DE GRUYTER
OPEN

DOI 10.1515/sbe-2015-0032

TAXATION IN CESEE COUNTRIES – SIMILARITIES AND DIFFERENCES

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Abstract:
The characteristics of fiscal revenues are the ones that demonstrate their importance for the formation of public financial resources, being considered as a product of historical development of the state. Numerous studies and researches on the taxes action in financial, economic and social level emphasized the link between fiscal policy, growth and level of development of a country. In this context, through this article, by presenting some general coordinates of taxation in countries of Central, Eastern and Southeast Europe (CESEE countries) we will identify the similarities and differences concerning the taxation system and the impact of taxation on the socio-economic development. Without claiming an exhaustive approach, we consider that issues outlined highlight in which country taxation is a stimulating factor for economic growth and development, so that good practice be elements worthy of consideration.

Key words: *tax burden, fiscal freedom, direct taxation, indirect taxation*

1. Introduction

The requirements that any reasonable tax system must comply are found in the principles of taxation, according to which it can set up a real partnership between the state and taxpayers. To the extent that clarity, development, equity, efficiency, effectiveness, ethics, non-discrimination, neutrality, optimization, rationality, relevance and simplicity are found as the main keyword of fiscal policy at the level of any state, the aim and role of taxation will be felt at financial, economic and social level, thus contributing significantly to economic growth and development.

The analysis of taxation area from the CESEE countries is reflected in many studies and research from specialized literature, having regard to the significant changes in these countries, both in economic and social plan, as well as in political plan. It is noted as follows: the presentation of recent developments and forecasts concerning fiscal and budgetary policy priorities, funding models and vulnerability to external financial shocks (IMF, 2014); the identification of the positive aspects concerning convergence policy during the post-crisis period (Király, Csajbók and Kovács, 2011); the specification of changes in fiscal policy, the fiscal vulnerability and the fiscal discipline (Leiner-Killinger, 2012); the presentation of fiscal position taking into account the automatic stabilizers (Eller, 2009); the identification of the impact of fiscal policy on FDI (Walch and Wörz, 2012) and attractiveness of the low corporate tax (Bellak and Leibrecht, 2009); the presentation of econometric relationships between public spending and economic growth (Alexiou, 2009); and so on.

The above considerations have led us to realize this article to identify similarities and differences concerning the taxation system and the impact of taxation on the development level from CESEE countries. Analyses will include both the current situation in the field of taxation, and the evolution of the main indicators in the field of taxation in the 22 CESEE countries, namely: Albania (ALB), Belarus (BLR), Bosnia and Herzegovina (BiH), Bulgaria (BGR), Croatia (CRO), Czech Republic (CZE), Estonia (EST), Hungary (HUN), Kosovo (UVK), Latvia (LVA), Lithuania (LTU), Macedonia (MKD), Moldova (MDA), Montenegro (MNE), Poland (POL), Romania (ROU), Russia (RUS), Serbia (SRB), Slovak Republic (SVK), Slovenia (SVN), Turkey (TUR, and Ukraine (UKR).

2. Direct taxation in the CESEE countries

Profit is the primordial test for the performance of a company, is the indicator which adjusts automatically the market processes, indicating what society resources should be allocated for different users. The gain (getting profit) is a requirement of businessmen to be capable of responding to the needs of society in a positive and effective way. Because in a free economy, profit growth in the business is the key to development, governments and companies must focus on the main alternatives to maximize profits (Thompson, 1989).

In the context of globalization, it is noted more frequently a competition among states for corporate taxation in order to reduce tax evasion (Farnsworth and Fooks, 2015) and increasing the attractiveness for investment (Pomerleau, 2015). In this sense, in the past ten years there has been a considerable reduction in the average corporate tax rate around the world, from 27.5% in 2006 to 23.68% in 2015 (KPMG, 2015). As shown by Fig. no. 1, the average corporate tax rate for CESEE countries has registered in the period 2006-2015 a decrease by 2.28 percentage points, being situated to an amount far below the global average and the Europe average.

