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FIVE QUESTIONS FOR STEFAN BACH

»The tax burden is surprisingly evenly distributed«

1. Mr. Bach, DIW Berlin analyzed the distribution effects of the German tax and social security contribution systems in cooperation with Freie Universität Berlin. Which income group in Germany makes the highest contribution to income tax revenues? High-income households generate most of the income tax. The wealthiest ten percent pays almost 60 percent of total tax revenue. On the other hand, the lower-income half of the population pays only five percent of the income tax revenue. This shows that the tax is highly progressive. However, it should be considered that the income tax generates only half of tax revenues—indirect taxes are responsible for the other half.
2. What does the indirect tax distribution look like? Indirect taxes are taxes on consumption: the value-added tax and other consumption taxes such as the electricity, energy, and tobacco tax. Here we have the opposite situation: these taxes have a regressive effect. This means the burden on households with lower incomes is much higher in relation to their income. The reason is that lower-income households spend all of their money, and sometimes even take out loans, in order to finance their consumption. This naturally results in a high consumption tax burden. Wealthy households save part of their income and consume it later, which means they pay the consumption tax later.
3. Which income segment must bear the highest overall burden? The overall tax burden distribution is surprisingly even. Lower-income segments consist of people who receive basic social security benefits and have to make do with a low income. They do not have to pay any income tax at all. But they pay high consumption taxes and therefore have a tax burden of 20 percent. In the lowest income segment the burden is even higher. Middle-income segments are also at around 20 to 25 percent, and the people who earn the highest incomes, subject to the highly progressive income tax, have an even higher tax burden. If you take into account that these people have more opportunities to avoid taxes, their actual tax burden is not necessarily higher than that of the middle-income segments. In conclusion: The tax burden is surprisingly evenly distributed and only slightly progressive.
4. To what extent has the tax burden shifted in recent years? The last decade has seen a shift away from direct taxes—from the progressive income tax—toward indirect taxes. This has reduced the progressive nature of the tax burden distribution. The tax system's role in state redistribution has weakened as a result, which has contributed somewhat to increasing inequality on the net household income level. If you take the "ability to pay principle" seriously, you would expect the tax burden to be more progressive. In reality, indirect taxes place a relatively large burden on lower-income households.
5. How could we relieve the burden on the lower-income segments? Indirect taxes are the first thing to consider when thinking about tax relief for lower-income households. However, to relieve people with low incomes from indirect taxes would be practically impossible due to the indirect tax method—you would have to set up a transfer payment system, which is complicated. This is why we would target the income tax and reduce the speed with which the tax rate rises, or focus on social security contributions, which could be used to relieve some of the burden on people with low incomes. But the problem here is that social security contributions are not directly part of the tax system.

Interview by Erich Wittenberg



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