

Institution: University of Southampton
Unit of Assessment: 18 Economics and Econometrics
Title of case study: 18-02 Labour Earnings: Taxes, Regulation and Giving. Shaping Labour Market Policies of European Governments and Global Institutions
<p>1. Summary of the impact</p> <p>Southampton based research on the interactions of a minimum wage policy and tax evasion has had a direct and clearly acknowledged impact on shaping the labour market policies of Hungary and other Southern European countries, while its research on the role of universal versus targeted benefits on employment has had a significant impact on Swedish fiscal policy. Looking at labour market policies in a broader context and from a behavioural economics point of view (e.g. payroll giving), our findings on charitable giving and workers' motivation have also been used by the UK government's Behavioural Insights Team and impacted its recommendations on giving. The same research is currently influencing US policy on the tax treatment of charitable contributions.</p>
<p>2. Underpinning research</p> <p>Labour market institutions - the rules, practices and policies governing labour markets and its participants - play an influential role in macroeconomic performance. They cover wage-setting institutions, mandatory social benefits, the unemployment insurance system and labour legislation, including minimum wage and employment protection legislation.</p> <p>Research by Dr Mirco Tonin, senior lecturer in Economics at the University of Southampton, focuses on evaluating the effectiveness of labour market policies in maximising economic performance. Tonin began this research at Stockholm University and developed and completed it at Southampton, which he joined in September 2007. The first strand of his work focused on the relationship between minimum wage legislation and tax evasion, and came to the unexpected conclusion that introducing or increasing a minimum wage can actually reduce people's disposable income [3.1, 3.5]. This is because it is common in developing and transition countries for people to underreport earnings in order to avoid paying tax on them. When minimum wage legislation is passed the tendency is to increase compliance rather than go underground completely. This produces a significant rise in declared earnings at the minimum-wage level, but the workers who appear to be receiving a higher wage are actually losing income as they swap undeclared earnings for declared, and therefore taxable, ones.</p> <p>Tonin's research into in-work benefits such as tax credits [3.2], which are designed to alleviate poverty while simultaneously boosting employment levels by creating incentives to work was carried out in collaboration with Ann-Sofie Kolm, Professor of Economics at Stockholm University. In-work benefits are increasingly common around the world, so this was a timely model for understanding their ability to make the labour market more efficient and finding the best way to finance them and set their levels. This research showed how universal benefits could be more effective than targeted benefits in fighting unemployment and encouraging participation in the labour market.</p> <p>Further research by Tonin explored employment protection legislation and was carried out jointly with Sandrine Cazes [3.4], Head of the Employment Analysis and Research Unit of the ILO. It looked at legislation in areas such as regular contracts, temporary contracts and collective bargaining to determine their impact on job tenure across the European Union. The analysis found evidence of a trend in many countries towards shorter tenure among young workers, associated with a weakening of employment protection laws and the protection provided by trade unions. This research called for a strengthening of employment protection for young people against the risk of job loss.</p> <p>A fourth research strand of Tonin's work looked at labour markets from a behavioural point of view. In this context, his core project featured a field experiment into workers' motivation [3.3, 3.6]. With</p>

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ESRC funding, Tonin devised the experiment with Dr Michael Vlassopoulos, Lecturer in Economics since 2007. They recruited subjects from among the university's students, targeting equal numbers of males and females, by offering them paid work inputting computer records. Participants were offered the chance to donate some of their earnings to charity in a way that allowed the effect of this altruistic motivation to be measured. The experiment produced evidence that what's known as warm-glow altruism – when helping others confers a sense of personal satisfaction – was instrumental in increasing effort by female workers but generally had no effect on males. These findings helped explain the overall gender earnings gap on the basis of gender differences in preferences rather than differences in household responsibilities, career interruptions, or discrimination. Thus, it suggests that policy interventions may not fully succeed in closing the gap.

