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Cross-validating administrative and survey datasets through microsimulation and the assessment of a tax reform in Luxembourg

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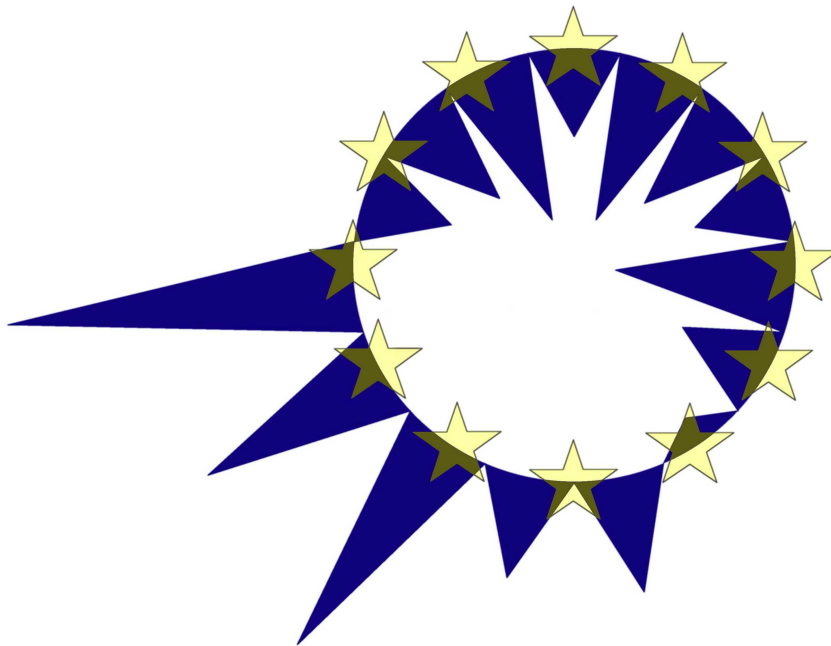
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**CROSS-VALIDATING ADMINISTRATIVE AND
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MICROSIMULATION AND THE ASSESSMENT OF
A TAX REFORM IN LUXEMBOURG**

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June 2010

CROSS-VALIDATING ADMINISTRATIVE AND SURVEY DATASETS THROUGH MICROSIMULATION AND THE ASSESSMENT OF A TAX REFORM IN LUXEMBOURG¹

Philippe Liégeois, Frédéric Berger, Nizamul Islam, Raymond Wagener²

Abstract

Using EUROMOD, we cross-validate two types of micro-data presently available in the Grand-Duchy of Luxembourg, administrative data on one hand and survey data on the other hand. While administrative data, extracted from the recently implemented Social Security Data Warehouse, contain information of the whole population of Luxembourg (449,000 observations) in 2003, survey data, extracted from the Luxembourg household panel PSELL3/EU-SILC for 2004 (incomes from 2003), is a representative sample of around 3,600 private households (9,800 individuals) living in Luxembourg with detailed information on incomes, household structure and other socio-economic dimensions. As a concrete application of this cross-validation, we analyze the 2001-2002 tax reform in Luxembourg. The main aspects of this reform are the reduction of the number of the tax brackets and the fall of the maximal marginal tax rate (from 46% in 2000 to 42% in 2001 and to 38% in 2002). The distributional effects of the tax reform are measured in terms of losers and winners, change in inequalities and poverty rates. The results issued from different types of input data are compared for cross-validation and allow us to emphasize methodological difficulties as well as to underline the advantages and limitations of each dataset.

JEL Classification: C81, C88, D63, I32, H24

Keywords: EUROMOD, Microsimulation, Tax reform, Validation

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¹ This paper uses EUROMOD version 31A. EUROMOD is continually being improved and updated and the results presented here represent the best available at the time of writing. Any remaining errors, results produced, interpretations or views presented are the authors' responsibility. This paper uses data from the PSELL/EU-SILC for 2004 (income 2003) made available by CEPS/INSTEAD.

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1. INTRODUCTION

The building-up of a comprehensive Social Security Data Warehouse was launched in Luxembourg a few years ago, the first operational dataset of which was recently made available for the year 2003.

Regarding the social debate, these administrative data might be seen as a complement to the “Luxembourg household panel/European Union Statistics on Income and Living Conditions” (PSELL3/EU-SILC) survey data which have sustained the analysis of social policies for years in Luxembourg. We could make profit, in the future, from available complementarities between administrative and survey data and create an operational link, for example through statistical matching, under the requirement of data privacy.

For the time being, our main objective is to participate in the preliminary cross-validation of the two datasets.

Given the constraints inherent to the data, we target our analysis on Luxembourg residents only. We thereby exclude all non-resident cross-border workers despite the fact that they represent as much as 37% of total employment¹ in 2003 (hence their importance regarding the tax-benefit system), a level which is a particularity of Luxembourg. While administrative data, extracted on that basis from the Data Warehouse, contain information of the whole population of Luxembourg (449,000 observations for residents in 2003), survey data, extracted from the PSELL3/EU-SILC household panel for 2004 (incomes from 2003), is a representative sample of around 3,600 private households (9,800 individuals) living in Luxembourg with detailed information on incomes, household structure and other socio-economic dimensions.

A common reference tool for the comparison of the monetary characteristics of the population is the “equivalised disposable income” of the household², which deeply depends on total earnings within the household and the tax-benefit system as a whole. This complex interplay of policies makes the evaluation of the indicator a rather demanding task. Fortunately, there are models dealing with taxes and social transfers that can help.

We have chosen to work with the EUROMOD static microsimulation model³ which lets us derive the equivalised disposable income of households through a nice implementation of the structure of the population, the distribution of earnings and the tax-benefit system in Luxembourg (as well as

done for most European countries).

Another important advantage of such a simulation platform is that a reduced set of input variables has to be implemented, prior to any simulation, from raw data. These variables are precisely defined and then compose a nice synthetic basis (which is here adopted) for a comparison of alternative datasets.

EUROMOD is to be used for the simulation and comparison of social policies, which is of main interest in the last step of our present analysis. Going ahead with the initial comparison of the datasets designed in order to fit the EUROMOD framework, we are considering the classic analysis of the outcome of a tax reform, both through administrative and survey data. Such a reform was implemented on individual and household income in Luxembourg in 2001 and 2002, including a reduction of the number of the tax brackets and a significant fall of the maximal marginal tax rate (from 46% in 2000 to 42% in 2001 and to 38% in 2002). In 2000, the taxes on individual and household income represented 7.2% of GDP in Luxembourg, one fourth of the total governmental receipts from taxes (see *Table 1.1*) and about one fifth of the total receipts, social contributions included. The burden was then cut down to 7.0 % of GDP in 2001 and 6.4% in 2002, before rising again, mainly because of fiscal drag.

Table 1.1 *Governmental receipts from 2001 to 2006 (in % of GDP)*

	Country	2000	2001	2002	2003	2004	2005	2006
Taxes on individual and household income	LU	7.2	7.0	6.4	6.6	6.7	7.2	7.5
Total receipts from taxes	LU	28.5	28.4	28.1	27.2	26.4	27.0	25.5
Total receipts from taxes and social contributions	LU	38.6	39.4	39.0	38.1	37.2	37.6	35.4
	EU-15	40.7	39.9	39.4	39.4	39.3	39.7	40.3

Source : Eurostat

The paper is organized as follows. *Section 2* describes the setting up of the datasets and points out the difficulty to make them as comparable as possible *ex ante* for a more confident cross-validation *ex post*. We compare the datasets in *section 3* and assess the effects of the 2001-2002 tax reform on the 2003 population⁴ in *section 4*. *Section 5* concludes.

2. SETTING UP THE DATASETS THROUGH THE EUROMOD INPUT FRAMEWORK

We introduce the main characteristics of the datasets, their initial setting-up in conformity with the EUROMOD input framework, adaptations needed for making them as comparable as possible, and finally the implications of some methodological choices.

2.1 Setting up initial data from the PSELL survey data

Luxembourg, as partner of the EUROMOD and MICRESA projects, is a user of the EUROMOD model, up to now based on the Luxembourg household panel (PSELL⁵). For this exercise we use the version 3/2004 covering income reference year 2003. The PSELL 3 data are used in Luxembourg as a basis for the European Union Statistics on Income and Living Conditions⁶ (EU-SILC). This is our first source of data. It is targeting the resident population of Luxembourg (“international civil servants” included) through a sample of about 3,600 private households (nearly 9,800 persons). Institutional households (mainly elderly people residing in institutions) are not covered by the survey. The unit of analysis is the “residence” household (living in the same house). The sample configuration relies on (i) estimations of the resident population as of 1st of January 2004 by the Luxembourg Central Service for Statistics and Economic Studies⁷ (STATEC) and on (ii) the most recent Luxembourg population census (15th of February 2001). The data collection method is the face-to-face interview.

Information about all kinds of gross earnings are collected through the survey, including labor income, investment and property income, social benefits in cash, private transfers, etc.

2.2 Setting up initial data from the Social Security Data Warehouse

Our second source of data for EUROMOD is the Social Security Data Warehouse recently built up by the IGSS⁸ administration in Luxembourg for the year 2003. The main objective of the Data Warehouse is to compose a normalized and exhaustive basis for the generation of statistics serving diversified purposes (general reports, OECD, etc). The Data Warehouse is gathering all information from several operational files of Social Security and other administrations (*e.g.* the National Population Registry) which are of interest for social protection analysis : monthly and yearly information on affiliation to social security, social contributions and benefits like pensions or family allowances, etc. The basic unit is the individual. Administrative data, exhaustive in their universe of definition, are neither related to a sampling process nor to high non response rates which require

weighting and imputation on the survey data side. Yet, these are not free of errors.

