The labour income taxation: Lithuanian case

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Abstract: The article discusses planned labour income taxation decisions and labour income taxation by taxes and contributions: personal income tax, social security and health insurance contributions. The improvement of labour income taxation is one of the priorities of the Government of Lithuania. The analysis reveals that so far there are no constructive planned solutions how to improve the government’s priorities related to the labour income taxation. There are only ongoing discussions on various aspects of labour income taxation. In order to reveal the influence of the basic tax elements on the evaluation of the level of the labour income taxation, a comparative evaluation has been carried out. During the research, Latvia and Estonia, the countries that are closely related to Lithuania, have been compared. The results of the research have shown that the comparison of the basic tax indicators, such as non-taxable minimum income and standard rates, only partially describes the national level of the labour income taxation. A more accurate description of the tax level could be provided only having applied and having evaluated such factors as tax base and tax exemptions.

Keywords: planned decision; labour income; tax; contribution; taxation; evaluation; Lithuania.


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1 Introduction

Income reveals the consumption and saving potential of a person as well as the socioeconomic development of a state. Taxation of income is related to the welfare of inhabitants – the higher the taxes, the smaller is the amount of income at their disposal. It is also related to the welfare of the state – direct taxes are one of its main resources of revenue. Income taxation is one of the most complicated elements of the state tax policy – it is the goal of the state to ensure sufficient revenue into the state budget as well as create a favourable labour taxation environment (high tax on labour income stimulates migration of labour force and, when generous social policy comes along, it encourages living on benefits). The fact that this area has become especially sensitive can be proven by the recent changes in income taxation introduced in most countries over the last years: a gradual reform of personal income tax has been implemented in Denmark since 2009, Latvia has been decreasing its personal income tax rate since 2011, since 2009 Poland has imposed two income tax rates (18 and 32%) instead of the former 3 ones (19, 30 and 40%), as of 2014 Lithuania will start increasing the non-taxable amount of income, France has increased the top income tax rate for high-income earners since 2013, in 2011 Hungary changed the progressive personal income tax rate into a 16% proportional rate. During the last ten years fundamental changes took place in the Lithuanian tax system (in improving tax administration, the legal framework and the taxation mechanism). It should be noted that the improvement of labour income taxation is one of the priorities in the Government of the Republic of Lithuania. It is often stated, however, that very high taxes are withheld from labour income in Lithuania. Is it really true? The aim of the research is to reveal the Lithuanian labour income taxation and after that perform a comparative analysis of income taxation in the Baltic countries (i.e., including Latvia and Estonia). In order to achieve the aim the following tasks were formulated:

1 to review the planned labour income taxation decisions as an efficient tool to tax labour income rationally
2 to clarify the labour income conception as the object of the research and the regulation of labour income taxation as the main source of information
3 to analyse labour income taxation with personal income tax as part of labour income taxation
4 to analyse labour income taxation with contributions as part of labour income taxation
5 to analyse labour income taxation with personal income tax and contributions to testify tax burdens and show the taxation differences between the Baltic countries.

A comparative and logical analysis of statistical data and literature was performed and synthesis methods were applied in conducting this research.

The issue of taxes is widely researched both in special as well as scientific literature and quite a lot of attention is paid to different taxation aspects. Taxation principles, functions of tax system, its conception were studied by Cheung (2001), Tušaitė (2003), Šinkūnienė (2005) and Ivaškaitė-Tamošiūnė (2013), an evaluation of its components was performed by Klun (2003), Lukyanenko (2003), Budrytė and Mačiulaitytė (2004), Lambert (2004), Medelienė (2005), Mažeika (2008) and Skačkauskienė (2011). The article does not aim to develop the subject of improving labour income taxation. It raises
the question of practical assessment of labour income taxation – whether a comparison of the core elements in labour income taxation allows having an objective evaluation of the extent of income taxation in a country. Such a research, having made comparisons of the main tax elements in the Baltic states, and having compared them to the relative indicators, would allow us to make conclusions about the validity of the evaluation. Therefore, the research is based on the method of systemic analysis, which let us carry out comparative analysis and synthesis of the received analytical results.