3. References to the research (indicative maximum of six references)

- 3.1 Tonin, Mirco, 'Minimum Wage and Tax Evasion: Theory and Evidence', *Journal of Public Economics*, volume 95 (2011), issue 11-12, pages 1635–1651. (Refereed Journal)
- 3.2 Kolm, Ann-Sofie and Mirco Tonin, 'In-Work Benefits and Unemployment', *International Tax and Public Finance*, volume 18 (2011), issue 1, pages 74-92. (Refereed Journal)
- 3.3 Tonin, Mirco and Michael Vlassopoulos, 'Disentangling the Sources of Pro-socially Motivated Effort: A Field Experiment', *Journal of Public Economics*, volume 94 (2010), issue 11-12, pages 1086-1092. (Refereed Journal)
- 3.4 Cazes, Sandrine and Mirco Tonin, 'Employment Protection Legislation and Job Stability: A European Cross-Country Analysis', *International Labour Review*, volume 149 (2010), issue 3, pages 261-285. (Refereed Journal)
- 3.5 Tonin, Mirco, 'Too Low to Be True: The Use of Minimum Thresholds to Fight Tax Evasion': in C. Fuest and G. Zodrow (Eds.), *Critical Issues in Taxation and Development*, 2013, MIT press. (Book chapter- refereed by editors and external referees).
- 3.6 Tonin, Mirco and Michael Vlassopoulos, 'Social Incentives Matter: Evidence from an Online Real-Effort Experiment', IZA Discussion Paper (2012) [Revised & Resubmit at Management Science].

ESRC Research Grant:

Tonin Mirco and Michael Vlassopoulos secured ESRC funding on 'An Investigation into the Sources and Implications of Pro-social Behaviour', 2009- 2011, RES-061-25-0461, £242,142.

4. Details of the impact

The University of Southampton's research on labour market instruments and worker motivation has been used widely by the US and several European governments and international agencies to help shape their economic policies (e.g. Hungary, Sweden, International Labour Organisation, OECD, World Bank), and has featured in the mainstream media to describe the latest thinking about the world of work. Moreover, the findings about what drives altruistic behaviour generated substantial interest among those concerned with charitable giving and other forms of philanthropy, as well as among policymakers in UK (Behavioural Insights Team of the UK Cabinet Office) and the US (Senate and House of Representatives).

Tonin's work on minimum wage legislation and tax evasion has been acknowledged by the Hungarian government (Tibor Draskovics, Minister of Justice and Law Enforcement), which used it in what it called its 'whitening' of the hidden economy project, that is, putting the black or illicit economy on a formal, open basis. During the early 2000s, the minimum wage affected directly 14% of employees in the country. The work has also been used by the World Bank and the Organisation for Economic Co-operation and Development (OECD) to underline the role of the minimum wage as an important policy tool for reducing undeclared work in other countries (e.g.

Turkey and Romania. See, World Bank, 2009, 'Reducing Undeclared Work in Turkey'[p. 32], and OECD Development Centre, 2008, Informal Employment in Romania [p.57]). Moreover, the OECD used the research to assess the role of the minimum wage as a policy tool in a wider context, citing the work in its 2008 Employment Outlook, where it suggested the introduction of a discounted minimum wage for workers with limited labour market experience. Tonin's work on the minimum wage also features as a chapter in Critical Issues in Taxation and Development, a volume published by MIT Press, investigating crucial challenges confronted by developing countries in raising revenues.

The Swedish Fiscal Policy Council, which is tasked with providing independent evaluation of the Swedish government's fiscal policies, cites in its 2009 (page 256) and 2010 (pages 174-175) reports the research on the impact of in-work benefits. These reports are presented to government and to parliament in Sweden to guide their policy deliberations. The Council used the research to support the extension of the benefits. The work has also been used in a report to the Swedish Ministry of Finance on 'Swedish Tax Policy: Recent Trends and Future Challenges' (2010, page 214). In line with the research recommendations, the tax credit has been gradually expanded in several steps since its introduction in 2007, becoming, in the government's own words, 'the single most important reform... to get more people working and reduce exclusion'. The research was also used in a report to the European Commission (2010) on 'Modelling of Labour Markets in the European Union' (page 33) to assess the use of active labour market policies in the European context.

Further evidence that the research in Kolm and Tonin (2011) has shaped government employment policy can be found in a recent report from the Economic Affairs Department at the Swedish Ministry of Finance. Such reports provide detailed analyses of economic policy matters that serve as the basis for government policy. The December 2011 report titled 'How should the functioning of the labour market be assessed?' highlights the importance of the research of Kolm and Tonin (2011) in its role for better understanding the role of taxes on labour force participation.

