Discussion of John Hills’
“Consolidation measures on the revenue side: Which tax bases to use to safeguard social equity?”

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A challenge

• Most people argue that the current economic crisis needs fiscal consolidation / austerity measures to offset public deficits
  – Though it is a non-Keynesian view and « continued focus on nominal deficit targets runs the risk of compelling excessive fiscal tightening if growth weakens” (IMF, 2012).
  – Able to restore trust in EU member states capabilities

• But those who most suffer of austerity programs are the most dependent people / the poorest, not those who bear « responsibility » in the raise of the crisis, the bankers, the richest people
« Regarding the composition of austerity measures, cuts in social benefits tend to worsen inequality more than other spending reductions (as in Germany, 1992–99, and Norway, 1993–97); tax-based consolidations that rely more on indirect taxes or are mixed with expenditure cuts tend to worsen inequality (e.g., that in Iceland, 2004–06). »

(IMF, Fiscal Monitor, October 12, p. 56)
There is room for a debate on social equity and fiscal consolidation

• Then how to manage austerity in such a way it is socially equitable = how to put the greatest burden of austerity on the largest shoulders?

• Knowing that two ways exist – which can be combined – for reducing deficits
  – Cuts in spending (the solution preferred by most governements)
  – Tax increases: tax bases broadening / tax rates increases / tax liabilities increases / novelties on the revenue side.
What social equity really means?

• The author rightly distinguishes various concepts (or cases relevant for) of social equity
  – Equal contribution / lump sum tax or loss in benefit?
    => actually a regressive device
  – Proportional contribution
    • Related to ability-to-pay / income – but which one: labor? global? / multi-dimensional welfare?
    • Related to largest gains prior to the crisis?
    • Related to responsibility in the crisis?
    => distributionally neutral possibly across time (some were singing yesterday who are crying today)
What a social equity target implies

• As author says, social equity implies fiscal consolidation at least distributionally neutral, if not progressive.
  – But across-the-board cuts in public spending
    – preferred option of governments (?) – very likely to be regressive.
  – By contrast, general tax increases are roughly proportional to income (in UK case).
  – Within taxes, progressivity of direct taxes could offset regressivity of indirect taxes.
Conclusion of the author

We share the author conclusion that…

“It is hard to avoid conclusion that use of all available tax bases – and tax rates – is necessary to protect social equity, rather than there being a choice between them, and that doing so is likely to be more equitable than most forms of spending cut.”

“But even the most attractive options for extending the tax base bring a series of issues that make them difficult, to say the least …”
Discussion

• I would like to devote my discussion to go beyond the presentation
  – Trying to propose tax packages
    => deemed to imply distributional neutrality
  – Trying to be imaginative
    => tax novelties
  – Being aware of the risk related to mobility
    => tax bases mobility and
    => the optimal decision making level.
Tax packages (1)

• A first tax package candidate for distributional neutrality is a combination of
  – A VAT increase
    = typically an indirect regressive tax
  – An income tax liabilities increase
    = typically a direct progressive element
    • E.g. a proportional increase of the progressive rate
    • With a removal of « tax niches » in favor of high income taxpayers
  – The two measures are convergent (revenue goes up)
Tax packages (2)

• A second tax package candidate for distributional neutrality is a combination of
  – A CO2 Tax
    = typically a regressive tax
  – The distribution of energy coupons / vouchers to poor people
    = a new government spending
  – The two measures are not convergent
    => where to put the income threshold?
Results for France suggest to distinguish between rural and urban municipalities
Tax novelties (1)

• Assume that taxing those who benefited of rents in the past is socially equitable, especially if their rent seeking activities bear some responsibilities in the crisis

=> Taxing financial activities

• « Too big to fail » Pigovian argument => tax on the size of the banks through their liabilities towards customers or their assets => kind of insurance premium against an adverse externality

• No VAT paid => tax on labor compensation in the financial sector
Tax novelties (2)

• In search of
  – relatively immobile and inelastic tax bases
  – on which a very small tax might generate large revenue,
  – with small distributive effect...

=> A two-sided tax on mobile telephone communications and/or textos?
The issue of mobility (1)

• Taxing more heavily capital income?
  – Conflict between efficiency rule (tax conversely proportional to mobility) and Haig-Simons equity
  – Raise the issue of, in case of mobility,
    • Rates: EU or upper level coordination
    • Base: how to « immobilise » the base? Exchange of information at EU level / collaborative FATCA (joint statement US and some EU MS, last February) / G20
    • Base: EU coordination => including capital gains (accruing? or realized?) in the tax base in all EU MS?
The issue of mobility (2)

• Taxing wealth?
  – On an annual basis vs inheritance/bequest/realization
  – Again conflict between efficiency rule (tax conversely proportional to mobility) and Haig-Simons equity
  – Raise issues
    • Expanding the scope of the savings directive
    • Adopting Dutch Box 3?
    • Rates: EU coordination
    • Base: exchange of information at least at EU level / collaborative FATCA
    • Base: EU coordination => including capital gains in the tax base in all EU MS?
Conclusion

• Assuming that fiscal consolidation is desirable and revenue increase is at stake, we have to
  – Create combinations of tax increases which are distributionally neutral or at least neutral for lower deciles
  – Create combinations of tax increases and compensations s.t. neutral for lower deciles
  – Be imaginative
  – Be aware of mobility issues and of the optimal geographical level for tax design decision making
    ...which then may be larger than for cuts in spending.