No information from the fiscal administration is made available for the building-up of the Data Warehouse. However, labor earnings are partially known from the IGSS administration as they are needed for the calculation of the social contributions paid either by the employer or the earner himself when self-employed or socially insured on a voluntary basis. Consequently, three limitations are to be noticed in the data. First, as in Luxembourg wages “declared” to the social security are allowed to be truncated when greater than seven times the Minimum Social Wage⁹, it may happen that labor earnings are truncated for high wages. Second, the earnings of the persons who pay social contributions on a voluntary basis are most probably far departing from the real state. Finally, farmers’ income cannot be properly determined either. On top of those limitations, no information is available in the Data Warehouse for capital income and private transfers.

Taking the relationships that can be observed between the individuals in the Data Warehouse, “Families” are constructed on a “fiscal basis”. “Residence” households, which are the unit of analysis in PSELL, cannot be identified through available administrative data¹⁰. The households are therefore built up in another way as follows. First, spouses¹¹ are identified as a basis for the household. This means that unmarried cohabitants do not appear as linked in the database (they belong to different fiscal households), indeed in conformity with fiscal rules which are described in the *appendix*. Second, a link is created between the children (basically, either unmarried and more than 21 years old or older but still a student or disabled) and their parents through the family benefits raised by the latter during the year¹².

Only persons for whom positive earnings (either income or allowance) can be identified in the Data Warehouse are included into the EUROMOD input database. The voluntary insured or coinsured individuals are included as well. An implication is that “international civil servants” residing in Luxembourg may not appear in the EUROMOD input database (they usually neither contribute to, nor benefit from -in monetary terms-, the social security system in Luxembourg). Of course, in conformity with the PSELL database, residents only are eligible¹³. A last remark concerns the persons living in institutional households. Due to the fact that it is impossible to identify them in the Data Warehouse, they are included in the EUROMOD input database built up from the Data Warehouse, as opposed to the one built up from survey data.

2.3 Improving comparability of the EUROMOD input datasets

Given our main objective (see *Introduction*), it seems important to dispose of identifiable dissimilarities between the initial datasets as regards their respective populations and the lack of precision in some important (income-related) variables. *Table 2.1* summarizes the question and gives an insight about complementary adaptations which are needed for an *ex ante* better comparability of the EUROMOD input datasets. We can see, for example, that capital income has to be dropped from the survey-based data because no information is available about such an income in the administrative-based data. Keeping capital income on one side only would bias our results and weaken comparability of outcomes.

Individuals receiving an income from agriculture are dropped as well (both sides, for comparability reasons) because methodological limits imply for the administrative-based dataset an imperfect link only between the reality of earnings and the contents of the income variable on this side. In all cases, when individuals are dropped, all members of the household follow in order to avoid bias due to a change in the structure of the household, a bias that might be transferred downstream (see *infra*).

While comparing monetary characteristics, the “equivalised disposable income” of households will play a crucial role. As it is well known, the equivalised disposable income is the ratio of total disposable income¹⁴ to the equivalent weight of the household. Following the so-called “OECD-modified scale”, we assign a value (weight) of 1 to the household head, of 0.5 to each additional adult member and of 0.3 to each child (less than 14 years old). The idea is to allow comparison (of well-being) between families whose compositions differ while taking into account the economies of scale a family of several persons is benefitting from compared to a single person. The equivalised disposable income (which is called from now on “equivalised income” for short) is evaluated at the household level. Each member of the household is then attributed this (common) value of equivalised income.

Most usually in the literature, the “residence” household does matter, rather than the “fiscal” one. Departing from this, we work with fiscal households, whatever survey-based or administrative-based data. This induces two effects which may generate some discrepancies between our results and the results based on (as they usually are) residence households.

Table 2.1 *Adaptation of EUROMOD input datasets for improving comparability*

Topic	EUROMOD survey-based data	EUROMOD administrative-based data	Action / Remarks
Number of individuals before the present adaptation process	443,642 (weighted)	449,025	Some information about cross-border workers available in administrative data, but not in survey data, hence initially dropped in the former, leading to 449,025 cases
Unit of analysis	Residence household	Fiscal household	All comparisons and actions to be based on fiscal households
Institutional households	Not included	Included but cannot be identified	None (**)
International civil servants	Included	Excluded but may happen that household's members still within the data	(**) <u>Administrative-based data</u> : Drop cases (*) if a married partner announced despite absent from the data (***) <u>Survey-based data</u> : Drop cases (*) if a member of the household not socially insured in GDL (***)
Voluntary insured	Included but cannot be identified	Included and can be identified (but earnings not reliable)	(**) Drop cases (*) in administrative-based data if a member of the household voluntarily insured
Capital income and private transfers	Information collected	Unknown	Variables set to "0" in survey-based data
Income from agriculture	Information collected	Information available (but earnings not reliable)	Drop cases (*)
Number of individuals left after the present adaptation process	419,030 (weighted)	418,861	<u>Administrative-based data</u> : 7% cases dropped <u>Survey-based data</u> : 5% cases dropped

Source : CEPS/INSTEAD

(*) "Drop cases" should be understood as "Drop all fiscal household's members" if the condition fulfilled. Dropping individuals separately (hence partially depriving households from members) would bias computations of equivalised disposable income (see *infra*), at-risk-of-poverty rates and other computations that are based on (fiscal) households as a whole.

(**) This decision, despite needed, generates some (or is unsuccessful in removing all sources of) non-comparability between datasets

(***) Which is most probably due to an "international civil servant" status (a proxy only)

First, the disparity in income is affected. *Table 2.2* gives an illustration for a “residence” household composed of 2 unmarried parents and 2 dependent children. In the residence framework, the total income (3,910) is divided by the total equivalent weight (2.3) to determine the equivalised income of each member of the household (1,700). In the fiscal framework, the father, unmarried, is fiscally separated from his partner and the children. To the father’s (fiscal) household is associated an equivalised income of 2,110¹⁵ whereas the equivalised income attributed to the rest of the family is 1,000¹⁶. Splitting households (from residence to fiscal units) then generates some disparity, even if it seems difficult to conclude about income heterogeneity within the whole population.

Table 2.2 *Equivalised income and the unit of analysis*

Household ID		Individual characteristics						Equivalised income	
Residence	Fiscal	ID	Age	Status	Net earnings	Weight		Residence	Fiscal
						Residence	Fiscal		
I	A	1	45	Unmarried partner (father)	2,110	1	1	1,700	2,110
I	B	2	42	Unmarried partner (mother)	1,800	0.5	1	1,700	1,000
I	B	3	20	Child (student)	0	0.5	0.5	1,700	1,000
I	B	4	13	Child (student)	0	0.3	0.3	1,700	1,000

Source : CEPS/INSTEAD

Second, the first moments of equivalised income (hence the poverty line, see *infra*) differ from the one evaluated on a residence household basis. From the illustration shown in *Table 2.2*, it can be seen that the average (*resp.* median) equivalised income is 1,700 (*resp.* 1,700) if residence households considered, 1,277.5 (*resp.* 1,000) when fiscal households. The outcome stems from the definition of equivalised income, even if it seems difficult, here again, to anticipate the impact of the splitting procedure¹⁷ over the whole distribution of income.

3. COMPARING THE EUROMOD INPUT DATASETS AND A FEW IMPLICATIONS DOWNSTREAM

The process of adaptation of variables and selection of the population, when needed, ends up in two EUROMOD input datasets made as comparable as possible *ex ante* and which are now cross-

validated at the household and individual levels.

3.1 The household level

Table 3.1 gives an insight into the comparison when the household is the unit of analysis. Survey-based data allow us to work both on a residence and a fiscal household basis.

As can be seen from *Table 3.1*, the survey-based EUROMOD input dataset is said to be “representative” of a population of 169,620¹⁸ residence households which lead, through the splitting procedure, to 205,802 fiscal households.

19% of residence households are composed of more than one fiscal household. 30% of residence households are composed of one person only; the difference with fiscal households (47% are of the “single” type) is obviously coming from the inclusion of the latter units within residence households. More generally, *Table 3.1* shows how close the survey-based data are, compared to administrative-based data, when fiscal households are considered, despite the *ex ante* difference in nature of the source data¹⁹.

3.2 Non-monetary characteristics at the individual level

Tables 3.2 and *3.3* compare the EUROMOD input datasets when the individual is the unit of analysis. 419,030 persons (*resp.* 418,861) are “represented” through the survey-based data (*resp.* administrative-based data). Once again, strong similarities can be observed between the non-monetary characteristics given in *Table 3.2* for the two datasets. One important discrepancy that is not mentioned, nevertheless, is about time needed for simulations, which goes from a few minutes for survey-based data up to more than 5 hours when administrative-based data are used.

3.3 Monetary characteristics at the individual level and downstream implications

Concerning the income components (*Table 3.3*) a divergence appears at the “primary income²⁰” level, which is 7% lower (on average) in administrative-based data than in survey-based ones²¹. This difference is mainly a discrepancy due to employment income (about 90% of primary income, out of capital income) for which the ratio survey/administrative is 1.09.

