Lessons from the Mirrlees Review - remarks

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Relevant issues

- **MIRRLEES REVIEW – TAX BY DESIGN**
  - Very coherent, detailed programme
  - Based on empirical findings
  - But for a different environment

- **LESSONS FROM THE MIRRLEES REVIEW**
  - Identifies the most important differences
  - Informal economy
    - nothing is more distortive than tax evasion
  - „MISSING MIDDLE” – dual economy
  - Different elasticity of tax base – even in case of capital
    - traded vs. non-traded sector, tax evasion at smaller firms
Principles of the review

• See the system as a whole
  ▫ Very important
  ▫ Dilemmas may materialize in conflicts between taxes (e.g. progressive PIT vs. regressive SSC)
  ▫ Organizational questions may play a role

• Neutrality
  ▫ May conflict with differentiation by elasticity
    • an important dilemma in practice
    • played an increased role during the crisis

• Progressivity
  ▫ Even income taxes may target poorly...
Recipients of employment tax credit by households’ equivalent income
Flat tax

- **Empirical findings**
  - elasticity on the intensive margin – top PIT rate around (or even above) the revenue-maximizing rate?
  - many low-income individuals living in middle-income or rich households
  - underreporting of earnings (50% of minimum wage earners or even more)
  - groups with high extensive elasticity identified (unskilled, young, old workers, mothers of childbearing age)

- **Policy answer**
  - flat PIT and SSC
  - general employment tax credit abolished
  - broad targeted incentives for high-elasticity groups (tagging)
ACE or cash-flow tax?

- We prefer the cash-flow approach
  - simplicity
  - no disincentives for risk-taking
- Small business tax (KIVA)
  - cash-flow base
  - employers’ profit and payroll tax rate equalized
  - eligible, preferential for the majority
- Experiences
  - learning costs hinder the transition
  - hard to explain and compare with the existing system
Thank you!
Long-term Laffer curve for the top PIT rate

Own estimation based on the model of Benczúr-Kátay-Kiss (2012)
Wage distribution, wage survey vs. monthly SSC returns (2010)
Recipients of tax allowances by households’ equivalent income