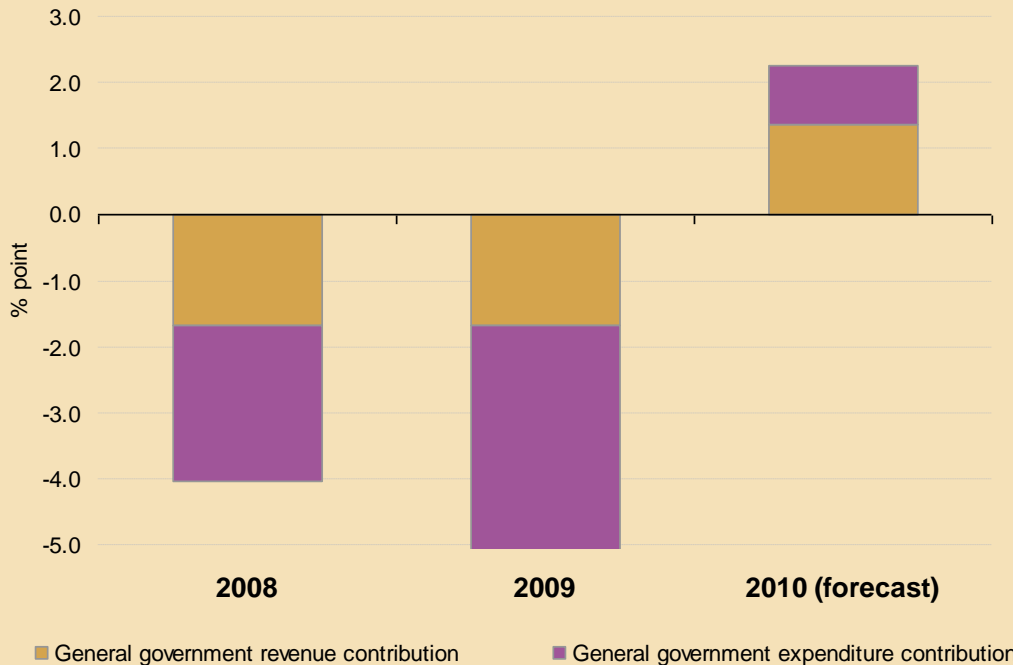


- In **euro area** revenue decline stronger 2008, but weaker 2009 – overall no big difference from EU as a whole (see previous slide)
- Overall, worsening in fiscal position is much more due to higher expenditure than lower revenues
- However, expenditure was made to sustain growth; had it been lower, tax revenue would have worsened more



Situation in Portugal, Ireland, Greece and Spain

Source of change in gov't balance, % GDP, PIGS average



- In 2009, Portugal, Ireland, Greece, Spain all showed a greater than average worsening in gov't balance
- The worsening of the balance started earlier than in EU-27
- On average greater negative revenue component than the EU-27 (almost 2% compared to 0.5%)
- Unlike EU-27, forecasts assume significant revenue-raising effort already in 2010



