



Tomasz Wołowiec

*Dr hab., prof. nadz., Faculty of Administration and Social Sciences,
University of Economics and Innovation in Lublin
(Lublin, Poland)*

** Corresponding author: e-mail: wolowiectomek@gmail.com
ORCID: <https://orcid.org/0000-0002-7688-4231>*

**DIRECTIONS, SENSE AND PURPOSE OF PERSONAL INCOME
TAXATION HARMONIZATION PROCESS ACROSS EUROPEAN
UNION MEMBER STATES**

**KIERUNKI, SENS I CELOWOŚĆ HARMONIZACJI
OPODATKOWANIA DOCHODÓW OSÓB FIZYCZNYCH
W KRAJACH UNII EUROPEJSKIEJ**

**НАПРАВЛЕНИЯ, СМЫСЛ И ЗАДАЧИ СОГЛАСОВАНИЯ
НАЛОГООБЛОЖЕНИЯ ДОХОДОВ ФИЗИЧЕСКИХ ЛЕСОВ
В СТРАНАХ ЕВРОПЕЙСКОГО СОЮЗА**

Abstract

The current taxation of personal incomes is a very complex phenomenon which should be analysed not only from the legal point of view, but also taking into account its social, cultural, economic, political and system aspects. We cannot isolate the economic sphere from the tax sphere, as income taxes directly affect the taxpayers function as well as their purchasing power; moreover, they determine labour costs for entrepreneurs and thus significantly influence the GDP growth rate. The issues of harmonizing taxation of incomes obtained by individuals who do not act as economic operators are practically absent in scientific literature. The only analysed issues are related to taxation of incomes from savings, transfers, capital gains, mergers and divisions. This is so because it is required by the nature of conducting economic operations within the common market.

Keywords: *personal income taxation, harmonization process, common market*

Streszczenie

Mimo, iż opodatkowanie dochodów osobistych leży w kompetencji każdego z państw członkowskich, w wielu sytuacjach potrzebna jest koordynacja na poziomie unijnym regulacji podatkowych, mająca na celu zapewnienie swobód określonych w Traktacie ustanawiającym Wspólnotę Europejską oraz wyeliminowanie barier podatkowych w ponadgranicznej działalności obywateli państw – członków UE. W szczególności niedopuszczalne jest stosowanie – bezpośredniej, czy pośredniej - dyskryminacji ze względu na narodowość ani też żadnych nieuzasadnionych ograniczeń czterech swobód Rynku Wewnętrzznego. Brak wymogów harmonizacyjnych (z wyjątkiem opodatkowania dochodów z

ISSN 2450-2146 / E-ISSN 2451-1064

© 2018 /Published by: Międzynarodowy Instytut Innowacji Nauka-Edukacja-Rozwój w Warszawie, Polska
 This is an open access article under the CC BY-NC license (<http://creativecommons.org/licenses/by-nc/4.0/>)

Wołowiec T. (2018) Directions, Sense And Purpose Of Personal Income Taxation Harmonization Process Across European Union Member States. *International Journal of New Economics and Social Sciences*, 1(7)2018: 77-99

[DOI 10.5604/01.3001.0012.2549](https://doi.org/10.5604/01.3001.0012.2549)

oszczędności) oznacza, iż konstrukcja PIT w krajach członkowskich jest silnie zróżnicowana z uwagi na odmienne uwarunkowania społeczne, polityczne i ekonomiczne. Z drugiej strony pojawia się pytanie, czy harmonizacja tej formy opodatkowania jest w ogóle możliwa, a przy tym celowa? Niewątpliwie zróżnicowany poziom wynagrodzeń, różnice w kształtowaniu podstawy opodatkowania i wysokości podatku, i często odmienne zadania nakładane na podatek dochodowy utrudniają jego ujednoczenie i harmonizację. Wydaje się, więc, że wszelkie próby związane z harmonizacją ww. obciążeń fiskalnych należy rozpocząć od zdefiniowania i ujednoczenia w ramach Unii Europejskiej pojęcia dochodu podatkowego (podstawy opodatkowania).

Słowa kluczowe: podatek dochodowy od osób fizycznych, proces harmonizacji, wspólny rynek

Аннотация

Хотя налогообложение личных доходов относится к компетенции каждого государства-члена, во многих ситуациях необходимо координировать налоговые правила на уровне ЕС, направленные на обеспечение свобод, установленных в Договоре об учреждении Европейского сообщества и устранении налоговых барьеров при трансграничной деятельности граждан ЕС. В частности, неприемлемо применять прямую или косвенную дискриминацию по признаку гражданства или любых необоснованных ограничений на четыре свободы внутреннего рынка. Отсутствие требований гармонизации (за исключением налогообложения доходов от сбережений) означает, что строительство ПНД в государствах-членах сильно диверсифицировано из-за различных социальных, политических и экономических условий. С другой стороны, возникает вопрос, возможна ли гармонизация этой формы налогообложения вообще и в то же время она преднамеренная? Несомненно, различный уровень вознаграждения, различия в формировании налоговой базы и суммы налога и часто разные задачи, связанные с подоходным налогом, затрудняют согласование и согласование. Поэтому представляется, что все попытки, связанные с согласованием вышеупомянутого Фискальное бремя должно начинаться с определения и согласования в рамках Европейского Союза концепции налоговых поступлений (налоговой базы).

Ключевые слова: подоходный налог с населения, процесс согласования, общий рынок

Article history: Received: 31.05.2018 / Accepted: 15.06.2018 / Published: 30.06.2018

JEL Classification: H 240

Statement of the problem in general outlook and its relations to important scientific and practical tasks.

Personal income tax (hereinafter referred to as PIT) has a short history, as it appeared in tax systems of EU countries at the end of the 18th century. As a specific universal construction it performs two economic

functions: providing financial means for covering some public expenses (fiscal function), leveling off – through its construction – inequalities in population incomes (redistribution function) and implements social

ISSN 2450-2146 / E-ISSN 2451-1064

© 2018 / Published by: Międzynarodowy Instytut Innowacji Nauka-Edukacja-Rozwój w Warszawie, Polska

 This is an open access article under the CC BY-NC license (<http://creativecommons.org/licenses/by-nc/4.0/>)

Wołowicz T. (2018) Directions, Sense And Purpose Of Personal Income Taxation Harmonization Process Across European Union Member States. *International Journal of New Economics and Social Sciences*, 1(7)2018: 77-99

DOI 10.5604/01.3001.0012.2549

functions of taxation through various tax reliefs and exemptions or the construction of the tax scale. Contemporary personal income tax in European countries has been shaped by many years of evolution. This process is continuing, taking into account the process of European integration and the processes of standardizing and harmonizing tax systems in the European Union countries. Most EU states only sporadically implement major reforms of personal income taxation. The scope of such changes is usually limited and determined by current fiscal needs or the need to stimulate a particular behaviour of taxpayers (European Tax Handbook, 1998-2017).

As for the legal solutions in tax law, the doctrine commonly accepts the view that taxes and the whole tax system should be neutral and should perform only the fiscal function of taxation. It means that taxes should be built in a way that does not interfere with the existence and activities of taxpayers and they shouldn't contain any preferences for selected groups of taxpayers. Favouring tax neutrality does not determine the negative attitude to achieving non-fiscal goals of the state through tax preferences. For example, using various forms of tax preferences may be a consequence of subjectively understood tax equity. Such equity requires noticing different material, family and social situation of each taxpayer. Non-fiscal functions of taxation are best realized by income taxes due to their specific construction (for example P.A. Samuelson, W.D. Nordhaus). Non-fiscal aspects of taxes gained popularity under the influence of J.M. Keynes theories. In classical economics, taxes were treated exclusively as a source of means for covering necessary public expenditure. The criterion for assessing financial policy should be its effectiveness in achieving the assumed goals, such as: high but stable economic growth, full employment, low inflation.(Szybowski

D. 2018 p.181-216) In Keynes' theory, taxes became a major instrument used by the state to influence the economic cycle. Stability of the economy within the countercyclical policy, along with the need to stimulate global demand, has led to the growth and stability of the redistribution of tax functions. A result of such approach to the use of taxes in fiscal policy was an increase in the budget deficit and public debt and the growing level of the tax burden. This led to popularity of neo-liberal theories, the most popular of them being the supply side economics. It claims that high tax burden generates low level of savings, high inflation and low productivity and innovativeness of the economy (C.R. Mc Connell, 1987, N. Acocella, 2002).