Table 3.1 Comparing EUROMOD datasets when unit of analysis is the HOUSEHOLD

Characteristics	Categories	Survey-based EUROMOD data		Administrative-based EUROMOD data (fiscal households only)
		Residence households	Fiscal households	
Number of households	Raw data (i)	3,296	4,274	212,646
	Weighted count (i)	169,620	205,802	
Number of fiscal households in the residence household	1	81% (ii)	non applicable	non applicable
	2	17%	non applicable	non applicable
	3 or more	2%	non applicable	non applicable
Number of persons in the household	1	30%	47%	50%
	2	28%	25%	24%
	3 or 4	33%	23%	21%
	5 or more	9%	5%	5%
Number of workers (iii) in the household	0	30%	34%	35%
	1	40%	48%	47%
	2 or more	29%	18%	17%
Type of household	Single (< 65)	19%	35%	37%
	Single (> 65)	11%	12%	14%
	Single with dependent(s) (iv)	7%	6%	5%
	Couple – 0 dependent	24%	21%	20%
	Couple – 1-2 dependent(s)	30%	20%	20%
	Couple – 3 dependents or more	9%	5%	5%

Source : CEPS/INSTEAD (NB : Proportions rounded to the closest percentage point)

(i) Raw data : number of surveyed households - Weighted counts : households' weights (from PSELL3/EU-SILC survey) taken into account

(ii) All results below in % of total number of households (households' weights taken into account)

(iii) Employer, self-employed or employee (from the employment status)

(iv) Dependent : neither head of household nor a partner in a couple

Guide to reader : 3,296 residence households have their characteristics reported from the 2004 PSELL3/EU-SILC in the EUROMOD survey-based dataset, "representing" 169,620 residence households within the population ; 19% of the residence households (household weights taken into account) are composed of one person who is less than 65 years old ; 17% are composed of 2 fiscal households.

Table 3.2 Comparing EUROMOD datasets when the unit of analysis is the *INDIVIDUAL* :
Non-monetary characteristics

Characteristics	Categories	Survey-based EUROMOD data	Administrative-based EUROMOD data
Number of persons	Raw data (i)	8,657	418,861
	Weighted count (i)	419,030	
Gender	Female	50.7%	50.5%
	Male	49.3%	49.5%
Age	Age < 18	22%	22%
	18 <= Age < 59	59%	59%
	Age >= 60	19%	20%
Type of household	Single (< 65)	17%	19%
	Single (> 65)	6%	7%
	Single with dependent(s) (ii)	7%	6%
	Couple – 0 dependent	21%	21%
	Couple – 1-2 dependent(s)	35%	35%
	Couple – 3 dependents or more	14%	12%
Number of workers (iii) in the household	0	25%	26%
	1	45%	45%
	2 or more	30%	29%

Source : CEPS/INSTEAD (NB : Proportions rounded to the closest percentage point)

(i) Raw data : number of surveyed individuals - Weighted counts : individual weights (from PSELL3/EU-SILC survey) taken into account

(ii) Dependent : neither head of household nor a partner in a couple

(iii) Employer, self-employed or employee (from the employment status)

The confidence interval shown in Table 3.3 for the primary income implies that the divergence cannot be statistically imputed, for a confidence level of 95%²², to the sampling process on the survey-side. Actually, the setting up of the data can help a little in understanding differences. Table 2.1 is mentioning, despite the adaptation process of the EUROMOD input datasets for improving their comparability, some lack of similarity regarding the institutional households. Moreover, individuals deceased or disappearing from the data records during the last year cannot be treated perfectly the same way in both datasets. Taking roughly into account those dissimilarities²³, it can be shown that the difference in primary income might be reduced and the results made statistically compatible given the sampling process²⁴. It is also worth mentioning some discrepancy regarding

income measurement. For example, survey-based data include in “employment” earnings sickness replacement wages when relating to very short periods.

The gap in primary income is transferred downstream, throughout the tax-benefit system. Of course, the progressive nature of the tax system helps in reducing the differences after taxes. This is also illustrated in *Table 3.3*. Thanks to EUROMOD microsimulation, social security contributions, family allowances, social assistance and taxes are determined and disposable as well as equivalised incomes are derived²⁵. As a benchmark, the “without tax reform” environment is chosen (see section 4 *infra*).

At the end of the process, mean (*resp.* median) equivalised income as evaluated from the administrative-based dataset differs by 1% (*resp.* 4%) only from its value derived from the survey-based (fiscal household) framework. *Table 3.3* also shows that a change in the unit of analysis, from the residence to the fiscal household, induces a drop of the mean equivalised income by 5%. The total household disposable income is indeed decreasing (see section 2.3 for a qualitative explanation) more, on average, than the equivalent weight (*resp.* 13% and 10%) while changing the reference unit.

Regarding the distribution of equivalised income, it can be seen from *Table 3.3* that measurements do not differ too much between the datasets. If the aversion to inequality is low (Atkinson index²⁶ with a coefficient of 0.5) or when we pay more attention to the “middle” of the distribution (through the Gini²⁷ coefficient and the interquartile ratio), the inequality indices derived from the administrative-based data are statistically compatible or close to be compatible²⁸ with those resulting from survey-based data. When the aversion to inequality becomes greater (Atkinson index with a coefficient of 2) or both “extremes” of the distribution of income matter (P90/P10 ratio), the measurements become fully compatible. Nevertheless, more discrepancies are observed when we concentrate on the leftist part of the distribution of income, as is now shown *e.g.* through the analysis of poverty²⁹.

Tables 3.4 and *3.5* give more details about the distribution of income (as determined through EUROMOD microsimulation in a without-tax-reform environment and on a “fiscal household” basis) and the at-risk-of-poverty rates, given different typologies and, within each of them, for all categories concerned. An “at-risk-of-poverty rate” is conventionally defined as the proportion of individuals whose equivalised income is below the so-called “poverty line” which is 60% of the median equivalised income.

Table 3.3 Comparing EUROMOD datasets when the unit of analysis is the *INDIVIDUAL* :
Monetary characteristics and implications downstream ^(*),
in EUR / month (except Equivalent weight and Inequality coefficients)

Characteristics	Categories	Survey-based EUROMOD data		Administrative- based EUROMOD data
		Residence households	Fiscal households	
Primary income (i), out of capital income (ii) (on average)		1,493 [1,416 – 1,570] (iii)		1,384
Capital income (ii) (on average)		78		Not available in source data
Standard disposable income (iv), (vi) (on average)		1,529		1,518
Total household disposable income (v), (vi) (on average)		4,395	3,811	3,720
OECD equivalent weight (on average)		1.97	1.77	1.74
OECD equivalised income (vi)	Mean	2,276	2,158	2,131
	Median	2,076	1,980	1,898
	Poverty line (60% of the median)	1,246	1,188 [1,171 – 1,205] (iii)	1,138
Gini coefficient		Not computed	0.243 [0.236 – 0.249] (iii)	0.248
P75 / P25 ratio		Not computed	1.727 [1.697 – 1.757] (iii)	1.760
Atkinson index (inequality aversion coefficient : 0.5)		Not computed	0.048 [0.045 – 0.050] (iii)	0.051
P90 / P10 ratio		Not computed	2.798 [2.728 – 2.868] (iii)	2.809
Atkinson index (inequality aversion coefficient : 2.0)		Not computed	0.227 [0.203 – 0.252] (iii)	0.223

Source : CEPS/INSTEAD (and EUROMOD microsimulation)

(*) All amounts before/without the 2001-2002 tax reform in Luxembourg (see section 4 *infra*)

(i) Primary income (see footnote 20) = Gross earnings all sources (out of public pensions), before Employee social contributions and Income taxation, and out of Social benefits

(ii) Capital income = Gross property income + Gross investment income

(iii) All 95 % STATA “bootstrap” confidence intervals (500 replications)

(iv) Standard disposable income = Primary income – Employee social contributions – Income taxes + Social benefits in cash (Reminder : the capital income is here excluded from computations)

(v) Total disposable income within the household, attributed to each member in conformity with the computation of the equivalised income

(vi) Evaluated through EUROMOD microsimulation

It is worth noticing that the usual basis for analysis of poverty is the residence household and not the fiscal one, which makes a difference regarding the household disposable income, the equivalised income of the members hence the poverty line and the at-risk-of poverty rates (see *Table 3.3*). Nevertheless, we are here mentioning indicators regarding the *fiscal* households. Indeed, we are constrained by the administrative-based data where no information is available about residence households. Fortunately, we can also remind our main objective which is the comparison of the datasets for cross-validation rather than a specific standard poverty analysis.

The at-risk-of-poverty rates are higher, on average³⁰ as well as for most categories³¹, when evaluated through the survey-based data³² (*Table 3.4*). It can also be shown that, regarding the whole population, the intensity of poverty, measured by the “income gap ratio”³³, is higher through survey-based data. More generally, usual findings follow : younger people, singles either less-than-65-years-old or with dependent(s)³⁴ and the members of households where nobody is working are more at risk of poverty than the other categories within the population, whatever the dataset under consideration. It can be seen that those populations are more concentrated in the first deciles of income distributions than others. Singles with dependent(s) and the households with no worker also experience less equivalised income, on average, than the members of the respective associated categories (*Table 3.5*). Nevertheless, no systematic link can be observed between the mean level of income within a category and its at-risk-of-poverty rate.

A few striking discrepancies are to be noticed between the datasets, for example concerning the “singles with dependent(s)” who are marked twice more at risk of poverty in survey-based data. But we should be cautious about interpretation, given the sampling nature of the survey which might induce bias as far as a sub-group (7% of the population, see *Table 3.5*) only is concerned. The gap in poverty between men and women is also shown close to 0% under administrative-based data but not far from 1% when survey-based data are considered.

