Flash Economics

N° 25
September 24th, 2024

What kind of tax reform in France?

The French tax system differs from that of other European countries in that:

- The standard rate of VAT is lower than in most other countries; the minimum rate of VAT is 15% in the EU and there is no upper limit;
- The burden of social security contributions (employee and employer) is very high;
- Income tax is low;
- Inheritance tax is higher than in other European countries;
- Wealth tax only affects real estate wealth; most other European countries have no wealth tax.

We could therefore consider:

- An increase in VAT and a reduction in employees' social security contributions; as VAT has a broader base (consumption and investment) than social security contributions (salaries), this would give employees more purchasing power;
- Increase VAT and reduce social security contributions for companies; we know that this substitution is equivalent to a devaluation since VAT does not apply to exports:
- Reduce income tax and increase inheritance tax, which would have a positive incentive effect on effort and initiative.

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Characteristics of the French tax system

The French tax system is characterised by :

- **A lower standard rate of VAT than in most European countries**. **Table 1** shows that the standard rate of VAT in France is 20%; it is only 19% in Germany, whereas in most European countries it is between 21% and 27% (21% in Spain, 22% in Italy, 25% in Sweden, etc.);

Table 1: Standard VAT rates applied in EU member countries (2024, countries ranked by increasing VAT rate)

Member State	Standard rate (as %)
Germany	19
Romania	19
Austria	20
Bulgaria	20
France	**20**
Slovakia	20
Belgium	21
Czechia	21
Spain	21
Lithuania	21
Latvia	21
Netherlands	21
Estonia	22
Italy	22
Slovenia	22
Ireland	23
Poland	23
Portugal	23
Greece	24
Finland	24
Denmark	25
Croatia	25
Sweden	25
Hungary	27

Source : European Commission

- **High social security contributions** and the cost of employer contributions. Employers' contributions account for 26.6% of total labour costs in France (**Table 2**), 24% in Italy, 23.3% in Spain, 23.9% in Sweden and 16.7% in Germany. The most extreme case is Denmark, where there are barely employer contributions. Total employer and employee contributions amount to 34.9% of total labour costs in France, compared with 28.3% in Italy, 28.2% in Spain, 29.2% in Sweden and 33.7% in Germany;

Table 2: Employee and employer social security contributions (2023, as % of labour costs, countries ranked by increasing social security contributions)

Country	Social security contributions		
	Employee	Employer	Total
Denmark	0.00	0.61	0.61
Netherlands	9.81	10.73	20.54
Lithuania	19.16	1.76	20.92
Finland	8.68	17.49	26.17
Estonia	1.20	25.26	26.46
Latvia	8.49	19.10	27.60
Hungary	16.37	11.50	27.88
Portugal	8.89	19.19	28.08
Spain	4.95	23.31	28.26
Italy	4.29	24.00	28.29
Sweden	5.32	23.91	29.23
Poland	15.32	14.06	29.38
Greece	11.34	18.23	29.57
Belgique	11.01	21.29	32.30
Slovenia	19.04	13.87	32.90
Slovak Republic	10.33	22.90	33.23
Czechia	8.22	25.26	33.48
Germany	17.05	16.66	33.71
France	**8.30**	**26.63**	**34.93**
Austria	14.08	21.67	35.75

Notes: Single individual without children at the income level of the average worker. Includes payroll taxes where applicable.

Source: OECD

- **A low level of income tax (Table 3)**, which is always calculated as a percentage of total labour costs, reaching 11.9% (of total labour costs) in France, 16.8% in Italy, 12.9% in Sweden, 14.1% in Germany and 12% in Spain;

Table 3: Income tax (2023, as % of labour costs, countries ranked by increasing income tax)

Country	Income tax
Poland	4.93
Czechia	6.74
Slovak Republic	8.40
Greece	8.91
Slovenia	10.42
Austria	11.72
France	**11.90**
Spain	11.97
Sweden	12.86
Estonia	12.90
Hungary	13.27
Latvia	13.46
Germany	14.14
Portugal	14.18
Netherlands	14.60
Italy	16.78
Finland	17.38
Lithuania	17.99
Belgium	20.43
Ireland	21.58
Denmark	35.77

Note: Single individual without children at the income level of the average worker.