Although personal income tax is commonly used to achieve various economic and social goals, its fiscal function is still considered as the most important one. We should also observe that the doctrine quite commonly tries to promote the thesis of tax neutrality as a specific panacea for weakened economic growth of EU countries and deteriorating competitiveness of European economies. The belief in tax neutrality stems from the fiscal function of taxes. According to some representatives of the doctrine, we should not use taxes to achieve various social goals, often contradictory to fiscal requirements of the state. It is difficult to agree with the concept of tax neutrality, because in practice it is impossible to separate tax legislation from the influence of widely understood policies. Moreover, the thesis of tax neutrality was easy to defend when taxes constituted below 20% of GDP share. In many countries these days tax revenues reach or even exceed half of their GDP. Therefore, such a large-scale redistribution leads to serious economic and social consequences (P.M. Gaudamet, J. Molinier, 2000).

ISSN 2450-2146 / E-ISSN 2451-1064

© 2018 /Published by: Międzynarodowy Instytut Innowacji Nauka-Edukacja-Rozwój w Warszawie, Polska
 This is an open access article under the CC BY-NC license (<http://creativecommons.org/licenses/by-nc/4.0/>)

Wołowicz T. (2018) Directions, Sense And Purpose Of Personal Income Taxation Harmonization Process Across European Union Member States. *International Journal of New Economics and Social Sciences*, 1(7)2018: 77-99

DOI 10.5604/01.3001.0012.2549

Harmonization of taxes in the European Union is very closely tied with the concept of the common market. If this concept makes sense, we must, above all, fulfil the requirement of equal rights for each market participant, that is, each entity from any member state. Due to the fact that companies compete mainly in price, the factors affecting it should be the same in all member states (harmonization of indirect taxes). Tax harmonization is a process leading to standardization of tax systems in various countries. The process aims to achieve a state in which tax issues do not affect the flow of goods, services and production resources between countries. Harmonization is necessary when the differences in tax systems between particular countries account for the fact that decisions made by one or a few countries bring particular effects to other countries. Thus, it comes down to the harmonization of tax systems of different countries and ensures their functioning in accordance with the objectives of the economic union. Tax harmonization is a necessary element of economic integration; it is closely related to the degree of integration level (K.C. Messere, 1998 and 2001).

The problems of tax harmonization, so important for the current European Union, are not a new issue. One may even say that it has extensive historical background. The work of Carsten Pallas: *Tax Harmonization: The Case of Germany At the Beginning of the Nineteenth Century Lessons for the Twenty First Century?* (C. Pallas, 2005) should be quoted as an example of this type of research work. The paper concerns tax harmonization problems in the process of unification of the German state at the beginning of the 19th century. As the author states, at the end of the 18th century there were 324 tax regimes in the German territory and of which there only 41 remained after the Vienna Congress in 1815. According to the author, during the period of 1790-

1815, the tax harmonization process was forced by the French occupation. In 1815-1871, the tax harmonization process continued, but it was slower. After the unification of Germany in 1871 under the leadership of Prussia, the tax administration (mainly indirect) was transferred to the central government which, due to the huge budgetary requirements, increased them quickly, although tax competition between individual parts of Germany still prevailed. Tax harmonization took place mainly through adjusting to the level of Prussia which had lower level of tax rates than other states of Germany. However, a further increase in taxes in Prussia forced tax progression also in other German states. The author emphasises the decisive role of external forces in tax harmonization: French occupation during the Napoleonic times and, currently – the wish to avoid a war in Europe. In the conclusion of his article the author points out the lesson which may be learnt by the EU from the harmonization in Germany in the 19th century: avoid the convergence of tax rates forced from grass-roots through the tax harmonization undertaken voluntarily and harmonization in other areas of economy (C. Pallas). Pallas's article illustrates the deep conviction of numerous authors that the grass-roots convergence of taxes has negative effects, and that there is a need for close coordination of fiscal policy in the face of growing public expenditure requirements. D. Mitchell from the Cato Institute indicates in his paper (D. Mitchell, 2000) that tax competition forces governments to adopt tax solutions which are beneficial for the taxpayer. According to his research various tax rates distort the optimal allocation of resources, including capital. The weakness of this theory is the adoption of assumptions about the full mobility of all resources. As the author claims, paradoxically, tax competition is the best way to reduce tax harmonization. C.

ISSN 2450-2146 / E-ISSN 2451-1064

© 2018 / Published by: Międzynarodowy Instytut Innowacji Nauka-Edukacja-Rozwój w Warszawie, Polska
 This is an open access article under the CC BY-NC license (<http://creativecommons.org/licenses/by-nc/4.0/>)

Wołowicz T. (2018) Directions, Sense And Purpose Of Personal Income Taxation Harmonization Process Across European Union Member States. *International Journal of New Economics and Social Sciences*, 1(7)2018: 77-99

DOI 10.5604/01.3001.0012.2549

Blackordy and C. Brutt in their paper (C. Blackordy, C. Brutt, 1999) turned attention to the distribution effects of tax harmonization. Those effects may affect the flow of goods between countries and may influence the government revenue generated. If there is no mechanism to neutralise those effects, additional flexibility of tax systems may be required in order to maintain balance both in the state budget and in the balance of payments. The authors thesis may be understood in the way that losses on harmonization e.g. of indirect taxes may be compensated by increasing competitiveness of indirect taxes. R.E. Baldwin and P. Krugmann in their work entitled *Agglomeration, Integration and Tax Harmonization* (R.E. Baldwin, P. Krugmann, 2002) state that simple tax harmonization, understood as the adoption of a common tax rate; it always harms at least one country in the model developed by them. It seems that the adoption of a rate between the two initial rates in both countries may be disadvantageous for both countries. As for examinations of harmonization costs, it is worth mentioning the paper of E. Mendoza (E. Mendoza, 2001). The author estimated the potential attempt to harmonize the taxation policy of capital gains in the member states of the European Union. The author developed a dynamic model of general equilibrium of two countries in order to assess the potential effects of the harmonization of taxes on capital gains in Europe using the previously assessed effective tax rates: for UK - 47%, France, Germany and Italy – almost 28% in 1996.

The need for harmonization of direct taxes, including taxes on personal and corporate income taxes and taxes on property income, was not clearly specified in the Treaty establishing the European Economic Community. The legal base for initiatives in harmonization processes was Article 100 of the Treaty, stipulating harmonization of

those regulations that directly affect the creation and operation of internal common market. The process of direct taxes harmonization covered different income tax regulations which limited the freedom of income flow in form of dividends, interests, license fees and capital between Community members (this will be discussed in a separate analysis of the principles of capital income taxation).

We should remember that the principles of income taxation in EU countries do not constitute such an important area of harmonization as indirect taxes. It is assumed that the differences found in direct taxations are less dangerous for the functioning of the common market. Moreover, harmonization of these taxes is much more difficult than indirect taxes from the political, technical and legislative points of view. Only some elements of corporate income tax are being harmonized, as they relate to international aspects of company operations that could cause potential discrimination in treatment of home and foreign companies and which refer to avoiding double taxation. Probably further elements of corporate income tax will be harmonized next – tax rates and taxation base. There are following areas of PIT harmonization: taxation of incomes from savings paid out in form of interests and mutual administrative assistance in tax issues. The main element differentiating direct taxation is its slight degree of normative harmonization. It is commonly believed that direct taxes exert less destructive influence on the functioning of common market; therefore work on their harmonization started later, lasted longer and did not go as far as in case of indirect taxes. Direct tax regulations in the European Union are left at the discretion of the member states (except for the need to observe the areas presented in the table). Particular member states enjoy significant freedom in shaping their home solutions in this area. However,

they are obliged to treat home and foreign operators equally as far as taxation is concerned (E. Aksman, 2002).