2 Planned labour income taxation decisions

The state educates its society in different ways, provides external, internal and social protection, and develops mechanisms that ensure justice. The action mode chosen by the state, which forms background to realise society’s interest and surpass expectations (public policy), is complex and multi-stage: the management decisions realised by the state include many areas of life and reflect many interests and expectations of the society that occur in different forms (Melnikas et al., 2008).

Today we will probably not find a single state management theorist or practitioner, who has doubts about the obvious importance of planned decisions (Bivainis et al., 2011; Tunčikienė and Skačkauskienė, 2012), in order to essentially carry out the basic functions of the state. Therefore, not incidentally a common research and practical discussion object in the state’s public sector is the improvement of the quality of planned decisions, their preparation, adoption and implementation. Normally, it is sought to get valid answers to questions how to effectively allocate, use and develop sets of various resources (human, financial, informational, etc.) of the public sector, all of them together and individually (Chlivilkas and Raudeliūnienė, 2007, 2008; Butkevičius and Bivainis, 2009; Bivainis and Tunčikienė, 2009; Skačkauskienė, 2013).

Financial resources are necessary to implement the obligations of the society. The questions of allocation, use and development of state’s financial resources are solved by applying budget planning means (Butkevičius and Bivainis, 2009). It is typical to treat budget income and expenses as the main planning objects. The implementation of planned decisions that are based on these objects at strategic, tactical and operational levels allows the state to smoothly carry out activities which the business sector due to some reasons is not able or is not willing to provide and at the same time to meet the diverse expressed and potential needs of the society.

The state accumulates a part of the needed revenue by collecting taxes. One of the main taxation objects is the income of population. Many factors can determine the collection of revenue from taxes to the state’s budget: the tax rate, the tax base, non-taxable income and other benefits. Average wages, the number of working people, unemployment rate, minimum monthly wage, etc. have an influence on the collection of personal income tax (Tamašauskienė and Žadvidaitė, 2011). Taking into account the entirety and the actual dynamics of the mentioned factors, of particular relevance are permanently arranged and taken planned decisions, such as how to tax labour income more rationally and efficiently, mitigating the tax environment [the conditions of state’s taxing environment are described by the parts of the competitiveness index, which are related to the taxation coverage and financial services. According to the taxation coverage and efficiency ratio, we are in the 22nd place in the European Union (for
example, Estonia is in the second place) (Lithuanian Progress Strategy ‘LITHUANIA 2030’).

The improvement of labour income taxation is one of the priorities of the Government of the Republic of Lithuania (government) (SRL, 2012b). The government’s programme (SRL, 2012b) reveals the essence of tax system reform, more even distribution of the burden of taxation between labour and capital, higher progressiveness of income and estate taxation, the application of socially relevant and targeted tax concessions. To present reasonable development means of income taxation is a complicated task for the Ministry of Finance. However, the strategic plan prepared by the Ministry of Finance of the Republic of Lithuania lacks the improvement accent of the labour income taxation, starting with the strategic objectives of the Ministry of Finance and ending with programs means (MFRL, 2012). Yet there are no constructive planned solutions how to improve the government’s priorities related to the labour income taxation, there are ongoing discussions on various aspects of labour income taxation (SPMRL, 2013).

3 The regulation of labour income taxation

Income in this work – the object of taxes and contributions – is analysed further on the level of inhabitants (the main difference between the revenue of the state and the income of its inhabitant being the fact that certain income earned by an inhabitant due to income tax and social security contributions, actually, is not received by the inhabitant). In economics the income of a person during a certain period of time – is an amount of money that he or she could spend without decreasing the value of his or her capital (Black et al., 2013). These are earnings or income received that can be spent on consumption or savings. In order to get the income to satisfy their needs, people use such resources as human ones, as well as physical property and financial assets. These resources provide income that can be classified into four categories according to the source of income:

1 employment income – labour remuneration according to the level of qualification of the employee, complexity of work, responsibilities, conditions, etc.
2 self-employment income – revenues derived from self-employment work in agriculture, business, crafts, and free professional activities
3 income from financial assets – interests, rental income, dividends
4 income in the form of social benefits – pensions, allowances etc. (Blažienė, 2002).

