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Motivation to work, labor income taxes and life satisfaction: Hungary, Estonia, Continental Europe and the United States

Orkhan Nadirov[a]*, Khatai Aliyev[b]

[a]*Tomas Bata University in Zlin, Faculty of Management and Economics, Zlin 760 01, Czech Republic*
[b]*Qafqaz University, Institute for Social Sciencies and Humanities, Khirdalan AZ0101, Azerbaijan*

Abstract

The primary findings of this paper are that the increase in hours worked per employee comes at the expense of life satisfaction, and differences in labor income taxes cannot account for differences in time allocation. Once life satisfaction is included, the hypotheses of previous neoclassical economic studies is almost irrelevant in determining the response of market hours to higher taxes. We find a negative relationship between hours worked across countries and life satisfaction. In the countries with the highest hours worked (Hungary, Estonia), leisure is generally preferred to wealth and in the lowest hours worked (France, Germany), wealth is preferred to leisure.

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1. Introduction

Recently, fervent arguments have been made in the United States and some European Union countries about taxation and labor supply. Most of the literature has focused on the impact of differences in labor market institutions. Blanchard and Summers (1986), Bentolila and Bertola (1990), and Blanchard and Jimeno (1995) have focused on the labor supply aspects of the role of institutions and labor market restrictions. However, Prescott (2002) disputes that differential taxation by itself might causes the differences in the current level of aggregate hours worked. For example, Prescott (2004) has identified the significance of tax rates in accounting for differences in labor supply for the major advanced industrial countries. Prescott's idea was defended by the statistical evidence of

* Orkhan Nadirov. Tel.: +420 776 831 939;.
E-mail address: nadirov@fame.utb.cz

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Davis and Henrekson (2003), who found that in wealthier countries a large labor supply leads to higher tax rates. Alberto et al. (2005) found that the impact of taxes on labor supply is negated by unionization management and labor market regulation. Ljungqvist and Sargent (2007, 2008a) found that unemployment benefits supplied by governments decreases the labor supply. Ohanian et al. (2008) apply Prescott's methodology to a larger sample of countries over a longer time span and conclude that much of the changing in hours worked over time and across countries can be clarified by taxes. Chen et al. (2015) contend that increases in labour taxes and unemployment benefits together explain roughly 75% of the declining labour supply in Europe relative to the United States over the past 3 decades.

This article begins with the basic facts on labor supply across countries (Hungary, Estonia, Germany, France). This paper provides an ample amount of evidence from both public finance and labor economics to draw certain conclusions. Numerous theoretical and empirical studies have identified a negative relation between tax rates (marginal and average) and work activity. However, 'work activity' is not same as 'motivation to work'. It comprises a more general explanation in comparison with work motivation. When we discuss 'work', we mean work in the market, not work overall; unpaid home production is part of ''non working time''.

Several interesting findings emerge in our paper, among them that differences in the motivation to work to tax-induced income changes are probably linked not only to the size of the labor income tax or to the characteristics of the labour market (culture, unionization, labor market regulations, generous welfare systems, unemployment compensation programs, etc.), but also to other factors that have not yet been efficiently explored. The primary finding of this section is perhaps that people who are more balanced in their approach to life are both happier and take more leisure. But a more persuasive story is that motivation to work has started to decline in Western Europe, due to high levels of life satisfaction, while in Eastern Europe motivation to work has started to increase because of low levels of life satisfaction.

The paper is organized as follows: Section 1 develops the theory; - Section 2 documents changes in hours worked, labor income tax and life satisfaction among Hungary, Estonia, France, Germany and the United States and presents quantitative findings. Section 3 concludes.

2. Theory Development and hypotheses

High tax rates and its impact on motivation to work is very broad and interdisciplinary. It draws on works from economics, accounting, psychology, and sociology. The topic is of great interest to academics, policy makers, and private-sector institutions worldwide. Because we are introducing psychological theory in addition to economic theory, this research can make a seminal contribution in the areas of taxation and economics. However, the research is not without challenges. This area has literally been researched for hundreds of years. But most of them has their own restiriction. We want to fill the gap in their studies. First, neoclassical economists only state individuals as rational agents who seek utility and maximal pleasure from their economic activities. Calibrations and numerical experiments (steady-state analyses) are used to test their predictions. Most of them are using coefficient values for analyisng the validity of their hypotheses, which is not fit to the real-economy parameters.

But, Veblen (1934) in his theory of the leisure class, he comprehended individauls as irrational, economic agents who follow up social status the prestige natural to a place in society with little regard to their own satisfaction. Especially, Veblen (1934) critised contemporary (19th-century) economic theoris, and indicated that economists should take account of how individuals behave, socially and culturally, rather than rely upon the abstractions of theoretic deduction to explain the economic behaviour of society (Veblen, 1934). Second, in the national tax debate, many ignore the effect of taxes on human motivation (Lowell Harris, 1985). But we know from Maslow's Hierarchy of Needs that one must satisfy lower level basic needs before progressing on to meet higher level growth needs (Maslow, 1943). Once these needs have been reasonably satisfied one may be able to reach the highest level called self-actualization. That is why, both of these theories are appealing in determining the differences of hours worked between these countries.

Following from the above discussion, it is hypothesized that:

H1.Even if labor income tax is the same between the highest hours worked countries and the lowest hours worked countries, there is a significant negative association between motivation to work and life satisfaction.