Competition between tax systems forces certain solutions in national tax systems, aimed at bringing closer constructions of certain taxes in order to ensure optimal functioning of the common market. Thus “quiet harmonization” is a consequence of progressing competition among national tax systems in particular taxation forms (T. Wołowiec, 2011). The effect of quiet harmonization is bringing closer construction solutions in personal income tax in European Union states and it leads to find out the main reference points for transformation of an individual’s taxation system in European Union countries has been limited to personal income of individuals who do not conduct any form of business activity and it reflects the short and long-term run (I. Joumard, 2002).

Referring to PIT it was emphasized that the tax should remain at discretion of member states. The only harmonization activities should concern removing barriers to four economic freedoms and providing uniformity of taxation.

Similarities in the personal income tax in Community states concern the following

areas (A. Krajewska, 2004, T. Wołowiec 2008, Taxation Trend in the European Union, 2002-2017):

- The tax is related to total (global) income of a taxpayer,
- Scales are progressive with various numbers of ranges and minimum and maximum tax rate values,
- Most countries use tax-free amounts,
- Tax burdens are usually adjusted to inflation rate through the system of automatic or semi-automatic indexation of changes to tax thresholds,
- Personal income tax reflects the principle of taxpayer’s payment capacity through its varied system of tax reliefs and exemptions;
- Different rules are used for taxation of family incomes, revenues from selling property and movable assets and capital incomes,
- There is a varied system of costs of obtaining revenues, related to the way in which revenue is gained,
- It does not differentiate tax burden due to sources of revenues from which it is obtained and its allocation,
- Income tax contains tax preferences related to the way the income is spent.

Analysis of latest research where the solution of the problem was initiated.

A feature of direct taxes is that there is a clear connection between the taxpayer’s situation (income, property) and tax burden. From the psychological point of view indirect taxes are the most hated sacrifice to be made by the taxpayer. Direct taxes may demotivate the taxed entities. Excessive tax burden may slow down income activity of entities, which may result in not only slower economic growth, but in its disappearance as well. That is why not only the size of tax burden in a particular country matters, but also the structure of the whole

tax system and the construction of particular taxes. The tax scales are vital in case of direct taxes. In a theoretical presentation, tax as an economic category is subject of numerous analyses, both referring to individual taxpayers, their groups and the whole economy. This concerns both indirect and direct taxes. Despite impressive theories of economics, theories of public finance, hundreds of years of experience, tax issues are still a controversial topic, which is evident in a discussion on line tax. The deficit of theories and polarization of opin-

ions concerns the role of tax in micro-economics, where it would seem easy to determine the relationship between tax burden, tax scale and an economic situation of a taxpayer and the decision made by him. This results from the fact that the taxpayer's situation is affected by a number of other factors, therefore it is difficult to isolate the tax factor, if we do not take into account abstract analyses. The situation is further complicated when the subject of our analysis is the influence of a particular tax on the whole group of taxpayers or the whole tax system on economy (for example the theory of automatic stabilizers in business cycle). The difficulty of tax analysis regarding the tax impact on the subjects and the economy will increase if we go beyond the state with such analysis. Tax relations are further complicated and tax effects are even more difficult to assess or quantify. This is an important statement, as it partly explains the source of controversies concerning opposite tax doctrines – tax harmonization versus tax competition (S. James Ch. Nobes, 1998, Inventory of Taxes in the Member States of the European Union, 2002-2015). We will use the phenomenon of transferring direct taxes in order to exemplify the difficulties. Direct taxes may concern: income from work – income from economic activities, income from property and property rights, income from capital and from money savings. The subject of direct taxes is then the resources of work, land, physical capital, and financial capital – essential factors (basis) of economic activity. Therefore of fundamental significance is how particular factors react to imposed taxes and changes. Also the flexibility of various factors to tax changes is vital (marginal analysis).

The theoretical analysis of the effects of taxation differentiation may be conducted on various levels. Below you will find some

of these levels (Kesti, 2002-2015, T. Wołowiec, 2011):

- tax influence on labour costs. High taxes increase labour costs, as income after taxation (disposable income) is low, which is a natural basis for employees' pay demands from employers, which implicates the position of the enterprise on competitive market and company profitability. It is understood that differentiation of tax conditions between countries (regions) exerts considerable influence on conditions of conducting business activity;
- changes in direct taxes always bring about changes in marginal production costs;
- taxes always constitute a burden on a given entity, therefore there is a defense reaction of a taxpayer who tries to transfer this burden onto other subjects. Hundreds of years of observations of taxpayers' reactions allow us to state that it is easier in case of indirect taxes and more difficult with direct taxes. Income taxes are not transferrable and the taxpayer's reaction may only consist in limiting income activities. This is especially visible in progressive tax scales, whose use increases marginal taxation and decreases marginal income. The final decision of a taxpayer in this matter implicates the income usefulness curve;
- the issue of direct tax transferability looks different in case of taxing an employer than an employee. The employer will try to transfer the increase of tax rates into manufacturing costs and then into prices. His possibilities depend on the type of taxed goods and the state of the market (competition), which is manifested in price flexibility of demand. The chances of transferring increased tax burden grow with lower price flexibility of demand. The second possibility consists in transferring the tax effects on employees by reducing their salaries. This constitutes the so-called retro-

ISSN 2450-2146 / E-ISSN 2451-1064

© 2018 /Published by: Międzynarodowy Instytut Innowacji Nauka-Edukacja-Rozwój w Warszawie, Polska
 This is an open access article under the CC BY-NC license (<http://creativecommons.org/licenses/by-nc/4.0/>)

Wołowiec T. (2018) Directions, Sense And Purpose Of Personal Income Taxation Harmonization Process Across European Union Member States. *International Journal of New Economics and Social Sciences*, 1(7)2018: 77-99

DOI 10.5604/01.3001.0012.2549

transferability, which is usually ineffective, as employees oppose such practices. The degree of transferability of increasing taxes on employees depends on the state of the labor market, unemployment rate, labour market flexibility and openness;

- measuring the phenomenon of tax transferability is difficult even in case of a closed economy, as the effects of growing taxes may be distributed, for example, into prices, non-pay manufacturing costs, entrepreneur's profit margin. These difficulties are multiplied in an open economy, as the mechanism of tax transferability affects the society (economy) of another country. In its theoretical meaning, tax (fiscal) dumping means that redistribution of social income takes place between countries through taxes. This is especially visible when countries belong to a uniform economic association, which has a mutual fund – budget, which also serves as a source of income for member states' budgets. The use of tax dumping means that part of income is transferred in an open or hidden way (transfer prices) to countries with lower taxes. An effect of this is further increase of taxes in countries which do not use tax dumping, as the budget increases its revenue deficit, or limiting expenditure, or increasing public debt. It should come as no surprise then that after admission of 10 new countries to the EU, France and Germany threatened to stop their payments to EU budget due to considerably lower corporate income tax rates in such countries as: Slovakia, Poland, Czech Republic and the Baltic states, where entrepreneurs began to move their economic activity. We should add today that it happened with closed labor markets.

In times of internationalization of economic relations and economic integration, the mechanism of tax transferability is becoming international. This concerns both taxation of income from work as well as income on economic activity, interests, capital

gains, etc. Personal decisions concerning taking up work – assuming that there are formal restrictions in flow of labour between countries – are determined by salaries and taxes. Therefore we experience a natural phenomenon of work migrations to places where pay and tax conditions are more favourable. While in case of taxation on incomes from work, possible change of place (country) of work is easier, in case of entrepreneurs it is a more daunting venture, as it requires complying with the legislation of the country where the activity or its part (establishing dependent companies) is transferred. The mobility of labour and capital implicates the issues of tax harmonization. From the economic point of view harmonization of direct taxes and tax competition force us to consider further theoretical and legal aspects, such as (W. M. Gentry, G. Hubbard, 2002):

- effects of harmonization of direct taxes on state budget, imbalance in public finance,
- allowed scope of realizing tax economic rent by international corporations (N. Jensen, 2007, N. Geaten, 2007),
- mechanism of reallocation of public debt between countries due to the above-mentioned rent,
- limiting the possibility of lowering taxation of personal incomes and consumption taxes when harmonization of direct taxes leads to lower public revenues,
- effects of labour mobility on home economy due to differentiated tax conditions,
- changes in the structure of tax system in relation: indirect taxes – direct taxes, as to how these relations attract foreign investment,
- motivating national investors to invest,
- scope of using tax credit.