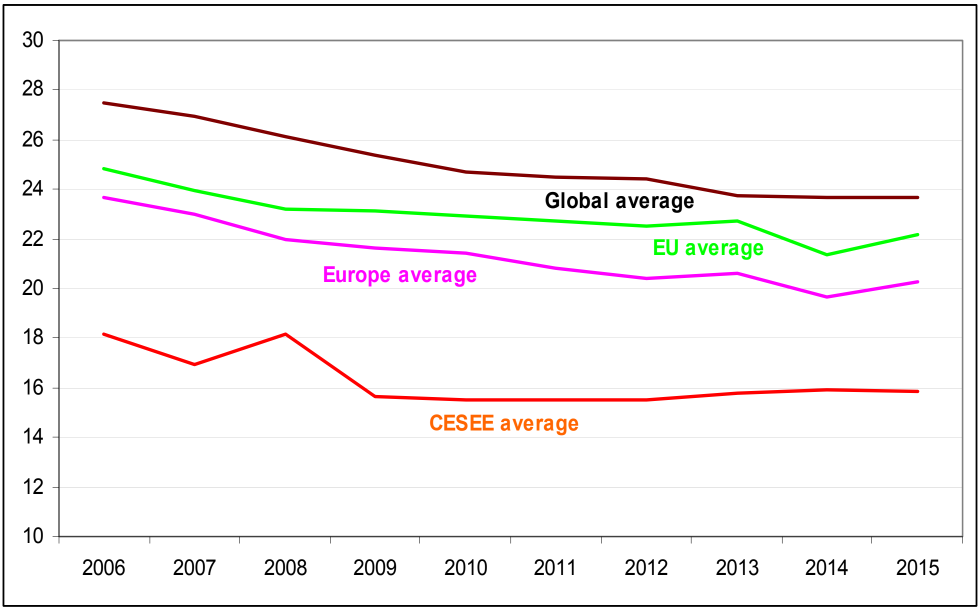

Fig. no. 1 Evolution of the average corporate tax rate
(Source: author processing based on data from KPMG, Kosovo-Law on corporate income tax, Moldova-Fiscal Code)

As can be seen in Tab. no. 1, in the period 2006-2015, most fiscal policy decisions from CESEE countries have targeted changes in the corporate tax rate. For 2015, top marginal corporate tax rate in CESEE countries is between 9% in Montenegro and 22% in Slovak Republic, most countries having top marginal corporate tax rate below 20%.

Tab. no. 1 Top marginal corporate tax rate in CESEE countries (%)

CESEE countries	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
ALB	20	20	10	10	10	10	10	10	15	15
BLR	24	24	24	24	24	24	18	18	18	18
BiH	10	10	10	10	10	10	10	10	10	10
BGR	15	10	10	10	10	10	10	10	10	10
CRO	20	20	20	20	20	20	20	20	20	20
CZE	24	24	21	20	19	19	19	19	19	19
EST	23	22	21	21	21	21	21	21	21	20
HUN	16	16	16	16	19	19	19	19	19	19
UVK	20	20	20	10	10	10	10	10	10	10
LVA	15	15	15	15	15	15	15	15	15	15
LTU	15	15	15	20	15	15	15	15	15	15
MKD	15	12	10	10	10	10	10	10	10	10

MDA	15	0	0	0	0	0	12	12	12	12
MNE	9	9	9	9	9	9	9	9	9	9
POL	19	19	19	19	19	19	19	19	19	19
ROU	16	16	16	16	16	16	16	16	16	16
RUS	24	24	24	20	20	20	20	20	20	20
SRB	10	10	10	10	10	10	10	15	15	15
SVK	19	19	19	19	19	19	19	23	22	22
SVN	25	23	22	21	20	20	18	17	17	17
TUR	20	20	20	20	20	20	20	20	20	20
UKR	25	25	25	25	25	25	21	19	18	18

(Source: author processing based on data from KPMG,
Kosovo-Law on corporate income tax, Moldova-Fiscal Code)

In many CESEE countries, along with standard corporate tax rate are found tax systems that involve reduced rates, taking into account the activity domain, the typology of companies, the area where the companies operate, the investment regime.

