Report "Tax Reforms in EU Member States" 2013

Q&A

What is the Tax Reform Report?

The annual report 'Tax Reforms in EU Member States' is published jointly by the European Commission's Directorate-General for Economic and Financial Affairs (DG ECFIN) and Directorate-General for Taxation and Customs Union (DG TAXUD). It analyses recent tax reforms in EU Member States and identifies tax policy challenges faced by them. The report provides substantial analytical contributions to the policy advice given in the context of integrated surveillance and coordination of economic policies at the EU level ('European Semester').

What information is provided on tax reforms?

The report provides a detailed overview of recent tax reforms carried out in Member States in 2012 and the first half of 2013. It summarises changes in overall tax revenue and identifies common trends across countries, offering a descriptive typology of reforms.

Which challenges does the report identify related to the tax structure and consolidation on the revenue side?

The report analyses tax policy challenges of Member States with regard to macroeconomic performance and GDP, employment, fiscal sustainability specifically.

- Around one third of the Member States are found to have scope for shifting taxation away from labour to tax bases less detrimental to growth. In these cases, a high tax burden on labour (including specific labour market groups) coexists with some room for increasing growth-friendly taxes, i.e. consumption taxes, recurrent housing taxes and environmental taxes.
- Indicator-based results show that a limited number of Member States could consider using taxation – in addition to expenditure control – to support the consolidation of their public finances and make them more sustainable. These countries face sizeable consolidation challenges and, at the same time, have some room for tax increases.

The report also provides findings from simulations of the effects of tax shifts and fiscal devaluation.

Which challenges does the report identify concerning the design of individual taxes and tax compliance?

Specific challenges faced by Member States are investigated in the areas of tax expenditure, the broadness of the VAT base, the debt bias in corporate taxation, housing taxation, environmental taxation, and tax governance:

- Certain tax expenditures can impact on the efficiency of taxation and reduce revenue. The release of information by Member States not regularly reporting and carrying out cost benefit analysis would be useful to identify scope for efficiency-enhancing reforms and potential revenue increases.
- A large majority of EU Members have a 'debt bias' in corporate taxation, as they allow for the deduction of interest paid, while there is no such deduction for equity

costs. The gap between effective marginal tax rates for debt and equity varies between Member States.

- VAT revenues collected are often far below the level that would theoretically be obtained if all consumption items were taxed at the standard rate. Widespread use of VAT exemptions and reduced VAT rates as well as a lack of tax compliance are amongst the main drivers of such a gap, the level of which is also influenced by the structure of the economies.
- Countries with relatively high transaction taxes on property transfers and relatively low recurrent tax on property could consider shifting taxation from transaction to recurrent taxes. Moreover, the taxation of housing continues to favour the accumulation of debt in many Member States, due to mortgage interest deductibility combined with low tax on imputed rents.
- Several countries may consider using taxation to meet agreed environmental targets or to improve the design of environmentally-related taxation.
- A large majority of Member States face challenges linked to tax governance, in the areas of improving tax compliance (in the presence of a large share of the non-observed economy and undeclared work) and the functioning of the tax administration specifically.

The report presents an initial horizontal analysis of tax policy challenges which needs to be supplemented by country-specific evidence and analysis.

Why is it important to consider redistributive aspects of taxation?

The report discusses the role of taxation in income redistribution and argues that distributional analysis should receive due attention in designing tax reforms. Proper tax design, including compensation measures, can meet the requirements of both, equity and efficiency. It is important to look at redistributive effects in the broader context of the national tax system as a whole.