It must be noticed again that, due to the fact that the calculation have been made on the “fiscal households” and not on “residence households”, it makes no sense to compare these figures with poverty rates published at the European and the national levels.

Table 3.4 *At-risk-of-poverty rates and distribution of categorical populations over income deciles*
(based on equivalised income determined through “fiscal households” in a without-tax-reform environment – see section 4 *infra*)

Characteristics	Categories	Data	Poverty rate	Share of categorical populations between equivalent income deciles (*)										
				Total	1st	2nd	3rd	4th	5th	6th	7th	8th	9th	10th
All		Administrative-based	7.4%	100%	10%	10%	10%	10%	10%	10%	10%	10%	10%	10%
		Survey-based	9.6%	100%	10%	10%	10%	10%	10%	10%	10%	10%	10%	10%
Gender	Female	Administrative-based	7.3%	100%	10%	11%	10%	10%	10%	10%	10%	10%	10%	10%
		Survey-based	9.9%	100%	10%	10%	10%	10%	10%	11%	10%	10%	9%	9%
	Male	Administrative-based	7.5%	100%	10%	9%	10%	10%	10%	10%	10%	10%	10%	10%
		Survey-based	9.2%	100%	10%	9%	10%	10%	10%	9%	10%	10%	11%	11%
Age	Age < 18	Administrative-based	7.9%	100%	11%	10%	11%	10%	10%	9%	9%	10%	10%	10%
		Survey-based	11.8%	100%	13%	12%	10%	8%	9%	10%	10%	8%	10%	9%
	18<= Age < 59	Administrative-based	8.8%	100%	12%	8%	9%	9%	9%	9%	10%	11%	11%	12%
		Survey-based	10.4%	100%	11%	8%	9%	9%	9%	9%	9%	11%	12%	12%
	Age >= 60	Administrative-based	2.6%	100%	3%	15%	11%	14%	14%	15%	12%	7%	6%	4%
		Survey-based	4.2%	100%	4%	11%	13%	14%	14%	13%	12%	8%	5%	6%
Type of household	Single (< 65)	Administrative-based	12.9%	100%	17%	11%	10%	8%	8%	8%	9%	11%	10%	8%
		Survey-based	15.9%	100%	16%	9%	10%	8%	7%	8%	10%	11%	11%	10%
	Single (>= 65)	Administrative-based	3.3%	100%	3%	20%	8%	9%	13%	18%	14%	9%	4%	3%
		Survey-based	5.7%	100%	6%	10%	13%	11%	15%	14%	16%	8%	5%	3%
	Single with dependent(s)	Administrative-based	16.8%	100%	23%	15%	11%	9%	9%	8%	8%	7%	5%	6%
		Survey-based	32.3%	100%	34%	14%	11%	10%	8%	3%	5%	6%	7%	2%
	Couple - 0 dependent	Administrative-based	2.6%	100%	4%	9%	10%	13%	11%	11%	10%	9%	10%	13%
		Survey-based	3.9%	100%	4%	10%	11%	12%	12%	10%	8%	10%	7%	15%
	Couple - 1-2 dependents	Administrative-based	6.7%	100%	9%	6%	9%	9%	10%	10%	10%	11%	12%	13%
		Survey-based	7.6%	100%	8%	7%	9%	9%	9%	11%	11%	12%	13%	11%
	Couple - 3 dependents or more	Administrative-based	6.7%	100%	9%	14%	13%	11%	10%	9%	9%	9%	9%	6%
		Survey-based	4.4%	100%	7%	15%	10%	12%	10%	12%	10%	7%	10%	8%
Number of workers in the household	0	Administrative-based	8.7%	100%	10%	17%	12%	13%	13%	13%	10%	6%	4%	2%
		Survey-based	15.9%	100%	16%	13%	13%	13%	12%	11%	10%	6%	3%	3%
	1	Administrative-based	8.6%	100%	13%	9%	10%	9%	10%	9%	10%	11%	10%	8%
		Survey-based	11.3%	100%	13%	10%	11%	10%	11%	10%	9%	9%	10%	8%
	2 or more	Administrative-based	4.5%	100%	6%	5%	8%	8%	8%	8%	10%	12%	15%	20%
		Survey-based	1.7%	100%	2%	7%	6%	8%	7%	10%	11%	14%	16%	18%

Source : CEPS/INSTEAD (and EUROMOD microsimulation)

(*) Income deciles as evaluated over the whole population (not the category only) ; the unit of analysis is the individual

Proportions rounded to the closest percentage point : the resulting total may differ from 100%

Guide to reader : 13% of the elderly (more than 60 years old) belong to the third decile of the general population equivalised income distribution

Table 3.5 *Distribution of equivalised income*
(determined through “fiscal households” in a without-tax-reform environment – see section 4 *infra*)

Characteristics	Categories	Data	Share in total population	Mean equivalent income (*)										
				All	Deciles									
					1st	2nd	3rd	4th	5th	6th	7th	8th	9th	10th
All		Administrative-based	100%	2,131	996	1,244	1,418	1,611	1,802	1,994	2,210	2,508	2,967	4,557
		Survey-based	100%	2,158	870	1,294	1,499	1,699	1,882	2,066	2,282	2,594	3,013	4,401
Gender	Female	Administrative-based	51%	2,109	1,000	1,249	1,418	1,611	1,802	1,994	2,208	2,507	2,967	4,554
		Survey-based	51%	2,117	880	1,292	1,502	1,693	1,883	2,065	2,286	2,592	3,007	4,369
	Male	Administrative-based	49%	2,152	991	1,237	1,417	1,610	1,802	1,993	2,212	2,509	2,966	4,560
		Survey-based	49%	2,199	859	1,295	1,496	1,704	1,881	2,067	2,277	2,596	3,019	4,428
Age	Age < 18	Administrative-based	22%	2,133	1,084	1,239	1,415	1,612	1,801	1,993	2,210	2,511	2,969	4,667
		Survey-based	22%	2,068	936	1,285	1,497	1,693	1,874	2,069	2,279	2,616	2,982	4,304
	18<= Age < 59	Administrative-based	59%	2,189	964	1,234	1,416	1,611	1,802	1,995	2,213	2,511	2,972	4,485
		Survey-based	59%	2,228	844	1,296	1,501	1,701	1,877	2,067	2,284	2,593	3,019	4,416
	Age >= 60	Administrative-based	20%	1,954	1,008	1,266	1,424	1,609	1,803	1,992	2,202	2,495	2,928	4,877
		Survey-based	19%	2,044	835	1,298	1,497	1,700	1,898	2,061	2,279	2,573	3,052	4,479
Type of household	Single (< 65)	Administrative-based	19%	1,960	846	1,227	1,414	1,609	1,803	1,997	2,214	2,507	2,969	4,358
		Survey-based	17%	2,103	692	1,301	1,507	1,702	1,880	2,067	2,278	2,598	3,013	4,507
	Single (>= 65)	Administrative-based	7%	1,887	1,003	1,304	1,425	1,616	1,804	1,997	2,198	2,493	2,920	4,194
		Survey-based	6%	1,959	768	1,297	1,494	1,696	1,895	2,059	2,270	2,549	3,033	3,958
	Single with dependent(s)	Administrative-based	6%	1,838	1,060	1,233	1,410	1,607	1,800	1,992	2,210	2,503	2,948	5,095
		Survey-based	7%	1,566	792	1,308	1,516	1,692	1,896	2,047	2,288	2,573	3,003	4,455
	Couple - 0 dependent	Administrative-based	21%	2,251	1,033	1,230	1,424	1,607	1,802	1,991	2,208	2,509	2,963	4,527
		Survey-based	21%	2,292	859	1,302	1,501	1,701	1,896	2,060	2,288	2,573	3,074	4,403
	Couple - 1-2 dependent(s)	Administrative-based	35%	2,301	1,076	1,242	1,419	1,614	1,802	1,993	2,212	2,511	2,972	4,609
		Survey-based	35%	2,296	1,041	1,292	1,493	1,698	1,874	2,076	2,283	2,599	3,014	4,418
	Couple - 3 dependents or more	Administrative-based	12%	1,984	1,092	1,240	1,412	1,611	1,800	1,992	2,210	2,511	2,963	4,553
		Survey-based	14%	2,079	1,145	1,273	1,491	1,698	1,862	2,057	2,279	2,642	2,952	4,240
Number of workers in the household	0	Administrative-based	26%	1,743	868	1,253	1,421	1,608	1,802	1,992	2,202	2,492	2,917	3,952
		Survey-based	25%	1,733	628	1,303	1,504	1,700	1,892	2,060	2,281	2,575	3,034	3,943
	1	Administrative-based	45%	2,079	1,034	1,235	1,415	1,611	1,802	1,995	2,213	2,509	2,964	4,605
		Survey-based	45%	2,098	1,020	1,284	1,501	1,691	1,880	2,065	2,277	2,597	3,008	4,426
	2 or more	Administrative-based	29%	2,553	1,064	1,243	1,418	1,614	1,803	1,993	2,213	2,515	2,981	4,585
		Survey-based	30%	2,599	1,061	1,299	1,487	1,713	1,875	2,073	2,288	2,598	3,015	4,450

Source : CEPS/INSTEAD (and EUROMOD microsimulation)

(*) Mean income for individuals belonging to the decile evaluated over the whole population (not the category only) ; the unit of analysis is the individual

4. A COMPARATIVE APPLICATION TO THE ANALYSIS OF A TAX REFORM

In the previous sections, we have emphasized similarities and discrepancies observed between the survey-based and administrative-based datasets seen as raw data, even if redesigned in order to fit the EUROMOD input framework. We are now going a step further and considering the implication of an alternative use of the datasets for the classic analysis of a tax reform.