In this respect, we note the following (KPMG, 2015a): in Belarus it applies reduced rates of taxation for activities in the field of high technologies (10%), for residents of free economic zones (9%) and for members of Science and Technology Association established by the State University (5%); in Croatia, under special schemes to boost investment, companies benefit of a total exemption from corporate tax or a reduction the tax rate to 50% or 70% for a period of up to 10 years and until 31 December 2016 companies registered in tax-free zones benefit of a decrease by 25% of the tax rates; in Czech Republic it applies special tax rates for profit funds, respectively 5% where at least 90% of the fund´s property is invested in investment securities and 0% to pension funds; Hungary applies a progressive corporate tax system, respectively a tax rate of 10% for taxable income up to HUF 500 million (approximately USD 1,800,000) and a tax rate of 19% for taxable income exceeding HUF 500 million; in Latvia, the companies operating in the four regions named Special Economic Zones benefit from a reduction of corporation tax of 80% and the very small companies with an annual turnover less than EUR 100,000 may opt for a tax system related to the turnover in rate of 11%; in Lithuania is practiced a tax rate of 5% for agricultural companies and small companies having average number of employees up to 10 and an income up to LTL 1,000,000 (EUR 289,620) and a tax rate of 0% for social companies and companies established in free economic zones; in Macedonia are exempt from taxation the companies investing in technological industrial zones for a period of 10 years; in Romania, alongside the standard corporate tax rate of 16% can be found the fiscal regime for micro – enterprises, respectively 3% on the income received and fiscal regime for taxpayers involved in activities related to nightclubs, casinos and discotheques who are obliged to pay a tax of 5% of the revenues derived from those activities, in the case of the relevant profit tax is lower than 5% of the revenues derived from those activities; in Ukraine, for income obtained by the companies from long–term life insurance, private medical and pension insurance it applies a tax rate of 0%, for income obtained by insurance companies from other insurance activities it applies a tax rate of 3% and the eligible domestic agricultural producers may choose to pay a fixed tax.

Noteworthy situations regarding company tax regime are also those in: Russia, where the standard rate of corporation tax contains both federal part - 2% and regional part - with values between 13.5% and 18% (KPMG, 2015a); Moldova, where since 1 January 2012 was eliminated the tax rate of 0%, a rate destined to attract FDI and has been introduced the tax rate of 12% of taxable income for legal entities, the tax rate of 7% of taxable income for peasant households (farmer), and the tax rate of 15% for the gross income recorded in the accounts of a taxpayer that exceeds the estimated revenue (The Fiscal Code of Moldova, 2015).

An important place in the direct taxation is that of personal income tax, taking into account the number and structure of individual taxpayers, the categories of income subject to taxation, the level of taxable income, the relationship between income earned and time dimension to achieve them, the system of deductions, the compulsory social insurance contributions, the horizontal and vertical equity in taxation.

In terms of personal income taxation, many studies and researches make reference to the tax form practiced, respectively taxation through flat rate or taxation through progressive rates, being specified the advantages and disadvantages for each form. Although it is not easy to identify the optimal form of personal income tax, public policy makers should consider: the relationship between the cost of administration, the level of voluntary compliance, the size of tax evasion and the fiscal equity (Fuest, Peichl and Schaefer, 2007); the change in taxpayer behavior depending on the level of taxation and the deductions system (Cook, Meyer and Reichenstein, 2015); the form of taxation that reduces work effort (Sandmo, 1983); possibility of establishing a tax scheme that combines taxation through flat rate with progressive taxation (Candamio and Rodríguez, 2014).

If the global average corporate tax rate has registered over the last decade a substantial reduction, the global average personal income tax recorded a decrease of only 1.3 percentage points, from 32.68% in 2006 to 31.38% in 2015 (KPMG, 2015b). Evolution of average personal income tax in CESEE countries, as resulted from Fig. no. 2, show a tendency to fiscal relaxation in most states, but its level remains well below global or European average.

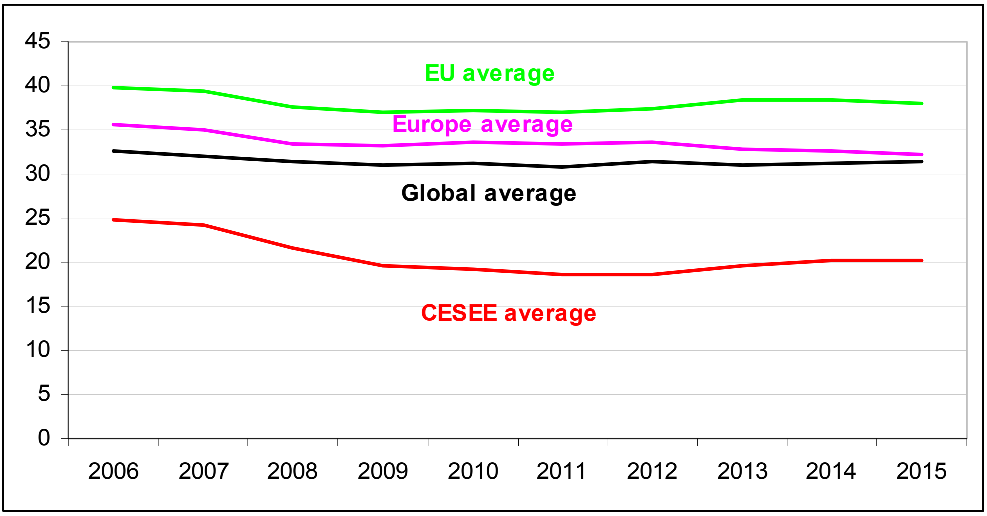

Fig. no. 2 Evolution of the average personal income tax rate
(Source: author processing based on data from KPMG, Trading Economics, Eurofast, Kosovo - Law on corporate income tax, Moldova - Fiscal Code)

