AUSTRIAN AND CZECH TAX POLICIES

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Abstract

The comparison of Austrian and Czech tax policies is motivated by parallel criticisms of the tax structures on the part of the OECD. The aim of the paper is to show, whether and to what extent it is justified to replace the "harmful" taxation of earnings with the taxation of consumption. The OECD has not yet rid itself of the one-sided approach of the "optimal tax theory", which uses the influence of taxation on long-term economic growth as its sole criterion. The more realistic "sustainability-oriented tax policy" respects economic, social and environmental objectives. From this perspective, it is not possible to simply shove any social security contributions into the taxation of labour and to require Czechia and Austria to reduce them. The key to resolving the problem of the amount of the social security contributions lies in the relationship between the insurance premiums and the benefits in the main branches of social security. In practice, the solution may come up against the interests of the stakeholders (for example the health insurance funds) and this is currently the greatest problem in the Czech tax policy. The irony is that the conflict of personal interests may also be "overcome" by the transition to a comprehensive business income tax.

Keywords

Tax Theory, Tax Structure, Social Security Contributions, Personal Income Tax, Corporate Income Tax, Self-employed Taxation

I. Introduction

Tax systems are usually the result of the long-term development of taxation in individual countries. Tax policies endeavour to introduce smaller or greater tax reform in the given country, ideally within the context of the government's overall economic and social policy. For example, the Czech government stated in its program declaration of 28 June 2018 that it would implement "a proposal for the new conceptual regulation of income taxation which would regulate taxation and the system of insurance levies on income with the objective of simplifying taxation and eliminating any tax distortions. We will conclude the process of recodifying income taxes by preparing an integrated system of tax and insurance levy administration which will enable the payment of these legal obligations in one place" (Babiš et al., 2018b).

The need for the "systematisation" of income tax and social security contributions has been readily apparent over the last decade, because the comprehensive neoliberal tax reform of the previous governments led by ODS was not implemented; this reform commenced with the transition to the calculation of the wage tax (tax on dependent activity) based on the so-called super-gross wage; this was supposed to be followed by a one-off increase in gross wages to include the employer social security contributions, whereby all of the social security contributions should have then been paid by the employees only. The reform included a transition to the payment of social security contributions from after-tax earnings; in the neoliberal system, the privatised social security is paid for by the insureds themselves. The partial or complete privatisation of the public health and pension insurances was essentially "on the agenda" in that time. The aim of our paper is to analyse the basic similarities and differences in the Czech and Austrian tax policies from the point of view of the modern tax theories in order to help the Czech Administration to realize its proclaimed tax policy.

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II. Neoliberal and sustainable tax policies

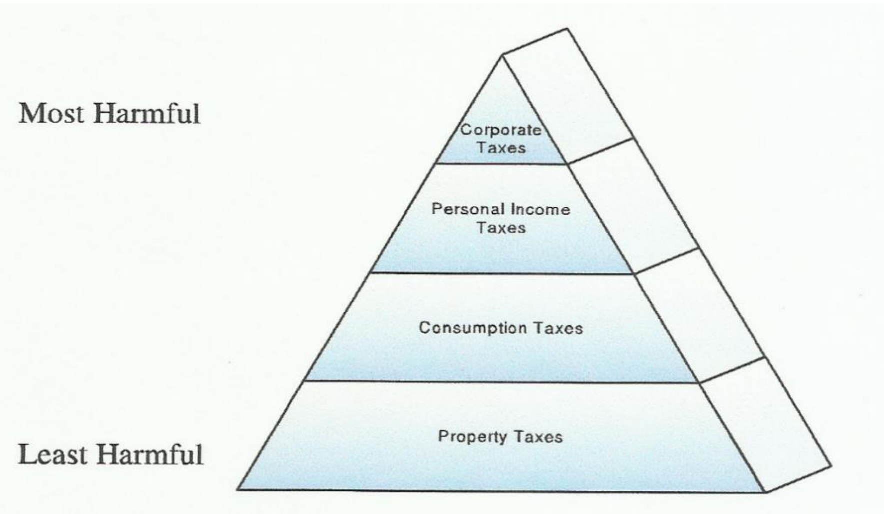
The neoliberal optimum tax is a direct taxation of consumption (expenditure) of the population, an alternative solution is the universal value added tax; the neoliberals have never been able to realise these ideals. The "second best solution" under these conditions was a substantially reformed personal income tax: all investments, capital gains, inheritance and so on had to be exempted from taxation here – so that this essentially involved the taxation of consumption (expenditure). This reformed personal income (consumption) tax may be supplemented with the universal value added tax.

In the United Kingdom the neoliberal "second best solution" was recommended by the Meade Tax Committee (Meade et al., 1978). „The central theme of the Meade Report was a preference for consumption over income taxation. Soon after the Report was published, a thoughtful commentator said to me 'you will never get the name expenditure tax, but you will get everything else'. Since 1978, the most important developments in the UK tax structure have been

− a rise in the relative significance of general consumption taxes (VAT) and payroll tax (national insurance) relative to income tax
− the introduction of savings and pension accounts, neutral as between asset categories, providing both TEE and EET reliefs
− a substantial reduction in the number of income tax rates which established an approximately linear structure above an exemption level" (Kay, 2008).

A group known as Americans for Fair Taxation developed the Fair Tax Plan of 2003: „it is a sales tax proposal to replace the current U.S. income tax structure. It abolishes all federal personal and corporate income taxes, and ends all taxes on gifts, estates, capital gains, alternative minimums, Social Security, Medicare, and self-employment. The plan replaces them with a federal retail sales tax of 23% to be administered by state sales tax authorities. … To make it … progressive, the Fair Tax Act proposes that all Americans receive a monthly "prebate", which would be equal to the … cost of living at the poverty level" (Amadeo, 2019). Fair Tax Plan has had an important support up to now, many proposals of this kind have been submitted, the nowadays recommended sales tax rate is at the level of 30 per cent.