These issues look different in conditions of small, open economies of the countries which suffer from foreign capital deficit. The situation of developing countries undergoing the systemic transformation is

ISSN 2450-2146 / E-ISSN 2451-1064

© 2018 / Published by: Międzynarodowy Instytut Innowacji Nauka-Edukacja-Rozwój w Warszawie, Polska
 This is an open access article under the CC BY-NC license (<http://creativecommons.org/licenses/by-nc/4.0/>)

Wołowicz T. (2018) Directions, Sense And Purpose Of Personal Income Taxation Harmonization Process Across European Union Member States. *International Journal of New Economics and Social Sciences*, 1(7)2018: 77-99

DOI 10.5604/01.3001.0012.2549

different in countries with established strong position within a given economic system or global economy. Considerations take into account the element of tax equity, in its international aspect and find out the main reference points for transformation of an individual's taxation system

in European Union countries has been limited to personal income of individuals who do not conduct any form of business activity and it reflects the short and long-term run.

Purpose of the article. Methods.

The purpose of the article is to determine whether harmonization of personal income taxation in the European Union countries is possible and desirable. The assessment of the possibility and desirability of harmonizing this form of taxation has been limited to personal income of individuals who do not conduct any form of business activity and it reflects the short and long-term run. The purpose of this article is formulated in such a way that it requires a comparative analysis of the personal tax revenues of systems in the countries of the European Union, taking into account the specifics, commonalities and differences in tax structures in the countries studied, as well as the areas, possibilities and possible directions for harmonizing this form of taxation. Within the conducted analysis we attempted at verifying the following research hypothesis: *there are economic, political and social reasons for harmonization of income taxation of individuals who do not conduct any business activity in the European Union countries.* It has been assumed that the verification of the adopted research hypothesis which is not more than a speculation or a guess made provisionally determines the necessity of obtaining answers to the following research questions:

1. Does large differentiation of personal income taxation systems in the European Union countries constitute a threat to the common market?

2. Does harmonization of personal income taxation of individuals who do not conduct any business activity make sense?

3. What benefits will we obtain thanks to harmonization of the analyzed taxation form and what costs do we bear as a result of its lack?

4. What and how did various economic and social conditions determine the heterogeneity of personal income taxation in the European Union countries?

5. What sources of similarities can be found in personal income taxation in tax systems of the European Union countries, taking into account the so-called "quiet harmonization" and the role of the European Court of Justice?

The main method of the research was induction. It consists in developing general conclusions or determining some regularity on the basis of empirically stated phenomena or processes. It is the kind of reasoning on the basis of details on general properties of a phenomenon or an object. The application of this method requires an assumption that only facts may constitute the basis for scientific reasoning. These facts are situations (economic, social, legal, and organizational) that actually took place. Induction methods cover various legal acts, analyses, experts' opinions, statistical data and scientific documents used in social research. Moreover, the paper uses two general research methods, namely analytic and synthetic methods, characterized by detailed presentation of the reality research. The analysis treats reality as a set of

single, specific features and events. Following this research method, we break down the subject of our research (personal income taxation) into parts (elements of tax technique) and examining each separately or we detect the elements of this object (the possibility and desirability of personal income harmonization). A downside of the analytic method is excessive exposure of details (technical details), which sometimes may lead to losing sight of the whole subject of our investigation. This hinders full and objective acquaintance with reality, which admittedly is a set of independent elements but also a set of parts closely related into an organic whole. The synthetic method consists in juxtaposing and presenting the tools and forms of personal income taxation in the holistic, final model of effective and efficient instrument not only fiscal but also social policy. This method treats reality as a combination of features. It is based on joining various notions (models, forms, tools) into one, and particular elements into the whole. Therefore its implementation consists in looking for common features of various phenomena and events and then putting them together into a homogeneous whole. Thus the synthetic method surveys and determines the whole subject of research. Using the complex (hybrid) research approach, we also used the so-called triangulation of data sources, that is comparison of information on personal income taxation from various tax systems, and theoretical triangulation – consisting in analysing obtained data from the point of view of various theoretical concepts of tax policy, but also of social policy.

The analysis and evaluation of the possibilities of harmonizing personal income taxation in the European Union countries will be conducted taking into account four basic criteria. These are:

1) evaluation of economic and social importance (weight) of personal income tax, taking into account its influence

on consumption, mobility of workforce, labour supply and starting business activity.

2) evaluation of the influence of direct taxation on economic growth, labour market and economic (macro-economic) policy of the government.

3) scope of originality and individuality of personal income taxation solutions in the European Union countries.

4) evaluation of the influence of ‘quiet harmonization’ being the result of competition among national tax systems and decisions of the European Court of Justice on unifying construction solutions for personal income taxation.

The basic tools for conducting a wide-ranging analysis and evaluation of the possibility of harmonizing personal income taxation in the European Union countries will be the following research methods:

a) comparative analysis of the specificity of personal income taxation in the European Union countries, with particular emphasis paid to construction elements of this taxation form;

b) functional analysis, applied in order to determine the cause and effect relationships of the examined phenomena and processes influencing the construction of the system personal income tax burden and the possibilities of harmonizing this form of direct taxation;

c) research method in dynamic presentation, essential both for the holistic look at personal income taxation systems as well as for the evaluation of the speed of progressing ‘quiet harmonization’ and for presenting the appearing development tendencies of this tax in the context of evolution of tax systems in the European Union countries;

d) methods of statistical analysis of the examined problems and relationships.

Explanation of main material of research with complete substantiation of obtained scientific results. Discussion.

The theoretical laws, scientific conclusions, practical proposals and recommendations made by the author in this dissertation all aim at the conclusion that although harmonization of personal income taxation is possible from a legal point of view in the long run, from the economic and social perspective it is unjustified to harmonize this form of taxation. Thus, proving the thesis that we can find out the main reference points for transformation of an individual's taxation system in European Union countries and there is no goal and sense in harmonizing and standardizing PIT constructions. (Tax revenue in EU Member States: Trends, level and structure 1995-2003, Tax and Economy a Comparative Assessment of OECD Countries, OECD Revenue Statistics 1965-2013).

In their pure form, income taxes do not stimulate inclination for investment and savings. Income tax is a burden on the saved and spent part of income. In order to stimulate saving and/or investing, it is necessary to introduce some reliefs and exemptions to the tax construction, granted for creating (developing) investment. The author conducted his own research on the relationship between the level of fiscalism (relation of PIT tax revenues and social insurance contributions to average annual GDP growth rate, calculated with purchasing power parity per capita) and the structure of tax system, and economic growth speed for 27 EU countries in 1991-2017. The research shows that in the short period of time it is difficult to prove the relationship between reduction of tax rates and GDP growth rate. Negative correlation means that the higher the level of marginal tax rates, the lower the GDP growth. The obtained correlation coefficients are statistically insignificant, that is so small that

there are no grounds for rejecting the hypothesis of the existence of a relationship between the levels of marginal tax rates in the short period of time. These results do not allow us to confirm the theoretical postulates of the supply side school of economics. Its advocates claim that reduction of marginal tax rates in income tax leads to lowering labour costs, stimulating consumption and production, and in consequence to shifting the global supply curve so that the balance point between demand and supply indicates higher level of GDP and prices. This activity is supposed to lead to economic growth and lower inflation. An effect of these activities may be increased trade deficit caused by growing demand for consumption and investment goods and increased capital surplus due to increased inflow of foreign capital and decreased outflow of national capital abroad.