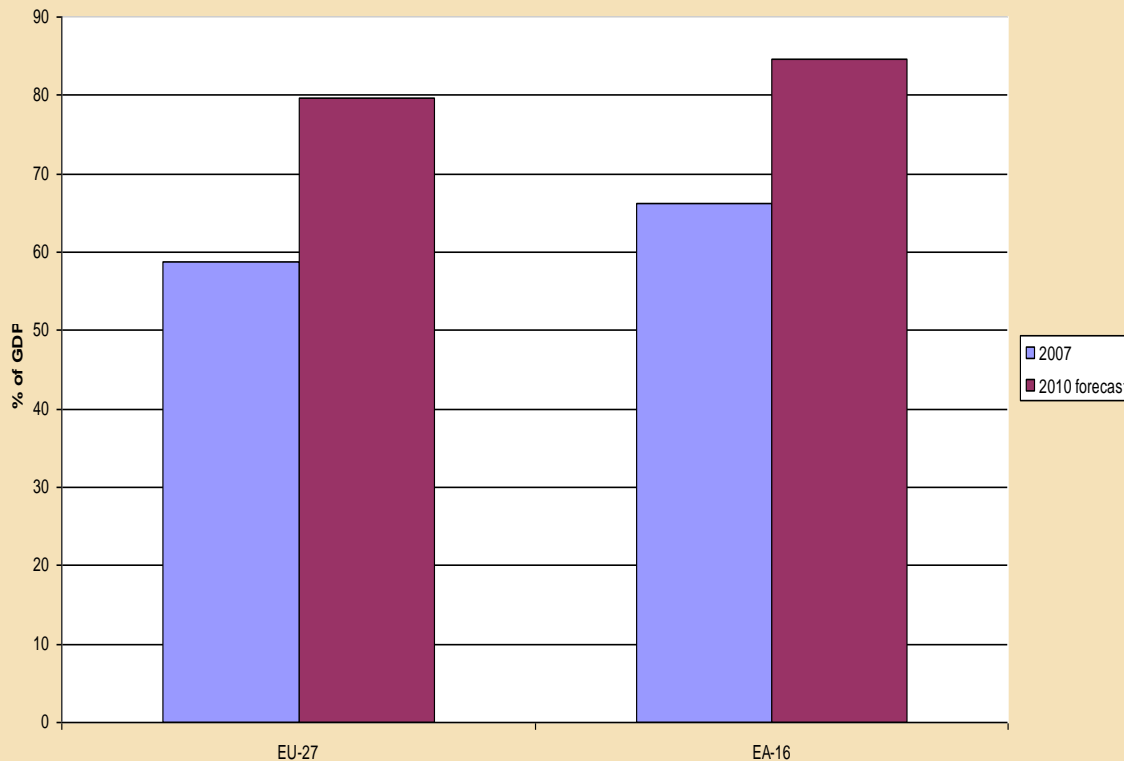
Situation in other countries

- Tax-to-GDP ratios of Portugal, Ireland, Greece and Spain are all lower than EU average – but in some of these countries this is also due to the size of the grey economy. Debt and deficit ratios differ however significantly.
- Also UK had sizeable deterioration in balance, revenue component fairly strong in 2009 (not 2008 or 2010)
- IT below average deterioration, revenue component in line with EU average



What happened to debt ratio during the crisis?

Government debt ratio



- 2007: lowest debt to GDP ratio for a decade
- 2010 forecast: debt ratio 20 percentage points higher
- Demographic challenges: ageing related costs increase by 4.7 pp by 2060
- 2009 assessment: EU debt to GDP ratio could reach 100% as early as 2014 and 130% by 2020.



How have Member States reacted?

- Quite activist stance – MS have adopted wide range of measures (an average of 10 important measures per MS)
- Several headline measures involved key rate changes (eg VAT) or reforms of PIT or SSC with substantial budgetary impact (frequently in range 0.5 - 1 % GDP)
- but overall high number of targeted measures
- Over 2008-2010 we find both tax cuts and tax increases even in the same MS and type of tax
- This is because initial tax cuts have been followed by consolidation measures



How have Member States reacted? (2)

- A distinctive feature of this recession is the introduction of a high number of schemes aiming at sustaining corporate liquidity by deferring tax payments
- Tax fairness has been a major concern: many countries increased PIT thresholds (also to offset indirect tax increases) or reduced taxation of food or basic items (frequent result = narrowing of tax base)
- Except UK, no widespread use of temporary indirect tax cuts to spur consumption, but many measures targeting expenditure on housing or business investment, or tourist expenditure
- Substantial resort to increases in excise duties, particularly in tobacco and alcohol and in second phase of recession



Type of measures adopted: CIT

Corporate Income Taxation		
Base or special regimes	Statutory rate	Timing (revenue effect)
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- This table shows the number of measures adopted and their impact (widening or narrowing of the base, changes in the rate, timing of tax payment)
- Most measures in corporate taxation involved tax relief
- Changes in the **rate** have been overwhelmingly cuts
- Most of the time the reforms have **narrowed** the CIT base although the opposite took place too
- Many measures **eased** the terms for paying taxes



