Taking into account the deduction at source of income tax in *Conjoncture in France*

In January 2019 the way income tax is collected in France will be transformed, with the introduction of a system of deduction at source. This reform will have an impact on the aggregates for households in the Conjoncture in France reports. This Focus article explains the accounting techniques used to handle this new reform, focusing solely on those aspects affecting analysis of the short-term economic outlook.

Deduction at source will change the dates of tax collection, but not of tax calculation.

Until 2019, household income tax was levied monthly (in ten instalments) or by quarterly instalments (three payments), with the outstanding balance settled at the end of each year. Moreover, the tax owed for year N was based on the income declared for year N-1, charged at a rate calculated following the tax declaration submitted in the spring of year N. From 2019 onwards, income tax will be collected monthly (over twelve months) for the majority of taxable households and the majority of regular income. For fixed income, tax will be levied at the rate determined by the previous year's declaration while the actual sum deducted will depend on contemporary income. Finally, certain tax credits will be paid in a first instalment of 60% in January 2019, with the outstanding balance settled in July.

The effect of these new collection dates on the total value of income tax will be neutralised by the methods used to adjust for seasonal variation.

The majority of the economic aggregates analysed in the Conjoncture in France reports present pronounced seasonal variation. For example, household consumption is greater in the festive period at the end of the year, while energy production and consumption are greater in winter than in summer. But these 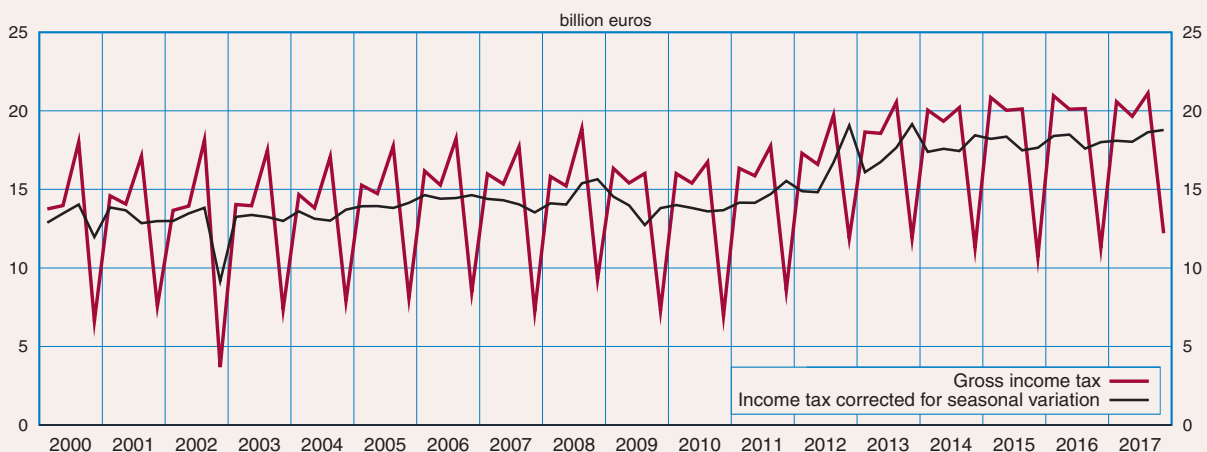periodic variations are in no way indicative of a weaker or stronger economic outlook. For this reason, the series in question are corrected for seasonal variation[1] to make them analytically pertinent.

Income tax is subject to seasonality induced by the tax collection calendar (*Graph*). Correcting for seasonal fluctuations cancels out the effect of these dates on the series as a whole. Finally, our analysis of the short-term outlook for income tax is limited to measuring variations in the sums collected which can be attributed to non-seasonal phenomena (or, to put it differently, factors already corrected for seasonal variation): fluctuations in payroll employment, changes to the tax brackets, etc.

The introduction of deduction at source, for those forms of income affected, will permanently alter the tax collection calendar. As a result, the outlook analysis would become incomprehensible if the seasonal correction measures previously applied were maintained; these are constructed on the basis of past data. To avoid any incoherency between the new collection calendar and the seasonal correction, the quarterly seasonal fluctuations in income tax will be neutralised in the accounting forecasts of *Conjoncture in France* from 2019 onwards, with fluctuations smoothed from one quarter to the next based on an annual target for variation in the total value of tax (see below). Similarly, the payment of tax credits, including the 60% instalment, will be spread across the whole year (as was the case previously). Finally, our analysis of these series, for those forms of income affected by deduction at source, will continue to function as it has done in previous issues of Conjoncture in France, i.e. without taking account of collection dates or tax credit payment dates.

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1. For a description of the methods employed, see *Insee Méthodes* n°126.

Income tax: raw monthly figures and figures corrected for seasonal variation

billion euros

Gross income tax
Income tax corrected for seasonal variation

Source: comptes nationaux trimestriels, INSEE

The total annual income tax paid by households should increase slightly

Above and beyond variations of a seasonal nature, the tax base for sums levied at source will now be contemporary. As such, the tax levied in 2019 will be deducted from income for the current year, not income for 2018. In theory, the total size of the payroll on which income tax is levied should be larger in 2019 than in 2018, as a result of the increase in employment and average wages. The budget bill for 2019 predicts a nominal increase of 4.0% for income tax in 2019, a figure which could be at least partly attributed to the change in collection system. As a result, the Conjoncture in France forecast for the total value of household income tax is for a nominal increase of 4.0% in 2019. This increase will be spread across the year, in line with the usual procedure.

The introduction of deduction at source could have unpredictable effects on consumption

Aside from the accounting changes required by this measure, the new monthly schedule for income tax collection, as well as the tax credit instalment, could nonetheless have a positive effect on household cash flow at the start of the year. In this case, household consumption might be more dynamic in the short term. On the other hand, this unprecedented and substantial transformation could provoke a wait-and-see attitude among households, prompting them to make precautionary savings. All in all, the effects of deduction at source on consumption are beset by a degree of uncertainty which cannot be counteracted by reference to similar precedents. ■

Bibliography

INSEE (2012) "Methodology of quarterly national accounts", Insee Méthodes n°126 - May ■