Figure 1: OECD hierarchy of taxes (2008)



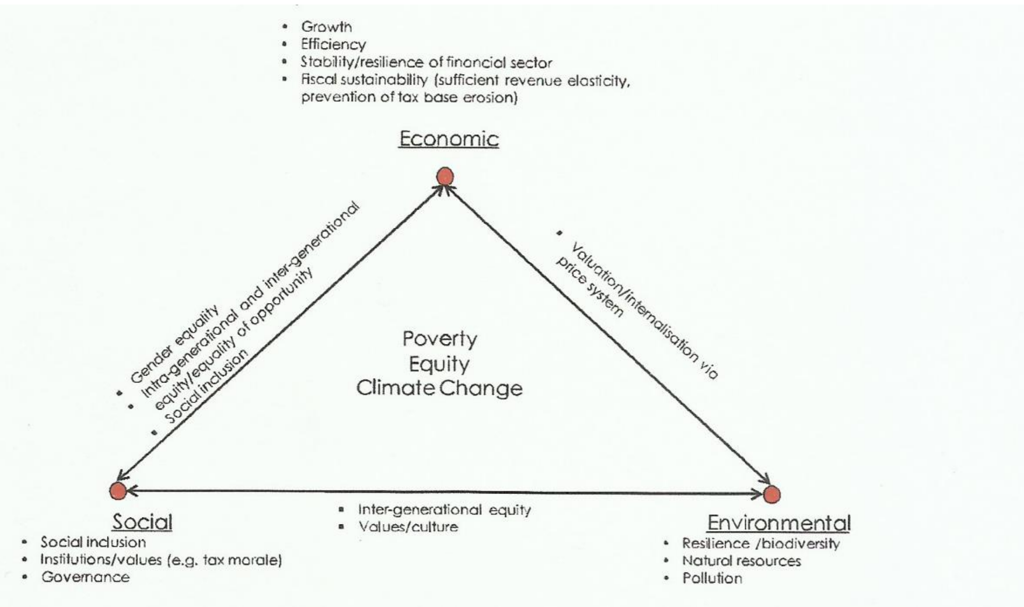
Source: Business Tax Team (2012)

Neoliberal tax policy was supported to a significant extent by the development of the so-called optimal tax theory from the 1970s. This theory generally reached the following conclusions::

1) Optimal marginal tax rate schedules depend on the distribution of ability; 2) The optimal marginal tax schedule could decline at high incomes; 3) A flat tax, with a universal lump-sum transfer, could be close to optimal; 4) The optimal extent of redistribution rises with wage inequality; 5) Taxes should depend on personal characteristics as well as income; 6) Only final goods ought to be taxed, and typically they ought to be taxed uniformly; 7) Capital income ought to be untaxed, at least in expectation" (Mankiv et al., 2009). Based on the optimal tax theory the OECD economists have „established a hierarchy of which taxes are most and least harmful for long-term economic growth. They determined that the corporate income tax is the most harmful for long-term economic growth, followed by high personal income taxes. Consumption taxes and property taxes were found to be less harmful to economic growth relative to taxes on capital and income" (Johansson et al., 2008) – see Figure 1.

In 2016, the OECD announced the reform of its tax "policy" in a Working Paper cunningly entitled Tax Design for Inclusive Economic Growth (Brys et al., 2016). „In the context of the OECD's New Approaches to Economic Challenges (NAEC) initiative, this paper seeks to re-assess the policy recommendations stemming from the 2008 Tax and Economic Growth report, which focused on the impact of taxes on economic growth from an efficiency perspective, to more explicitly take account of equity considerations. Drawing on recent developments in the academic literature and in countries' tax policies, the paper examines how the basic design aspects of each tax can be improved to better achieve inclusive growth" (Brys et al., 2016). … „it's a pleasant surprise when OECD produces a paper calling for Governments to use tax policy to drive forward economic agendas that seek to boost growth while sharing the benefits more evenly within society." And it also says, "with fiscal consolidation, there is scope for tax policy to play a bigger role in income redistribution" (Sweeney, 2016). Figure 2 presents elaborated economic, social and environmental objectives of the new „sustainable" tax policy.

Figure 2: Objectives of a sustainability-oriented tax policy



Source: Schratzenstaller (2016)

Tax policies at the level of the European Union define five tax priorities, used in the Commission's country-specific analysis in the context of the European Semester):

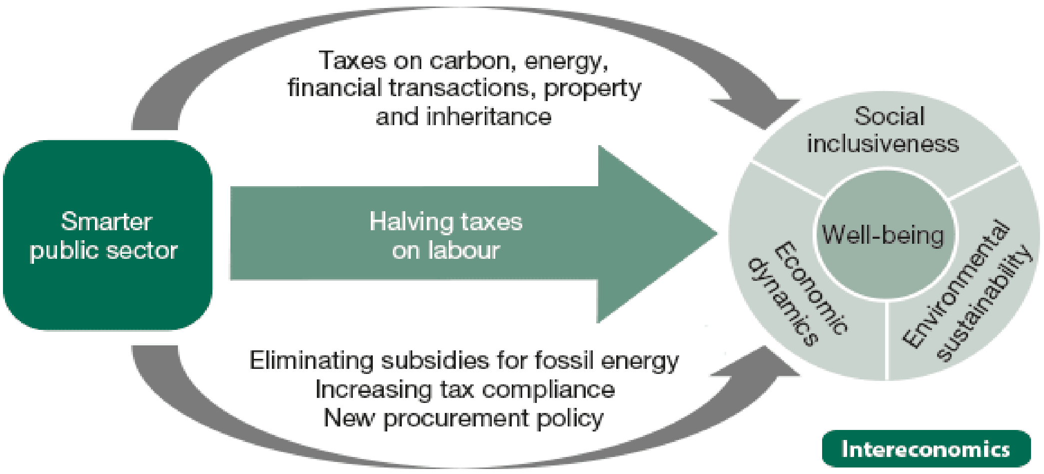
- stimulating investment and addressing positive and negative externalities,
- improving tax administration and tax certainty,
- boosting employment,

- reducing inequalities,
- ensuring tax compliance (European Commission, 2020).