Such a reform was implemented on individual and household income in Luxembourg in 2001 and 2002. The characteristics of the reform are described in the *appendix* and we are here highlighting its main (rather common) outlines only :

- The first tax bracket is enlarged, which means that the minimum income before tax is increased, from 6,693 EUR in 2000 up to 9,750 EUR in 2002
- The number of tax brackets is reduced, from 18 down to 17 in 2002 and band widths are made uniform to 1,650 EUR in 2002
- The maximum tax rate significantly decreases, from 46% to 38% in 2002

This section analyses the distributional effects of the reform on the 2003 population. All results are derived from both the administrative-based and survey-based datasets. We first develop the methodological framework chosen for the analysis in order to make the comparison as accurate as possible. Then, we present an overall view on inequalities, with and without the tax reform, and on changes in disposable income by category of population. Finally, we concentrate more on the left-hand side of the distribution through looking into the proportion and characteristics of non-tax payers and finally examining the at-risk-of-poverty rates.

4.1 Methodological framework for analysis

Given the 2001-2002 fiscal changes in Luxembourg, the initial idea is to compare the 2000 situation with the 2002 one, whatever the way for proceeding. Nevertheless, the changes over a 2-year period regarding the economy and the social field reflect several influences, not limited to the evolution of fiscal rules. During this period, the population (age, composition of households, etc) changes, the economy faces some inflation and hopefully economic growth (hence an impact on real earnings), the distribution of primary income may be altered, policies other than the fiscal one can be amended, unemployment may not be stable, etc (Fuchs and Lietz, 2007, Immervoll *et al.*, 2006). All these first-round effects can still be completed either through behavioral answers of the population

(*e.g.* labor supply), or through feedback effects from the economy as a whole (*e.g.* prices), or through sectorial budgetary constraints (*e.g.* individual or public accounts).

We would like to strictly avoid the changes not directly resulting from the tax reform in itself. Moreover, our main objective remains the comparison of specific datasets. These are the reasons why we choose to concentrate on a given year, as far as the economy and the social field are concerned, with a simple treatment of the tax-benefit environment. In the benchmark³⁵, the tax system is designed as before the 2001-2002 reform, conforming to the brief description made earlier (and completed in the *appendix*). The alternative is then simply to set up the tax system as on 2002, that means in its post-reform state. On the benefit side, no change is to be mentioned between the benchmark and the alternative. The year 2003 (rather than 2002) is chosen as a basis for analysis. This is simply due to a constraint on administrative data the first set of which was made available for the year 2003 only.

Altogether, these options lead to the following story. We compare two situations, one where the Luxembourg population in 2003 faces the real tax-benefit system of 2003, the other one where the tax system of 2000 is applied to the same population, everything else (*e.g.* benefits) untouched. In other words, we ask what had happened for the population in 2003, had the 2000 tax system either been frozen, on one side, or be replaced by the new 2003 tax system, on the other side. The hypothesis of an invariant tax system through time makes sense in Luxembourg where the tax rules are basically not changing between reforms (*e.g.* no adaptation relating to the consumption price index is made on an automatic basis), what was observed *e.g.* from 2002 up to the beginning of 2008. The benefit side, on the contrary, is following in Luxembourg a more dynamic track, which makes quite natural our hypothesis of a benefit system designed in 2003 as it really was, whatever the tax system.

Given our framework for analysis, we assess the distributional effects of the tax reform on individual income through the tax-benefit static microsimulation model EUROMOD. EUROMOD is a flexible tool that enables research on the first-round effects³⁶ of policy reforms that have an impact on earnings (mainly through social contributions, taxes and cash benefits), hence on poverty and inequality (Sutherland, 2001). Microsimulation models rely on micro-data representative of a population (households and individuals) and designed so that we can hold most influences constant (*e.g.* the benefit system, including non-take-up behavior, and demographic characteristics) and focus on the effect of one change at a time (*e.g.* the tax system and/or the dataset).

4.2 An overall view on the redistributive effects and inequalities

The Gini coefficient, the Atkinson inequality indices³⁷ and the percentile ratios give us an overall view of inequality in the distribution of equivalised income. The values of these coefficients are reported in *Table 4.1* for administrative-based and survey-based data, with and without the tax reform.

Table 4.1 *Redistributive effects of the tax reform and changes in inequality (*)*

	Survey-based data		Administrative-based data	
	Without tax reform	With tax reform	Without tax reform	With tax reform
Gini if “no tax” (i) (1)	0.308		0.318	
Gini “with tax” (ii) (2)	0.243	0.256	0.248	0.263
ΔG (3) = (1) – (2) = (4) – (5)	0.066	0.052	0.070	0.055
Reynolds-Smolensky index of vertical equity (4) = $\frac{(7)}{1 - (7)} * (6)$	0.067	0.053	0.071	0.056
Re-ranking index of horizontal inequity (5)	0.001	0.001	0.001	0.000
Kakwani index of tax progressivity (6)	0.332	0.400	0.351	0.420
Rate (iii) (7)	0.168	0.116	0.169	0.117
P75 / P25	1.727	1.807	1.760	1.845
Atkinson index (inequality aversion = 0.5)	0.048	0.053	0.051	0.057
P90 / P10	2.798	3.003	2.809	3.004
Atkinson index (inequality aversion = 2)	0.227	0.246	0.223	0.243

Source : CEPS/INSTEAD (and EUROMOD microsimulation)

(*) Based on the distribution of individual equivalised income – When applying formula, rounding effects sometimes

(i) Based on the individual equivalised income when all taxes dropped = household total disposable income if no tax /equivalent weight of the household (see section 2.3 *supra*)

(ii) Based on the individual equivalised income when all taxes included (normal case) = household total disposable income /equivalent weight of the household (see section 2.3 *supra*)

(iii) Mean rate, based on the distribution of equivalised income

Table 4.1 clearly shows that the values of the inequality coefficients are increased due to the reform meaning that the inequalities in the distribution of equivalised income are deepened. Moreover, the changes in the indices seem quite comparable regarding the data sources.

The impact of the tax system is explored further in *Table 4.1*. For example, the Gini index if all taxes were dropped would be 0.308 through survey-based data. It becomes 0.243 when the tax system (as before the reform) is implemented. This drop in the inequality coefficient is mainly due to vertical redistribution³⁸ of the tax system (Reynolds-Smolensky index). The horizontal redistribution appears to be negligible³⁹.

The Reynolds-Smolensky index of vertical redistribution can still be decomposed into “progressivity” (Kakwani index) and “magnitude” (a coefficient depending on the average rate of taxation), both factors playing a positive role on the vertical redistribution. This decomposition helps in understanding what is at stake in the tax reform. Clearly, the reduction in vertical redistribution due to the reform (0.067 down to 0.053, regarding the survey-based data) results from a drop in the rate of taxation (from 16.8% down to 11.6%) and not from the progressivity which is increased (from 0.332 to 0.400) as measured by the Kakwani index⁴⁰.

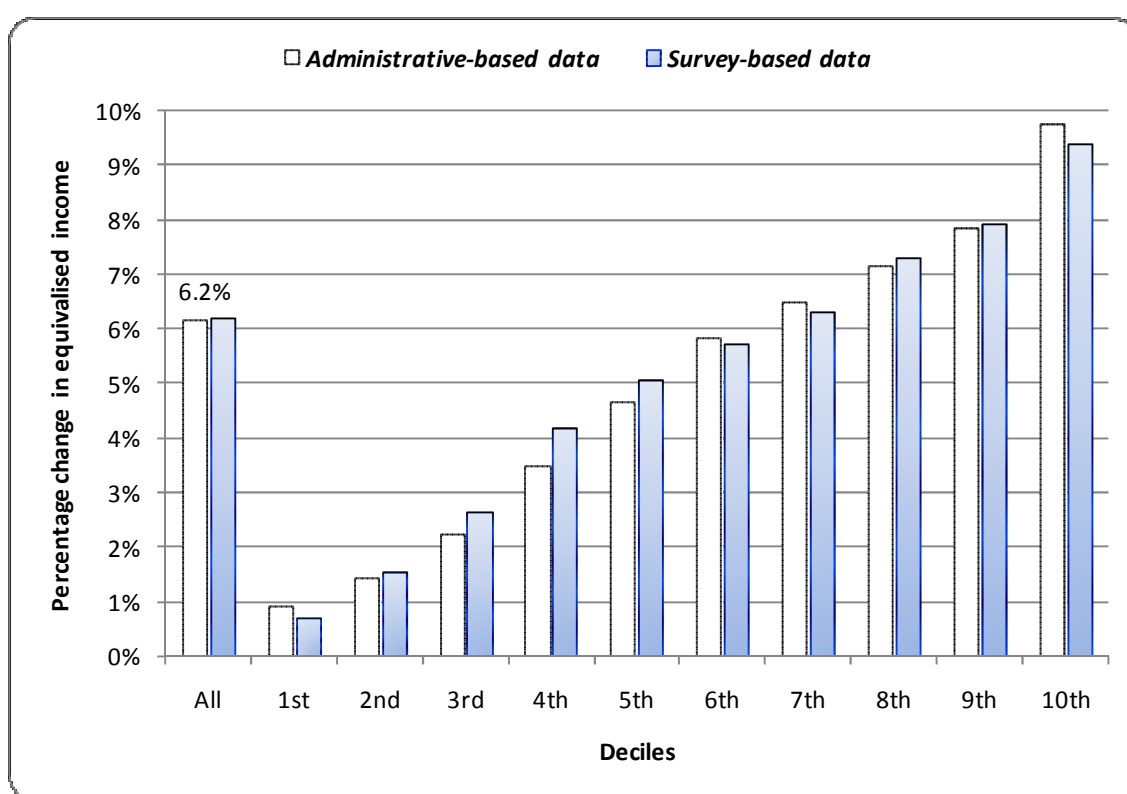
4.3 Changes in equivalised income

Figure 4.1 shows the average change in individual equivalised income for different income groups (deciles) due to the tax reform. In all results below, the benchmark is the without-tax-reform value of the equivalised income shown in *Table 3.5*. The members of the deciles are frozen and their change in income is examined⁴¹. Given the characteristics of the 2001-2002 tax reform, each Luxembourg resident is a “gainer” (which means either null or positive impact on the equivalised income). On the whole, the reform increases equivalised income by 6.2%. This positive change in equivalised income is observed for all deciles and the higher the income the higher the gain. This confirms that the new tax structure increases the inequality of income distribution (see section 4.2).

