TAXATION IN SWEDEN

Dan Johansson, Arvid Malm and Mikael Stenkula

Introduction

This country report for Sweden is part of the European Index on Taxation (EIT) project, which is a Europe-wide project intended to provide an overview of key aspects of the various tax systems of EU countries.

The Swedish tax system is of particular interest as Sweden has a large public sector and high levels of taxation. Furthermore, Sweden has in recent years carried out a number of tax reforms that have reduced the tax level significantly.

Level of taxation

This section discusses the history of taxation in Sweden and charts the growth and decline of taxes over time, measured as a percentage of GDP.

1960–1990 The growth of the welfare state

Contrary to common belief, Sweden has not always been a high-tax country. As late as 1960, overall taxation as a share of GDP (Gross domestic product) in Sweden was 28.7 percent, which as in line with the United Kingdom (27.3) and the United States (27.5), but below France (33.4). And West Germany (33.9) [taxes as a share of GDP in parentheses].[1] Sweden was not an outlier by OECD standards at that time.

Starting in the 1960s, however, the welfare state underwent a large expansion. This expansion was financed through a large increase in taxation, primarily large increases of labor income taxes (in particular local income tax), social security contributions and value added tax (Stenkula 2014). Taxes as a share of GDP grew gradually and peaked in 1990 at 52.3 percent of GDP.[2]

1990–2000 Crisis and recovery

In 1990–1991 the Swedish tax system underwent major reform, aimed at broadening the tax base, simplifying the tax system and cutting marginal tax rates. The goal was to increase the effectiveness of the tax system through reducing distortion without lowering the total tax burden (Stenkula 2014). In 1991 taxes on capital gains, dividends and interest income were cut further by the new center-right government, but these cuts were abolished by the new Social Democratic government that came to power in fall 1991 (Johansson et al. 2014). The 1990–1991 tax reform coincided with a domestic depression caused by, among other things, failed economic policy during

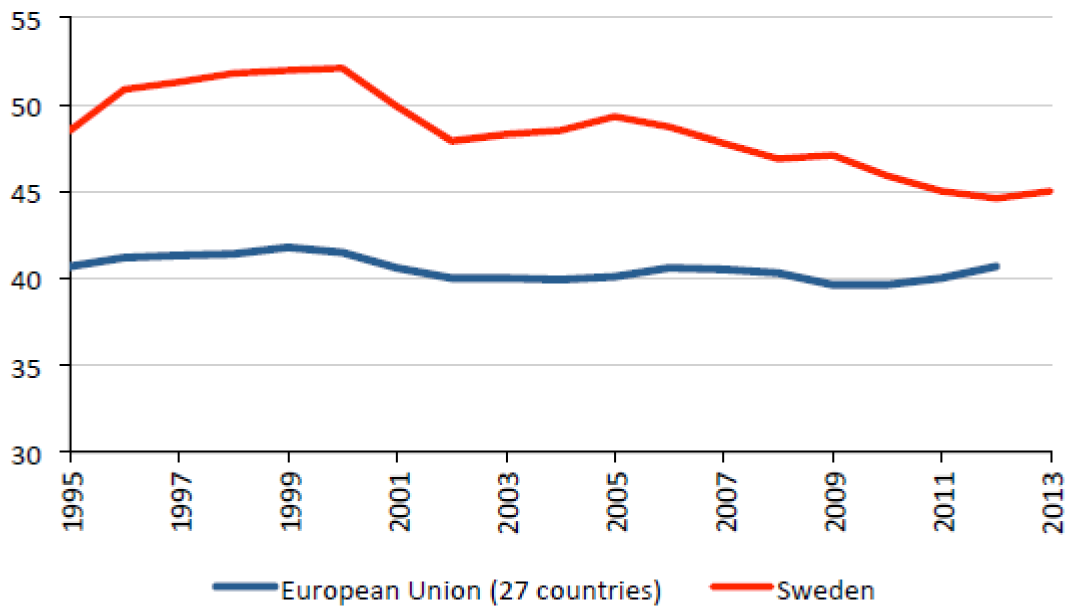
1 Rodriguez (1981, Table 2.1).