The methodology of Statistics Lithuania (SLG, 2010) defines the combined household income as all the income of the household received from employment or self-employment, property income or land rental, social benefits, regular cash transfers from other households, dividends and other income. It is obvious that, according to this methodology, an inhabitant’s income is the sum of different kinds of income – salary, income from personal business, rent as well as transferrable state allowances (EC, 2013a). The Law on Personal Income Tax of the Republic of Lithuania (SRL, 2002) defines income as positive income, remuneration for the works or services performed, assets or funds sold or otherwise transferred or invested and any other benefit in cash
The labour income taxation

and/or in kind. This law definition corresponds to the forms of income 1–3 as mentioned above.

Meanwhile, the labour income is defined as a traditional way of earning money, i.e., selling man-hours for a certain fee (Ramsden, 2007). The Law on Personal Income Tax defines employment related income or corresponding income as follows: income received for the work performed under the contract of employment or corresponding contracts as well as income received by the owner of a sole proprietorship from a sole proprietorship, a general partner of a general partnership or a member of small partnership from a corresponding partnership. In this work labour income is treated as remuneration for work performed – income that an employee receives for his or her work. Employment income is the main source of personal income. In 2012 in Lithuania, for example, remuneration for work accounted for about 70% of all personal income (SLG, 2013). It is also the main source of revenue of the state from direct taxes. In 2012, for example, personal income tax revenue labour income accounted for 81.1% of all the revenues from this tax.

There are four types of taxes and contributions imposed on labour income in Lithuania: personal income tax, state social insurance, compulsory health insurance and guarantee fund contributions. These taxes and contributions are regulated by relevant legislation presented in chronological order in Table 1.

Table 1 Legislation regulating income taxation in Lithuania

<table>
<thead>
<tr>
<th>Year</th>
<th>Legal act</th>
<th>Short content (main provisions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1990</td>
<td>Provisional Law on Income Tax of Natural Persons of the Republic of Lithuania (Official Journal ‘Valstybės žinios’, 1990, No. 31-742)</td>
<td>Tax payers – persons receiving income, the object – income of natural persons. There were eight different rates set. A progressive rate was imposed on income received from the second job. Invalid as of 1 January 2003.</td>
</tr>
<tr>
<td>1996</td>
<td>Law on Health Insurance of the Republic of Lithuania (Official Journal ‘Valstybės žinios’, 1996, No. 55-128)</td>
<td>Defines the persons whose health insurance is compulsory, the basics of drawing the budget and compensating the expenses, institutions responsible for arranging the insurance, the rights of the insurance subjects, their duties and responsibilities. The new edition of the law entered into force on 1 January 2003.</td>
</tr>
<tr>
<td>2000</td>
<td>Law on Social Insurance of Occupational Accidents and Occupational Diseases of the Republic of Lithuania (Official Journal ‘Valstybės žinios’, 1999, No. 110-3207 )</td>
<td>Persons are compulsorily insured by the employer who pays social insurance contributions from the gross earnings of the employee for the work performed, the rates of the contributions depend on the level of the risk of the company’s economic activity.</td>
</tr>
</tbody>
</table>

Source: Own elaboration based on the legal acts included in the table
Table 1  Legislation regulating income taxation in Lithuania (continued)

<table>
<thead>
<tr>
<th>Year</th>
<th>Legal act</th>
<th>Short content (main provisions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2000</td>
<td>Law on Guarantee Fund (Official Journal ‘Valstybės žinios’, 2000, No. 82-2478)</td>
<td>The payers – legal persons, the rate – 0.2% of the gross earnings of the employees from which state social insurance contributions are calculated.</td>
</tr>
<tr>
<td>2003</td>
<td>Law on Personal Income Tax of the Republic of Lithuania (Official Journal ‘Valstybės žinios’, 2002, No. 73-3085)</td>
<td>Defined the order of taxation on personal income, its principles, the rights and duties of the payers. The object – personal income. The object of the tax differs depending on the permanent and non-permanent residence in Lithuania. Two rates were set – 15% and 33%. According to the payment order, the income is divided into two categories – A and B. In 2005, when an amended law came into effect, the main tax rate was reduced as follows: starting from the second half of 2006 – to 27%, starting from 1 January 2008 – down to 24%. The rate as of 2009 – 15%.</td>
</tr>
<tr>
<td>2009</td>
<td>Law on Replacing Clauses 2, 6, 8, 15, 16, 17, 18, 19 and supplementing the Health Insurance Law of the Republic of Lithuania (Official Journal ‘Valstybės žinios’, 2008, No. 149-6022)</td>
<td>Contributions for compulsory health insurance were separated from the personal income tax, the 3, 6 and 9% contributions rates were set; compulsory insurance on health insurance was introduced.</td>
</tr>
</tbody>
</table>