Type of measures adopted: PIT

Personal Income Taxation		
Base or special regimes	Rates	Timing (revenue effect)
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- Most measures in personal taxation have involved tax relief, but also many increases are present
- Slightly higher number of **rate** cuts than increases
- As in CIT, most reforms have **narrowed** the base but the opposite has frequently happened, too
- Many measures **eased** the terms of payment



Type of measures adopted: excise duties

Excise duties		
Base or special regimes	Rates	Timing (revenue effect)
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- Excise duties have been **widely used** to raise revenue
- Clear prevalence of **rate** increases over cuts
- Limited use of **base** measures – mostly to widen base
- No business liquidity measures



What are tax rates now? 1 – VAT (standard rates)

EE: 18 -> 20

LV: 18 -> 21

LT: 18 -> 21

HU: 20 -> 25

ES: 16 -> 18

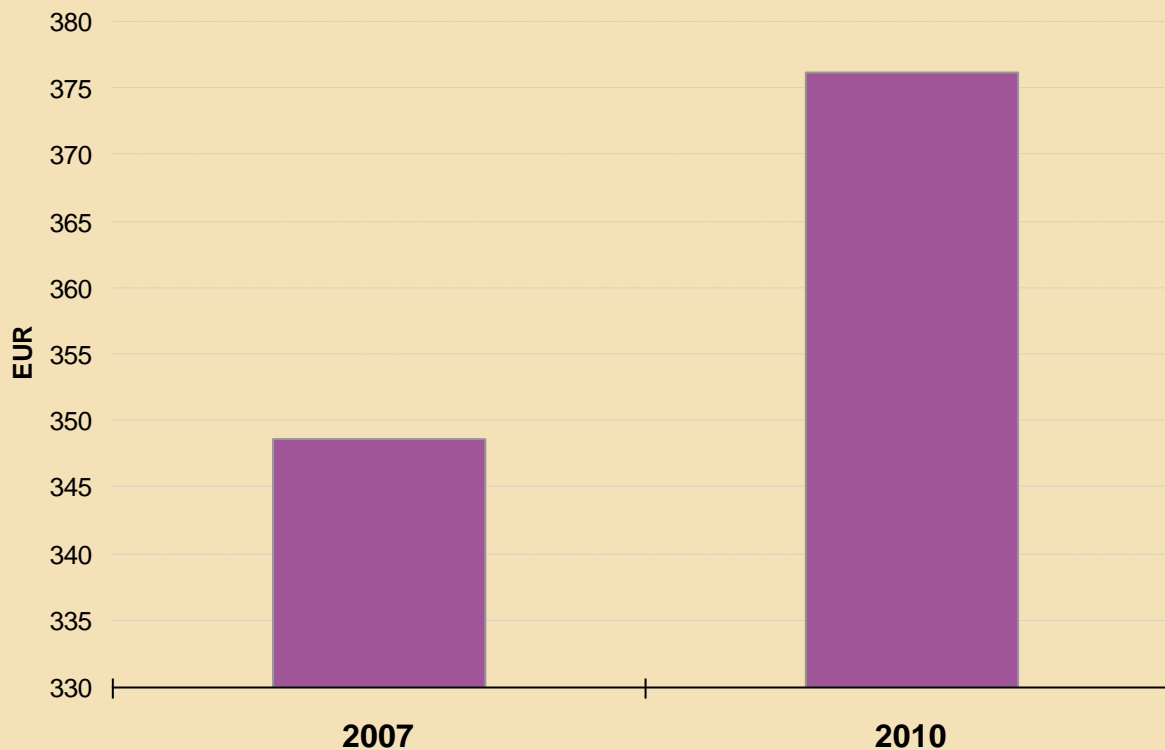
FI: 22 -> 23

EL: 19 -> 23



What are tax rates now? 2 – excise duties on fuel

Rate on diesel fuel, euros/ 1000 litres, EU 27 average

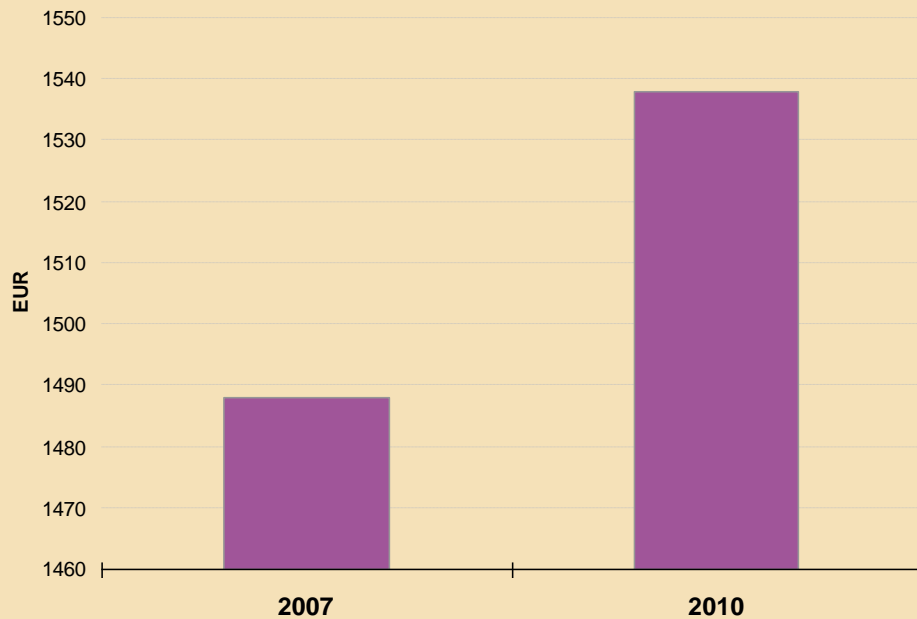




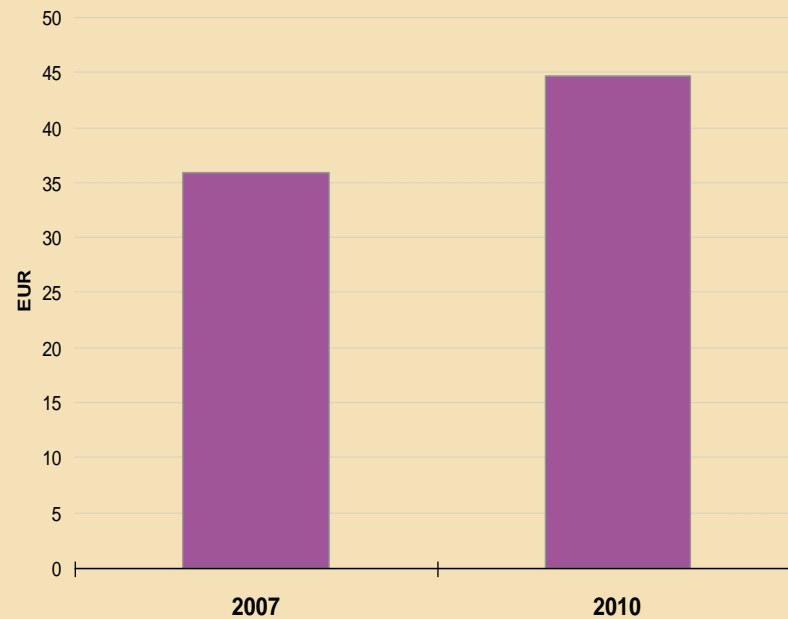
What are tax rates now?