From the data presented in Tab. no. 2, most CESEE countries has retained the taxation form for personal income in the period 2006-2015 (taxation through flat rate or taxation through progressive rates), except Albania, Belarus, Bulgaria, Czech Republic, Hungary, Macedonia and Slovak Republic where the tax regime was changed. However, it is noted that since 2008 more CESEE countries the personal income taxation is made based on the flat tax (see Fig. no. 3).

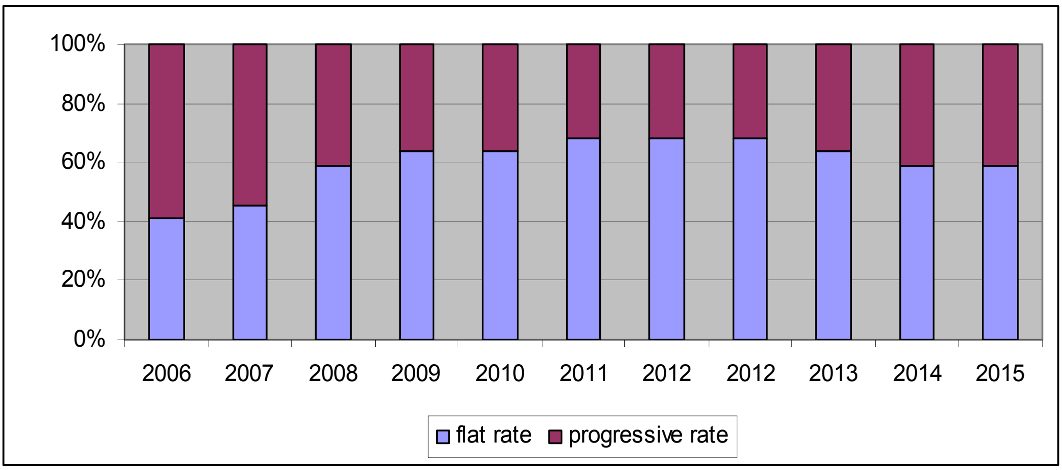

Fig. no. 3 Structure of personal income tax system in CESEE countries
(Source: author processing based on data from KPMG, Trading Economics, Eurofast, Kosovo - Law on corporate income tax, Moldova - Fiscal Code)

Even though the average tax rate for personal income taxation in CESEE countries has changed, the minimum and maximum level recorded in 2015 is the same as the level recorded in 2006, respectively 9% in Montenegro and 50% in Slovenia.

Tab. no. 2 Top marginal personal income tax rate in CESEE countries (%)

CESEE countries	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
ALB	20	25	10	10	10	10	10	10	23	23
BLR	30	30	30	12	12	12	12	12	12	13
BiH	10	10	10	10	10	10	10	10	10	10
BGR	24	24	10	10	10	10	10	10	10	10
CRO	45	45	45	45	40	40	40	40	40	40
CZE	32	32	15	15	15	15	15	22	22	22
EST	23	22	21	21	21	21	21	21	21	20
HUN	36	36	36	36	32	16	16	16	16	16
UVK	20	20	20	10	10	10	10	10	10	10
LVA	25	25	25	23	26	25	25	24	24	23
LTU	33	27	24	15	15	15	15	15	15	15
MKD	24	12	10	10	10	10	10	10	10	10
MDA	20	20	18	18	18	18	18	18	18	18
MNE	9	9	9	9	9	9	9	9	9	9
POL	40	40	40	32	32	32	32	32	32	32
ROU	16	16	16	16	16	16	16	16	16	16
RUS	13	13	13	13	13	13	13	13	13	13
SRB	10	15	15	15	15	15	15	15	15	15
SVK	19	19	19	19	19	19	19	25	25	25
SVN	50	41	41	41	41	41	41	50	50	50
TUR	35	35	35	35	35	35	35	35	35	35
UKR	13	15	15	15	15	17	17	17	17	20

flat rate	progressive rate

(Source: author processing based on data from KPMG, Trading Economics, Eurofast, Kosovo - Law on corporate income tax, Moldova - Fiscal Code)