Source: Own elaboration based on the legal acts included in the table

4  Income taxation with personal income tax

In order to analyse labour income taxation in Lithuania and compare it to labour income taxation in Latvia and Estonia we should, first of all, discuss the established minimum monthly wage that ensures minimal income of working people. Lithuania, Latvia and Estonia have established a minimum monthly (hourly) wage that the employer has to pay to the employee regardless of his or her position.

During the analysed period the rate of minimum monthly wage both in Latvia and Estonia differs from that of the established rate in Lithuania. According to Eurostat (EC, 2013b) data, Lithuania had the lowest minimum wage from 2009 to 2012 (on 1 August 2012 the minimum monthly wage in Lithuania was increased to 850 Lt but, nevertheless, it remained the lowest one in comparison with other Baltic states), and in 2013 it was the lowest in Latvia (see Table 2).

The minimum monthly wage in Lithuania in 2013, as compared to 2009, increased by 25%, in Latvia – 13%. The minimum remuneration in Estonia did not change over the period of 2009–2011 and in 2012 it increased by 41 Lt, in 2013 by another 104 Lt and, if we compare the year 2009 and 2013, the minimum monthly wage here increased by 15%. To sum up the rates of minimum wages in the three Baltic states, an observation can be made that the minimum monthly wages in Lithuania, Latvia and Estonia kept increasing. The minimum monthly wage in the period of 2009–2012 was the lowest in Lithuania whereas in 2013 it was the lowest in Latvia which has been slightly overtaken by Lithuania (9 Lt).
The labour income taxation

Table 2 Parameters related with personal income taxation

<table>
<thead>
<tr>
<th>Indicator</th>
<th>State</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
</tr>
</thead>
<tbody>
<tr>
<td>Minimum monthly wage (in Litas)</td>
<td>Lithuania</td>
<td>800</td>
<td>800</td>
<td>800</td>
<td>800</td>
<td>1,000</td>
</tr>
<tr>
<td></td>
<td>Latvia</td>
<td>877</td>
<td>876</td>
<td>973</td>
<td>987</td>
<td>991</td>
</tr>
<tr>
<td></td>
<td>Estonia</td>
<td>960</td>
<td>960</td>
<td>960</td>
<td>1,001</td>
<td>1,105</td>
</tr>
<tr>
<td>Tax-exempt amount (in Litas)</td>
<td>Lithuania</td>
<td>470</td>
<td>470</td>
<td>470</td>
<td>470</td>
<td>470</td>
</tr>
<tr>
<td></td>
<td>Latvia</td>
<td>173</td>
<td>148</td>
<td>222</td>
<td>222</td>
<td>222</td>
</tr>
<tr>
<td></td>
<td>Estonia</td>
<td>497</td>
<td>497</td>
<td>497</td>
<td>497</td>
<td>497</td>
</tr>
<tr>
<td>Standard rates of personal income tax (percent)</td>
<td>Lithuania</td>
<td>15</td>
<td>15</td>
<td>15</td>
<td>15</td>
<td>15</td>
</tr>
<tr>
<td></td>
<td>Latvia</td>
<td>23</td>
<td>26</td>
<td>25</td>
<td>25</td>
<td>24</td>
</tr>
<tr>
<td></td>
<td>Estonia</td>
<td>21</td>
<td>21</td>
<td>21</td>
<td>21</td>
<td>21</td>
</tr>
</tbody>
</table>

Source: EC (2013b)

Most countries, including the Baltic states, apply a non-taxable income amount on labour income. Table 2 presents the changes of the non-taxable income amount during the period of 2009–2013 (EC, 2013b).