2 OECD (2014).

the 1980s. Economic growth was negative three years a row and private employment dropped by one fourth. Tax receipts dropped significantly while government spending increased substantially, creating severe budget deficits.
In the years following the crisis, some taxes and social security contributions paid by employees were raised by the incoming Social Democratic government. Driven mostly by recovery from the crisis tax receipts again reached a near-record in 2001.

2000– Tax reduction
The overall picture since 2000, however, is one of decreasing taxes: While the European Union overall has been fairly stable with regards to tax receipts as a share of GDP over time, Sweden has meanwhile been trending downwards (figure 1). The causes of this gradual decline can be divided into two broad categories: Growth and reform.
First, strong economic growth during the 2000s allowed for a declining tax share. Following the brief downturn following the collapse of the IT boom, the Swedish economy grew at a strong pace.
To further improve the working of the economy, the Social Democratic government executed some tax cuts, such as abolishing the inheritance tax in order to facilitate small business transfers.

Figure 1. Total taxes as % of GDP.



Source: Eurostat (2014a).

Meanwhile, employment had emerged as a major political issue. Long-term unemployment and extensive use of early retirement had created a persistent underemployment problem. In 2006 a center-right coalition won power by running on a job growth platform. A cornerstone in their policy was to improve the tax incentives for accepting job offers and to increase the demand for household services by reducing taxes on certain services.

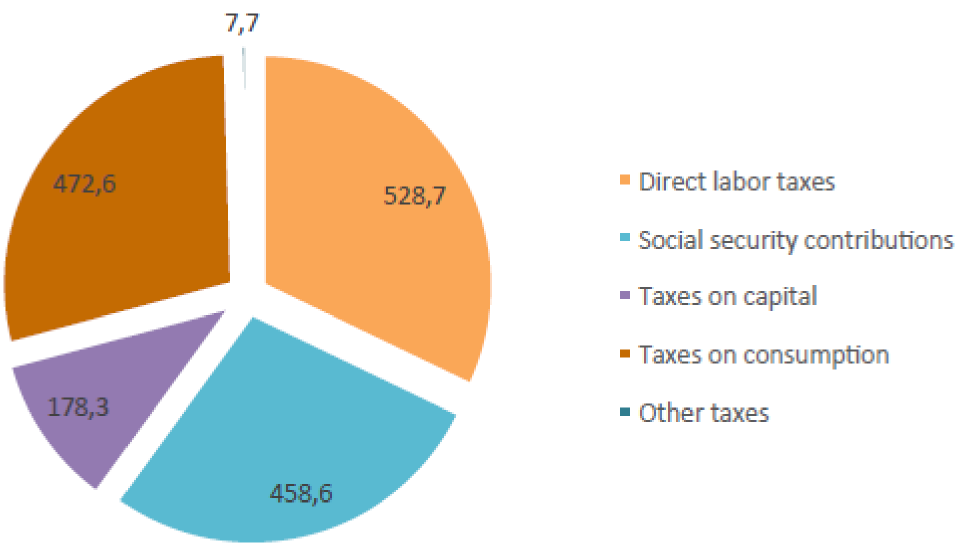
Labor taxes were cut significantly for low and middle-level incomes through the use of an extensive earned income tax credit (*skattereduktion för arbetsinkomster*, the so-called *jobbskatteavdrag*), which was introduced in 2007. This tax credit has been gradually expanded in five steps until 2014. Furthermore, several tax reductions and deductions targeted at the service sector have been introduced.

In 2008, the "ROT-avdrag" provides an extensive tax reduction on personal income tax granted purchasers of personal construction and repair services. A similar tax reduction ("RUT") exists for personal household services such as cleaning, babysitting, etc. since the year before. This reform created a new market, in particular for female and immigrant entrepreneurs. Furthermore, targeted social security contributions reductions that are intended to incentivize the hiring of high-unemployment groups such as youths are in force since 2007. For the same reason, the VAT for eating at restaurants has been reduced from 25 to 12 percent in 2012.