„There has been no major shift in terms of tax reforms implemented in Member States between June 2018 and June 2019. While, on average, all categories of tax revenue in the EU are increasing, headline corporate income tax (CIT) rates continued their downward trend in 2019. Member States continued to adopt measures to stimulate investment at home and attract it from abroad. While the entry into force of a number of provisions of EU directives and some national measures will contribute to fighting tax abuse, this remains an important issue“ (European Commission, 2020). The coronavirus crisis may simplify tax reforms. Figure 3 indicates the possible direction of the "new" tax policy. WWWforEurope has drawn up an ambitious tax restructuring proposal for the EU, under which the level of labour taxes should be reduced from the current 20% to just 10 per cent of GDP and this reduction should be compensated for with the following ambitious measures:

- improving tax compliance for value added taxes and corporate income tax on the profits of multinationals would yield additional tax revenues of 1.6% of GDP,
- introducing a financial transaction tax – a tax rate of 0.05% on all financial transactions in a scenario of high tax avoidance and high elasticity of the tax base would yield tax revenues of 0.9% of GDP,
- increasing revenues from taxes on tobacco and alcohol consumption to the level of the three member states with the highest revenues from these taxes would yield additional tax revenues of 1.3% of GDP,
- doubling current environmental taxes would yield additional tax revenues of 2.4% of GDP,
- introducing a carbon tax – a tax rate of €100 per tonne of CO_2 would yield tax revenues of 2.0% of GDP,
- eliminating tax exemptions for fossil fuels would yield additional tax revenues of 0.2% of GDP,
- increasing revenues from real estate taxes to the level of the three member states with the highest revenues from these taxes would yield additional tax revenues of 1.1% of GDP,
- moderately increasing inheritance and gift taxes, thereby generating additional tax revenues of 0.1% of GDP,
- introducing a very moderate tax on net wealth, thereby generating tax revenues of 0.4% of GDP.

Figure 3: A sustainability-oriented tax shift



Source: Aiginger and Schratzenstaller (2016)

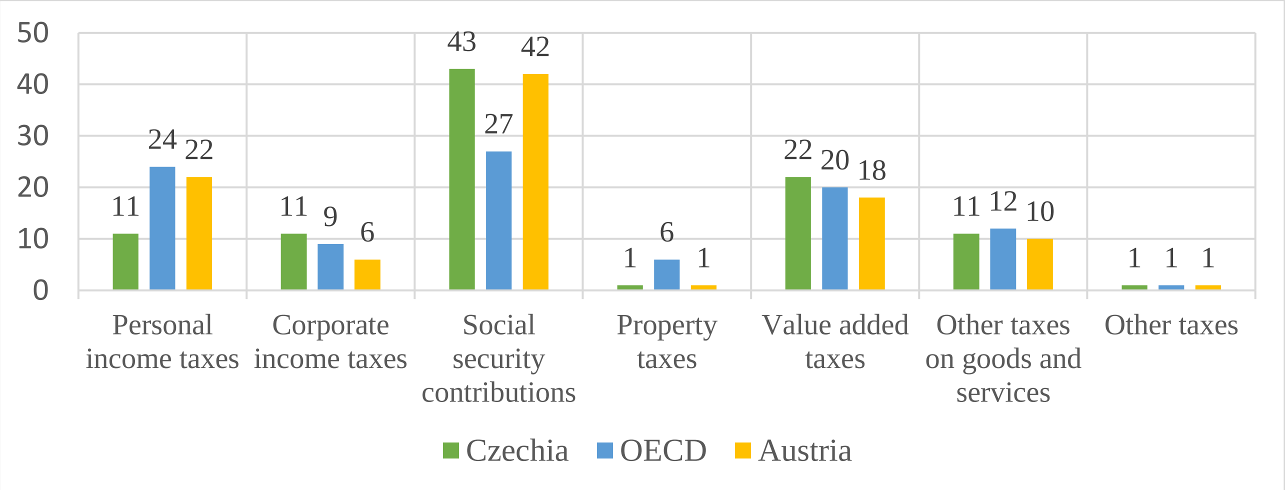
A less ambitious, more moderate approach, which could be implemented in the short run based on less supranational tax coordination, would be to reduce labour taxes by around a third, from 20% to 13.3% of GDP" (Aiginger and Schratzenstaller, 2016).

It can be expected that internationally acknowledged taxation theory and policy will be based on the stated illustrative conclusions of the WWWforEurope project, but the "simple" neoliberal recommendations may yet long remain in politics. We will now focus on the fundamental shifts in Czech taxation policy to date and compare them with Austrian taxation policy which the OECD has evaluated as being similar to the Czech model using the former neoliberal "metrics".

III. Austrian tax structure and policy

Austrian tax structure (according to the OECD methodology) is substantially different from the average in OECD countries in two types of fiscal receipts: Austria has a very high share of social security contributions and a very low share of property taxation – see Figure 4. Ten years ago, the OECD's tax consultancy oriented itself according to the theory of optimal taxation: „Despite some recent improvements, the tax structure continues to be biased towards distortive taxes on labour and entrepreneurship, while the share of growth-friendly taxes on immoveable property and consumption is lower than in other countries ... While average tax rates are high for almost all workers, marginal tax rates are particularly high at low income levels, due to the interaction of social security contributions, personal income tax and the benefit system. This reduces incentives for transition from inactivity to employment and from part to full-time employment. Priority should therefore be given to lowering the fiscal burden on low-skilled workers, who are most likely to respond to stronger work incentives. *This group of workers could be best helped by reducing social security contributions or introducing in-work benefits that top up wages… Valuations of real estate and land should be brought to market values…* International practice differs greatly, but *the reinstatement of inheritance and gift taxes should be considered, within the wider context of a review of capital taxation in general"* (OECD, 2011).

Figure 4: Austrian and Czech tax structures (in %) in comparison with the OECD average in 2017



Source: Author, data: OECD (2019a)

A comprehensive tax reform came into force from 2016. „The stated aim of the tax reform was to noticeably reduce personal income taxation. The reform package included an increase in the number of brackets in the personal income tax system from four to seven, an increase in the amounts of several allowances and tax credits, and an increased reimbursement of social security contributions for low-income earners" (Ivaškaitė-Tamošiūnė et al., 2017). Part of this tax reform included, amongst other things, increased tax rates on capital gains (with the exception of the personal savings) from 25% to 27.5% and from 25% to 30% in the case of the taxation of capital gains from the sale of assets. The tax reform was significant, but the tax wedge remained high.

The ÖVP and FPÖ right-wing coalition included the objective of reducing the composite tax quota "towards 40%" in its government program in 2017 with the justification that Austria's quota was the sixth highest in the world and moreover that the tax system remunerates performance in very low regard. An extensive Austrian study into the Austrian tax structure in comparison with the EU and into its influence on growth and inequality points in this regard the results of OECD survey, according to which 73% of the people in Austria wanted the government to take more care of economic and social security. At the same time, over 70% of the recipients felt that the rich should face more taxation in order to enable the support of the the poor (Banabak a Gerhartinger, 2019).

