

THE COMPARISON OF THE LEVY BURDEN ON LABOR AMONG THE SLOVAKIA AND GERMANY BUSINESS ENVIRONMENT

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Abstract

The article deals with the income taxes and levies on the social security, their theoretical definition and practical influence in the business environment. The Aim of this paper is to present the results of the levy burden analysis on labor for employees and employers in the Slovakia and Germany business environment in order to provide ideas for improving the business environment in Slovakia. In this article presented results of the levy burden on labor represent a partial outputs of the Slovakia and Germany business environment comparison.

Introduction

Constantly creating a favorable business environment is an important prerequisite for the existence of the markets (including the social-markets) economy and increasing its performance. Since 2006, the long-term trends of the Business environment index indicators by the Business Alliance of Slovakia show the worsening Slovakia business environment due to legislation regulating the taxes and levies area.⁵⁹ Therefore the article focuses on the issue of taxes on personal income tax and obligatory levies on social security⁶⁰, and their influence in the business environment in term of selected subjects - employers and employees.

Compared countries are Slovakia and Germany. Both countries have undertaken significant tax reforms (in Slovakia effected from January 1, 2004; in Germany effected from January 1, 2009) to approximate to the current trends of the direct tax burden reducing on labor and income from business activities within the EU Member States, to attract or to maintain the capital and to prevent tax evasion. Concurrently both countries deal with the issue of sustainability of the social security system and they have a relatively high levy burden on the labor within the EU Member States. We believe that despite the differences of compared countries in terms of the different historical development of the states, applicated traditions of the tax collection, state size, territorial division of

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⁵⁹ Business Alliance of Slovakia. 2011. *Business environment index*. [online]. [cit. 31.05.2011]. Available on internet: <http://www.alianciapas.sk/menu/pravidelne_indexipp.htm>.

⁶⁰ The concept of social security is not generally theory or formal-law clearly defined. Under the broader definition of M. Bělina it can be understood as a set of institutions, facilities and measures, that help prevent, mitigate and eliminate consequences of citizens' social events (unemployment, sickness, old age, etc.). Source: STANEK, V. 2008. *Social policy*. Bratislava : Sprint dva, 2008, p. 197 - 199. 375 p. ISBN 978-80-89393-02-2.

the state and economic policy with the different target range in its function, the results of this research may offer ideas for improving of Slovakia business environment.

1 The theoretical basis

The term **levies** is referred to different kinds of contributions, taxes and charges collected by a statutory community (i. e. State, regional authorities, the municipality, the ecclesiastic community in Germany, etc.). Differences in the sense of these economic categories are based mainly on the use of public services or facilities of the community: the tax is not return service for a specific community service; contribution is a levy for which the subject may request a specific community service; a fee is imposed in return for a specific community service.⁶¹ Other differences are resulting from the principle of expenditure coverage from the statutory community: taxes are collected in order to achieve objectives of the community serving for the public and in principle can not be fixed to certain public expenditure; for the contributions is applied the group principle (the principle of solidarity) and in the charging case the individual principle of cover expenditure from the statutory community. For purposes of this article includes the term *levy the personal income taxes and obligatory levies of employees and employers to social security, whose an integral part is the social insurance as well as the health insurance.*

In view of the objective of taxation, which is to ensure sufficient revenue from taxes, while ensuring balanced allocation of the subjects tax burden in the business environment, the tax theory give particular attention to two mutually contradictory requirements on the tax system⁶²: *the equity of taxation* and *the efficiency of taxation*. According to an equity taxation, each subject should contribute to the financing of public expenditure depending on how tax burden is able to bear. Nevertheless, subjects with the same payment capacity would have to pay the same amount of tax (the horizontal equity of taxation), while subjects with higher paying capacity should have to pay more tax (the vertical equity of taxation). Because taxes put a strain on private financial resources of subjects, which are compulsory to pay the levy to the state, thereby affecting their behavior in the business environment. Through the application of efficiency requirements of taxation in the tax system is monitored, so that costs of taxation (tax payments, direct and indirect administrative costs, etc.) were the lowest for tax administration and subjects, which are liable to pay taxes.

Like taxes, also levies on social security affect the behavior of subjects in the business environment. Although levies on social security reduce in many countries the tax basis to calculate

⁶¹ KAMINSKI, B. - STRUNK, G. 2007. *Besteuerung unternehmerischer Tätigkeit. Grundlagen - Auswirkungen - Beispiele*. 2. Auflage. Wiesbaden, Germany: Betriebswirtschaftlicher Verlag Dr. Th. Gabler I GWV Fachverlage GmbH, 2007. 256 P. ISBN: 978-3-8349-0093-7.