Decomposing Swedish taxation

The principal source of tax income for the Swedish public sector is direct labor income taxation, followed by consumption taxes (primarily VAT) and indirect labor taxation (primarily social security contributions) (see figure 2).

Figure 2. Swedish tax structure in 2014 (bn SEK).



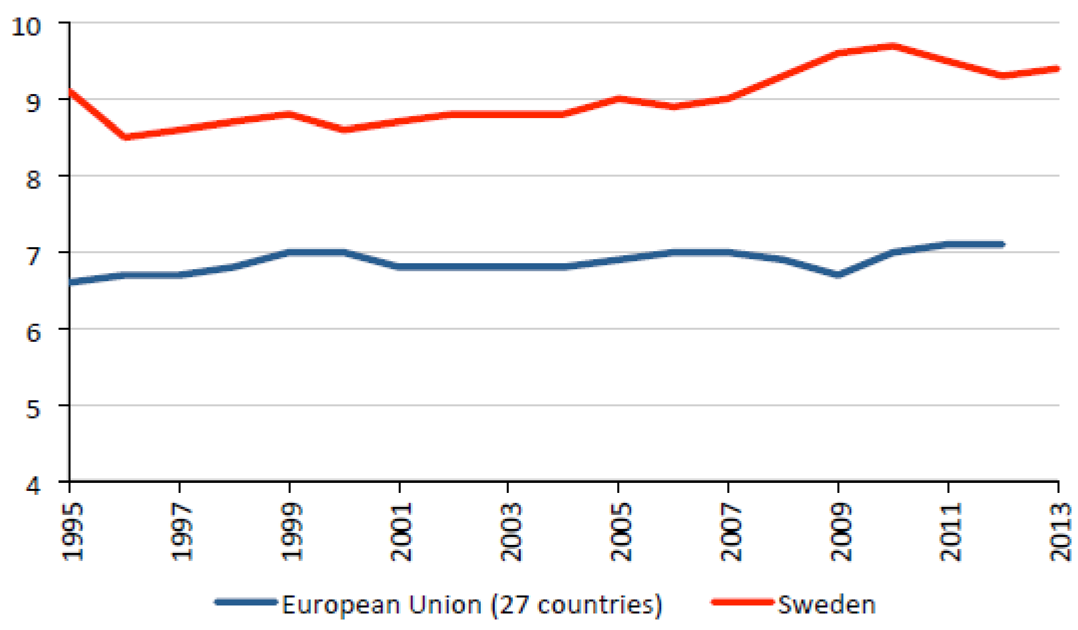
Source: The Swedish National Financial Management Authority (2014).

As figure 3 shows, Sweden is more reliant on value added tax for its tax receipts than the EU average. This reliance has increased somewhat over time. The standard Swedish VAT rate is 25 percent, but reduced rates apply to some goods and services as follows:

- 12 percent VAT is the rate for foodstuffs (excluding alcohol), restaurants, hotels (and similar) and some works of art.

- 6 percent VAT is the rate for books, magazines, newspapers etc., transportation of people, concerts, sporting events, museums, libraries and (some) intellectual property.

