Taxes and Benefits in the Polish Parliamentary Election Campaigns

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The upcoming parliamentary elections in Poland, scheduled for the 25th of October 2015, have on the one hand stimulated debate on the record of the current coalition government, and on the other opened the debate on the nature of socio-economic policy to be conducted in the coming years. In this brief, we draw on two recent pre-election reports published by the Centre for Economic Analysis, CenEA. We discuss developments in tax and benefit policies under the coalition of the Civic Platform and the Polish People's Party over the last eight years, as well as the pre-election pledges regarding tax and benefit policies to be implemented after the elections. We show a significant shift in policy priorities with respect to the distributional effect of the tax-benefit policies between the first (2007-2011) and the second (2011-2015) term in office, towards more support for low-income families. We also argue that, judging by the presented electoral pledges, Polish voters face a difficult choice between the promises of the opposition parties, which seem too costly to be realistic, and an enigmatic tax overhaul reform proposed by the governing Civic Platform, which is supposed to substantially benefit nearly all working households at a low cost for the state budget, with details of the reform design, however, kept away from public scrutiny.

The parliamentary elections to be held in Poland on the 25th of October, 2015 follow eight years of stable coalition government formed by the center-right Civic Platform (Platforma Obywatelska, PO) with the Polish People's Party (Polskie Stronnictwo Ludowe, PSL), a party with grass-root support among farmers. The coalition has governed Poland since the elections in 2007 and managed the country over the years of the economic crisis, as well as over a serious political uncertainty following the tragic crash of the presidential aircraft in Smolensk in April 2010. During these years, despite the global recession, the Polish economy has continuously grown and the cumulative GDP growth between 2007-2015 amounts to 24%. At the same time, while unemployment peaked in 2007 at 15%, by the end of the summer 2015 it fell to 10%, with significant increases in employment, in particular among older individuals.

The macroeconomic environment over the last eight years has to a large extent determined the choices the coalition has had to make regarding tax and benefit policies. While in January 2009, the government went ahead with a substantial cut in the personal income tax (legislated as early as 2006, hence long before the outbreak of the recession), it also had to patch up the deficit with an increase in the VAT just two years later and higher social security contributions in 2012. Details of the eight years of tax and benefit policies of the PO-PSL coalition have been recently analyzed in a report published by the Centre for Economic Analysis, CenEA (Myck et al. 2015a).

Consequences of Tax-Benefit Policies 2007-2015

Overall, our estimates suggest that Polish households have seen some small gains resulting from the government's policy, directly affecting their financial situation estimated to an annual total of 2.1 billion PLN (corresponding to 0.5 billion euro or 0.1% of GDP). Interestingly, these gains have come not from tax cuts, which the Civic Platform (PO) proclaimed in the election campaigns in 2007 and 2011, but rather from increased spending on social benefits, in particular those targeted at families with children (3.8 billion PLN, 0.9 billion euro) and pensioners (2.2 billion PLN, 0.5 billion euro). The government implemented two important reforms of the personal income tax, including the reform of 2009, in which a three rate system with taxes charged at 19%, 30% and 40% was replaced with a two rate scheme (18% and 32%) and a recent change, which increased the generosity of a child tax credit to low-income families. At the same time, however, the government pursued a policy to freeze nominal elements of the tax system which, given growing incomes, translated into a higher tax burden. The total net effect of these policies in the direct tax area has been only a modest fall in the tax burden of 1.6 billion PLN (0.4 billion euro). This combined with higher rates of the VAT, increased social security contributions, and changes in some other taxes implied an increased total tax burden on households of 9.7 billion PLN (2.3 billion euro, 0.6% of GDP).

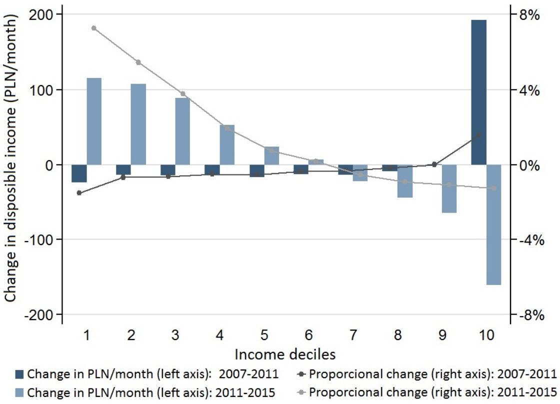
On the benefits side, the government strongly prioritized families with children which received support through higher levels of family benefits, extended duration of paid parental leave, and a generous guaranteed minimum benefit for those parents of newborn babies who were not insured in the public system. These benefits amount to a total of 8.9 billion PLN per year (2.1 billion euro, 0.5% of GDP). These benefits, together with the increased pension benefits (2.2 billion PLN) and the higher support through social assistance, more than outweigh the increased tax burden on households, giving a net benefit of 2.1 billion PLN.