Table 4.2 also shows the average change in individual equivalised income for different categories of population and each decile of the income distribution. The overall changes are clearly positive for all categories⁴². Moreover, whatever the category and the dataset, the higher the income the higher the relative gain⁴³. More specifically, when all deciles are included (last column in *Table 4.2*), singles without a dependent gain relatively more than couples, especially when dependent(s) are associated to the latter. Younger people (age less than 18) benefit less from the reform than the

others, whatever the decile, which is consistent with the previous result concerning the households with dependent(s). The overall increase of equivalised income for the intermediate age category ($18 \leq \text{age} < 60$) is most often slightly less than the one observed for the elderly. Finally, it can be observed that the households with one worker or more gain less from the reform, on average and within each decile, than the members of the no-worker category. Concerning gender, in general, only small differences are observed between men and women due to the tax reform.

Figure 4.1 Average percentage change in equivalised income due to the tax reform, by decile (*)



Source: CEPS/INSTEAD (and EUROMOD microsimulation)

(*) Decile groups based on equivalised income without tax reform.

The benchmark is the without-tax-reform value of the equivalised income shown in Table 3.5

4.4 Proportions and characteristics of non-tax payers

Table 4.3 shows that 14% of the fiscal households would not have paid any income tax in 2003, had no tax reform been implemented. Thanks to the tax reform, 20% of them pay no tax in 2003, what maybe also contributes to the higher progressivity of the tax system due to the reform (see *supra*). When individuals are chosen as the unit of analysis, the proportion of non tax payers is increasing from 16% to 24%. The results prevail whatever the data source.

Table 4.2 Average change (in %) of equivalised income for different categories of population, by decile (*)

Characteristics and categories	Data	Deciles										
		(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	All
Type of household												
Single (< 65)	Administrative-based data	2.8	3.4	4.3	5.5	6.4	7.2	7.8	8.4	8.9	10.3	7.2
	Survey-based data	2.0	3.8	4.8	5.9	6.5	7.5	7.4	8.5	8.9	10.6	7.6
Single (> 65)	Administrative-based data	0.0	0.0	1.6	5.4	7.4	8.7	9.2	9.7	10.0	11.8	7.0
	Survey-based data	0.0	0.0	3.1	6.2	7.6	9.0	9.7	10.3	8.7	12.3	7.7
Single with dependent(s)	Administrative-based data	0.0	0.1	0.4	1.9	4.0	5.5	6.7	7.6	8.9	11.9	5.1
	Survey-based data	0.2	0.7	1.5	3.6	6.2	6.3	8.0	7.5	10.3	11.6	4.8
Couple – 0 dependent	Administrative-based data	1.1	3.1	4.1	4.9	5.5	6.1	6.5	6.8	7.7	9.3	6.7
	Survey-based data	1.6	3.1	4.1	5.0	5.8	6.2	6.8	7.4	7.8	9.1	6.8
Couple – 1-2 dependent(s)	Administrative-based data	0.2	0.5	1.3	2.3	3.5	4.6	5.6	6.5	7.5	9.5	5.9
	Survey-based data	0.3	0.8	1.5	3.4	3.7	4.5	5.1	6.4	7.5	9.1	5.7
Couple – 3 dependents or more	Administrative-based data	0.1	0.1	0.4	1.3	2.6	4.0	5.2	6.3	7.2	9.7	4.4
	Survey-based data	0.2	0.2	0.3	2.4	3.5	4.8	5.0	6.9	7.2	8.7	4.7
Age												
Age<18	Administrative-based data	0.1	0.1	0.5	1.5	2.9	4.2	5.4	6.4	7.4	9.7	5.2
	Survey-based data	0.1	0.3	0.7	2.2	3.7	4.3	4.9	6.4	7.3	8.9	4.8
18<=Age<59	Administrative-based data	1.3	1.8	2.4	3.4	4.4	5.4	6.3	7.1	7.8	9.5	6.3
	Survey-based data	1.0	1.7	2.8	4.1	4.8	5.5	6.1	7.3	8.1	9.4	6.4
60<=Age	Administrative-based data	1.1	1.8	3.8	5.3	6.5	7.6	8.0	8.5	8.9	10.8	6.8
	Survey-based data	1.0	2.8	4.1	5.8	6.6	7.7	8.3	8.6	8.6	10.4	7.1
Number of workers in the household												
0	Administrative-based data	1.7	2.0	3.6	5.1	6.3	7.3	7.8	8.3	8.7	9.8	6.0
	Survey-based data	1.0	2.5	4.2	5.7	6.6	7.7	8.0	8.9	8.7	10.4	6.4
1	Administrative-based data	0.9	1.2	2.2	3.3	4.6	5.8	6.7	7.6	8.3	10.3	6.2
	Survey-based data	0.6	1.3	2.4	4.1	5.2	5.7	6.6	7.8	8.5	10.0	6.2
2 or more	Administrative-based data	0.1	0.3	0.7	1.5	2.6	3.9	5.1	6.1	7.2	9.3	6.2
	Survey-based data	0.9	0.6	0.6	2.4	2.7	4.2	4.7	6.2	7.3	8.9	6.1
Gender												
Female	Administrative-based data	0.8	1.2	2.1	3.5	4.8	6.0	6.6	7.2	7.9	9.7	6.1
	Survey-based data	0.8	1.4	2.4	4.1	5.2	5.9	6.5	7.3	8.0	9.4	6.1
Male	Administrative-based data	1.1	1.7	2.4	3.5	4.5	5.6	6.4	7.1	7.8	9.7	6.2
	Survey-based data	0.7	1.7	2.9	4.3	5.0	5.5	6.1	7.3	7.9	9.5	6.3
All	Administrative-based data	0.9	1.4	2.3	3.5	4.7	5.8	6.5	7.2	7.9	9.8	
	Survey-based data	0.7	1.6	2.6	4.2	5.1	5.7	6.3	7.3	8.0	9.4	

Source: CEPS/INSTEAD (and EUROMOD microsimulation)

(*) Decile groups of individuals are based on equivalised income without tax reform (the benchmark is the without-tax-reform picture of the equivalised income shown in Table 3.5).

Table 4.4 is telling more about the characteristics of non-tax payers. Younger people, singles (either when more-than-65-years-old or with dependents) and the members of households where nobody or one person only is working are more often exempt from taxes on income. The proportion of tax payers is also clearly decreasing with the number of dependents.

Table 4.3 Proportions of households and individuals paying taxes with or without the tax reform

Unit of analysis		Fiscal households		Individuals	
Data		Survey-based	Administrative based	Survey-based	Administrative based
Number of units (weighted count [i])		205,802	212,646	419,030	418,861
Do not pay taxes	No tax reform	14.2%	14.0%	16.0%	16.4%
	Tax reform	20.4%	20.0%	23.6%	23.8%
Pay taxes	No tax reform	85.8%	86.0%	84.0%	83.6%
	Tax reform	79.6%	80.0%	76.4%	76.2%

Source : CEPS/INSTEAD (and EUROMOD microsimulation)

[i] Weighted counts : for survey-based data, households' and individuals' weights (differing from 1) are taken into account.

It is to be noticed that a higher at-risk-of-poverty rate does not systematically imply a significantly lower proportion of tax payers within the category (see *Table 3.4*). For example, less-than-65-years-old singles are more often taxed on their income than couples with 1 or more dependents, despite a higher at-risk-of-poverty rate for the former. All these effects partially result from both the overall distribution of income⁴⁴ and the particularities of the Luxembourg tax-benefit system⁴⁵. We can also see from *Table 4.4* that, most often, the lower the proportion of tax payers within a category with no reform, the stronger the proportional drop with the reform implemented.

4.5 Impact on the at-risk-of-poverty rates

In order to see the effect of the tax reform on the poorest, we calculate changes of the at-risk-of-poverty rates due to the tax reform. At-risk-of-poverty rates are shown in *Table 3.4* (see section 3.3) for the “without-tax-reform” environment, which is our benchmark. *Table 4.5* presents changes of the rates when the tax reform is implemented.