3 – excise duties on alcohol and tobacco

Excise duty on ethyl alcohol EU-27 average

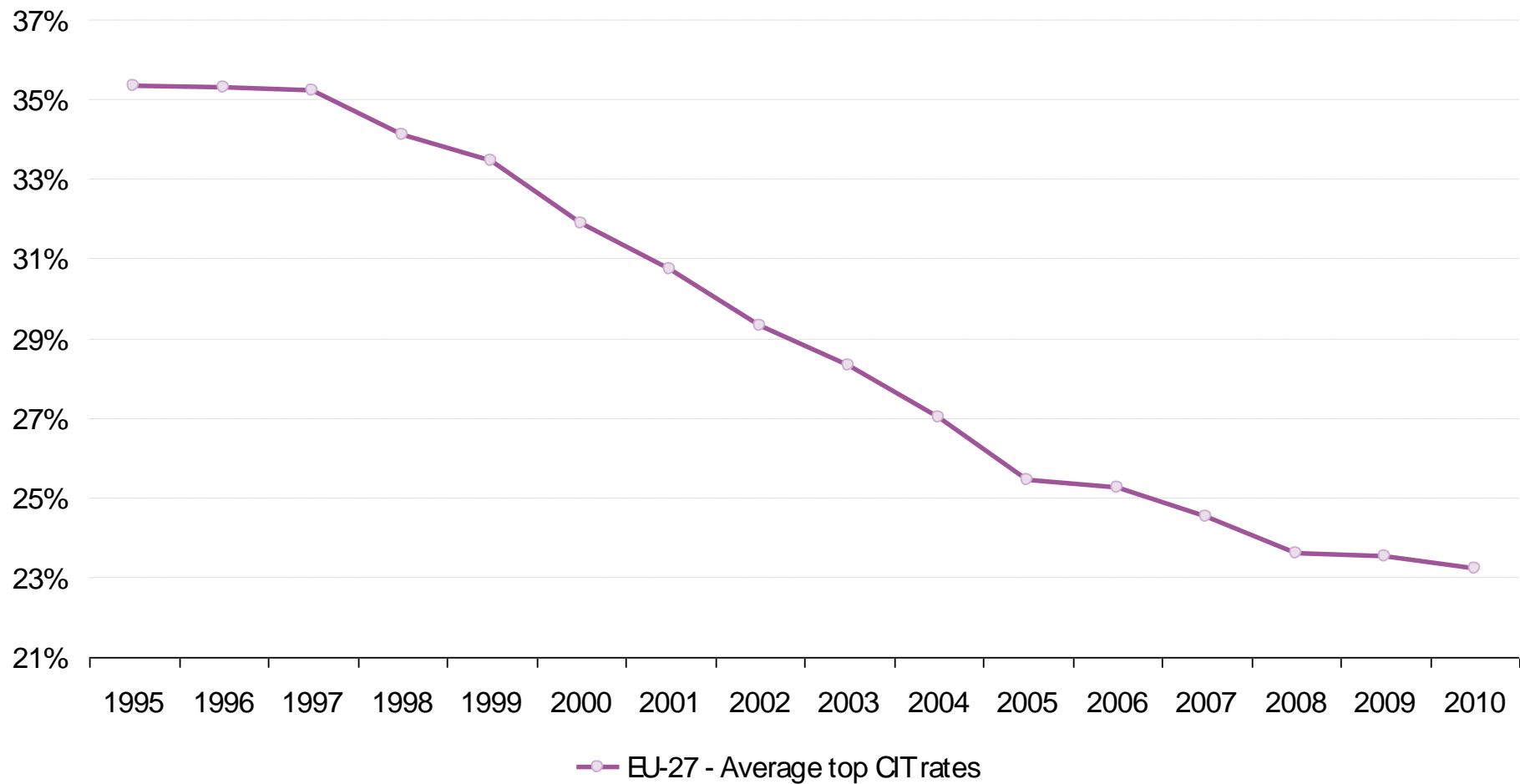


Excise duty on cigarettes EU-27 average



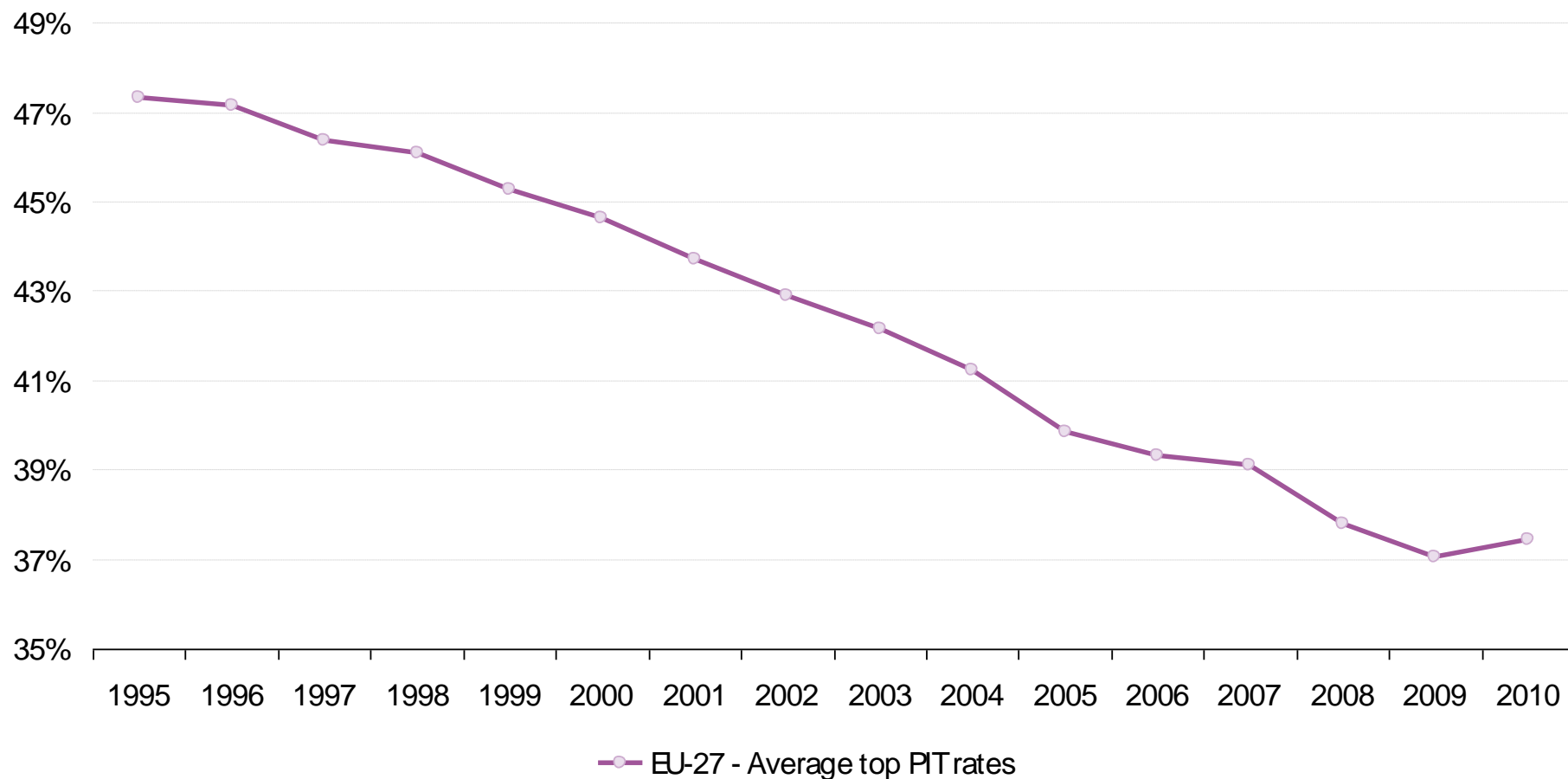


What are tax rates now? 4 - CIT





What are tax rates now? 5 – top PIT rates





Assessment of recent tax reforms (1)

- Although the most recent news point towards a prevalence of expenditure cuts, most tax systems will probably have to contribute to budgetary consolidation in the next few years
- During the crisis, a wide range of measures have been adopted, but on balance we see a continuation of the recent trend towards higher indirect taxes and lower top PIT and corporate rates
- The latest measures have mostly increased VAT and excise duties, while CIT has on balance been cut; PIT is less clear-cut owing to base measures going both ways



Assessment of recent tax reforms (2)

Are these changes good or bad?

- From a growth viewpoint, there are arguments for cutting CIT and PIT and funding the change by increasing consumption and recurrent property taxes...
- but these reforms find resistance on equity grounds (consumption taxes) or simply because they are unpopular (recurrent property taxes)
- Apparently, many tax systems have used base narrowing to address equity concerns (by raising basic allowances), to sustain spending or just to bolster acceptance....
- but in the long run base narrowing drives up marginal rates, whose growth cost increases rapidly



Thank you!