Taxation and consolidation

Distributional issues – Denmark

by

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1. Goals and restraints:
   1. Budgetary restraints
   2. Macroeconomic impact of taxation
   3. Distributional effects

2. Fiscal consolidation and tax policy in practice:
   1. Plan for fiscal recovery
   2. Reducing deferred taxes
   3. Tax reform 2012
Trade-offs between goals and restraints

2020-plan:
- Structural balance on public finances in 2020, GDP growth of 2½ pct. 2014-2020, increase employment by 180,000, long term sustainability.

EU Fiscal compact:
- Structural public sector deficit of no more than ½ pct. of GDP in any year.

EU excessive deficit procedure
- Structural public sector balance in 2013.

Budgetary restraints

Macroeconomic impact of taxation
- Investments
- Savings
- Labour demand
- Labour supply
- Private consumption

Distributional effects
- One year effects
- Life time effects
- Remaining life effects
The answer to the trade-offs and restraints

What should we be looking for?

• Fully financed tax changes where the degree of self financing of cuts in spending/increases in taxes are lower than the degree of self financing of increased spending/decreases in taxes.

• Temporary measures with limited impact on long term growth and sustainability.

• Other measures that affects the real economy only limited.

• Pigouvian taxes?
Plan for fiscal recovery -2010

- Postponing already decided tax cuts – 10 billion DKK
  - Top tax threshold
  - Indexation of allowances and tax brackets.
  - Ceiling on yearly child benefits

- Reprioritisations – 10 billion DKK towards health, education and week groups
Reducing deferred taxes

• In the 2010 tax reform yearly savings on annuity pension schemes were capped to 100,000 DKK a year.

• In the 2012 budget the cap was reduced to 55,000.

• In 2012 tax reform the deduction of up to 46,000 DKK a year for savings in capital pensions schemes were abolished.
Tax reform 2012 – main elements

Income tax cuts

- Increased EITC, new EITC for single parents, increased top tax threshold

Fully financed by:

- Cuts in public expenditure for defence, reduced contribution to the EU, reduced indexation of social benefits.
- Indexation of excise duties, increased taxation of financial sector, increased taxation on cars, tax planning and compliance.
Tax reform 2012 – change in disposable income, %

One year  Remaining life

Decile 1  Decile 2  Decile 3  Decile 4  Decile 5  Decile 6  Decile 7  Decile 8  Decile 9  Decile 10  All

-1 -0.5  0  0.5  1  1.5

Decile 1

Decile 2

Decile 3

Decile 4

Decile 5

Decile 6

Decile 7

Decile 8

Decile 9

Decile 10

All
### Tax reform - Change in gini coefficient

<table>
<thead>
<tr>
<th>Distributional effect</th>
<th>Change i gini</th>
<th>Change in gini if dynamic effects are included</th>
</tr>
</thead>
<tbody>
<tr>
<td>Life</td>
<td>0.16</td>
<td>0.11</td>
</tr>
<tr>
<td>Remaining life</td>
<td>0.15</td>
<td>0.08</td>
</tr>
<tr>
<td>One year</td>
<td>0.27</td>
<td>0.17</td>
</tr>
</tbody>
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Total gini in 2010: 25.7