Thanks to the reform, equivalised income is increased for all individuals, which might let part of them get out of poverty. Nevertheless, the poverty line (60% of the median equivalised income) is also rising⁴⁶, which interferes with the previous effect. *Table 4.5* presents, on one side, changes of the at-risk-of-poverty rates, due to the tax reform, when the poverty line is frozen on its former state⁴⁷ (60% of the without-tax-reform median equivalised income). The “new-poverty-line” total change, taking into account the shift in the poverty line, is also shown, on the other side.

Table 4.4 Proportions of individuals paying taxes, given their characteristics, with or without the tax reform

Characteristics	Categories	Data	Share in total population	DO NOT PAY taxes		PAY taxes	
				If NO tax reform (I)	If NO tax reform (II = 100% - I)	If TAX REFORM	
						% among "tax payers when NO tax reform" (III, in % of II)	% of population (IV = II * III)
All		Administrative-based	100%	16.4%	83.6%	91.1%	76.2%
		Survey-based	100%	16.0%	84.0%	91.0%	76.4%
Gender	Female	Administrative-based	51%	18%	82%	90%	74%
		Survey-based	51%	17%	83%	91%	75%
	Male	Administrative-based	49%	15%	85%	92%	79%
		Survey-based	49%	15%	85%	91%	78%
Age	Age < 18	Administrative-based	22%	29%	71%	85%	61%
		Survey-based	22%	28%	72%	84%	61%
	18<= Age < 60	Administrative-based	59%	14%	86%	92%	79%
		Survey-based	59%	14%	86%	92%	79%
	Age >= 60	Administrative-based	20%	11%	89%	94%	85%
		Survey-based	19%	8%	92%	94%	86%
Type of household	Single (< 65)	Administrative-based	19%	8%	92%	98%	90%
		Survey-based	17%	11%	89%	98%	87%
	Single (>= 65)	Administrative-based	7%	28%	72%	86%	62%
		Survey-based	6%	20%	80%	84%	67%
	Single with dependent(s)	Administrative-based	6%	53%	47%	77%	36%
		Survey-based	7%	53%	47%	75%	36%
	Couple - 0 dependent	Administrative-based	21%	2%	98%	95%	93%
		Survey-based	21%	3%	97%	95%	92%
	Couple - 1-2 dependent(s)	Administrative-based	35%	15%	85%	89%	75%
		Survey-based	35%	13%	87%	88%	76%
	Couple - 3 dependents or more	Administrative-based	12%	32%	68%	84%	57%
		Survey-based	14%	26%	74%	89%	66%
Number of workers in the household	0	Administrative-based	26%	16%	84%	93%	78%
		Survey-based	25%	19%	81%	92%	74%
	1	Administrative-based	45%	21%	79%	89%	71%
		Survey-based	45%	21%	79%	89%	70%
	2 or more	Administrative-based	29%	10%	90%	92%	83%
		Survey-based	30%	6%	94%	93%	88%

Source : CEPS/INSTEAD (and EUROMOD microsimulation)

Guide to reader : 72% of the less than 18-years-old individuals are paying taxes in the no-tax-reform environment (survey-based data). 84% of them only are still paying taxes if the tax reform is implemented, which implies that 61% of the less than 18-years-old individuals are taxed under tax reform.

We can first observe from Table 4.5 that the change of the at-risk-of-poverty rate, when the poverty line is frozen on its initial state, is negative. On the contrary, the total change is positive (the risk of poverty is increased). The former result is of course that expected as all individuals are gaining (equivalent) income through the tax reform. The latter result can be explained by the vertically inequitable nature of the tax reform (see Figure 4.1 and section 4.2), which induces the shift-in-poverty-line effect overcoming the gain-in-income one.

Second, the total effect appears to be stronger for singles with dependents, couples with dependents, households with workers and younger individuals.

Table 4.5 *Changes in at-risk-of-poverty rate due to the tax reform (*)*

Characteristics and categories	Administrative-based data		Survey-based data	
	Frozen poverty line(**)	New poverty line(***)	Frozen poverty line(**)	New poverty line(***)
All	-0.3%	3.3%	-0.7%	3.1%
Type of household				
Single (<65)	-1.1%	3.3%	-1.9%	1.0%
Single (>=65)	-0.0%	0.3%	-0.0%	1.4%
Single with dependent(s)	-0.1%	10.0%	-0.0%	5.6%
Couple - 0 dependent	-0.2%	1.2%	-1.3%	0.4%
Couple - 1-2 dependent(s)	-0.1%	3.3%	-0.2%	3.2%
Couple - 3 dependents or more	-0.1%	5.0%	-0.0%	9.3%
Number of workers in the household				
No worker	-0.4%	1.5%	-0.5%	1.2%
1 worker	-0.5%	4.9%	-1.0%	4.4%
2 workers or more	-0.0%	2.3%	-0.2%	2.8%
Age				
Age<18	-0.0%	5.4%	0.0%	6.4%
18<=Age<59	-0.5%	3.5%	-1.0%	2.7%
60<=Age	-0.1%	0.3%	-0.5%	0.6%
Gender				
Female	-0.2%	3.3%	-0.7%	3.0%
Male	-0.4%	3.3%	-0.6%	3.3%

Source : CEPS/INSTEAD (and EUROMOD microsimulation)

(*) Changes as compared to the without-tax-reform at-risk-of-poverty rates shown in Table 3.4

(**) 60% of the former (without-tax-reform) median equivalised income

(**) 60% of the new (with-tax-reform) median equivalised income

Finally, regarding the comparison between administrative-based and survey-based simulations, important differences can be observed, both on the qualitative side (ranking of gainers or losers) and on the quantitative side (see for example the total effect for singles with dependents and couples with three dependents or more).

It can also be shown that the income gap ratio is reduced thanks to the reform : from 28% (resp.

18%) down to 24% (*resp.* 15%) through survey-based (*resp.* administrative-based) data.

5. CONCLUSIONS

We initiate, through the EUROMOD microsimulation framework, the cross-validation of administrative data derived from the recently implemented Luxembourg Social Security Data Warehouse, on the one side, and of the PSELL3/EU-SILC survey data, on the other side.

We choose to work on the 2003 population in Luxembourg in all cases. As a benchmark, the “without 2001-2002 Luxembourg tax reform” environment is chosen.

Administrative data have some obvious limitations compared to survey data, because in general administrative data record only information needed for administrative purposes like collecting social contributions or paying social benefits, whereas the questionnaires for survey data may be designed specifically for defined research purposes, including a need for standardization and comparability between countries⁴⁸. On the other hand, the kind of data provided by the Luxembourg Social Security Data Warehouse have also some important advantages over survey data, like completeness⁴⁹, timeliness, availability of time series of data of different granularity, like yearly or monthly data⁵⁰. Moreover, administrative data include some information not available in survey data, *e.g.* in relation with health and long term care, cross-border workers (37% of the employment in 2003, what is essential regarding the tax-benefit system in Luxembourg), etc.

Before comparing the datasets as set up through the EUROMOD input framework, it seems important to dispose of dissimilarities that we can control for, regarding the target populations and the lack of precision in some important (income-related) variables. We have then to drop about 6% of the initial population in both datasets and adapt variables like capital income-related ones which are missing in the administrative-based dataset.

An important implication is also to adopt the fiscal household as the unit of analysis, rather than the more usual residence household. This may play a role concerning the comparison of outcomes to other studies. The fiscal household being included into residence units, this leads to a distribution of equivalised income which departs from usual ones, with lower values for both means (10% less when fiscal households, if the benchmark) and medians (-5%). The at-risk-of-poverty rate and the gain or loss for the different categories of population are also affected.

Regarding several non-monetary characteristics, like the age classes and the types of households, the two EUROMOD input datasets appear to be satisfactorily similar. For monetary characteristics a first discordance is observed, mainly stemming from a gap in primary income which is, on average, 7% lower in administrative-based data, an observation to be further explored. The difference in primary income implies downstream effects on equivalised income.

Under the benchmark environment, the Gini coefficient and other inequality indices most often show a similar distribution of equivalised income in both datasets. Nevertheless, regarding the leftist part of the distribution, the at-risk-of-poverty rates are higher through survey-based data, for all categories under study⁵¹. Whatever the dataset under consideration, usually more at-risk-of-poverty categories are shown up, like “singles with dependent(s)” and the members of households where nobody is working. Nevertheless, next to the qualitative comparison of outcomes, a few striking discrepancies appear, for example for the “singles with dependent(s)” who are marked twice more at risk of poverty through survey-based data in the without-tax-reform environment.

It is shown that the 2001-2002 tax reform in Luxembourg results, for the resident population of 2003, in a rise of mean equivalised income by 6%. More specifically, the elderly and singles without dependent(s) seem to experience better gains, on average, than other categories in the corresponding typology. The higher the income, the higher the relative gains, whatever the category under consideration. The average gain for the highest decile of the population is about 9%, to be compared with less than 1% for the lowest decile, whatever the dataset. The Gini coefficient, higher with the reform, follows. This increase in inequality due to the reform is shown to result from a magnitude effect, *i.e.* the drop in the average rate of taxation, and not from the progressivity which is augmented, indeed. The at-risk-of-poverty rates of the different categories are increasing. But some, like singles with dependents and couples with three dependents or more are experiencing a rise which may considerably differ in intensity between administrative-based and survey-based data.

On the whole, we can conclude at a satisfactory “proximity” (*e.g.* a statistical compatibility as assessed through confidence intervals) between the administrative-based and survey-based data, whether as input data for EUROMOD or as far as the effects of the 2001-2002 tax reform are concerned. Nevertheless, this robustness in the results regarding the source data is less observed when some monetary characteristics and the at-risk-of-poverty rates (whatever absolute levels or changes due to the tax reform) are considered. Even if the change of the average at-risk-of-poverty rate is similar with the two datasets, outcomes for specific categories may strongly differ⁵².