Apart from the influence of the level of fiscalism on economic growth, we also analysed and researched the structure of budget tax revenues (including quasi-taxes). It allowed us to answer how particular types of fiscal revenues affect the GDP growth dynamics. The analysis covered three tax groups. The first one comprises income taxes (PIT, CIT and taxes on capital gains), the second one – social insurance contributions and their derivatives, the third one – incomes from work (jointly PIT and social insurance contributions and their derivatives). Distinguishing the fourth group was justified by the fact that social performance can be financed with general taxes or with premiums outside the budget, as burden classified as social insurance.

ISSN 2450-2146 / E-ISSN 2451-1064

© 2018 /Published by: Międzynarodowy Instytut Innowacji Nauka-Edukacja-Rozwój w Warszawie, Polska
 This is an open access article under the CC BY-NC license (<http://creativecommons.org/licenses/by-nc/4.0/>)

Wolowicz T. (2018) Directions, Sense And Purpose Of Personal Income Taxation Harmonization Process Across European Union Member States. *International Journal of New Economics and Social Sciences*, 1(7)2018: 77-99

DOI 10.5604/01.3001.0012.2549

Analysing the influence of the share of income taxes in fiscal revenues on GDP growth rate we obtain the coefficient of Pearson's linear correlation $r_{xy} = 0.13$. The obtained value of the coefficient means that there is no statistically significant relationship between the share of income taxes in fiscal revenues and average annual GDP growth rate. Similar results were obtained when considering the discussed relations annually in certain years (with the exception of the Netherlands). Analysing the power and direction of the correlation between PIT and CIT separately and average annual economic growth rate, we also obtain statistically insignificant relationships. The obtained coefficients of correlation are respectively $r_{xy} = 0.039$ and $r_{xy} = 0.38$. Therefore the share of income taxes in the structure of budget fiscal revenues does not significantly affect the economic growth dynamics (either in the short or in the long term).

Determining the power and direction of the relationship between the share of social insurance contributions in total fiscal revenues and average annual GDP growth rate per capita we obtain the coefficient of correlation $r_{xy} = -0.42$. This result proves the existence of negative relationship between the analysed variables. The power of this relationship does not allow us to treat it as statistically significant, therefore the thesis of negative influence of high level of burden related to social insurance premiums on economic growth cannot be fully proved.

Combining in one group personal income tax and social insurance contributions, we obtain a category of incomes placing bur-

den on work. These performance are complementary and determine the so-called tax wedge, that is labour costs (difference between labour costs – pay cost for the employer, and net pay – pay income), extremely important for the willingness of employers to create new jobs. Moreover, these terms are often used interchangeably. Examining the span between the share of particular fiscal tributes in the EU countries with their highest and lowest level, we can notice that in the EU countries the span of the PIT share indicator in total fiscal revenues was around 37% in 2012, while in case of social insurance contributions – 35%. In case of total burden of income from work, the span amounted to 22%, therefore it is justified to examine the joint influence of tributes placing burden on labour costs on economic growth.

On the basis of the above data we obtained the coefficient of correlation $r_{xy} = -0.54$, which denotes the existence of statistically significant, negative relationship between the share of burden on income from work in fiscal revenues and the GDP growth rate. The coefficient of correlation calculated on this basis informs us that the average GDP growth rate in the analysed years is explained in 27% by the share of burden placed on income from work in total fiscal revenues. The obtained results allow us to state that an increase of average share of burden on salaries in total fiscal revenues by 1% accounts for a decline in GDP per capita of 0.10%. Thus we can state that high level of burden on income from work negatively affects economic growth. High labour costs weaken the competitiveness of national economy, increase the tendency to

escape into shadow economy and increase unemployment and, in consequence, hamper economic growth.

Examining the relationship (for years 1991-2017) between average annual level of unemployment (dependent variable) and average share of tributes placing burden on income from work, we will notice a strong relationship, assuming a three-year delayed reaction of the unemployment rate. With this assumption, the coefficient of correlation is $r_{xy} = 0.91$. An increase of average share of burden on pay (PIT and contributions) in total fiscal revenues of EU countries causes, assuming a three-year delay, an increase in unemployment rate of 1.44%. The research also shows that each increase of tax and quasi-tax burden may translate into decline in economic growth rate. The research demonstrates that the most negative influence on economic growth, especially on unemployment level, is exerted by fiscal burden which determines the so-called labour costs. It is interesting that, contrary to generally accepted beliefs, the study does not prove the existence of any correlation between the influence of the burden on the economy on income taxes and economic growth.

The obtained results of the research do not allow us without first conducting detailed microeconomic analyses (household prosperity level, structure of household expenses, price flexibility of demand, etc.) to propose a thesis that it is more beneficial for the social and economic prosperity to increase revenues from indirect taxation in the structure of budget tax revenues. Lowering the burden placed by income taxes re-

quires offsetting the lost revenues with increased indirect taxes in order to maintain neutrality of revenues.

In their pure form, income taxes do not influence the choice of socially beneficial structure of production and choice of production factors or on using technologies saving natural environment. Achieving these goals also requires application of the system of tax reliefs and exemptions.

Income taxes do not affect the socially beneficial structure of consumption. We can talk of appropriate structure of consumption only in case of personal income taxpayers. It does not seem possible to introduce reliefs and exemptions into the structure of this tax that would allow us to steer household expenses. Income taxes are of little use for such influence (these statements are vital both for understanding the specificity of income taxes and from the point of view of the analysis of the purpose and nature of preferences used in income taxes. Knowing the specific structure of these taxation forms, reliefs and exemptions – often given contradictory evaluations – may be justified by the implementation of socially or economically important goals).

Tax systems in the European Union countries are a product of long evolution and feature a lot of similarities. Similarities of Community states tax systems are the effect of the same factors affecting a particular tax policy and features of legal solutions in taxes. These factors include: degree of economic development, social and economic systems and doctrines of economic policy, similar social, demographic and economic problems, Integration of the European

economy, globalization of the world economy and principles of cooperation with international organizations. These factors are a result of similar economic and social structures, determined by similar cultural, historical, sociological and political factors. In practice, the shape of the tax system reflects the necessity to take into consideration interests of various social groups and a consequence of frequent changes in legal solutions, being an effect of political plays. As a result, the functioning tax systems are determined both by model and actual (mostly political) factors. The economic structure of the European Union countries is characterized by high level of exchange, combined with a certain tax system, whose features include: high level of tax burden, similar structure of tax systems (the core are personal and corporate income taxes and universal consumption and excise taxes), significant role of accounting and minor role of inheritance and donations tax and taxes on taxpayer's assets and real estate (Tax Guide to Europe, 2010, S. Cnossen, 2001).

The tax doctrine formulates guidelines on what rational and effective tax policy the

state should run. These postulates are determined in various ways, depending on adopted criteria concerning goals to be achieved thanks to tax policy. First we should ask about the functions of tax policy and then about norms and ways of their implementation. The primary goals of tax policy are presented as: efficiency in implementing the income function, efficiency in implementation of non-fiscal functions, equitable distribution of tax burden and low costs of tax collection. Tax policy often quotes the doctrine, but in reality it may differ from it considerably.

Personal income taxes, due to their significance in national fiscal policy should not be harmonized, due to their role in fiscal policy, as automatic stabilizers of business cycle. Using income taxes, we can affect taxpayers' behaviour in various ways, through tax reliefs and exemptions as well as shape and structure of tax scale. It is necessary to realize national tax policy, whose specificity and economic, historical and social idiosyncrasies require freedom in constructing PIT.

Conclusions.

