

**TAX-BENEFIT SYSTEMS AND  
GROWTH POTENTIAL IN THE EU**

**TAXBEN**



*What the Old EU Members Could Learn from  
the New in Tax/Benefit Policies?  
(And vice versa)*

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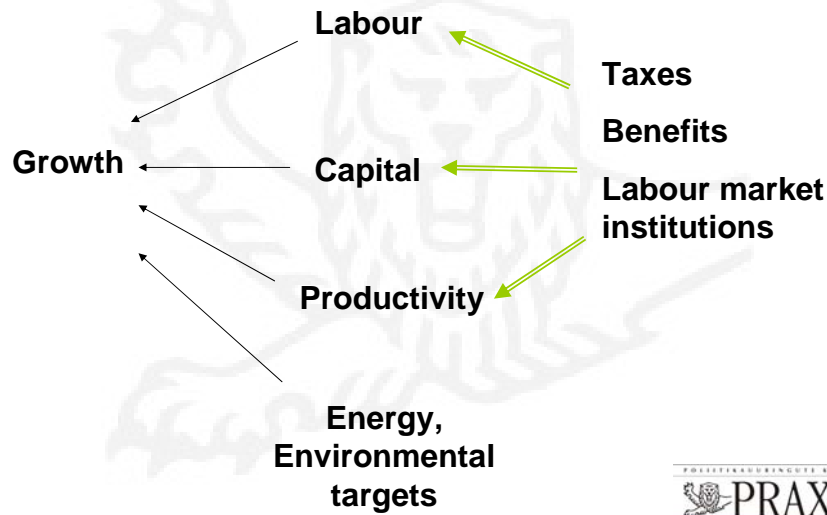
27.11.2006

## **Motivation**

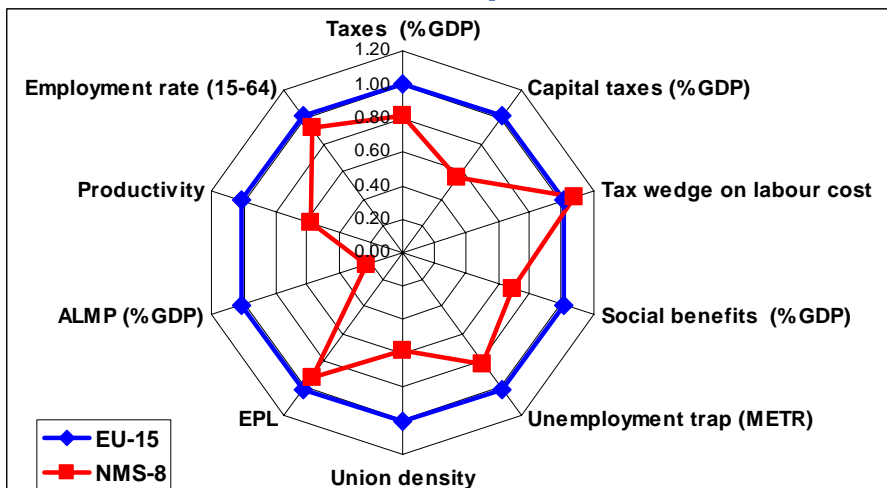
- **What can we conclude from the analyses of the TAXBEN project on the New Member States from CEE?**
- **What can we learn from the experience of the New Member States?**
- **What implications might the developments in taxes, benefits and labour market institutions have on economic development in the NMS?**