During the whole analysed period (from 2009 up to 2013) both in Lithuania and Estonia the main tax-exempt amount applied on personal income tax did not change. During the analysed period the tax-exempt amount applied on personal income in Lithuania reached 470 Lt, in Estonia – 27 Lt (that is 5%) more. As a matter of fact, starting from 2014 the established tax-exempt amount is going to be 570 Lt. Meanwhile, the tax-exempt amount on personal income in Latvia during the analysed period kept fluctuating and only in 2011 it settled and reached 222 Lt.

The biggest difference in the tax-exempt amount was in Estonia and Latvia in 2010 when the tax-exempt amount in Latvia was 148 Lt whereas in Estonia it reached even 497 Lt, i.e., in Estonia the tax-exempt amount on the income of its inhabitants was three times bigger (if we compare Latvia and Lithuania, the difference is slightly smaller but also exceeds it three times). In 2013, the tax-exempt amount on personal income of the inhabitants of Lithuania is more than two times bigger than the one applied in Latvia and 5% smaller than in Estonia.

It is obvious that the highest non-taxable amount applied during the analysed period was in Estonia. Although the minimum wage in Latvia by the end of 2013 was 16% higher than in Lithuania, the non-taxable income amount was 2.5 times smaller. We may state a priori that, under such conditions, an employee in Latvia receiving a minimum monthly wage pays an income tax from a higher taxable income amount.

As mentioned above, an amount of non-taxable income is applied in taxation of labour income with personal income tax. The personal income tax is calculated according to the personal income tax rates set by every individual state.

The rate of personal income tax imposed in Lithuania and Estonia within the analysed period, i.e., from 2009 to 2013 did not change: during all the five years the personal income tax in Lithuania was 15%, in Estonia – 21% (see Table 2). Meanwhile, the personal income tax rate in Latvia keeps slightly changing. The highest tax rate imposed in Latvia was in 2010. At that time it was 26%. In 2011 it was reduced by 1% point – down to 25% and in 2013 by one more percent point – down to 24%. If we compare 2013
and the beginning of the analysed period (2009) the personal income rate in Latvia has increased by 1% point.

The personal income tax rate in Lithuania in comparison with Estonia and Latvia is the lowest one. During the analysed period the rate of this tax, if Lithuania and Estonia are to be compared, is smaller by 6% points. Therefore, if other conditions are excluded, we may state that taxation of personal income in Lithuania is smaller than that of Estonia.

Comparison of the three Baltic states shows that the highest standard personal income tax rate is imposed on personal income in Latvia. Personal income tax rate in Latvia during 2011–2012 was 10% points higher than in Lithuania (in 2013 – 9 points higher). The biggest difference in rates between Latvia and Lithuania was in 2010 when personal income tax rate in Latvia was higher by 11% points.

To sum up the labour income taxation with a personal income tax, we can make an observation that even though the minimum monthly wage in Lithuania in 2009–2012 was the lowest one (on average by 21% as compared to Estonia and by 16% if compared to Latvia), the non-taxable income amount was on average 2.5 times bigger than in Latvia and only by 5% smaller than in Estonia. The imposed personal income tax rate in Lithuania during the analysed period was the lowest one as compared to other Baltic states – 40% smaller than in Estonia and on average 60% smaller than in Latvia. It can be assumed that the burden of taxable personal income in Lithuania is the lowest one: in 2013 an employed person in Estonia that receives a minimum monthly wage pays 123.04 Lt in taxes, in Latvia – 184.56 Lt, and in Lithuania – only 85.5 Lt. The fact that the burden of personal income tax in Lithuania is the lowest one has also been confirmed by Eurostat data (EC, 2014). For example, in 2011 the revenue from the personal income tax in Estonia was 5.3% of gross domestic product (GDP), in Latvia – 5.6% of GDP and in Lithuania – only 3.5% of GDP (Eurostat methodology also includes other taxes directly related to income, such as church tax, etc.).

