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PROPOSALS FOR A TAX REFORM IN GERMANY

IN FAVOUR OF A FLAT TAX

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The present German tax system suffers from an excess of steering elements, exceptions and privileges. Hundreds of special elements in the income and corporation taxes make the tax payer believe that he is privileged and causes him to defend this preference and to attain additional privileges. The politicians reaped applause for these gifts and hope to get more applause still. Nobody seems to realize that one taxpayer’s privilege must be paid for by another, that the abolition of all privileges would make all taxpayers better off.

If the legislative were able to get rid of all exceptions and privileges in the tax statutes and to return the thus increased tax revenue to the general public by reducing the tax rates, a general top tax rate of 25 percent would suffice. In addition, there is a triple gain in freedoms: the taxpayer’s economic behaviour remains unencumbered by tax law paternalism, a reduction in tax rates allows him to keep more of his earned income, and tax simplification permits him to understand the system and to escape the present uncertainty in planning and provision.

If seven types of income are substituted with just one type of profitable use of an income base, the equality of the tax burden is guaranteed from the start. If there is no longer a distinction between labour income and capital income, there is no longer the risk that capital income is subject to lower taxation and labour income to higher taxation. We should also no longer distinguish between a personal income tax and a corporation tax, especially between the taxation of unincorporated and incorporated businesses, because the choice of the legal form of organisation does not justify differences in taxation. Profits taxed at the level of the legal person, regardless of whether this is a partnership or a corporation, that are passed on to the owners or shareholders are income that has already been taxed or wealth and therefore not subject to personal income taxation. This would be a boom for the German capital markets.

The current tax law with its complexity and inconsistencies impairs the freedom of people to thrive economically and thus proves to be a disadvantage for Germany as a business location. If, however, the tax burden were distributed equally across all tax payers (with lower marginal tax rates of 0 percent, 15 percent and 20 percent for the lower income brackets), the taxpayers could enjoy their freedom much more fully: decisions on investment, organisation, supply would no longer be distorted; the tax law would remain decision neutral. Above all, the inescapable, therefore measured tax burden would guarantee that at least 75 percent of each income could be utilised privately and up to 25 percent would flow into the general government budget. This would increase the work incentive of the income recipient and at the same time guarantee the participation of the general public in this individual’s earnings success.

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