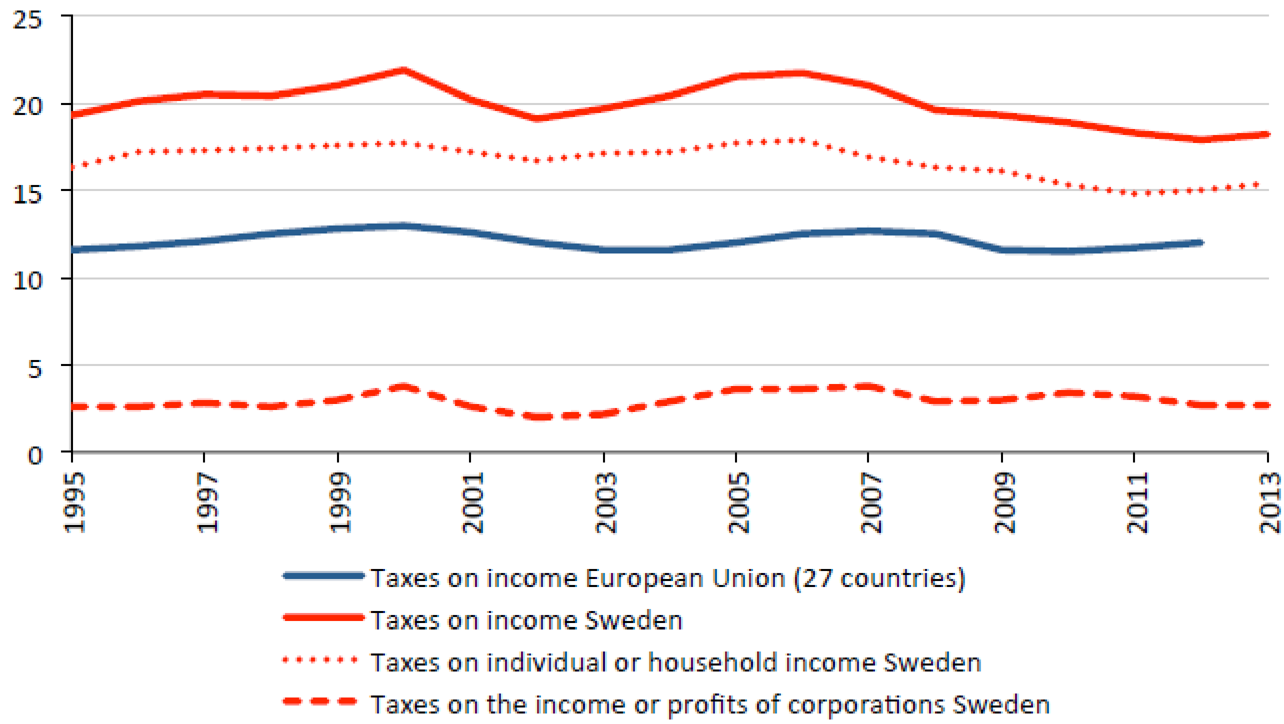
Figure 3. VAT as % of GDP.



Source: Eurostat (2014a).

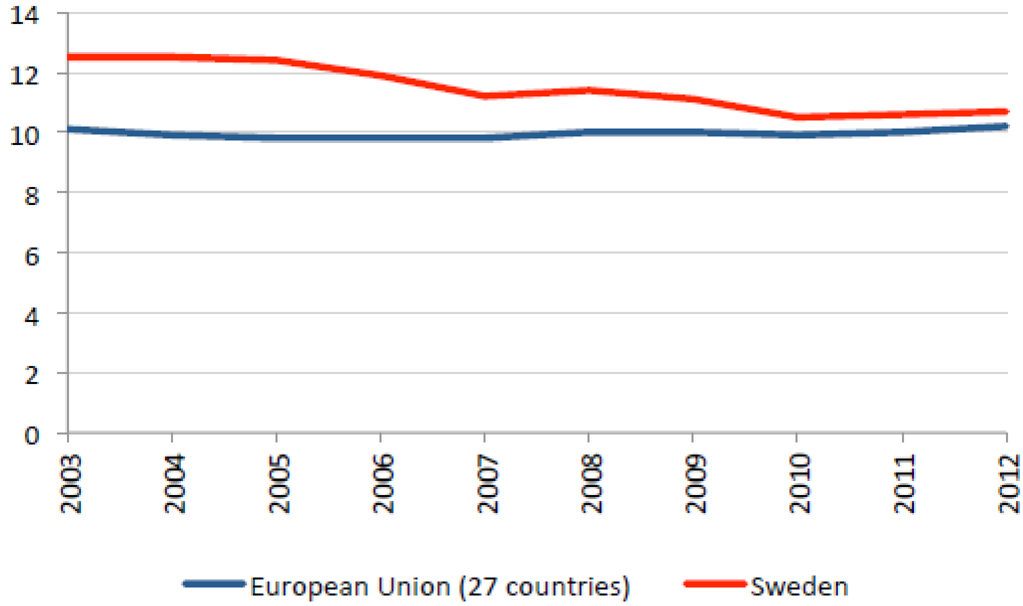
Turning to income taxes (figure 4) and in particular income taxes on labor (figure 5), the importance of personal income taxes in Sweden has meanwhile declined somewhat, primarily due to the introduction of the earned income tax credit (*jobbskatteavdraget*) for labor income.
Corporate taxes are far less prominent as a source of revenue and have remained roughly constant as a share of GDP over time, mostly fluctuating in accordance with the business cycle. The statutory rate of corporate income tax has been reduced in two steps, from 28 to 26.3 percent in 2009 and from 26.3 to 22 percent in 2013.