5 Taxation of labour income with contributions

State social insurance and compulsory health insurance contributions are imposed on labour income in Lithuania. The total state social insurance contribution rate paid by the insurer and the insured (SSI) that is imposed on remuneration and other employment related income is 40%. The insurer pays the main part – contributions of 31% and the insured pay contributions of 9% (see Figure 1). An attention should be drawn to the fact that this contribution rate also comprises the compulsory health insurance (CHI) contribution rate (3% as contributions paid by the employer and 6% as contributions paid by the employee). In order to clarify the structure of SSI contribution rate, it is necessary to discuss the changes implemented in 2006. Starting from 1 January 2006 the contribution rate for insurance against the accidents at work has been differentiated according to the insurers’ risk and potential injury indicators in organisations. The social security contribution rate for accidents at work and occupational diseases that has to be paid by the insurer was set according to three affirmed groups of social security contribution rates: they are affirmed of annually through the law on confirming the budget indicators of the state social insurance fund. In 2012, group IV for social contributions on accidents at work and occupational diseases was added...
(this group is supposed to be the most risky one considering the level of insecure labour in an enterprise), however, none of Lithuanian enterprises has been included into the list so far.

**Figure 1** Distribution of the general rate of the state social insurance into different social insurance types in 2013 (see online version for colours)

![Diagram showing distribution of social insurance contributions]

*Source:* SRL (2012a)

In 2008 the following general rates of state social insurance contributions were applied in Lithuania: 31% of the contribution (3% of which was allocated to the compulsory health insurance) for the insurer, the insured had to pay 3% contributions. The biggest changes in state social insurance rates took place in 2009. First of all, the general SSI contribution rate significantly increased as a rate of 6% was affirmed of to be paid by the insured persons for the compulsory health insurance that had earlier been integrated into the income tax of natural persons (up until 2009 the health insurance contributions had to be paid only by the insurers). Therefore, a new taxation rate scheme was introduced where the employer pays state social insurance contributions of 31% (with an integrated compulsory health insurance contribution rate of 3%) and the employee pays a contribution of 9% (with an integrated compulsory health insurance contribution rate of 6%). The pattern of paying sickness and maternity social insurance contributions has also changed. Since 2009, these contributions must be paid only by the insurers (i.e., the insured do not have to pay the 0.5% contributions on sickness and maternity social insurance). It should also be noted, however, that since 2009 the insured has had to pay a 0.5% point higher rate of pension insurance contributions. Therefore, these changes have not had any significant influence on the total amount of contributions.

In 2009, Lithuania started a social insurance scheme for persons receiving authorship agreements, income from performing and sports activities, farmers and their partners. The order of social insurance of self-employed people has also changed: in 2009 self-employed people paid contributions from 1/3 of their income, in 2010 – 2/3 of their income and in 2011 they already had to pay social insurance contributions from the whole amount of their income. Although the contribution rate for CHI did not change in 2013, however, when the minimum monthly wage was increased, which is the contribution base for CHI, persons conducting individual activity under a business certificate as well as self-employed persons must pay a contribution of 90 Lt (up until now the rate for these contributions was 77 Lt).
### Table 3
State social insurance contribution rates in Lithuania in 2013