Last year the OECD expressed this opinion: „The current tax system is not employment friendly and plays a very limited role in income and wealth re-distribution… The tax reform could reduce further labour taxes (including social security contributions) for lower income households, widen the consumption tax base and raise environmental taxes. The authorities should also consider increasing recurrent property taxes and re-introducing inheritance taxes. Widespread VAT reductions should be replaced with direct transfers to low-income households – at lower fiscal costs… The corporate tax system is biased towards debt-financing and Austrian firms have one of the highest average debt-to-equity rations among OECD countries" (OECD, 2019b).

The ÖVP and FPÖ coalition government enacted a wide-ranging parametric tax reform from 2020 (spread out until 2022) which was mainly motivated by the reduction of the tax burden. Austria is a country with structured rates of personal income tax; it has had 7 rates and bands of this tax since 2016, the first band has a zero rate. The tax base involves the individual incomes after the deduction of social security contributions which are overly complex and correspond to the Christian-Democratic concept of social insurance. At the same time, almost all sickness insurance funds were merged into a single Austrian Health Insurance Fund from 2020. The overall basic amount of the social insurance contributions for blue-collar workers/employees currently amounts to 39.35%, of which the insured pay 18.12%. The greatest entry in these contributions is accounted for by pension insurance, where the employer pays 12.55% and the employee 10.25%. The second-biggest entry is sickness insurance with rates of 3.78% (employer) and 3.87% (employee). Social insurance contributions were not part of the tax reform, as they are not part of the tax system in Austria (as is also the case in Germany); they are, however, taken into account when considering the overall "tax" burden. A component of the tax reform from 2020 is the introduction of a social insurance bonus (negative tax, tax bonus) in the amount of 50% of the social sickness insurance premium in the case of a zero income tax base, up to a maximum of €400 per annum. This is taken as a significant support for those employees (and pensioners) with such low income (under ca €1260 gross income per month) that they pay no income tax.

Austrian social insurance continues to have a substantial nature of "genuine" social insurance based on the principle of equivalence; an exception in this regard involves – to a substantial extent – sickness insurance because the universal healthcare is its benefit in kind. In a broader sense, the social insurance premium also includes the contributions paid to the Family Policy Fund (3.9%, paid by the employer). On the other hand, pension insurance essentially has the full characteristics of social insurance; pensions are fully earnings-related; the state subsidises the childcare credits only.

"Small entrepreneurs" in Austria are exempt from paying the value added tax and they can use lump-sum expenses. The limit for these entrepreneurs was raised from 30,000 to 35,000 € per annum as part of the tax reform from 2020. The lump-sum expenses have 2 rates: 20% on the income from services and 45% on the income from trade and production.

Table 1 Income taxation of small entrepreneurs in Austria from 2020: an example (€ per annum)

Turnover	**30,000**
Lump-sum expenses 45%	-13,500
Social insurance contributions	-3,991
Profit	12,509
Basic deduction	1,626
Assessment base for income tax	10,883
Income tax	0

Source: WKO (2020)

The Austrian personal income tax or wage tax table has 6 non-zero rates; as part of the tax reform, the marginal rate of 25% will be reduced to 20% from 2021 and the other two rates of 35% and 42% will be reduced to 30% and 40% respectively from 2022 – see Table 2. The given income bands are before the deduction of social security contributions from the tax base.

Dividends in Austria are taxed by a "capital gains tax" (Kapitalertragssteuer) at a rate of 27.5%; this will remain unchanged. The tax reform will lead to a reduction in the rate of corporate income tax from the current 25% to 23% from 2022 and to 21% from 2023. The overall tax burden in the case of the full allocation of profit to dividends is due to fall from the current 45.625% to 42.725% in 2023.

Table 2 Personal income tax (wage tax) in Austria (€ per annum)

Income over	Income to	2020 marginal rate	New rate
0	11,000	0 %	
11,000	18,000	25 %	20 % from 2021
18,000	31,000	35 %	30 % from 2022
31,000	60,000	42 %	40 % from 2022
60,000	90,000	48 %	
90,000	1,000,000	50 %	
1,000,000		55 %	

Source: WKO (2020)

The Austrian tax reform also includes an entire range of further parametric changes; for example, increased employee lump-sum expenses. Or the new Family Bonus Plus (Familienbonus Plus), which replaced the deduction from the tax base since the tax settlement for 2019; it is a non-refundable tax credit of 1,500 € per child per annum, provided there is an entitlement to the child benefit.

The tax reform includes also increases in some taxes, such as the tax on cigarettes. The reform also involves the introduction of a digital tax with a 5% rate on the advertising turnover of international digital concerns from 2020.

An extensive WISO study into the Austrian tax structure in relation to the EU and its influence on growth and inequality points to the erroneousness of the OECD's mechanical comparison of the tax burden on labour, which concerns social insurance contributions. In Austria, these insurance contributions serve for transparent financing of the individual branches of social insurance. It is possible to view the thus-conceived insurance contributions as part of the wage. Every reduction in social insurance contributions would directly endanger this insurance and would lead to pressure on the citizens to finance the social security system from their own pockets. The introduction of the social insurance bonus is a suitable tool for reducing the tax burden (see above). At the same time, it is also necessary to view corporate taxation in a wider context, especially with regard to the fall in the share of wages in GDP in Austria in recent decades. The study reached the conclusion that corporate income taxation in Austria is significantly below average; the flat-rate reduction of the corporate tax rate emerged as the worst variant. The study pitched the option of introducing a general property tax on assets in excess of 1 million € at a 1% rate in connection with the low property taxation. It also states that inheritance and gift tax has been cancelled in Austria, even though 40% of property inequalities in Austria can be explained by inheritance and gifts (Banabak and Gerhartinger, 2019).

The new Austrian government consisting of the ÖVP and the Greens has decided to carry out the tax reforms in 2021 and 2022, which would lead to a reduction of taxation on low and middle-income families and companies. The Family Bonus Plus is to be increased. The tax system should also undergo a process of "ecologization".

IV. Czech tax structure and policy

The Czech tax structure is significantly different from the average of the OECD countries – for three public revenues: we apply a very low taxation for personal incomes and property and, on contrary, we have a high share of social security contributions – see Figure 4.