Without specifying personal income taxation in all CESEE countries, we consider noteworthy particularities from: Albania, where the progressive system is used only for income from salaries and other compensations deriving from labour agreements, with 3 tax rates (0%; 13%, 23%), and other kind of incomes are taxed at a flat tax of 15% (Eurofast, 2015); Czech Republic, where the flat tax of 15% it applies for the income of an employee not exceeding CZK 1,242,432 annually - about 50,000 EUR (respectively, for 48 times the average wage), and for the income exceeding this ceiling is charged an additional solidarity tax of 7% (Alexio, 2015); Montenegro, where for the income from wages is used standard rate of 9%, plus an additional tax for monthly salary above 720 EUR (Deloitte, 2015); Russia, where the standard rate of 13% applies for the resident individuals and 30% for non-resident individuals (KPMG, 2015b); Serbia, where progressive tax system takes into account the average annual wage, so that the total annual taxable income of up to 3 times the average annual salary is exempt from income tax, and the maximum tax rate of 15% applies to the total annual taxable income exceeding 6 times the average annual salary (Eurofast, 2015).

3. Indirect Taxation in CESEE countries

Since the appearance of consumption taxes up to the present, in many research studies are analyzed criteria that must be taken into account in order to establish an optimal structure of the tax system. In this respect, efficiency, equity, administrative simplicity and usefulness for stabilization policies are the criteria unanimously accepted for evaluating alternative tax structures (Atkinson and Stiglitz, 1972).

The relationship between direct taxation and indirect taxation is inextricably linked to value added tax, the main tax related to consumption. If in the early 60s the value added tax was found in a relatively small number of countries, now this tax is included in the tax system in more than 130 countries, becoming for many of these a significant source for the formation of public financial resources (Keen and Lockwood, 2010).

Any change in the VAT tax regime must be based on substantial and relevant analysis, taking into account the VAT place and role in the formation of public financial resources and the repercussions of this tax on the final consumer.

The impact of financial crisis on public finances resulted in more fiscal policy decisions to increase indirect taxation, a form of taxation very often considered as certain and significant source of income for the public budget. This aspect can be observed in Fig. no. 4, when as opposed to the average tax rate of direct taxes, the average tax rate of VAT has increased in the period 2006-2015.

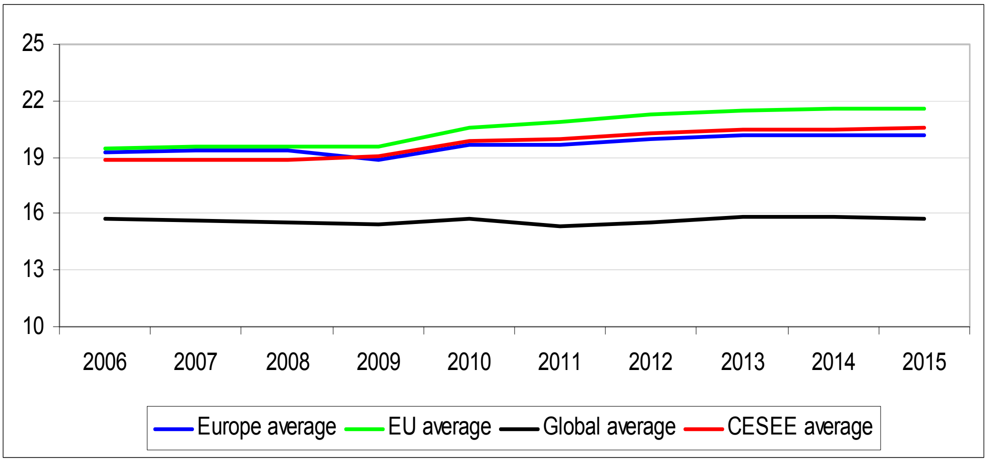

Fig. no. 4 Evolution of the average rate of indirect taxation
(Source: author processing based on data from KPMG, Trading Economics, Eurofast, Tax Administration of Kosovo and The Fiscal Code of Moldova)

From the perspective of fiscal policy of the European Union, VAT and excise duties are subject to tax harmonization, so that through EU Directives are established clear and precise rules to be applied by all Member States regarding the tax base and tax rate (Council Directive, 2006). For this reason, the standard VAT rate trend in CESEE countries is similar to standard VAT rate trend in the EU, as shown in Tab. no. 3.