The idea of a single economic and currency area is based on enabling the free flow of goods, capital and people (labour) while subject to a single currency regime. The idea deals effectively with currency risk, trade barriers, assures easy access to the labour market and provides opportunities for investing in all member states. Full economic integration requires consideration of taxes as an important factor in the furthering of integration processes, since EU

member states are tax nations, e.g. countries where budgetary incomes come primarily from taxation. EU member state tax systems are strongly diversified, due to individual developmental paths shaped by national history of various lengths, civilization development, culture, value systems, social and economic policy, which also define the state's current financial needs. Even in a single state, taxes cannot remain

ISSN 2450-2146 / E-ISSN 2451-1064

© 2018 / Published by: Międzynarodowy Instytut Innowacji Nauka-Edukacja-Rozwój w Warszawie, Polska
 This is an open access article under the CC BY-NC license (<http://creativecommons.org/licenses/by-nc/4.0/>)

Wołowicz T. (2018) Directions, Sense And Purpose Of Personal Income Taxation Harmonization Process Across European Union Member States. *International Journal of New Economics and Social Sciences*, 1(7)2018: 77-99

DOI 10.5604/01.3001.0012.2549

neutral towards economic and social processes. Therefore, the challenge faced by EU creators was not the outright neutralization of the impact that taxes had on the integration process, rather they worked towards limiting the negative consequences of overly diversified national tax systems. Gradual, long-term harmonisation emerged as a continent-wide process. During the development of the Treaty of Rome it was decided that, to assure a common market, it was enough to harmonise indirect taxes and remove trade barriers as they were the prime inhibitors to the flow of goods and services. The harmonisation of direct (income) taxes was not considered as they were seen as not significantly affecting the single internal market. Problems tied to direct taxation became visible as integration proceeded, the EU grew, its citizens began to migrate, multinational enterprises increased in size and scope and their financial flows (capital and profit transfers between headquarters and subsidiaries in different EU countries) became seriously affected. It should be noted two main questions about European integration: trade union entrepreneurs suggested that income taxes would be neutral to integration processes and natural convergence of the tax systems of nations belonging to the economic and monetary union would occur.

It is a fact that the high and increasing international mobility of capital is not only a European but also a global phenomenon, associated with the ongoing globalization process. Thus, the current tax competition issue in Europe is part of a wider question of economic policy in a constantly changing and integrating world economy. However, in view of EMU and EU enlargement, there is a question of how the present applied regulations in the field of EU taxation could be further developed so as to, on the one hand, face the increasing pressure of globalization and tax competition, and, on

the other hand, remove another obstacle to free cross-border activity in the SEM (completing thus the integration of the market) and foster economic integration in Europe. A satisfactory reply presupposes the examination of at least two issues, namely: whether globalization and European economic integration are in some sense complementary or rival to each other, and whether tax competition in Europe subserves the integration or disintegration among EU states (T. Wołowiec, 2011, T. Wołowiec, M. Duszyński, 2009).

Although it may seem that globalization – as a process of global economic integration – includes European integration, the latter is a process of regional economic integration with objectives such as the avoidance of the "adverse effects" of globalization and international competition for members via the enlarged and more favorable economic space (which is institutionally assured), and the continuous deepening of economic integration, co-operation and socio-economic cohesion among member countries. It is obvious that, on the one hand, economic integration in Europe exhibits a much higher degree of integration and moves towards a deeper and more complete form of economic integration than the globalization process induces, and on the other hand, that the objectives of those two integration processes are quite different for a number of issues.

Particularly, it means that tax competition is not a problem for the globalization process itself, where the integration among the world's economies is much weaker. By contrast, within the European Union fiscal externalities arising from intra-EU tax competition are more significant. Furthermore, tax competition among EU states is in contrast with the objectives of European economic integration as indicated by official EU documents and treaties. The tax competition

phenomenon and the recent trend of undercutting corporate tax rates in the EU have not been induced by the requirements of the European economic integration process. It is rather the result of the general trend of falling corporate taxation in the world economy.

From the preceding discussion it should become clear that the current EU tax system – for both indirect and direct taxation – constitutes a temporary solution and it is at transitional stage. In fact, the different tax systems in the SEM create a diverse and chaotic picture in the field of EU taxation, which cannot be in accordance with the current state of integration. On the other hand, the response to increasing economic integration and tax competition in Europe cannot be simply tax harmonization. As emphasized by the literature, in certain cases such a development would have negative welfare effects for some members and does not fully address the fiscal aspects of the integration process.

Personal income taxes are strongly differentiated in EU member states in terms of setting the size of tax brackets and taxable income level, where the differentiation focuses on different perceptions of what should constitute the basis of taxation, different tax scales, tax credits and allowable deductions. This process destroys the tax base. Most nations have a tax-free income that represents the expenditure for minimal biological survival. Tax credits and allowable deductions are not only differentiated country by country but also are subject to fluctuations due to a changing social and economic national environment, the preferences of ruling political parties, phase of the business cycle.

EU member states have to consider the taxpayer's ability to pay (occurring jointly, separately or as selected elements) when creating different components of Personal

Income Tax (PIT) policies, which may include (T. Wołowiec, A. Suseł, 2009):

- Setting a tax-free level of income that is offered to an unemployed spouse (e.g. in Slovakia), offered for each child being supported by the parents (e.g. Belgium, Czech Republic, Estonia, Holland, Germany, France, Greece, Slovenia, Lithuania).
- Joint taxation of married couples (e.g. in Ireland, where we can find separate tax scales for single taxpayers and married couples).
- Specific and unique taxation of family income (France operates family quotient taxation that considers the number of children in the family).
- Constructions that permit the deduction of certain costs incurred while bringing up children (e.g. France) or even when supporting the family (e.g. Germany).
- Size and breadth of tax brackets.
- Systems defining the permissible and deductible expenses.
- Systems of preferences depending on the family's situation.

When analysing tax credits and allowable deductions present in EU member states (as subject-specific credits, deductions from tax and tax base), four main categories can be identified (T. Wołowiec, A. Suseł, 2009):

1. Compensation-type preferences: equivalency and compensation pay-outs for used tools, clothing, travel costs, refunding travel-to-work expenditures, etc.
2. Social-type preferences: deductions for social support for foster families, support for foster families, war veterans, victims of crime, handicapped, elderly, etc.
3. Stimulation-type (economic) preferences: aimed at stimulating the taxpayer to engage in specific activities or modi-

fyng his behaviour. We can include deductions for housing (development and renovation), preferential treatment of savings, purchasing of stocks and bonds, educating children, professional development, health expenditures and retirement fund investments.

4. Differentiated incomes, for example gambling wins, research grants, rewards for scientific activity, scholarships, contributions towards professional associations, etc.

So we should expect rational individuals to pursue tax-benefit-seeking mobility of labour force. In reality the extensiveness of this mobility would be dependent not only on "tax wedge" levels (share that PIT and national insurance consume from gross income) but also on level of wages, gross income levels, the nature of the labour market, quality of public services and infrastructure. Such rent-seeking tax migration would lead to increasing the supply of qualified labour in the market of the accepting country (with a competitive tax system and good labour market) while worsening the labour market situation in the country from which a worker has departed. As a result, countries keen to gain valuable workers could consider setting competitive tax rates to lure in new employees who would migrate and stay, contributing to national economic growth and pay their taxes in the accepting state. In this context harmonisation would be seen as a process of equalisation of life and employment conditions that would reduce the need for "tax wedge" oriented analyses by workers.

Income taxes are characterised by a clear link between the taxpayer's situation (income, wealth) and the tax burden placed upon him. As such, income taxes can have a negative impact, be de-motivating, as the tax will inhibit income-generating and investment activity and that will negatively impact the speed of economic. This means

that not only the sheer size of the tax burden is important, but also we have to consider the entire structure of the tax system, each tax and the definition of tax scales/brackets. Inadequacies of tax theories combined with a polarisation of opinion maker positions concerning personal income taxes impact even the microeconomic approach, where it should be easy to establish a causal link between the tax burden, tax scale and the taxpayer's economic situation and resulting decisions. This is a result of multiple interacting factors affecting the taxpayer; therefore isolation of the tax factor is difficult, if we bypass highly abstract analyses. The situation will be more complex, if the subject of analysis becomes the impact of a given tax on a specific group of taxpayers or of a specific tax on the entire economy (e.g. automatic stabilizer theory). We have to add the fact that income taxes are only part of a wider burden, since they are combined with national security contributions (social insurance) and often it is those social security contributions that are modified to increase governmental revenues, while maintaining an illusion of tax rate stability.

A theoretical analysis of the effects of tax differentiation can occur on several axes, including:

- 1) Impact of PIT on costs of labour. High taxes increase labour costs since after-tax income (disposable) is low and thus causes pay-increase demands from the workers and this in turn complicates the company's competitive standing and affects its profitability (when compared to companies operating in other, more beneficial tax environments).