⁶² Many economists formulated requirements on the tax system in their work (A. Smith, A. Wagner, J. Stiglitz, R. Musgrave and P. Musgrave, A. Sandmo and others) and also international organizations (e. g. OECD) present their own requirements on the tax system. This issue is not subject of the article, therefore it is also no pay.

the income tax, also they are wholly or partly deductible tax expenses (costs), affect the disposable income of individuals (employees and entrepreneurs-natural persons) and employers costs of labor.

Table 1 shows some aspects of the influence of personal income taxes and levies on social security in the business environment

Table 1 Aspects of the influence of personal income taxes and levies on social security in the business environment

Economic category	Influence in the business environment
Personal income tax	Influence on: households disposable incomes, spending standards of consumers, standard of living of the population, welfare society, the health of individuals, culture, education, motivation and willingness of employees to work, a review of preferences, the size of effective market, incentive for the initiation and development of entrepreneurship, business risks, making jobs and employment, investments, savings, and more.
Levies on social security	Influence on: creating and maintaining jobs, migration between forms of employment or business, illegal work, employment, respectively unemployment (also in relation to extending the retirement age because of the financial unsustainability of the system), disposable incomes of population, the burden on business profits with labor costs and effectiveness of business, decision on the location of the company in relation to the level of labor costs, motivation and willingness of individuals to work, productivity and more.

Source: Own work.

2 Material and methodic

The basis solution of the issue of levy burden on labor were these assumptions:

1. *The levy burden on labor may be more favorable for the employee in the German business environment in comparison to Slovak business environment in term of achieved employees net incomes.*
2. *According to taller levy burden of employers in Slovakia compared with the German are the labor costs on employee (as measured by labor price) for an employer in the Slovakia business environment taller as in the German business environment.*

The research of the issue of levy burden on labor in the business environment of Slovakia and Germany was performed using a comparative analysis based on the 27 variant comparisons completely for three categories of employees: Employee I, Employee II and Employee III. When creating different categories of employees, the criterion of employment, marital status, number of children and age of employee were considered (please see Table 2).

Table 1 Characteristic of employees categories

Subject	Criterion			
	Employment	Marital status	Number of children	Age
Employee I.	full-time	single	Childless	> 23 years \wedge < 62 years
Employee II.	full-time	single	1 child	> 18 years \wedge < 62 years
Employee III.	full-time	married (wife hasn't own income)	Childless	> 23 years \wedge < 62 years

Source: Own work.

Other relevant input data considered at the analysis processing of levy burden on labor were: minimum wage in Slovakia (there is not a minimum wage in Germany), the amount of the average wage, the rate of obligatory levies to individual types of the social security insurance (including compulsory social and health insurance) in terms of employees and employers, the personal income tax rate, non-taxable items, the tax bonus in Slovakia, tax deductibles lump sums in Germany, tax allowances for children and for single parents alone educated a child in Germany, the amount of the maximum assessment base for determining of levies on social security.

The research of the issue of levy burden on labor (i. e. determining of the levy rates, the way of determining of the income tax assessment base, etc.) is based on the legislation status in force as per January 1, 2011 in both compared business environments - in Slovakia and in Germany.

Results of the comparative analysis of the levy burden on labor were assessed by comparison of nine indicators values:

- On the employees level: the levy on social security burden of employees gross income, the personal income tax burden of employees gross income, the total tax and levy on social security burden of employees gross income, the employees net annual income, the employees net income from gross income, the levy wedge of labor costs, net income from labor costs.
- On the employers level: the labor price (the labor costs), levy burden of an employer.

Within the results evaluation, the tools of descriptive statistics, graphs and tables, has been used.

