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PRESS RELEASE

Linear reduction in employers' contributions

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Belgium is among the European countries with the largest tax wedge on earned incomes, notably on account of the predominant role of social contributions in the social security funding system. Its employment rate is also below the European average. Since Belgium is also weak in terms of cost competitiveness, it seems attractive to base social security funding on alternative methods of taxation which place less of a burden on labour costs while maintaining the balance of public finances. This is the context in which Noname, the Bank's new macroeconomic model, was used to assess measures which could modify the demand side of the labour market. The model simulates reductions in employers' contributions and alternative financing measures: increase in VAT, introduction of a value added levy, and a general social contribution. For one of these alternative financing measures, namely the value added levy, the automatic financial effects on the various branches of activity are examined via national accounts data.

A measure to reduce employers' contributions always has a favourable impact on employment, since it encourages substitution between factors of production in favour of labour, and it enhances the competitiveness of firms, thus boosting output and employment. These beneficial effects are much more marked if the reductions in charges are not reflected in gross pay, but if the employees are able to recoup all or part of any cut in employers' contributions, that positive impact is considerably diminished. Given the inherent limitations of all models and the uncertainty regarding the most appropriate way of introducing the measures into simulations, the assessment of the simulated impact must be approached with caution. Nonetheless, it seems that compensatory measures always destroy jobs and generate public revenues. These negative effects on employment and positive effects on public finances are attenuated if the increase in wages caused by these measures is neutralised. Moreover, all the alternative funding methods will have a contrary effect on at least one of the channels through which a cut in contributions produces its effects.

- A VAT increase has a highly inflationary impact. If wages respond in full to this increase in inflation, this measure will be detrimental to growth, competitiveness and employment. If this link is neutralised, these negative effects are greatly moderated.

- A value added levy is problematic not only because it destroys more jobs than the other measures considered (except for a non-neutralised VAT increase), but also because it has a major impact on competitiveness, particularly to the detriment of the most capital-intensive businesses.

- A general social contribution has relatively modest effects provided it does not trigger pay rises via the ensuing increase in the tax wedge.

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