- 2) Taxes as a burden. They force a defensive response from the taxpayer in the form of seeking opportunities to transfer the burden onto other entities. Centuries-long observation of taxpayer reactions to tax burdens shows that, even if desirable, burden

shifting is much easier in the case of indirect taxes than direct ones (in this case the most common technique involves limiting economic activity).

3) Tax burden transferability is different for employees and employers. Increased labour costs will affect production costs and this affects final product/service prices. Opportunities open to the employer will depend on the type of the good/service under taxation and the state of the market (competition), which is defined through elasticity of demand. Inelasticity of demand for a good will assure easier transfer of tax burdens by the employer onto the client. A second possible reaction is to transfer the burden onto the employees by lowering their wages. Opportunities here will be defined by the current state of the labour market, its openness, the level of unemployment and elasticity of labour supply.

4) Measuring the transferability of the tax burden. The process is difficult even in the case of a closed economy because the effects of increasing taxes can be hidden in prices, non-wage production costs, producer profitability. These difficulties are multiplied in an open economy where the mechanism of transferring the tax burden affects the society and economy of a different nation. In a theoretical sense, “tax dumping” (The term “tax dumping” was popularised by Chancellor Gerhard Schroeder in 2004, when he challenged new EU member states and their tax reforms that were aimed, as Schroeder claimed, at affecting fair competition policies in the Union by offering good operating conditions for companies from the “old” Europe) leads to a redistribution of income between different societies as it assures that part of the income is transferred to nations with lower taxes through transfer pricing or through the transfer of company operations to locations with favourable tax

regimes. The impact on nations not operating “tax dumping” policies is a need to increase tax rates to maintain governmental revenues (for those taxpayers that remain) or reduce governmental expenditures (politically difficult) or increase national debt (finding lenders willing to fund continued expenditures) (On 26th May 2004, Ministers of Finance from Germany and France, worried that their countries would suffer the most from tax-benefit-seeking company migration, proposed the first unification of corporate (CIT) tax rates: minimal rates, formalising the methods of calculating incomes, profits, defining expenses).

In the era of internationalization of economic relations and integration, the tax burden transfer mechanism becomes international, in terms of taxation on incomes, labour, economic activity, interest, capital returns, etc. Personal decisions regarding where to undertake paid employment (with the assumption that there are no restrictions on the movement of labour) will be affected by offered wages and required taxes. Income migration therefore becomes natural as people gravitate towards locations where incomes and taxes are the most beneficial. Of course, changing the location of activity is much easier for an employee than for an employer and entrepreneur as the latter two have to adapt to the requirements of the host country to where their activity is being transferred (for entire company or its part, subsidiary). Both labour and capital would therefore benefit from tax harmonisation as it would simplify operations and create a more balanced environment that would reduce the need for mobility oriented purely on seeking tax benefits (J. Gałuszka, 2002). Economic aims of tax harmonisation may be unachievable due to legal reasons, since a tax is not only an economic category but also a legal one, and its legal side is affected by:

ISSN 2450-2146 / E-ISSN 2451-1064

© 2018 / Published by: Międzynarodowy Instytut Innowacji Nauka-Edukacja-Rozwój w Warszawie, Polska
 This is an open access article under the CC BY-NC license (<http://creativecommons.org/licenses/by-nc/4.0/>)

Wołowicz T. (2018) Directions, Sense And Purpose Of Personal Income Taxation Harmonization Process Across European Union Member States. *International Journal of New Economics and Social Sciences*, 1(7)2018: 77-99

DOI 10.5604/01.3001.0012.2549

1) Relationship between national and Community law, and when considering the supremacy of EU law over national rules, many issues emerge (e.g. conflicting regulations, different interpretations).

2) Problems of applying (and in what measures) unlimited tax duty (Unlimited tax duty applies to those residing in a country for more than 183 days of a tax year, while limited tax duty is applied to those who spend less than 183 days) in one country compared to applying unlimited tax duty in one country with a limited duty in the second country and, finally, how to apply unlimited tax duties in both countries (R. Gordon, M. Dietz, 2006).

3) How to formulate and agree upon treaties on avoiding double taxation (not only achieving consensus between nations but also following local political patterns, taxation trends).

4) Problems in whether to collect the tax in country of residence or non-residence and in what proportions.

Harmonization of income taxes is much more difficult than harmonization of indirect taxes from the practical, technical and legal perspective and is a result of:

- When creating the Treaty of Rome it was decided that direct taxes would not have a notable impact on the operations of the internal market, and that approach led to a lack of appropriate regulations, especially in the area of personal income taxes.
- Income taxes, as forms of direct taxation are an important tool for fiscal policy that affects social and economic activities and it is difficult for politicians to abandon this tool for managing national policies.
- Directives requiring the formulation of direct tax harmonisation must be agreed upon with a majority vote in the national Assemblies (Parliaments), which leads to a lack of consensus on desired aims, costs and benefits, procedures.

- Progress in direct tax harmonisation creates an aura of challenges to the tax independence of nations and leads to entrenchment of state and elite positions.

- EU member states have different rules for remunerating employees, setting incomes from retirement funds and affecting the structure of income-generating costs and expenditures that reduce the tax base.

Despite the lack of Directives to regulate the rules of taxing personal income, the rules are emerging spontaneously and tax burdens are slowly equalising. This process is the result of competition between EU member state tax systems—nations extensively are utilising the construction of the personal income tax to utilise the stimulating functions of the tax system, which in turn impacts the possibilities open to spontaneous PIT harmonisation. Due to the effects of “quiet” paralegal harmonisation, several common PIT characteristics can be found in the EU:

1. Placing subjectivity on the principle of residence. Rules on limited (<183 days), and unlimited (>183 days) tax duty.
2. The dominant concept is of a global tax. Joint taxation of all incomes obtained by the taxpayer from different sources (only the rules regarding capital interests are exempt from being combined with other incomes).
3. The tax is progressive and specific solutions concern different tax rates, types of scales, rules regarding progression and the size of the minimal and maximum rates.
4. Tax burdens are designed to follow inflation through a system of automatic or semi-automatic indexation or through the change of tax brackets.
5. Different regulations are applied to a family income, sale of real estate, assets and investment incomes.

6. In every construction there exists a sum free from taxation and, in varying degrees, considers the minimal level of (biological) existence and costs of obtaining an income.
7. Tax burdens are considerable of, in varying degrees, state of the family and capabilities to pay through a system of rebates and deductions.
8. Multiple rebates and deductions exist that are of a simulative and social character (investment, building and renovation, health, donations).

The analysis of Union laws indicates that personal income tax harmonisation is extremely difficult due to historical, political, social and technical factors. Decisions by the European Court of Justice (ECJ) concern mostly tax deductions by individuals who are not Union residents and the deductions of contributions made to retirement funds operating outside the EU. The ECJ decisions cannot affect the rules for harmonising personal income taxes because they concern the taxing of income from savings and the exchange of tax information, while the progressing “quiet” harmonisation is rather a result of international competitiveness and not of any formal ECJ rulings.

Alongside minimal law-making at the European level, minimal progress of harmonization is a result of (Wołowiec):

- Political factors: PIT payers are the largest group in any nation. Politicians are unwilling to abandon PIT techniques in pursuing regulatory and stimulatory tax functions that are of a political nature, e.g. any activity in this area will have an impact on the political balance of the nation. PIT setting is an important and valuable tool in maintaining relations with voters.
- PIT harmonization is not an important factor in the evolution of the Common Market. It is neutral to internal trade and does not affect intra-EU competition and

as such will not become a European priority for some time.

- PIT taxes mainly incomes from work and retirement and the level of taxation does not increase intra-EU migration (although in the long-run this may change).
- In EU member states, social support systems are funded from different sources: taxpayer contributions, direct funding from the state budget (social security contributions are then contained within standard taxes, e.g. Denmark) and as they form part of the total “tax wedge”, their harmonisation will be even more difficult (while exerting sizeable influence on the PIT system).
- EU member states possess different systems of labour remuneration and shaping of citizen income levels, different methodologies of designing tax progression. Therefore even creating a holistic and long-term understanding of existing complexities will be difficult.