## Links investigated in the TAXBEN project



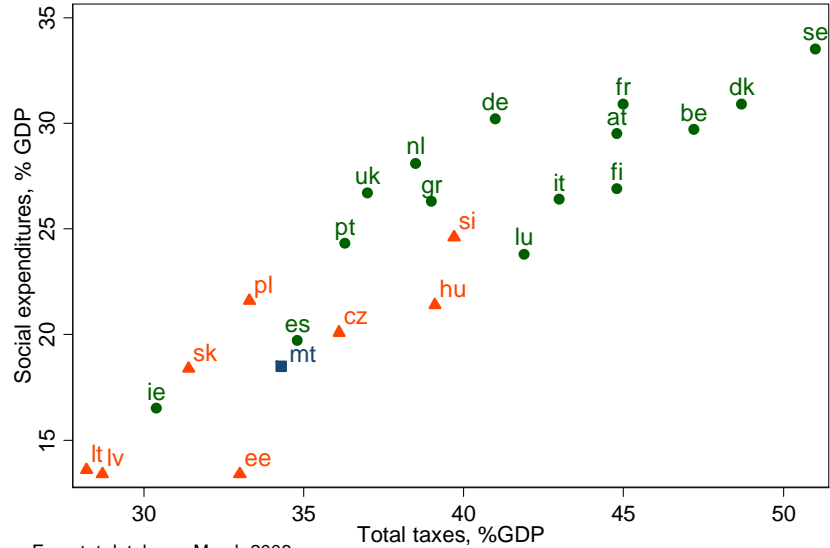
## EU-15 and NMS-8 compared



Source: various sources, most recent data 2002-2004. Note: relative scale, EU-15=1

## Both taxes and benefits lower in NMS-8, large variation within NMS-8

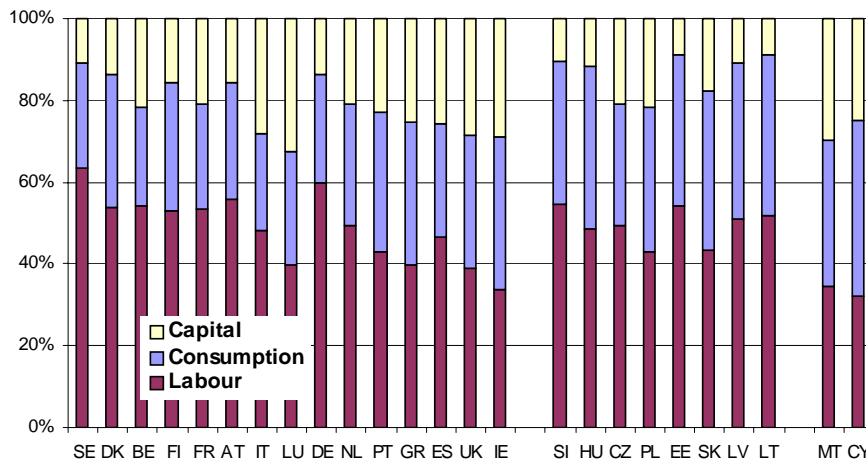
Taxes and social expenditure in 2003



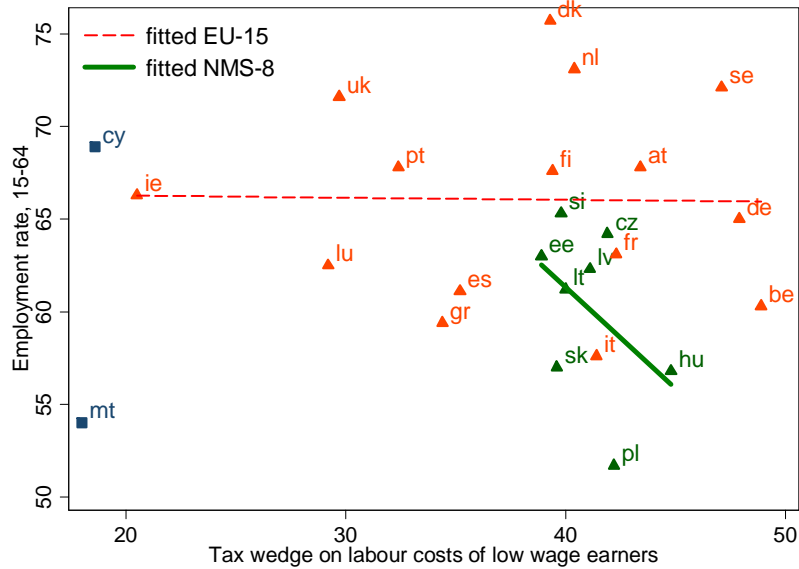
Source: Eurostat database, March 2006

- In NMS-8 Taxes on capital lower
- Decline in labour taxes and capital taxes
- Move from progressive to proportional taxes