OECD notes that „imbalances in the [Czech] structure of government revenues contribute to relatively high cost of labour. The tax wedge is the 6th highest across the OECD and the average rate of employers' social contributions is the second highest… Up to now, this has not been detrimental to labour market performance, in particular to employment, only because the average wage is low compared to other EU countries. Indeed, the Czech Republic has built its comparative advantage by holding wages low to attract foreign direct investment, in particular in the manufacturing industries. … However, as wage convergence towards OECD and EU averages is continuing and given the recent acceleration of wage growth, the high level of wage taxation could become burdensome. To maintain wage competitiveness, the government should consider shifting part of the financing of social protection from wages towards taxes on goods and services or on all kinds of income (e.g. capital and property income) and environmental taxes. …, indirect taxes are less harmful for growth than taxes on wages" (OECD, 2018).

More specifically, OECD recommends us to reduce the overall rate of employer social security contributions from 34% to 31% and to increase the value-added tax rates (4 scenarios, from which we can choose). To support the argument for reducing the rate of employer social security contributions, OECD attached a chart showing the rates of these contributions in the OECD countries. The argument for less harmful effect of indirect taxes comes from the neoliberal front. The current above-average Czech standard VAT rate within OECD as well as lower VAT rates in the three neighbouring countries are being ignored by the OECD. In the recent years, the standard VAT rates have stabilized at a historically high level; the average standard rate was 19.3% in 2019 (OECD, 2019c). For these reasons, it is not possible to agree with the recommendation to increase the Czech standard VAT rate, moreover by some 3 percentage points.

"It is a paradox that the entire political spectrum agrees about the overly high price of labour in Czechia – without any exceptions. Yet nothing is done" … "The price of labour is truly high in our country and we would like for more money to stay in employees' pockets in the future", said Prime Minister Babiš. And his words have [allegedly – the author] been supported by the leader of the Czech Social Democrats, Mr Hamáček: "There is no reason why an Austrian or German employee should receive many times more than his colleague in the Czech Republic for the same work". … The leader of the Pirates, Mr Bartoš stated that: "The state should guarantee that the wage is sufficient to cover basic household needs, which can be achieved by reducing the taxation of labour, which is among the highest in Europe, so that people do not have to borrow money for common things." According to a survey undertaken by MF DNES, the Civic Democratic Party, the Christian Democrats, the Freedom and Direct Democracy Party, the Communists and the TOP 09 party are in complete accord with these ideas. However, there is no concrete proposal on the table and the electoral term is slowly drawing to an end (Janouš and Kvasnička, 2020).

The 2018 keynote address of the Czech government promises "to abolish the super-gross wage construct for personal income tax and propose a new reduced rate at 19% of the gross wage. The existing solidarity levy will be retained by introducing a 23 % rate from the gross wage. … In relation to employees, the systemic changes must result in a tax burden decrease by 1 percentage point. … We respect the principle of tax neutrality. We will ensure that tax exemptions are revised and merged, and we will prevent the introduction of any new ones, which will create scope for decreasing the tax burden across the board. We will promote a new draft design-oriented statutory adjustment in the income tax, which will introduce new provisions governing taxation and the system of insurance contributions paid from such income, to simplify taxes and eliminate tax distortions. The process of income tax recodification will be completed with the preparation of an integrated tax and compulsory insurance contribution administration system, which will provide for a one-stop scheme for the payment of these statutory obligations" (Babiš et al., 2018). The aim of the transition to the 19 % rate of the gross wage was simple: the effective personal income tax rate was 20.1 % of the gross wage (equivalent to the existing 15 % rate from the super-gross wage) and the employees would pay less by 1.1 % of gross wage. It is a simple political marketing.

The personal income tax reform scheduled by the government is simple and clear; it is about the elimination of the concept of the super-gross wage taxation (which ought to be finalized by the augmentation of the gross wage to the full labour costs supplemented by the takeover of employer social security contributions by the employees). The Finance Minister Schillerová submitted the respective tax bill yet in 2018, it was fully in consistence with the government keynote address: a shift to a standard rate of 19 % of the gross salary, together with the introduction of an increased rate of 23 % instead of the existing solidarity surcharge, which is set at 7 % of the gross salary exceeding 400 % of the national average earnings. But the Prime Minister Babiš rejected the proposal of the Finance Minister, he argued that he was not able to win political support for the proposal; in fact the proposal had not been presented in detail even to the general public. More recently, the Minister of Finance explained the problematic nature of this proposal by saying that "the interdepartmental commenting procedure … showed that there would be certain groups of taxpayers, for whom this measure would imply a tax increase from 15 % to 19 %, and that is something we simply do not wish to happen" (Schillerová, 2020). From an expert point of view, however, this increase is in accordance with the principle of equal taxation. We can imagine that the reason of the Prime Minister veto was the increase of the dividend income tax rate from 15 % to 19 %. (In Austria he would pay 27.5 %.)

In the beginning of 2019 the Ministry of Finance made a second attempt to realize the government tax reform programme: the idea was to decrease the personal income tax to 1 5% of the gross wage and to increase the employee health insurance premium from 4.5 % to 8.2 % of the gross wage, with a simultaneous abolition of the insurance premiums paid by the state for the "state insureds". The rate of the personal income tax would thus effectively decrease by 5.1 % of the gross wage, so the employees would gain 1.4 % of their wage from this tax reform

(Pergler and Ťopek, 2019). The capital income tax rate would thus remain at 15 %. This second proposal for a personal income tax reform escaped from the expert discussions between the Ministry of Finance and Ministry of Health at the end of February 2019. The reform proposal was opposed by "health care experts" (mainly lobbyists): they consider the periodical increases of the low state payments to the "dedicated account for public health insurance" to be a more advantageous way of promoting growing expenditure for health care than pursuing an increase in the premium rate. Later, the proposal of the Ministry of Finance was also opposed by the Prime Minister, obviously due to the media campaign of the lobbyists. This marked the end of the plan for a "major tax reform comprising lower taxes and higher health insurance contributions".

Until June 2019 the employer social security contributions amounted to 34 % of the gross wages. Since mid-2019, the sickness contribution rate paid by employers was reduced by 0.2 % of the gross wage in connection with the abolition of the waiting period in the sickness insurance scheme, which slightly influenced also the assessment base of the tax paid by employees; the effective nominal personal income tax rate now amounts to 15 * 1.338 = 20.07 percent of the gross wage.