Gainers and Losers

Interestingly, there has been a substantial difference in the targeting of the tax and benefit policies in the first (2007-2011) and the second (2011-2015) term in office of the PO-PSL coalition. This is represented in the figure below, which shows the combined effects of the tax and benefit policies implemented in the first and the second term. The results represent the total average monthly gains per household (in PLN) and the gains proportional to income divided by income decile groups, i.e. the groups of the population from the poorest to the richest 10%. As we can see, while parliamentary decisions from the first term brought gains only to households in the top income decile, the richest households saw their incomes fall as a result of government policies in the second term.

Proportionally to income, gains for the richest in the first term, coming mainly from the introduction of the two-rate income tax system, were comparable to their losses in the second term amounting on average of 1.4% of their income. Losses in the second term were mainly due to the freezing of the nominal parameters of the tax system and raises in the social contributions. Households in the 7 to 9 income decile faced decreases in income in both terms. While drops in incomes of the first half of the distribution were minor in the first term, the second term (2011-2015) brought them substantial gains: for the poorest 10% of the population, on average up to 7.3% of their income. Those households benefited mainly from higher social and family benefits and increases in pensions. The figure shows that over one term of office, the PO-PSL coalition turned quite significantly away from liberal tax and benefit policies favoring the rich, to a more social agenda with greater tax burden at the top of the income distribution and higher spending on poorer households.

Figure 1. Consequences of tax-benefit policies introduced in the two terms of the Polish parliament in 2007-2015, by income deciles



Source: Myck et al. 2015a.

Electoral Pledges in 2015

In the heat of the elections campaigns for the parliamentary elections scheduled to the 25th of October 2015, the tax and benefit policies have again taken headlines. Most of the parties fighting for electoral success have not shied away from extremely generous give-away packages with very few details on how these would be financed. These electoral programs have been the focus of attention in CenEA's most recent report (Myck et al. 2015b).

First, the main opposition party (Law and Justice, Prawo i Sprawiedliwość, PiS) presented a very generous quasi-universal support scheme for families with children and substantial increases in the universal tax credit with a total cost for the package of 45 billion PLN (2.6% of GDP).

Second, the total cost of the package proposed by the United Left (Zjednoczona Lewica, ZL) is almost twice as high (98 billion PLN), and apart from a proposal of even higher increases of the universal tax credit, it includes promises like raising substantially social and family benefits and providing every citizen with an annual bonus based on the GDP growth.

Third, a new party on the liberal end of the political spectrum (Nowoczesna, the Modern Party) proposes a single-rate VAT scheme and a linear income tax with rates in each case set at 16% level. Such a scheme, combined with a compensation mechanism for the poorest that would lose out on it, would cost the public finances up to 9.5 billion PLN.

Fourth, at the other end of the political spectrum, a new left-wing party, Together (Partia Razem), proposes a highly progressive tax scheme and increases in social benefits at the total cost of about 15.7 billion PLN.

In all of the above cases, the source of financing for the proposed programs has not been specified, except for claims to curb the grey economy in particular in the area of the VAT fraud. Given the very tight situation of the Polish public finances, rapid realization of these generous programs is highly unlikely and the programs will have to be significantly reevaluated by those who take responsibility for the government after the 25th of October.

Finally, electoral promises of the coalition parties have been relatively modest, with the exception of a very radical reform of the tax system proposed by the Civic Platform (PO), as a result of which the total tax burden on labor would be substantially reduced with gains to nearly all working tax payers. The surprising thing about this proposal is that the tax formula behind it has remained a tightly kept secret, which has made it impossible for the policy to be independently evaluated. This makes the total cost of the change, which according to the PO is only 10 billion PLN, highly questionable.

Thus, with respect to the choices over policies that would directly affect the financial wellbeing of Polish households, the voters will on the 25th of October face a dilemma. They will have to choose between a number of highly unrealistic electoral programs of the opposition parties and an enigmatic tax reform of the main party in government.

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