Harmonisation in general is a difficult challenge, and any debate about harmonising PIT systems brings out major counterarguments:

- Further loss of sovereignty in national financial policies, which will inhibit the state’s ability to affect economic processes and (especially) social ones. Harmonisation of the rules for calculating the basis for taxation and the acceptance of unified rates would mean the transfer of tax-setting prerogatives to a trans-national institution: the EU. In such a situation, each nation must conduct its own analysis of costs and benefits (of transferring those competencies versus their retention).
- Different social models and retirement systems, when combined with varied degrees of PIT integration with retirement contributions, determine various financial

needs of the state, therefore harmonisation would have to reach far beyond “mere” PIT systems.

- Historical, cultural, social factors that have shaped national tax systems enforce claims that path-dependent process will be difficult to reverse.
- Competitive inequality between taxpayers who operate in one market and those that function in multiple EU member states. Depending on their primary country of residence it can be an advantage to pay taxes elsewhere (when the other nation's tax regime is friendlier, e.g. for Poles employed and taxed in the UK) or a disadvantage (when British taxpayers operating in Poland or Poles earning in the UK are subject to Polish taxation).

In the field of taxation and cross-border workers at the Community level, there are no rules concerning the definition of cross-border workers, the separation of tax rights between member states or the applicable tax rules. Neighbouring Member States with many persons crossing borders to work often agree special rules for cross-border workers in their bilateral double taxation conventions. Since these rules reflect the special situation between two Member States and are the result of negotiations between them, it follows that these rules vary from one double taxation convention to another. This applies both to the definition and the division of taxing rights between the Member States concerned. Normally any special rules for cross-border workers are limited to people who live and work close to the border and are employed. They may even be limited to persons employed in the private sector (as opposed to the public sector). Income earned by a cross-border worker may be taxed in one or both of the Member States concerned, depending on the tax arrangements. In the latter case, tax paid in the Member State where the work is carried out would normally be taken into

account when determining the tax liability in the Member State of residence, in order to avoid double taxation. There are no rules which guarantee the cross-border worker the right to the most favourable of the tax regimes of the Member States involved (see the Gilly case, para 46. C-336/96).

The EC Treaty freedoms and the non-discrimination principle mean that the cross-border worker may not be discriminated against in his State of residence, because he works in another Member State. To the extent that he/she is taxed in the State of residence on income from employment or self-employment exercised in another Member State, he/she should therefore normally have the same right to deduction for work-related costs or costs of a personal kind in the State of residence as if the work had been carried out there. This may be the case for instance as regards costs for travelling to and from work, social security contributions paid in the Member State of employment/self-employment, child-care fees, pension contributions etc.

In terms of employment status, a cross-border worker refers to a broad category of non-resident workers, which means that they have their tax residence in another place. According to Article 39 EC and Article 7 of Regulation 1612/68, non-resident workers shall enjoy the same tax advantages as national workers. This rule applies for tax advantages related to the personal and family situation as long as the situation of a non-resident worker is comparable with the situation of a resident worker. The Court of Justice has constantly held that residents and non-residents are not generally in the same situation. Thus, differences in taxation between residents and non-residents may not necessarily constitute discrimination. However, where a non-resident worker - including a cross-border worker - is virtually in the same situation as a resident worker (for instance because

he/she earns all or almost all of his/her income in that State), the non-resident worker may not be subject to less favourable tax rules in the State of employment than residents of that State. National rules denying

the deduction of costs and expenses from a taxable income are not allowed if the costs and expenses are directly linked to the economic activity which generated the taxable income (A.J. Auerbach, 2006).

References:

1. Acocella N. (2002). *Zasady polityki gospodarczej*, PWN, Warszawa 2002.
2. Aksman E.(2002). *Redystrybucyjny efekt podatku dochodowego w Polsce*, „*Ekonomista*”, No 4/2002.
3. Auerbach A.J. (2006). *The Future of Capital Income Taxation*, „*Fiscal Studies*”, vol. 24, no 4/2006.
4. Cnossen S. (2001). *Tax Policy in the European Union: A review of Issues and Options*, OCFEB Studies in Economic Policy, Erasmus University Rotterdam, 2001.
5. Convention on Consular Relations from 24th April 1963 (Journal of Laws from 1982, No 13, item 98 –attachment).
6. *European Tax Handbooks 1995 - 2017*. (ed.) J.KESTI, *International Bureau of Fiscal Documentation*, Amsterdam 1995 – 2013.
7. Gałuszka J. (2002), *Podatek od dochodów osobistych krajach Unii Europejskiej*. „*Przegląd Podatkowy*” No 2.
8. Gaudamet P.M. Molinier J. (2000). *Finanse publiczne*. Warszawa: PWE. .
9. Geaten N. (2007). *Computing effective corporate tax rates: comparisons and results*, MPRS, “*Munich Personal RePEc Archive Papers*” No 3808.
10. Gentry W.M. Hubbard G. (2002). *The Effects of Progressive Income Taxation on Job Turnover* National Bureau of Economic Research, Working paper 9226, September 2002.
11. Gordon R. Dietz M.(2006). *Dividends and Taxes*, NBER “*Working Paper*” No 12292.
12. *Inventory of Taxes in the Member States of the European Union*, Luxembourg 2002-2017.
13. James S. Nobes CH.: (1995). *The Economics of Taxation*. Prentice Hall.
14. Jensen N. (2007). *Fiscal Policy and the Firm: Do Low Corporate Tax Rates Attract Multinational Corporations?*, Department of Political Science, Washington University in St. Louis, St. Louis, 2007.
15. Joumard I. (2002). *Tax systems in European Union Countries*. OECD Economic Studies, No 34.
16. Kesti J.: (2002-2017). *European Tax Handbook (years) 2009-2012*. IBFD, Amsterdam.
17. Krajewska A. (2004). *Podatki, Unia Europejska, Polska, Kraje nadbałtyckie*. Warszawa, PWE.
18. Mc Connell C.R. (1996). *Economics*, McGraw-Hill Book Company, New York 1987.
19. Messere K.C. (1998). *Tax Policy in OECD countries. Choices and Conflicts*. IBFD Publications BV, Amsterdam 1998.

20. Messere K.C. (2001). *Tax Policy in Europe: A Comparative Survey*. „European Taxation” no 12.
21. OECD, *Tax and Economy a Comparative Assessment of OECD Countries*, „Tax Policy Studies”, no 6/2001.
22. *OECD Revenue Statistics 1965-2013*.
23. Szybowski D.(2018) *Public Debt and Budget Deficit in Economic and Legal Terms* (in) *International Journal of Legal Studies* 1 (3) Published: International Institute of Innovation «Science-Education-Development» in Warsaw
24. *Tax Guide to Europe*, 2010; OECD Tax Data Base 2011.
25. *Tax revenue in EU Member States: Trends, level and structure 1995-2003*, “Statistic in Focus – Economy and Finance”, No 3/2005.
26. Wołowiec T. (2008). *Koncepcje pojęcia dochodu i ich wpływ na cechy podatku dochodowego od osób fizycznych w krajach strefy euro. /in/ Polska w strefie euro – szanse i zagrożenia.* (ed.) by J. Ostaszewski, SGH, Warszawa.
27. Wołowiec T. (2008). *Sprawiedliwość opodatkowania a ekonomiczna efektywność – wybrane aspekty.* „Studia Prawno-Ekonomiczne”, Volume LXXVII.
28. Wołowiec T. (2008). *Podmiotowy i przedmiotowy zakres opodatkowania dochodów osób fizycznych w krajach UE.* „Przegląd Prawa Europejskiego Międzynarodowego”, No 1.
29. Wołowiec T. (2011). *Wybrane zagadnienia harmonizacji opodatkowania osób fizycznych*, *Finansowy Kwartalnik Internetowy „e-Finanse”*, vol 7, nr 2.
30. Wołowiec T., Duszyński M. (2009). *Selected issues in harmonisation and taxation of PIT in EU member states.* „Держава Та Региони”, nr 7