The Czech self-employed are exempt from paying the value added tax upon achieving a turnover of 1 million CZK per annum. Lump-sum expenses have four rates: 80 % (agriculture, forestry, water management and craft production), 60 % (other craftsmen), 40 % (independent professions, experts, interpreters, authors) and 30 % (individuals with incomes from renting). The turnover limit, from which the maximum expenses are calculated, amounts to 2 million CZK from 2020 which is the level applied until 2018. This threshold has been repeatedly the subject of political and marketing games. The Czech threshold is more than double the Austrian threshold of 35,000 € (using the exchange rate from the beginning of July 2020). The Czech rates for lump-sum expenses are also substantially more advantageous. This also applies as far as social security contributions of self-employed are concerned. According to an older international comparison, only the Isle of Man and Russia have more favourable self-employed taxation (AGN, 2017).

Czech social security contributions have no comprehensive concept: the structure of the insurance contributions for pension insurance and the contribution to the state employment policy give rise to the impression of an insurance system, with the specifics of self-employed (voluntary sickness insurance and optional extent of the pension insurance and of the "state employment policy"). On the other hand, the health insurance contributions appear to be an unjust health tax at first glance. The insurance premiums for the mandatory employer liability insurance for work injuries and occupational illnesses would be better suited – according to their name – to mandatory private insurance; in terms of their contents, however, this naturally involves supplementary social accident insurance. At the same time, it would be optimum, if the entire Czech social security system were based on a single welfare regime. In this regard, it is characteristic for the consultancy of the OECD and the EU that they do not concern themselves with the actual concept of Czech social security at all – they merely think that social security contributions should be reduced on the basis of the tax structure (tax mix). This is a simple reflection of the fact that they have included the insurance premiums among taxes and they anticipate that they can manipulate the (entire) rate of the social security contributions according to the general considerations of the so-called theory of optimal taxation. However, we consider it essential to first analyse the justification of the very existence of the contributions for the individual branches of social security.

The social security contributions should, in principle, correspond to the design of the different social protection branches, they should not substitute taxation of income or consumption, as is the case primarily with the Czech health insurance premiums which constitute unfair income taxation. The efforts to privatise public health care financing were cut off by the 100 % redistribution of the insurance premiums and the Reimbursement Decree of the Ministry of Health, which provides for the financing of the different health care segments. The pension insurance premium with the rate of 28 % of the gross salary is justified for roughly 30 % only because the flat-rate old-age pension is predominant in Czechia and should, similarly to general health care, be financed from general taxes – not from insurance premiums. Under these circumstances, the primary solution lies in integrating the employee insurance premiums into the personal income tax and in integrating the employer social and health insurance premiums and the premium for the employer statutory liability insurance for work injuries and illnesses into a single comprehensive social security contribution to be paid to the state budget via a single collection point. The reduced overhead expenses would also cover the deficit from the abolishment of the existing health insurance premium paid by the "persons with no taxable income".

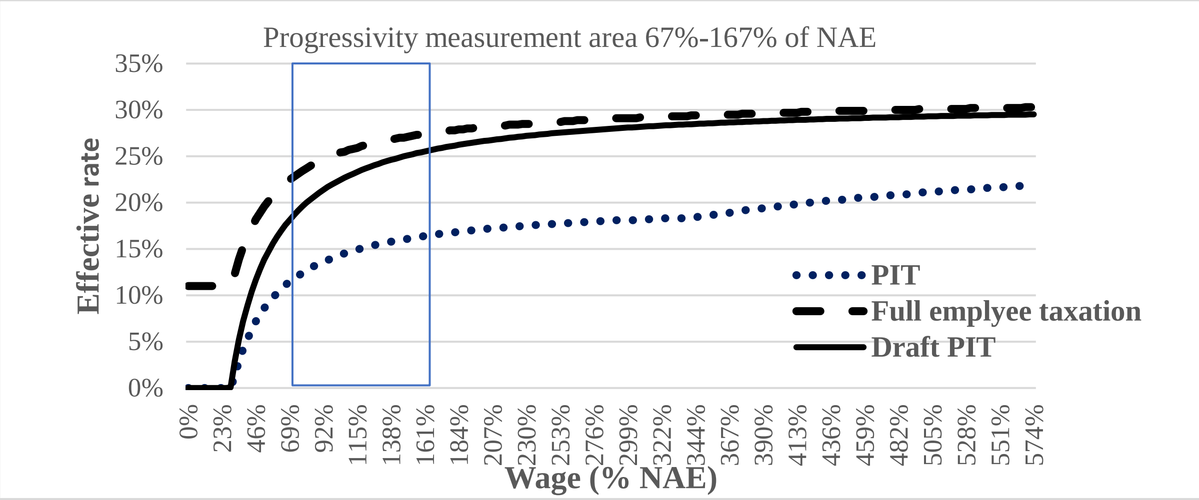
The low level of the Czech personal income tax can be increased by integrating the (fully redundant) employee insurance premiums into this tax, with a total rate of 20.0 7% + 11 % = 31.07 % from the gross wage. The (basic) flat rate of the Czech income tax need not be necessarily abolished because the progressivity of the flat-rate income taxation depends also on the basic tax credit, which is low in Czechia due to its non-indexation from the 2008 tax reform. I am not aware of any politician having ever requested an increase in the basic tax credit per taxpayer prior to 2019. (This year a group of MPs learned the fact and prepared a simple bill requesting (only) a one-off increase of the tax credit.) In 2008, the progressivity of the overall income taxation (including the social security contributions) in Czechia was average, but now it is clearly below average (index 127 in 2018). We measure progressivity in the same way as the OECD: using the relation (index) of the taxation of a single, childless employee with a wage at the amount of 167 % of the national average wage (NAE) and the taxation of the same taxpayer with a wage at the amount of 67 % of NAE. In Austria, this index was 140 in 2018, while the average for OECD countries was 146. Using the example of Austria, we can see the actual progressive boundary rates for income taxation may give rise to the impression of a distinctive progressive tariff, but the deduction of employee insurance contributions from the income tax base, including the ceiling for the assessment base for the insurance contributions which is usually at the level of 150 % of the NAE, plays a significant role.