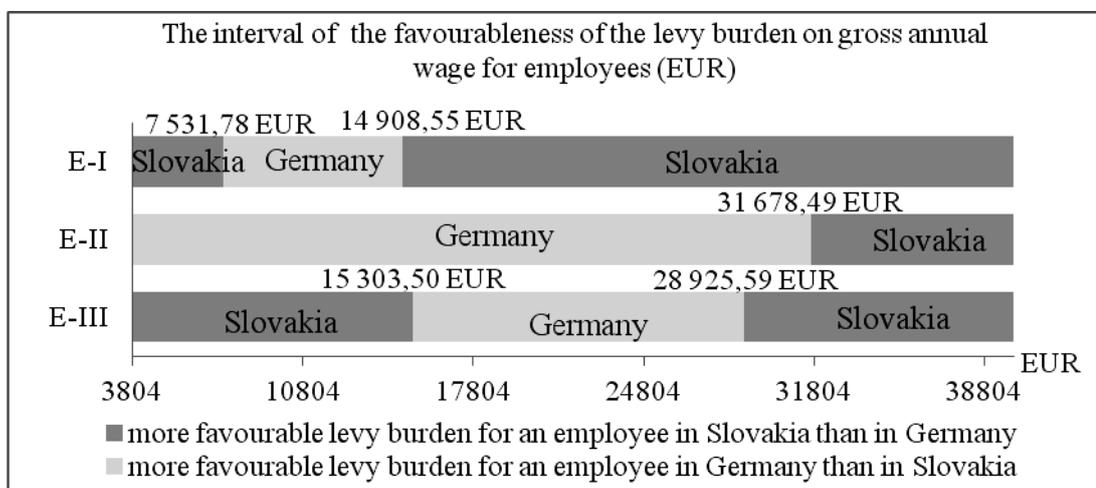
The analysis of levy burden on labor was processed in own spreadsheet program created in the English version of the Excel 2007 by using of selected mathematical, logical, statistical, lookup and reference, information and text functions of the program. When modeling variants, the numerical analysis of the target search values "Goal Seek" has been used, which is automatically built in the program.

3 Results

Below are presented results, which are achieved by the research.

3.1 Results of the levy burden on labor analysis for an employee

Analysis results of the levy burden on labor for an employee indicated, that the employee may in all three categories in view (ZI, Z-II, Z-III) to achieve higher net income in Germany than in Slovakia in establishing the same level of gross wages in both business environments. This *confirmed the first assumption of the research*. Achieved results shows the following chart 1.



Graf 1 The favourableness of the levy burden on labor for employees in the Slovakia and Germany business environment. Source: Own work.

Attained results are affected by several factors: the point is notably, that there is used the proportional taxation of an employee income in Slovakia, which is until the achievement of a certain amount of gross wages for the employee less favorable than moving the progressive employee income taxation in Germany. An employee in Germany may in consequence of the influence of sliding-progressive personal income tax rates, starting at 14 % opposite to 19 % proportional income tax rate in Slovakia and by the impact of the application of tax deductible lump sums, non-taxable items and tax allowances, to achieve at a defined niveau of gross wages, higher net income as an employee in Slovakia. This trend is promoted despite the fact, that the levy burden on social security of employees gross income in Germany is significantly higher (20.625 % for an employee with a child, 20.875 % for a childless employee) toward Slovakia (13.4 %).

May be to notice on the chart, that the employee II, who is single and alone educates a child, the levy burden on labor is favorable in the business environment in Germany than in Slovakia from

under the minimum amount of gross annual wage valid in Slovakia, than there is not set a minimum wage in Germany. This is because of applicable allowances for a child, which are in Germany over nine times higher than the tax bonus in Slovakia, for comparison with the average wage in Germany (2 361.08 EUR), this is almost three times higher opposite to Slovakia (797.45 EUR). This suggests a greater social role of the state in Germany than in Slovakia in the family support area.

3.2 Results of the levy burden on labor analysis for an employer

Achieved results of the levy burden of an employer in the Slovakia and Germany business environment are volatile, because they are strongly influenced by the needs of Germany to balance economic differences between the West German and the East German economy through the application of different legislative measures. The nominal amount of levy rates for employers in Slovakia (35.2%) is significantly higher than in Germany (about 20.695%). However, taking the maximum assessment base for the calculation of obligatory levies on the social security of the employer's (e. g. the assessment basis for the calculating of pension levies in Slovakia does 35 736.00 EUR counter to 66 000.00 EUR in the old federal countries of Germany (former German federal republic, GFR), respectively 57 600,00 EUR in the new federal countries of Germany (former German democratic republic, GDR), it leads to this, that the levy burden may be under certain conditions more favorable for the employer in Slovakia than in Germany. This *partly confirmed the second assumption of the research*. The chart 2 shows more closely the present trend.