Tab. no. 3 Standard VAT rate in CESEE countries (%)

CESEE countries	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
ALB	20	20	20	20	20	20	20	20	20	20
BLR	18	18	18	18	20	20	20	20	20	20
BiH	17	17	17	17	17	17	17	17	17	17
BGR	20	20	20	20	20	20	20	20	20	20
CRO	22	22	22	22	23	23	25	25	25	25
CZE	19	19	19	19	20	20	20	21	21	21
EST	18	18	18	18	20	20	20	20	20	20
HUN	20	20	20	20	25	25	27	27	27	27
UVK	15	15	15	16	16	16	16	16	16	18
LVA	18	18	18	21	21	22	21	21	21	21
LTU	18	18	18	19	21	21	21	21	21	21
MKD	18	18	18	18	18	18	18	18	18	18
MDA	20	20	20	20	20	20	20	20	20	20
MNE	17	17	17	17	17	17	17	19	19	19
POL	22	22	22	22	22	23	23	23	23	23

ROU	19	19	19	19	24	24	24	24	24	24
RUS	18	18	18	18	18	18	18	18	18	18
SRB	18	18	18	18	18	18	20	20	20	20
SVK	19	19	19	19	19	20	20	20	20	20
SVN	20	20	20	20	20	20	20	22	22	22
TUR	18	18	18	18	18	18	18	18	18	18
UKR	20	20	20	20	20	20	20	20	20	20

(Source: author processing based on data from KPMG, Trading Economics, Eurofast, Tax Administration of Kosovo and Fiscal Code of Moldova)

It is noted that in tax system of all CESEE countries the value added tax can be found (KPMG, 2015c) and the minimum standard rate imposed on EU member states (European Commission, 2015), respectively 15% is achieved also in countries that are not part of the EU.

Considering the repercussion of value added tax on the final consumer, most CESEE countries practice alongside the standard rate of VAT, reduced VAT rates or establishes categories of goods and services exempt from VAT. Reduced VAT rates or exemption from VAT is the prevalent for foodstuffs, pharmaceutical products, books, medical and dental care, educational services, financial services, insurance and reinsurance services, social housing and tourism services.

With a standard VAT rate of 17%, Bosnia and Herzegovina is the only CESEE country that does not practice reduced VAT rates, but the export of goods is zero-rated and certain categories of services are exempt from VAT, such as: the leasing and subletting of residential houses, apartments, and residential premises for a period of longer than 60 days; financial services; insurance and reinsurance services; educational services; postal services (PwC, 2015). Turkey is the only CESEE country who practice alongside the standard VAT rate of 18%, a reduced VAT rate of 8% (for basic foodstuffs, medical products, books and other) and a super reduced VAT rate of 1% for agricultural products, certain residential properties, newspapers and periodicals (Avalara, 2015).

4. The tax burden versus fiscal freedom in CESEE countries

For each country, a special importance by economic, financial and social point of view is owned by the part of gross domestic product taken to the state through taxes, respectively the tax burden. Thus, to determine the level of taxation are taken into account taxes (personal income taxes, corporate income taxes, value added taxes, excise taxes, tariffs) and other revenues received by the national government (social contributions, grants and net revenues from public enterprises). According to rankings made by the Central Intelligence Agency, based on estimations for 2014 (CIA, 2015) it is observed that CESEE countries have a very different level of tax burden, with values between 51.1% (in Hungary) and 16.8% (in Poland), thus occupying very different positions among the 214 jurisdictions analyzed, as shown in Fig. no. 5.