When including Czech employee insurance contributions into personal income taxation, the so-called solidarity surcharge in the income taxation of natural persons with a rate of 7 % of the gross wage above 400 % of NAE and a concurrently existing earnings ceiling of 400 % of NAE for pension insurance contributions with a rate of 6.5% fall away; after all these instruments involve about 1 % of taxpayers only. When the insurance contributions are integrated into the personal income tax, the experienced problem of the collection of insurance contributions from even very low wages in Austria, which they have resolved in the form of a social insurance bonus, also falls away.

The entire personal income taxation in Czechia needs to be adjusted to the integration of the employee insurance premiums into the income tax. First, it is essential to revise all tax expenditures; the common Western practice of tax expenditure reporting should be implemented at the same time, preferably as part of the draft bill on national budget and national closing account. In this regard, Czechia needs to eliminate, in particular, the fiscal costs of supplementary pension savings scheme and private life insurance scheme which are (already at present) extremely high (the largest item is the exemption of the employer contributions from the payment of insurance contributions and the personal income tax), as well as the state contribution for the building savings (which is also drawn for the so-called bridging loans!) and the tax deductibility of interest on mortgage loans and building savings loans. We may confirm that "pressure groups (lobbies, etc) and politicians had discovered that the income tax was an ideal tool for permanently promoting certain preferred activities, through the use of "tax expenditures" rather than through public spending that need legislative approval each year. "Tax expenditures were justified on grounds that they improved equity and promoted some worthwhile objectives. This made income taxes progressively more complex and, horizontally and perhaps vertically, less equitable" (Tanzi, 2010). Here "the political economy of revenue-neutral income tax reforms aims at cutting back these expenditures in exchange for lower tax rates: "tax-cut-cum-base-broadening" (Barbaroa and Suedekumb, 2016). That is the best tax policy for Czechia as well.

The second-best policy or even the alternative best tax policy is the switch of the (unfair and unconstitutional) Czech state support of the financial products referred to above for specific individual savings accounts (ISA), e.g. the Canadian tax-free savings accounts (TFSA). Their basic behavioural trick is that the client is limited in an annual or lifetime deposit/investment (in our conditions for example CZK 30,000 per year) and time and amount of savings withdrawal is unlimited. That is why TFSA is said to be best used as a pension savings instrument (Kasper, 2019). The tax regime for these products is TEE (savings from after-tax income, no further taxation): the only regime that can possibly be recommended for Czechia. These products are provided by common financial institutions.

Figure 5: Effective Czech personal income tax rates (PIT) and full employee taxation rates (PIT + employee social security contributions) in 2020 and the draft PIT with indexed basic tax credit (8.9% of NAE, 2020)



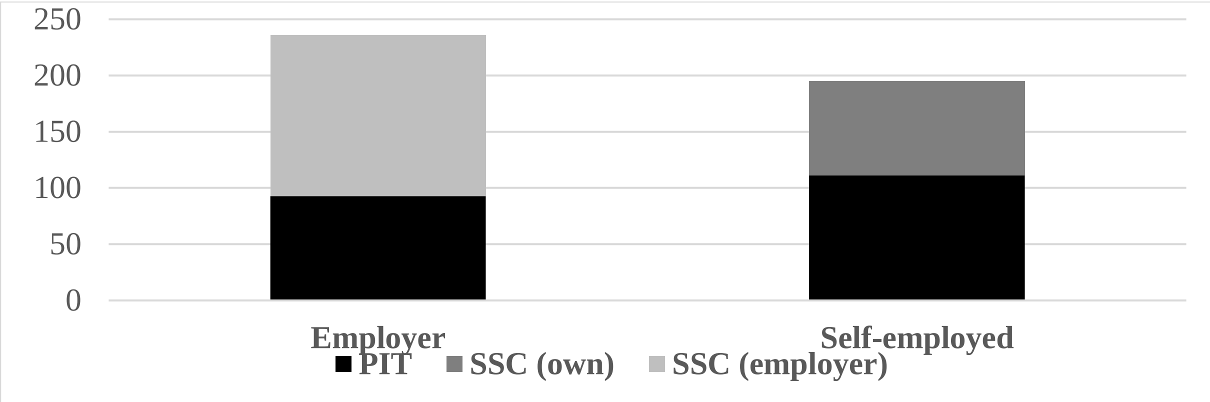
Source: Author

When carrying out tax reform consisting in the inclusion of employee insurance contributions into the personal income tax, it is expedient to eliminate the "cold regression" in income taxation which has accumulated since 2008 or rather to set the progressivity of the new tax with a flat rate of 31.0 7% (politicians will surely round this rate) at the average of the OECD (or Austria). One solution is to increase the basic tax exemption of 2,070 CZK per taxpayer per month to 8.9 % of NAE, which would amount to 3,100 CZK per month under 2020 conditions. This would reduce the effective tax rate for employees with NAE to 22.2 %. The political effect is also important; in relation to the existing recipients of state support for financial products, amongst other things. Figure 5 shows the impact of personal income tax reform on the existing income tax for natural persons and employee insurance contributions – the dependency of the average effective rates on the amount of the wage expressed as a percentage of NAE.

The existing employee insurance contributions consist of pension premium (6.5 %) and health premium (4.5 %); the total health insurance contribution rate is 13.5 % of the gross wage. The entire health premium is unnecessary from a systemic point of view, so we can preferentially include it in the employee insurance contribution (11 %), which we will integrate into the personal income tax. We transfer the remainder of the health premium (2.5 %) and the employee pension premium to the insurance contribution paid by the employer. We also include here the accident insurance premium (employer mandatory liability insurance for work injuries and occupational diseases), the separate collection of which also does not make any sense; at the same time, we can unify its rate, for example, at 0.45 %, according to the Austrian or Slovak model. Employers would thus now pay insurance contributions of 34.25 % of the gross wage; these contributions predominantly would have the character of a (payroll) tax. Given this situation, the variant involving the fully integrated collection of these social security contributions into the state budget is optimal with the possible inclusion into law on the budgetary designation of taxes. The social security contributions used in Sweden could be taken as the model, for example.