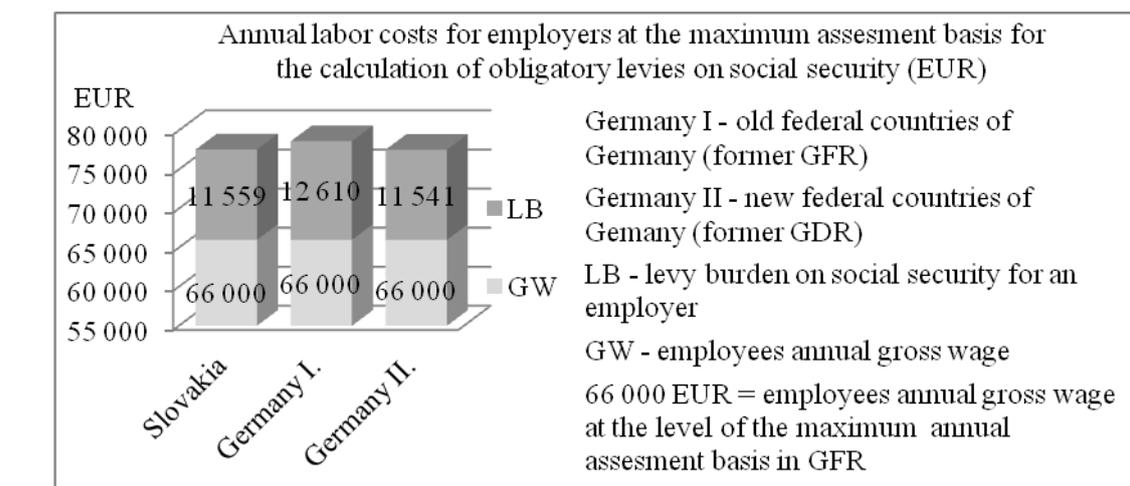


Chart 2 Annual labor costs for employers in the Slovakia and Germany business environment at the maximum assessment basis for the calculation of levies on social security.

The levy burden on labor is for the employer in Slovakia lower than in Germany in the case, in which the following assumption are together accomplished:

- the employer operates in the old federal countries of Germany (former GFR),
- the employer does not employ more than 30 employees (i. e. this employer has an obligation to pay insurance payments for the case of sickness absence of employees),
- employees gross annual wage exceeds the amount of 57 741.75 EUR (please see the Chart 3).

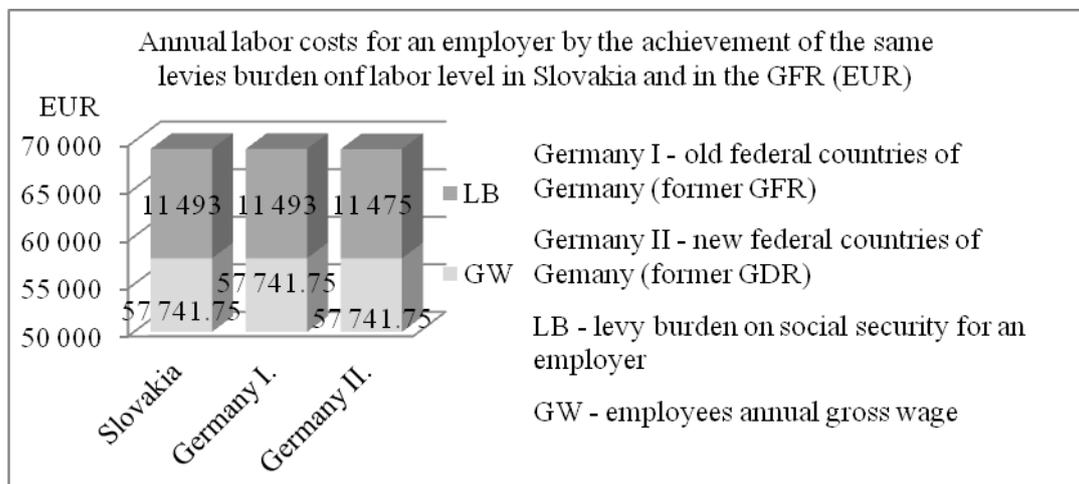


Chart 3 Annual labor costs for an employer in Slovakia and Germany by the achievement of the same levy burden on labor level in Slovakia and in the GFR. Source: Own work.

If the employer acts in an old federal country of Germany and employs more than 30 employees, labor cost is for this employer in Germany lower than in Slovakia under defined conditions of the business environment. It is also appropriate here to emphasize, that the levy burden on labor is under the conditions of the business environment stated above always taller in Slovakia as in the new federal countries of Germany (i. e. countries of former GDR) (Figure 3).