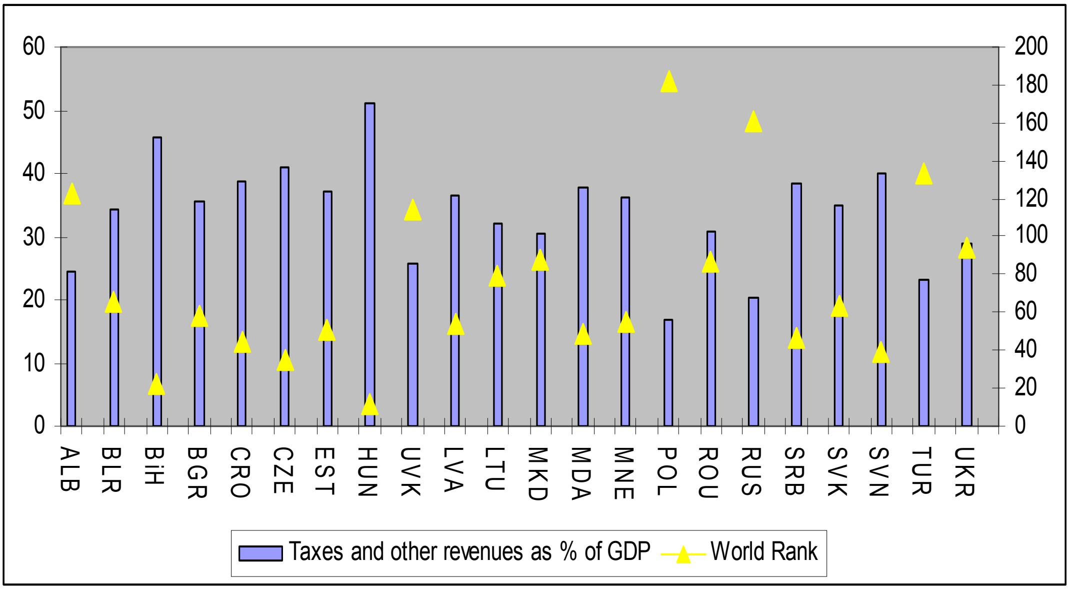

Fig. no. 5 Taxes and other revenues records as % of GDP from CESEE countries, in 2014
(Source: CIA, The World Factbook, 2015)

As an essential component in the life of any nation, taxation contributes significantly to establishing the level of economic freedom. Thus, among the 10 qualitative and quantitative indicators taken into account in determining the Index of Economic Freedom is identified the fiscal freedom (the top tax rates on individual incomes; the top tax rates on corporate incomes; the overall amount of tax revenue as a percentage of GDP) which, together with the government spending indicates the level for Limited Government (Heritage Foundation, 2015). Also, the indicator top marginal tax rate (the top marginal income tax rate; the top marginal income and payroll tax rate) is taken into account in determining the level for Size of Government, an essential component of the report Economic Freedom of the World (Gwartney, Lawson and Hall, 2015).

By analyzing the data for CESEE countries from the 2015 Index of Economic Freedom for overall score (Heritage Foundation, 2015), as can be seen from Fig. no. 6, is found the following: 59.09% of countries are in the moderately free area, with the highest value in Latvia (69.7); Czech Republic, Lithuania and Estonia are in the mostly free area; Russia, Moldova and Bosnia- Herzegovina are in the mostly un-free area; Ukraine and Belarus are in the repressed area; Kosovo is not included in the rankings.

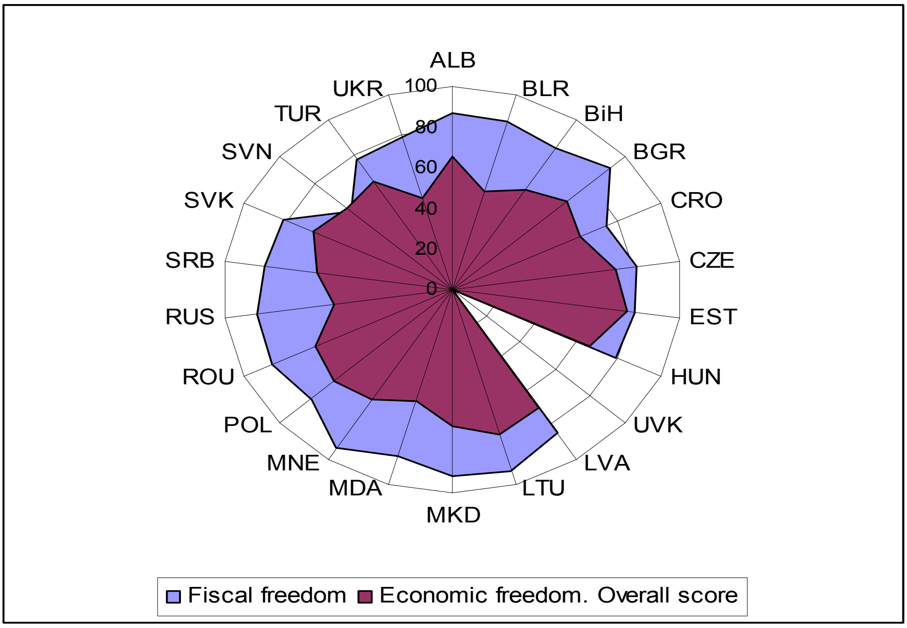

Fig. no. 6 Index of Economic freedom (overall score) and Fiscal freedom from CESEE countries in 2015

(Source: Heritage Foundation, 2015 Index of Economic Freedom)

From the perspective of the fiscal freedom index (Heritage Foundation, 2015), the situation is totally changed, as can be seen from Fig. no. 6, so that: most countries (72.72%) are in the free area, with the highest value in Albania (87.2); Croatia, Hungary, Turkey and Ukraine are in the mostly free area; Slovenia is in the mostly un-free area; Kosovo is not included in the rankings.