<table>
<thead>
<tr>
<th>The payer</th>
<th>The taxable base</th>
<th>Insurer rate, %</th>
<th>Insured rate, %</th>
<th>Contribution base ceiling</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>1 gr.</td>
<td>II gr.</td>
<td>III gr.</td>
<td>IV gr.</td>
</tr>
<tr>
<td>Persons working under an employment contract</td>
<td>Remuneration for work</td>
<td>30.98</td>
<td>31.22</td>
<td>31.7</td>
</tr>
<tr>
<td>Persons related to the insurer by employment relationship or corresponding relationship (e.g., receiving income from sports or performing activities)</td>
<td>Income</td>
<td>30.98</td>
<td>31.2</td>
<td>31.7</td>
</tr>
<tr>
<td>Persons not related to the insurer by employment relationship or corresponding relationship</td>
<td>50% of the income</td>
<td>28.50</td>
<td></td>
<td>9</td>
</tr>
<tr>
<td>Persons receiving income under authorship agreements, related to the insurer by employment relationship</td>
<td>Income</td>
<td>30.98</td>
<td>31.22</td>
<td>31.7</td>
</tr>
<tr>
<td>Persons receiving income under authorship agreements not related to the insurer by employment relationship</td>
<td>50% of the income</td>
<td>29.70</td>
<td></td>
<td>9</td>
</tr>
<tr>
<td>Self-employed people (except the persons that conduct an activity under a business license and owners of individual enterprises as well as practical members of partnerships)</td>
<td>50% of the taxable income</td>
<td>28.50</td>
<td></td>
<td>9</td>
</tr>
<tr>
<td>Persons conducting activities under a business license</td>
<td>50% of the basic pension</td>
<td>26.30</td>
<td></td>
<td>9</td>
</tr>
<tr>
<td>Owners of individual enterprises; practical members of partnerships and limited partnership business entities; members of small partnerships</td>
<td>An amount withdrawn by the owner of the individual enterprise or the partnership for his or her personal use that is declared at the state tax inspection as employment related or corresponding income</td>
<td>26.30</td>
<td></td>
<td>9</td>
</tr>
</tbody>
</table>

Notes: *II – insurable income (in 2013 – 1,488Lt), 4 II – the amount of four insurable incomes (5,952Lt), 48 II – the amount of 48 insurable incomes (71,424Lt)

Source: SRL (2012a)
Different types of income in Lithuania are taxed with different contribution rates (see Table 3). In 2013, as compared to 2012, the contribution rates on labour income did not change: the 31% rate paid by the insurer was allocated to different types of insurance – state social pension insurance, sickness and maternity social insurance, insurance against unemployment, accidents at work and vocational diseases insurance as well as health insurance. The 9% contribution rate paid by the insured was allocated to pension social insurance (3%) as well as health insurance (6%).

The amount of state social insurance contributions depends on the income amount received and declared by a person or the amount of the remuneration for work, however, persons with business licenses are an exception here. Attention must be paid to the fact that certain activities have a contribution base ceiling (see Table 3, column 5). It means that the income is exempt of taxes starting from the amount that exceeds the set insurable income amount. In Resolution No. 5 of 9 January 2013, the government approved the taxable earnings amount of 2013 – 1,488Lt. Such an amount, however, is not fixed for persons working and receiving income under employment agreements.

Similarly to Lithuania, in Latvia and Estonia labour income is taxed with state security and compulsory health insurance contributions. Compulsory social security contributions in Latvia are paid both by the employer and the employee. An observation should be made that during the whole analysed period of 2009–2013 the contribution rate imposed on the employer in Latvia remained stable whereas the contribution rate levied on the employee kept changing. Starting from the beginning of the analysed period up until 2011 the contribution rate imposed on the employee reached 9%, in 2011 the rate was increased by 2% point up to 11%. Such a tendency has also remained in 2013 – the total contributions amount in 2013 is 35.09%, 24.09% of which is paid by the employer and 11% – by the employee.

In Estonia the employer pays a social tax on the labour income of every employee before any other taxes. Revenues from this tax finances health and pension insurance. Differently from Lithuania and Latvia, the social tax is paid only by the employer (except the case when an employee participates in the second pillar funded pension scheme and transfers 2% from the remuneration before taxes to the personal pension account). During the whole analysed period of 2009–2013 the social tax rate in Estonia remained unchanged – 33%, 20 of which is allocated for pension insurance and 13% – health insurance contributions (besides, there is a set maximum taxable base – 198720Lt a year, above which contributions are not calculated). The employer and the employee are compulsorily insured against the unemployment, the contribution rate in 2012 was respectively 1.4 and 2.8% of the remuneration. According to the Eurostat data (EC, 2013b), the social tax in Estonia in 2011 is accounted for 12.1% of GDP.