Figure 4. Income tax as % of GDP.



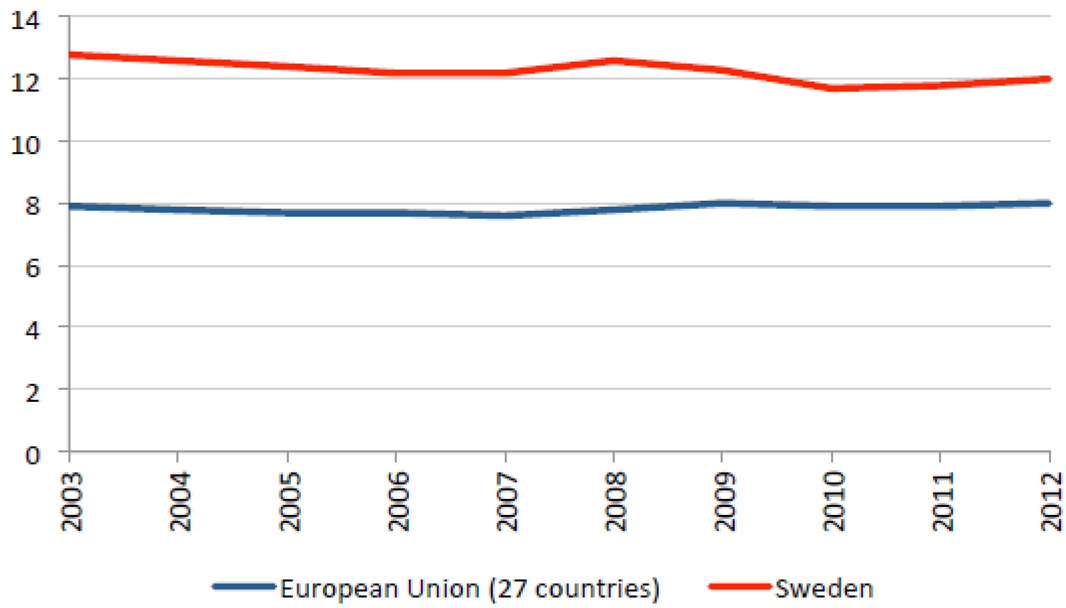
Source: Eurostat (2014a).

Figure 5. Taxes on labor paid by employees as % of GDP.



Source: Eurostat (2014b).

Figure 6. Taxes on labor paid by employers as % of GDP.



Source: Eurostat (2014b).

Figure 6 shows that Sweden also takes in significantly more labor taxes paid by the employer than the EU average. This is primarily due to payroll taxes and social security contributions.

The employer must pay social security contributions (*arbetsgivaravgifter*) for every employee. The standard rate is 31.42 percent (the social security contributions for self-employed (*egenavgifter*) is 28.97 percent).

It can be decomposed into the components depicted in table 1.

Table 1. Social security contributions paid by employers (Arbetsgivaravgifter) (%)

Fee	***Percent***
Pension	*10.21*
Survivor´s pension	*1.17*
Sick leave	*4.35*
Work injury	*0.30*
Parental insurance	*2.60*
Labor market	*2.91*
Payroll tax	*9.88*
Sum	***31.42***

Source: Swedish Tax Authority (2014).