5. Conclusions

Based on the data presented above and in close correlation with the main macroeconomic indicators, we believe that fiscal decisions in CESEE countries should consider improving the growth rate of GDP, reducing unemployment, reduction of inflation and increasing the volume of foreign direct investment. The direct link between tax indicators and the main indicators of economic growth (World Bank, 2015) can be seen from Tab. no. 4.

Tab. no. 4 The highest level and the lowest level of the macroeconomic indicators from CESEE countries

Indicators	Highest level		Lowest level	
Taxes and other revenues as	Hungary	51,1 %	Poland	16,8%
	Bosnia and Herzegovina	45,7%	Russia	20,2%

% of GDP (2014)	Czech Republic	41,0%	Turkey	23,3%
Top marginal corporate tax rate (2015)	Slovak Republic	22%	Montenegro	9%
	Croatia, Estonia, Russia, Turkey	20%	Bosnia and Herzegovina, Bulgaria, Kosovo, Macedonia	10%
	Czech Republic, Hungary, Poland	19%	Moldova	12%
Top marginal personal income tax rate (2015)	Slovenia	50%	Montenegro	9%
	Croatia	40%	Bosnia and Herzegovina, Bulgaria, Kosovo, Macedonia	10%
	Turkey	35%	Belarus, Russia	13%
The standard VAT rate (2015)	Hungary	27%	Bosnia and Herzegovina	17%
	Croatia	25%	Kosovo, Macedonia, Russia, Turkey	18%
	Romania	24%	Montenegro	19%
GDP growth-annual % (2014)	Bosnia and Herzegovina	4,4%	Ukraine	-14,6%
	Czech Republic	4,3%	Belarus	-4,4%
	Turkey	3,8%	Russia	-4,1%
Unemployment, total - % of total labor force (2013)	Kosovo	35,3%	Moldova	5,1%
	Macedonia	29,0%	Russia	5,6%
	Bosnia and Herzegovina	28,4%	Belarus	5,8%
Inflation, consumer prices - annual % (2014)	Ukraine	12,2%	Montenegro	-0,7%
	Turkey	8,9%	Bosnia and Herzegovina	-0,9%
	Russia	7,8%	Bulgaria	-1,4%

(Source: author processing based on data from KPMG, Trading Economics, Eurofast, World Factbook, Tax Administration of Kosovo, Fiscal Code of Moldova, and World Bank)

Evolution of macroeconomic indicators from CESEE countries highlight the link between taxation and economic growth, link proven by the specialized literature, namely: within a framework of endogenous growth, it is considered that inflation is a problem of public finances, respectively an inefficient tax system causes a high rate of inflation (De Gregorio, 1993); non-distortionary taxation and productive expenditures positively influence the economic growth (Kneller, Bleaney and Gemmell, 1999);

reducing the corporate tax rate and increasing personal income tax rate reduces the entrepreneurial activity and thus diminishes the economic growth (Johansson, Heady, Arnold, Brys and Vartia, 2008); replacing progressive taxation with flat taxation, by significantly reducing the top marginal personal income tax rate, allow increased consumption or investment, which determines an economic growth (Mele and Carbone, 2015); taxes and other revenues as % of GDP, top marginal corporate tax rate and top marginal personal income tax rate are indicators with great influence on the economic freedom index (Heritage Foundation, 2015).

In these conditions, are noteworthy measures taken in: Czech Republic, that although it has recorded a high value for taxes and other revenues as % of GDP, fiscal relaxation measures since 2008 (reducing the top marginal corporate tax rates and flat tax introduction for personal income) along with the increased demand for goods produced in the Czech Republic has positively influenced economic growth; Bosnia and Herzegovina, which upon social and economic crisis suffered by war sought to improve economic opportunities and promoting a favorable business environment (agriculture, wood products and tourism are the sectors with the greatest potential for growth) thus practicing a low level of taxation; Romania, which in the last period has maintained the flat tax and proceeded to reduce indirect taxation, thus being recorded the highest rate of GDP growth in the EU, consumption became the main catalyst for growth.

Without claiming an exhaustive approach, we consider that issues raised in this article emphasizes once more that taxation remains an essential component in the life of any nation, a component with major impact on economic growth and development.

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