Tonin's research on the impact of employment protection on job tenure has been used by the ILO; The Head of its Employment Trends Unit, Dr Ekkehard Ernst, says it '*has proven to be very helpful to underpin policy recommendations brought forward in my unit... [the] analysis has been very valuable in informing our policy discussion on the role of employment protection in high unemployment rates for young people in Southern European countries.*' The research has also been used in the ILO report, Global Employment Trends for Youth (2010, page 19), to analyse the impact of the global economic crisis on young people and provide policy recommendations and in the ILO World of Work Report 2012 (2012, pages 42-43). The research has also been discussed in the OECD report, Off to a Good Start? Jobs for Youth (2010), to help shape a new agenda of youth-friendly employment policies and practices.

Besides the above traditional labour market policy oriented research Tonin's work has also expanded into the more novel area of behavioural economics, looking at workers motivation and pro-social behaviour in the context of labour market policies. With growing governmental interest in policy recommendations in areas such as payroll giving Tonin's work in this area has been picked up by policy makers from both sides of the Atlantic.

The influence of Tonin's research on charitable giving and worker motivation for instance has been acknowledged by the Behavioural Insights Team of the UK Cabinet Office in drawing up its 2011 White Paper on Giving, which sought to renew Britain's culture of philanthropy. The same research has also been used by the Joint committee on taxation of the US congress [p. 36] to evaluate the policy related to the federal tax treatment of charitable donations and presented to the House Committee of Ways and Means (February 11, 2013). The committee on Ways and Means is the main committee in the US congress whose role is to write tax policy.

This research also attracted widespread media coverage, with the emphasis on gender disparities

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in worker motivation, from 2010 onwards, including in The Independent on Sunday, The Daily Telegraph, The Economist, The Wall Street Journal, Grazia and on the website of Philanthropy UK. In addition, various aspects of Tonin's research have been presented to several institutions directly linked to policymaking, including the German Federal Employment Agency, the ILO, the World Bank, the Hungarian Central Bank, the Bank of Estonia and the Lithuanian Institute of Labour and Social Research. All these presentations, made by Tonin from 2008 onwards, related to the research on the minimum wage and tax evasion, with the exception of the presentation to the ILO, which dealt with employment protection legislation.

More generally, Tonin has been asked to comment, on the basis of his expertise in labour market regulations, on current economic matters in media outlets that include Time, The Ottawa Citizen of Canada, Il Gazzettino of Italy and UniNews, the magazine of UniCredit Bank.

5. Sources to corroborate the impact

Official Reports:

- 5.1 ILO, 2012, World of work report 2012: Better jobs for a better economy, Geneva, ISBN 978-92-9251-010-7 (research cited at pages 42-43).
- 5.2 OECD, 2008, Employment Outlook, Chapter 2, ISBN 978-92-64-04632-0 (research cited at pages 92 & 127).
- 5.3 World Bank, Hungary - Reducing Undeclared Employment in Hungary. Synthesis Report of the World Bank Study, 2008 (research cited at pages 30-31, 35).
- 5.4 Fiscal Policy Council, Swedish Fiscal Policy Report, 2010, ISBN 978-91-633-5211-9 (research cited at pages 174-175).

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- 5.5 Richard Alley, 'Caring, not cash. It's why women work', Daily Telegraph, 30 March 2010
- 5.6 Joint Committee on Taxation, Present Law and Background Relating to the Federal Tax Treatment of Charitable Contributions (JCX-4-13), 11 February 2013 and (JCX-55-11), October 14, 2011.

Users' Details:

- 5.7 Corroborating letter by the Chief, Employment Trends Unit, International Labour Office. (available upon request)
- 5.8 Research Fellow, Behavioural Insights Team, Cabinet Office – can verify the use of research by the Cabinet Office.
- 5.9 Deputy Chairman, Swedish Fiscal Policy Council – can confirm the use of research by the Swedish Fiscal Policy Council.
- 5.10 Corroborating letter by the former Minister of Justice and Law Enforcement in the Hungarian Government to confirm the use of research by the Hungarian Government. (available upon request)