

FISCAL ASPECTS OF LABOUR TAXATION IN LATVIA

NODOKĻU NO DARBA FISKĀLIE ASPEKTI LATVIJĀ

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The labour taxes in the European Union are mainly personal income tax and social security contributions. In Latvia, the revenue from labour taxes form slightly more than a half of total tax revenue. Historically in the European Union, also, there has been a high tax burden on the labour income with a growing trend which was based on the ability of labour taxes to provide additional government expenditure due to their progressiveness unlike consumption taxes, for instance.

According to the calculations of the European Commission the implicit tax rate on labour describing the tax burden in the European Union on average tends to decrease starting already from early 90ties. Similar trend is observed in Latvia. The decrease in implicit tax rate on labour in recent years was mainly due to reduction of nominal tax rate of social security contributions from 38% to 33.09% from 1995 till 2003, consistent rise of personal income tax allowances, as well as reduction of personal income tax rate from 25% to 23%.

Although the above mentioned tax policy measures have a negative fiscal impact in recent years, taking into account rapid increase of wage bill, there was also a rapid increase in personal income tax revenue and social security contributions. It should be noted that less revenue from labour taxes in the budget are forecasted as a result of worsening of economic situation, including decrease in the labour income and increase in unemployment. Moreover, it is observed that due to uneven development of tax allowances and tax arrears revenue trends of personal income tax and social security contributions are different, i.e. the personal income tax revenue decreases more rapidly than the revenue from social security contributions although tax bases are basically equal. The decrease in social security contributions significantly affects also the social security budget expenditure (pensions, benefits etc.) which in the economic downturn tend to increase.

In the article revenue aspects of labour taxes are analysed in detail and attention is paid to fiscal impact of tax allowances as well as recommendations for further adjustment of labour tax bases in order to balance both fiscal goals and the goal to avoid rising the tax burden on the labour income.