TAX DESIGN IN THE MIDDLE INCOME COUNTRIES: LESSONS FROM THE MIRRLEES REVIEW

Ex-policymaker’s biased commentary from Poland

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Tax design
Share of tax and SSC in GDP, 2011
Tax design - PIT

Why a flat rate tax?
- simplicity?
- efficiency?
- fairness? Will it win in a national referendum?
- a sign of reforms?
- to prevent the politicians from doing stupid things?

Once you abandon proportional taxation, “you are at sea without rudder or compass, and there is no amount of injustice and folly you may not commit.”

John McCulloch
Tax design - PIT

PIT – Polish experience with non-flat and unfair PIT – case of self-employed vs employees. An example of bad policy

Till 2007 - 3 tax brackets: 19%, 30% and 45%; 95% taxpayers in the first bracket

From 2007 – 2 brackets: 18% and 32%; 98-99% taxpayers in the first bracket

From 2004 self-employed can use a flat 19% PIT
Tax design - PIT
Tax wedge in Poland - selfemployed (lump sum SSC + 19% PIT)
VAT – why does one rate occur so rarely?

Are we sure that one rate is *first best*? I assume YES, but:

- Redistribution
- Labour intensive services – shadow economy / barriers of entry – is a high threshold a solution? Pros and cons
- Why do advanced economies not have a uniform rate? Why has Slovakia abandoned one rate? Just politics? Or was it a rational choice taking into account efficiency, fairness and compliance?
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Key practical lessons:

Successes:
- Significant elimination of tax credits/deductions (e.g., for housing), but they reappeared as child credits
- Tax expenditure surveys
- Taxation of resources – case of copper and silver mining
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Key practical lessons:

Failures:
- No vision, no tax policy
- Excises
- Tax expenditures
- Farmers
- Immovable property taxation
- No formal body between MoF and taxpayers
- Tax wedge for employees and self-employed – already shown
- Inefficient tax administration
- And many many many more
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Key practical lessons:

Challenges:
- Taboo topics (e.g., cadaster tax, joint taxation of spouses)
- Taxation of small business – shadow economy

Practical issues:
- VAT on cars used both for private and business use
- Excise duty on heating oil and diesel oil
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Lessons from review:

- Neutral (efficient)
- Progressive
- System

YES, YES, YES

We may add:

- Simple
- Stable
- Predictable

as much as possible
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Role of models and empirical evidence:

- Limited at this stage, but anyway it would be nice to know if a tax system can:
  - make families have more kids
  - make firms invest more, especially in R&D
  - make people save more, especially for retirement
  - create more jobplaces
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Major obstacles:

- Politics
- Politics
- Politics
- Politics

Possible solutions:

- Non-opportunistic politicians, that cheat voters
- Education – no free lunch
- Any hints?