4 Discussion

Achieved results of the analysis can be developed to topics solved the issue of the levy burden on labor and the improving the business environment in Slovakia:

- In relation to the price of labor is possible to refer on positive motivation of employees or negative incentives of employers. Overall levy burden on social security of employees and employers is in the Germany business environment (42.42 %, respectively 42.67 %) lower than in the Slovakia business environment (48.60%). Hereby more balanced distribution of mandatory levy on social security between an employee and an employer in Germany (20.625%, respectively 20.875% for an employee, about 21.795% for an employer) compared with Slovakia (13.4% for an employee, 35.2% for an employer) reduces labor costs for employers in Germany (i. e. gross wage + employer's mandatory levy on social security calculated from the employee's gross salary). An

Employer in Germany can at the same labor price (labor costs) positively motivate employees by higher gross wage as an employer in Slovakia. Through the legislation conditional higher labor costs, due to the high levy burden, should in turn encourage employers to seek ways to reduce labor costs of employees. The effort to reduce the levy burden on social security of labor can lead to so-called wage spiral (depress the level of gross wages down) or forced migration of employees to the other forms of employment (creation of compelled agreements for work) or business (creating a compelled trade), and thus to the business environment distortion. By the reducing of the levy burden of subjects in the business environment would reduce dependence on state entities, which could contribute to the promotion of business development, to maintain employment forms in Slovakia and to mitigate the distortions of the business environment.

- The application of the proportional personal income tax rates (in Slovakia and in Germany) and of the sliding-progressive personal income tax rates (in Germany) in the business environment is in terms of the principle of taxation horizontal equitable (both tax rates separately present the levy of the same size by the same amount of tax paying capacity of subjects) and vertically equitable (both tax rates separately lead to the levy of higher absolute amount of income tax for subjects with a higher paying capacity). Using of the sliding-progressive income tax rate may allow a lower gross wages employee to achieve higher net income than by the application of a proportional income tax rate. The application of the proportional income tax rate leads to increasing of social inequalities in the economy and in the business environment, because there is a difference whether or not is using the same proportional tax rate at a minimum, average or above average wage in the economy (an aspect of the tax capacity is concerned). Another aspect of the taxation is the effect on employee motivation and willingness to work and support for legal work in the business environment. Compromise in this respect may be a combination of the two rates that is used by the income taxation of subjects in Germany. The progressive tax rate is applicable on lower incomes by individual tax brackets; higher incomes are taxed at a proportional tax rate which should be avoided disincentives of subject in the business environment to achieve high earnings. The disadvantage of a progressive income tax rate may be faster growth in income tax than the income itself (so-called cold progression), when the tax calculating does not reflect the inflation increase. This deficiency can be remedied by adjusting of the income tax calculation.

- The comparison of the tax burden of subjects in the business environment in Slovakia and Germany showed on the different states approaches to the labor taxation of employee. The approach to the employees taxation in the business environment in Germany observed in our opinion more on maintenance of the living level and standard of employees and also the equality of employees as compared with some forms of business (trades) than in Slovakia. This is reflected not only through the possibility of the tax deductible lump sums applying or actual expenses for securing and

maintaining of incomes, but also through many other tax deductible costs incurred by employees in Germany to maintain the living niveau and to improve living standards of employees and their families. It is concerned for example about the application of the tuition and training cost, relocation, reconstruction of the apartment, travel, tax advisors and others in relation to the individual personal life situation of the individual. In terms of taxation, there is maintained a parallel between the way an employee taxation and the taxation of business entity, which applies to tax charges in connection with the business. Such an approach, in our opinion, reduces the incentives for migration from employment forms to artificial business forms, e. g. to a forced trading business and at the same time leads to a reduction of social inequalities in the economy. The idea for the improvement of the business environment in the Slovakia economy could be an unification, respectively the approximation of the approaches of employees taxation towards businesses - trade business taxation, e. g. by establishment of options also for employees to apply costs spend on the income maintaining and income security or to apply of other costs related to maintaining of living niveau and of standard of employees.

- Results of the levy burden on employees labor comparison in the business environment showed on a stronger social role of the state in Germany in promoting family as the fundamental unit of society compared with Slovakia (significantly higher proportion of child allowances in relation to average wages in Germany than in Slovakia). There is an subsidiary approach of Germany to social policy, therefore the state recognizes the positive importance of a market and businesses and promotes independence and responsibility of human for his decision. The state performs in the social economy a residual role, whereby the dependance formation of entities from the state is limited. So that the family in society could have freely carry out their mission in the education of children, elderly care etc., it is important to have legislative and economic instruments to promote the natural functions of the family and society and thus create a reliable basis for the economic development.

Conclusion

Taxes and levy on social security are important components of the business environment that significantly affect the behavior of subjects in the business environment and thus creating a favorable business environment and reducing it's distortions. To what extent and how the levy to the state loaded the subjects in the business environment, depends on the philosophical views and approaches of the state to the society. Research of levy burden on labor issues in the business environment in Slovakia and in Germany has shown that there is a space in this direction for improving the business environment in Slovakia. The role of the state should focus on the creating

of the framework conditions for businesses, which encourage subjects to free creative activity and to the development of business activities, lead to reduction of subjects dependence from the state, to jobs creation and to promote employment of labor in the economy.

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