Only the 10.21 percent pension fee is directly tied to an individual benefit system for the employee that tracks contributions directly (i.e. public pension credits), and even this system contains a contribution cap that transforms the fee to a pure tax above a monthly income of 35 562 SEK (4 900 USD) / month.

Other parts of the insurance system, such as sick leave compensation, parental insurance and unemployment insurance (that is partly financed by additional direct fees) are indirectly contribution based, as benefits are calculated based on your previous wage.

In practice this makes it difficult to estimate precisely how much of social security contributions that should be classified as taxes and how much that should be classified as fees.

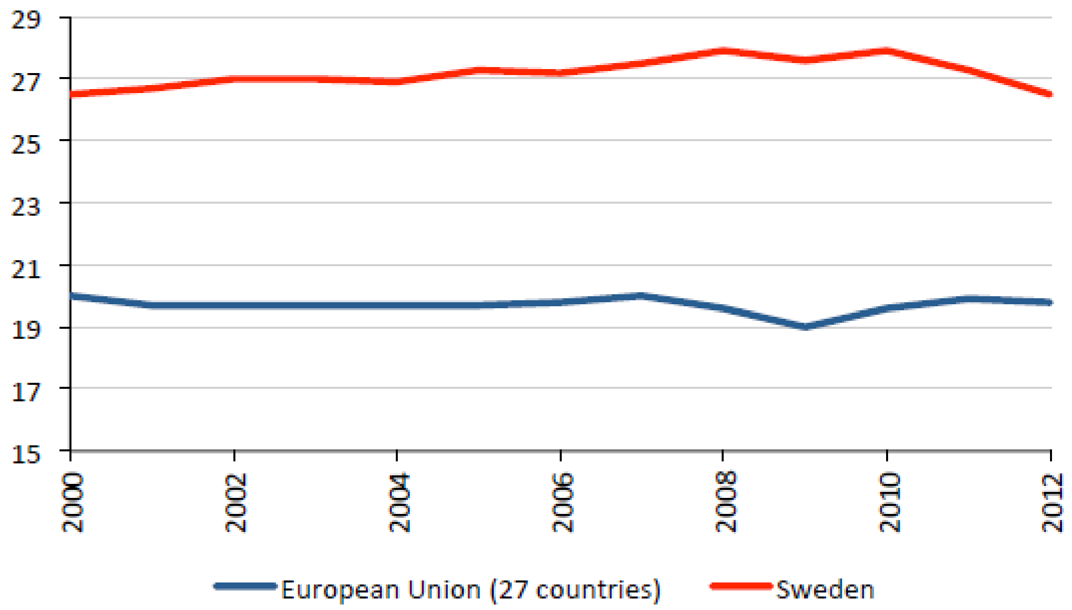
Implicit tax rates

While charting the share of taxes relative to GDP tells you something of their relative prominence, this approach has limitations. It is also worth assessing the ratio of taxes collected to the overall value of the taxed activity. This gives an indication (with certain limitations) of how heavily taxed an individual economic activity is.

Eurostat creates such measures of implicit tax rates on consumption, labor and capital.

As Figure 7 shows, Sweden taxes consumption at a high rate, which has been roughly constant over time, even as other taxes have decreased.

Figure 7. Implicit tax rate, consumption.