Structure of taxes by economic function, 2003



- Tax wedge is relatively high in NMS-8.
- Negatively correlates with employment rates



Source: Eurostat database, October 2006, data for 2004

**In NMS-8:**  
**Much lower ALMP & PLMP, lower union densities, average level of EPL, average level of labour taxes**

**Changes in labour market institutions in NMS-8 (mid-1990s to post-2000) => trend towards more flexibility**

Country	UI generosity	ALMP	Union density	Bargaining coverage	EPL*	Labour taxes
Czech R	0	-	-	0	0	+
Estonia	+	-	-	0	-	-
Hungary	-	+	-	-	+	-
Latvia	-	-	-	-	-	-
Lithuania	0	-	-	0	-	-
Poland	-	-	-	-	+	-
Slovakia	-	-	-	-	-	-
Slovenia	0	-	-	0	-	0

Note: 0 – no change, + increase, - decrease; Source: from Anspal et al (2006)

## Conclusions from the analysis of NMS in TAXBEN

1. Taxes and benefits influence employment
  - E.g difference of the tax wedge between Estonia and Poland explains about 2% difference in their employment rates
2. Policy recommendations depend also on other labour market institutions
3. Capital flows (FDI) into NMS are affected much by the labour market institutions, perhaps more than capital taxes
4. So far, simple convergence hypothesis explains most of the growth in productivity. Regarding the future, the experience of OECD countries imply:
  - Effect of taxes and benefits on productivity growth unclear.
  - Flexible labour market encourages growth.
5. Potentially large costs to align with efficient climate policy

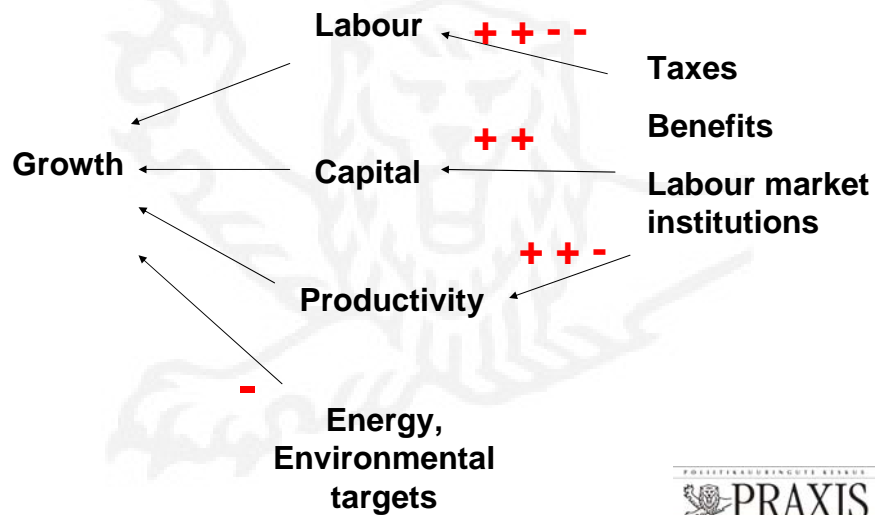


## Challenges in the NMS-8

- Growth in productivity in NMS-8 still mainly as a catching-up process
  - The catching-up process ends sooner or later
  - Increasing labour and energy costs
    - Then what? More R&D?
- To approach the “golden flexicurity” model, drastic increase in ALMPs, reduction of EPL, increase in social benefits is needed
- Labour emigration
  - => shortage of labour, especially in some occupations, brain-drain
- Impact of demographic developments on long-term labour supply



## Summary of positive and negative influences for NMS-8



## Lessons

1. Reduce labour taxes for low-income earners!
2. Stay flexible!
3. But do not race to the very bottom!