Source: OECD

- **A higher inheritance tax burden than in other European countries**, representing 1.4% of all taxes, whereas in most European countries it is zero or negligible (**Table 4**). **However, in absolute terms, the weight of inheritance tax (0.6% of GDP) is low in France;**

Table 4: Inheritance tax rates and inheritance and gift tax revenues (2019, countries ranked by increasing inheritance and gift tax revenues)

Country	Lower inheritance tax rate (as %)	Upper inheritance tax rate (as %)	Inheritance, estate, and gift tax revenues (as % total tax revenues)
Austria	0	0	0.00
Czech Republic	0	0	0.00
Estonia	0	0	0.00
New Zealand	0	0	0.00
Portugal	0	0	0.00
Slovak Republic	0	0	0.00
Lithuania	0	10	0.01
Poland	0	20	0.04
Hungary	0	18	0.07
Slovenia	0	39	0.09
Italy	0	8	0.11
Greece	0	40	0.19
Netherlands	0	40	0.51
Germany	0	50	0.52
Denmark	0	36	0.57
Spain	8	82	0.58
Ireland	0	33	0.68
Finland	0	33	0.74
France	**0**	**60**	**1.38**
Belgium	0	80	1.46

Source: OECD

- **by taxing only property wealth (Table 5)**. Most European countries have abolished, or never had, wealth taxation. Wealth is taxed at a fairly high rate only in Spain.

Table 5: Wealth taxation (2024)

Country	Tax base	Taxe rate (in %)
Belgium	Securities for a value that exceeds EUR1 million.	0.15
Spain	Net wealth	0.2 à 3.75
France	Real estate assets for a value that exceeds EUR 0.8 million.	0.5 à 1.5
Italy	Financial assets held abroad Real estate properties held abroad	0.2 à 0.4 1.06

Source: EY

What kind of tax reform does this comparison between France and other European countries suggest?

1- An increase in VAT and a reduction in employees' social security contributions

The wage bill only represents 50% of GDP excluding exports. A 1-point reduction in employees' social security contributions is therefore balanced, in terms of tax revenue, by a 0.5-point increase in VAT. **Substituting VAT for employees' social security contributions therefore increases the purchasing power of employees, at the expense of the self-employed and companies.**

2- An increase in VAT and a reduction in social security contributions for companies

The key issue is the taxation of companies' selling prices. If companies pass on the whole of the reduction in the social security contributions they pay in their selling prices, **prices including VAT will not change** (the increase in VAT offsets the reduction in social security contributions) **and this measure is equivalent to a devaluation.** Indeed, since VAT does not apply to exported products and does apply to imported products, the relative price of exports compared with imports will fall. The risk, if this policy of replacing company social security contributions with VAT is pursued, is that companies will increase their mark-up in response to the reduction in social security contributions, which would lead to inflation and the disappearance of the favourable effect on foreign trade.

3- Reduce income tax and increase inheritance tax

This proposal may seem surprising, since we have seen that income tax in France is low and inheritance tax high compared with other European countries. But this change in taxation:

- **reduce inheritance rents**; in France today, 60% of wealth has been inherited, compared with 30% in 1970, which constitutes a rent and does not encourage effort;
- **increase the dynamism of the economy**, with more work leading to a greater rise in income net of tax.

There is an **anomaly in the taxation of inheritance in France**: the wealthiest 0.1% of heirs pay an average of just 10% of inheritance tax. **One could therefore consider capping the *Dutreil pact*** inheritance tax exemptions, which would also lead to the opening of the capital of family businesses (to private equity funds, for example), which would also be conducive to a dynamic economy.

4- Adopt international wealth tax rules.

The G20 proposed a global tax of 2% on the wealth of billionaires (in dollars). To avoid the risk of relocation, France would have (?) to adhere to this international proposal and not take national measures to tax wealth.

Summary: Two key measures for effective tax reform

These two key measures are:

- Lower social security contributions, for both employers and employees, offset by a rise in VAT (which increases net salaries and has the same effect as a currency devaluation);
- A reduction in income tax offset by an increase in inheritance tax (which reduces inheritance rents and helps to boost the economy).

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