Summarising, we may note that compulsory social insurance contributions must be paid in Latvia, a social tax which finances health and pension insurance is applied in Estonia, whereas in Lithuania people pay state social insurance as well as compulsory health insurance contributions. Each of the mentioned contributions differs not only in their names but also in contribution payers and contribution rates.
6 Analysis of personal labour income taxation

The burden of personal income taxation born by the inhabitants of Lithuania, Latvia and Estonia are different. In order to analyse the burden imposed on labour income, we compared the personal income tax, state social insurance and compulsory health insurance contribution rates and other related indexes of each country. Figure 2 shows personal labour income taxation in Lithuania, Latvia and Estonia in 2013.

Figure 2 Standard rates of personal income taxes and contributions from the gross salary in 2013 in percent (see online version for colours)

![Graph showing personal income taxation rates](image)

Source: Eurostat (EC, 2013c)

We may tentatively note that in 2013 the highest rate income taxation was specific to Latvia where personal income taxation rate was 35%, 24 of which was personal income tax and 11% – compulsory social insurance contributions. Personal income in Lithuania is taxed at a rate of 24% (15% of which are personal income tax, 3% state social insurance and 6% compulsory health insurance contributions), i.e., lower by 11% points than in Latvia. In Estonia the personal income is taxed only at the rate of 23% (21% of which constitute the personal income tax rate and 2% – insurance from unemployment) – which is lower than in Lithuania by 1% point and even 12% points lower than in Latvia. However, if we analyse the situation of the taxes paid by the employer from the earnings of a person, the situation is cardinally different: the highest burden is carried by Estonian employers – the taxes are higher by 3% points here than in Lithuania and even by 9.91% points higher than those of the Latvian employers (see Table 4).

Table 4 The main rates applied to employment earnings in 2013 in percent

<table>
<thead>
<tr>
<th>Taxes and contributions</th>
<th>Lithuania</th>
<th>Latvia</th>
<th>Estonia</th>
</tr>
</thead>
<tbody>
<tr>
<td>SSI and CHI</td>
<td>Employer</td>
<td>31</td>
<td>24.09</td>
</tr>
<tr>
<td></td>
<td>Employee</td>
<td>9</td>
<td>11</td>
</tr>
<tr>
<td>Personal income tax</td>
<td>Employer</td>
<td>15</td>
<td>24</td>
</tr>
<tr>
<td>Labour income taxation, % of GDP (in 2011)</td>
<td>12.7</td>
<td>13.8</td>
<td>16.8</td>
</tr>
</tbody>
</table>


It can be stated that labour income taxation with personal income tax, social security and compulsory health insurance in Lithuania in comparison with labour income taxation in
7 Conclusions

Planned labour income taxation solutions are considered as important prerequisites for the targeted reduction of the burden of taxation of business subjects and working people. It should be noted that the measurement of the improvement of labour income taxation has already been determined in Lithuania, however, the implementation solutions of specific aspects are of controversial nature.

Labour income received by employed people for their work is the main source of personal income. Personal income tax and social security as well as health insurance taxes are imposed on labour remuneration. The main and the highest tax paid by employees on remuneration is personal income tax. Proportional tax rates are applied for calculating this tax in the Baltic states. There is a fixed non-taxable income size, the application of which adds features of progressiveness to the applicable taxation model.

During the analysed period the highest personal income tax rate as well as the lowest non-taxable amount was applied in Latvia. The lowest personal income tax burden was born by Lithuania.

Social security and health insurance contributions are imposed on labour income. Payment of these contributions, according to the proportion established by the state, is shared between the employer and the employee. In Lithuania (and Latvia also), it is the employer that pays the bigger part of the taxes (respectively 31 and 24.09%), the other smaller amount of contributions – respectively 9 and 11% – is deducted from the remuneration of the employee and other employment related income. Social tax in Estonia is paid only by the employer; however, the tax on unemployment social security is shared by the employer and the employee at the ratio of 1:2.

Although the performed research revealed that the highest rate labour income taxation is applied in Latvia, the implicit tax rate shows that the average effective tax burden on the labour income is highest in Estonia. Comparison of the main taxation rates (non-taxable minimum, standard rates) only partially reveals the national level of the labour income taxation. A more accurate description of the taxation level can be provided only having evaluated the taxation base of taxes and contributions, tax exemptions and having evaluated such factors as the implicit tax rate or taxation of labour income as the percentage of GDP.
References


The labour income taxation