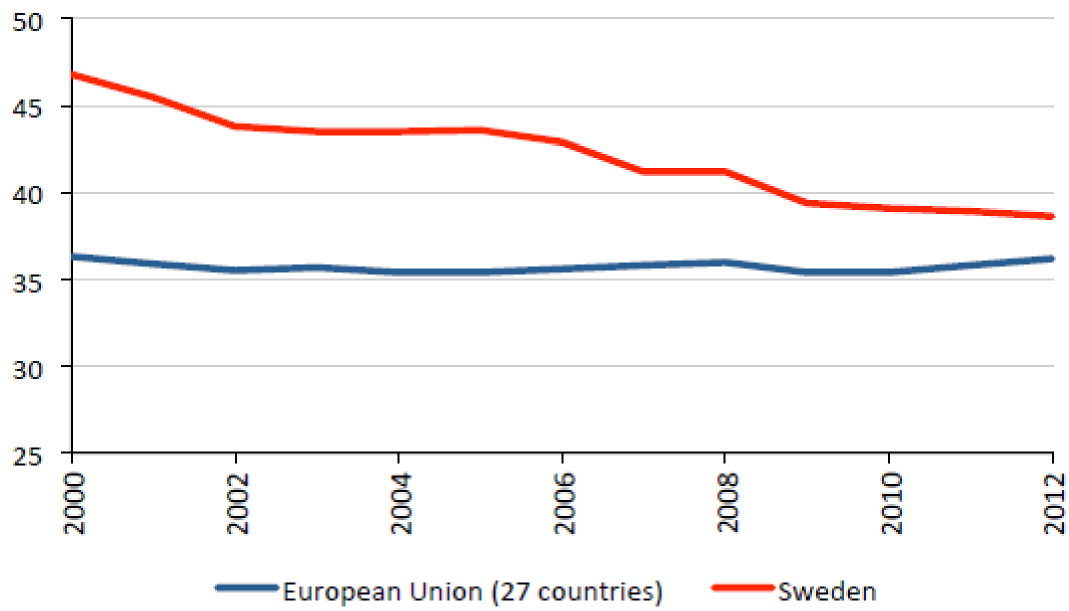
Source: Eurostat (2014c).

As expected, and as is shown in figure 8, the implicit tax on labor has declined over time, and is now approaching the average EU level. It is important to note however, that this is an average rate.

Giving a rough outline of Swedish wage taxes, the primary direct wage tax is the local (municipal and county) tax. Tax rates for local income taxes vary between municipalities, with the lowest tax rate being 29.19 and the highest 34.7 percent, with an average rate of 31.86 percent. Top Swedish tax rates are still high. Incomes above a sum equivalent of roughly 47 000 Euro per year are required to pay a state income tax on top of local income tax. In total, this yields an effective marginal tax rate of approximately 52 percent, excluding social security contributions. Above the equivalent of 67 000 Euro, the rate increases to 57 percent.

It is interesting to note that despite the 20 or 25 percent additional state income tax that is introduced at fairly "normal" incomes, this tax only accounts for somewhat less than 3 percent of total tax revenue.

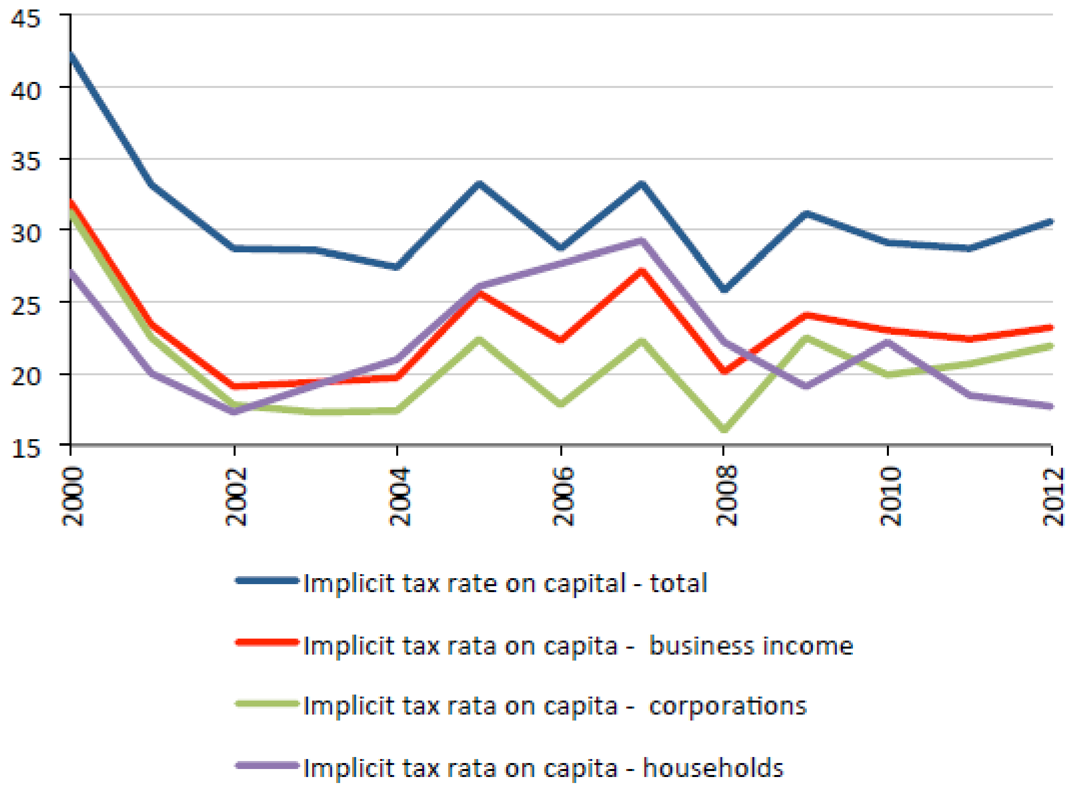
Figure 8. Implict tax rate, labor.