It would also be expedient and fair to apply the stated concept/construction of the social security contributions to the self-employed. Here too, the current social and health insurance contributions should be replaced with a single social security contribution, the rate of which takes into account the lower scope of social security for the self-employed and the calculation of the contribution as a deduction from the assessment base (the corporations pay a surcharge to the assessment base). In this way, we arrive at a social security contribution rate for self-employed at the level of ca 15 % of the excess of receipts above expenses. We add this contribution to expenses/costs and arrive at the personal income tax base used to assess this tax with a general rate of 31.07 %. Figure 6 illustrates the comparison with employees at NAE designated by the Ministry of Labour and Social Affairs for the purposes of pension insurance for 2020.

Figure 6: Social security contributions and personal income tax: employee with NAE and self-employed with comparable income in thousands of CZK (draft)



Source: Author

In 2018, the government undertook, amongst other things, to prepare an integrated tax and insurance premium administration system which will enable the payment of these mandatory contributions all in one place. In this regard, pending legislation on the “flat-rate” taxation for self-employed individuals with an annual turnover of up to 800,000 CZK has been prepared and it should come into effect from 2021. This “flat tax” should amount to 5,740 CZK a month (68,880 CZK per annum) in 2021 and it should consist of 3 components: health insurance premium (2,514 CZK per month), social insurance premium (3,126 CZK per month) and income tax (100 CZK per month). The new “flat tax” is an optional alternative for the self-employed; when choosing this option, it will not be possible to apply any tax deductions or credits (not even for children). Judging by the examples in the newspapers, this “merely” involves a tax optimisation tool for a narrow group of the self-employed, which will increase the costs of the state administration. I am not aware of anything similar existing abroad. From a systematic point of view, the "flat tax" for a couple of the self-employed is a total nonsense at the first glance.

In Czechia, dividends are taxed by a withholding income tax with a 15 % rate "derived" from the flat income tax rate. With regard to the current taxation of wages, the corresponding rate for taxing income from dividends should be at least 20 %. The OECD (2018) recommends that we introduce the payment of health insurance premium from all income, i.e. collect insurance contributions (13.5 %) from dividends: this would be in addition to the current 15 % rate, resulting in overall taxation of 28.5 %, which would be slightly more than in Austria (27.5 %). Low capital taxation is typical for post-communist countries. However, we should abandon the tax policy of pandering to western capital.

The classic corporate income tax system is based on the so-called material ability to pay of the companies (Engliš, 1929): corporate profits should be taxed regardless of the personal income taxation, including dividend incomes. This system is still used in Austria (25 % rate) and in Czechia (19 %). Neither of the countries have displayed any tendencies to change this system. A number of countries in the world has several combined systems. Under Czech conditions, where the aggregate taxation of corporate and personal income is the 6th lowest one of the 36 OECD countries, we recommend to apply the comprehensive business income tax (CBIT) with a rate of 31.15 % (= the overall rate of the existing combined taxation of corporations and personal income from dividends), which involves a system of taxing corporate profits and the interest on corporate bonds without any further subsequent taxation of capital incomes. The objective is to tax these incomes in the country of its origin; this should be significantly advantageous for Czechia. „The current regimes give rise to various instate and interstate spillovers, which violate the basic tenets – neutrality and subsidiarity – of the single market. The trade-offs between the implications of these tenets – harmonization and diversity, respectively – can be reconciled by a bottom-up strategy of strengthening source-based taxation and narrowing differences in tax rates. The strategy starts with dual income taxation, proceeds with final source withholding taxes and rate coordination, and is made complete by comprehensive business income taxation. Common base and cash flow taxation are not favored" (Cnossen, 2018).

Two comments on property taxes: Czechia has no road tax for motor vehicles owned by citizens. Austria has an insurance tax based on engine size (motorbezogene Versicherungssteuer) which was called a motor vehicle tax until 1993; this tax is collected by insurance companies along with the motor liability insurance. The Czech government initiated lately the cancellation of the tax on the acquisition of a real estate (4 % rate) with the justification that it is highly unfair. Austria has a real estate acquisition tax at a rate of 3.5 % (registration in the Land Register costs another 1.1 %).

V. Conclusion

The Austrian and Czech tax structures display a high tax burden on labour and low property taxation, both in comparison with other OECD countries. Modern social and tax theory is not satisfied with the mechanical comparison of tax structures and does not infer from them the automatic need to restructure the tax systems according to the supposed harmful nature of the individual tax channels. This is clearly visible in the example of Austria and Czechia: even through both countries have above average rates of social security contributions, they have also a substantial difference in the dependence of the insurance benefits on earnings. Austria is still patterned on the Christian-Democratic model of financing social security, but the universalisation of the social systems for individual layers of society has also become apparent, for example in the merger of almost all the sickness insurance funds into a national-wide

Austrian health insurance fund. On the other hand, the post-communist Czechia has slipped in the direction of the neo-liberal model of several health insurance funds and their lobby has so far successfully deflected any attempts at the even partial rationalisation of health insurance premiums in association with the promised reform of personal income tax and social security contributions.

The latest Austrian governments have systematically endeavoured to modernise taxes, including regarding ecological objectives. The room to reduce the social security contributions is, however, relatively small, because public pensions are relatively high and they are a highly earnings-related system; the reduction of the insurance premium rate (22.8 %) would result in significant pressure on the reduction of Austrian pensions. On the other hand, less than one third of average Czech public pension is earnings-related, so the insurance contribution rate of 28 % can be substantially reduced commensurate to that. The Czech government has not developed any initiatives in this regard. The entire Czech political spectrum agrees that the price of labour is overly high, but no adequate proposal is on the table yet. The reason for this may be the high degree of segmentation in the political spectrum and the apparently associated emphasis on marketing politics.

Even the programme declaration of Babiš' government on the reform of income tax and insurance contributions appears to be merely a marketing ploy: the Prime Minister vetoed the abolishment of the super-gross wage with the transition to the taxation of the gross wage at a marketing rate of 19 % (described in the government declaration) because of his conflict of interest. The basic solution of the disproportions in the labour taxation involves the inclusion of the entire employee insurance contribution into the personal income tax (and the increase of the basic tax credit). Moreover, it is possible to reform the capital income taxation by integrating it into a "comprehensive business income tax" (with a rate of 31.15 %), which taxes corporate profits and interest costs, but abandons the double taxation of dividends, meaning that the aforementioned conflict of interest would fall away. Knowledge of the modern tax theory would be of help to the Czech tax policy.

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