Source: Eurostat (2014c).

Implicit tax rates on capital income (figure 9) have meanwhile remained relatively stable overall following an increase during the heyday of the IT bubble. Household capital taxation has dropped somewhat following 2006, partially due to the abolishment of the wealth tax and the effective cap placed on household property taxation.

Figure 9. Implicit tax rate, capital, Sweden.



Source: Eurostat (2014c).

Administrative burden of fiscal procedures

In the past, doing your taxes in Sweden was a major undertaking, involving a wide variety of more or less obscure forms. Today, however, most people can perform their annual tax declaration using a text message from their mobile phone, or by merely signing off on a pre-filled filing online or in paper form. In 2013, 67 percent of filers chose to file electronically.[3]

Today, the administrative burden of the tax system is hence trivial for a large majority of private individuals.

This is not the case for businesses, however. Still, according to the World Bank and PWC, Sweden compares favorably to the international average when it comes to the amount of time required to comply for a model medium-sized business, as well as in regards to the number of annual tax payments that are required.

Table 2. Doing business in Sweden vs OECD average.

	Time to comply (hrs/yr)	*Payments (no/yr)*
Sweden	*122*	*4*
OECD average	*175*	*12*

Source: World Bank / PWC (2014).

Taxation and federalism

All corporate income tax and capital income / gains taxation is set on the national level. As are social security contributions[4] formally paid by the employer (*Arbetsgivaravgifter*) and VAT. Hence, there is no intra-regional corporate tax competition in Sweden.

Municipal taxation does vary, however. These taxes are only assessed on individual wage income, and there is a certain level of variation in tax rates across the country. Furthermore, there is some econometric evidence for the presence of tax competition between municipalities.[5]

3 Swedish Tax Authority (2013).
4 With some minor exceptions with regards to regional development policy in rural areas.
5 See Edmark and Ågren (2007).

As mentioned above, the highest total local tax rate (including county tax) in 2014 was 34.7 percent, while the lowest was 29.19 percent. County tax rates varied between 12.1 and 10.18 percent.

While counties and municipalities in Sweden enjoy rather extensive administrative autonomy[6], in practice they have limited leeway to deviate significantly from nationally set standards in their service provision. While they administer important services such as schools and care for the elderly, these activities are heavily regulated on the national level.

Furthermore, there is substantial intra-regional and intra-municipal redistribution via the national state budget, further limiting the practical fiscal impact of local policy.

Conclusion

While Sweden remains a high-tax country, and tax rates remain above the EU average in most areas, it is worth noting that Swedish taxes have not always been exceptionally high. Furthermore, the overall tax burden has been reduced significantly in recent years.

Any country that is about to embark on extensive tax reform can hence use Sweden as a useful example.

6 See for instance Wollmann (2004) for an international perspective on Swedish local government.

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