Of course, this promising cross-validation outcome lies on the treatment we have chosen to impose to the initial datasets for making them targeting closer populations and getting rid of the effect of some income-related missing or unevenly biased variables.

The next step might be to further explore these questions, especially on the administrative side or regarding the income measurement, in order to make those methodology-based arrangements essentially no longer necessary. An important extension concerning administrative data in Luxembourg would also be to properly deal with (postal) addresses, *e.g.* in order to make residence and institutional households identifiable and spatial analysis feasible.

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APPENDIX : THE TAX SYSTEM IN LUXEMBOURG AND THE 2001-2002 REFORM

In this appendix, we describe the main characteristics of the tax system in Luxembourg and the modalities of the 2001-2002 reform. We focus on elements relevant to the present analysis only.

A.1 The tax system in Luxembourg

In Luxembourg, the tax unit is the “family” which might not include all members of a “residence household”⁵³. To belong to the same family, you must either be (official) spouse or a dependent child. Two cohabiting but non-spouse persons are then members of separate tax units. A “child” belongs to his/her parents’ tax unit if unmarried and less than 21 years old. As soon as married, a son/daughter enters his/her own tax unit. The same prevails if a person is older than 21 years and is neither a student any longer nor a disabled person. Of course, the set of rules includes many other aspects, related to the questions of “earnings” of dependent children, children living part-time only with their parents, status changing during the civil year, spouses separating/being divorced, etc. These questions, although essential to the system as a whole, are not discussed here because they are not necessary for a clear understanding of the present analysis.

The tax system on income being progressive, it is important to know how the tax basis is defined. The taxable income is firstly involving the yearly gross earnings of all the members of the family (as defined earlier) : wages, business profits, income from farming and forestry/self-employment/pensions, investment and property incomes, etc. Social contributions and several tax allowances (*e.g.* for travel expenses or if a lone parent) are then deducted from gross amounts to define the *adjusted taxable income*. The adjusted taxable income is rounded⁵⁴ before applying the *tax schedule* (brackets and marginal rates) which is described in *Table A.1* for the years 2000 up to 2003. This tax schedule is used depending on the tax class the tax payer belongs to : class 1, class 1a or class 2. The *tax class* is defined given both family and individual characteristics of the tax payer, as shown in *Table A.2*.

Table A.1 Income tax schedule from 2000 to 2003 (tax brackets in EUR)

BAND #	2000		2001		2002		2003	
	Tax BRACKETS (*)	Marginal tax RATES	Tax BRACKETS (*)	Marginal tax RATES	Tax BRACKETS	Marginal tax RATES	Tax BRACKETS	Marginal tax RATES
1	6,693	0%	9,668	0%	9,750	0%	9,750	0%
2	8,775	6%	11,378	14%	11,400	8%	11,400	8%
3	10,486	16%	13,089	16%	13,050	10%	13,050	10%
4	12,196	18%	14,799	18%	14,700	12%	14,700	12%
5	13,907	20%	16,510	20%	16,350	14%	16,350	14%
6	15,617	22%	18,220	22%	18,000	16%	18,000	16%
7	17,328	24%	19,931	24%	19,650	18%	19,650	18%
8	19,038	26%	21,641	26%	21,300	20%	21,300	20%
9	20,749	28%	23,352	28%	22,950	22%	22,950	22%
10	22,459	30%	25,062	30%	24,600	24%	24,600	24%
11	24,170	32%	26,773	32%	26,250	26%	26,250	26%
12	25,880	34%	28,483	34%	27,900	28%	27,900	28%
13	27,591	36%	30,193	36%	29,550	30%	29,550	30%
14	29,301	38%	31,904	38%	31,200	32%	31,200	32%
15	31,011	40%	33,614	40%	32,850	34%	32,850	34%
16	32,722	42%	> 33,614	42%	34,500	36%	34,500	36%
17	65,444	44%			> 34,500	38%	> 34,500	38%
18	> 65,444	46%						

Source : Fiscal administration and CEPS/INSTEAD (*)

(*) Limits of bands rounded to nearest unity in 2001 and 2002 (originally in LUF : EUR becomes legal tender on 1st of January 2002 only)

Guide to reader : In 2002, an adjusted taxable income of 12,000 EUR is taxed

$0\% + 8\% * (11,400 - 9,750) + 10\% * (12,000 - 11,400) = 192 \text{ EUR}$ (rounding error included).

Tax payers belonging to “class 1” (e.g. a single person) are taxed directly following the schedule shown in *Table A.1*. For “class 2” tax payers (e.g. a married couple), the adjusted taxable income is initially halved, then the tax liability is first calculated as for single (“class 1”) persons and finally it is multiplied by two⁵⁵. For “class 1a” tax payers (e.g. a lone parent with children), the story does appear to be more complex. The adjusted tax income is reduced by a part (fixed to 25% in 2000) of its complement to a given basis (fixed to 40,159 EUR⁵⁶ in 2000) and, then, the tax liability calculated as for “class 1” tax payers⁵⁷. Additionally, the marginal tax rate can never exceed its

maximum possible value (46% in 2000, see *Table A.1*)⁵⁸. Up to the year 2000, an additional rule is applied. The tax liability resulting from the previous calculation is reduced, when needed, insofar the “net” income (adjusted taxable income – tax liability) reaches a minimum threshold fixed to 8,924 EUR⁵⁹ for “class 1” tax payers, 15,865 EUR⁶⁰ for the others classes⁶¹. Finally, several tax credits (*e.g.* for dependent children) can still be deducted from the liability just evaluated, and an additional tax is imposed as a contribution to the unemployment fund.

Table A.2 *Tax classes and tax payer characteristics*

Class	Characteristics (*)
1	Non-married single without dependent children and less (<) than 65 years old Separated or divorced since at least 3 years (>=) without dependent children and less than 65 years old
1a	Non-married single with dependent children Separated or divorced since less than 3 years with dependent children Non-married single more than 64 years old Widowed since more than 3 years
2	Married people Separated, divorced or widowed for less than 3 years

Source : Fiscal administration (selection of criteria from CEPS/INSTEAD)

(*) All characteristics (most often) as observed on 1st of January of the fiscal (civil) year

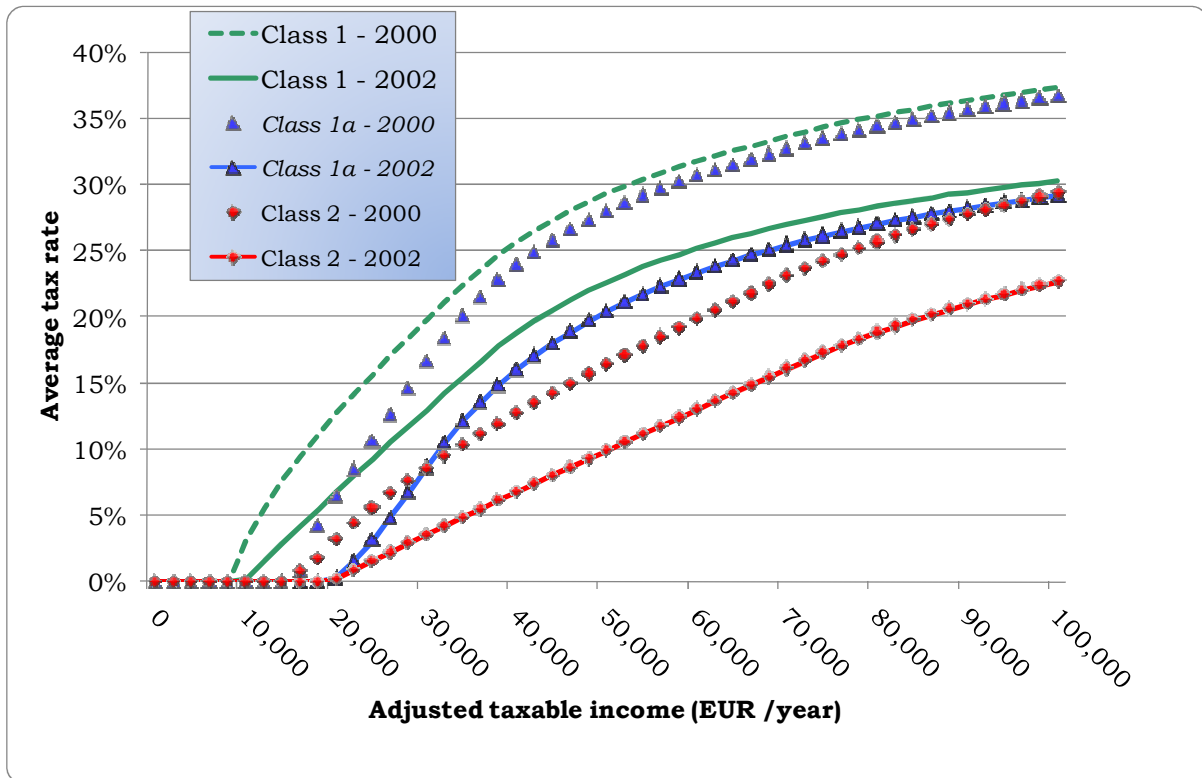
A.2 The 2001-2002 tax reform

We now describe the characteristics of the 2001 and 2002 tax reform (one of our concerns in the present paper), which is implemented in two steps. Having a look at *Table A.1* :

- The first tax bracket is enlarged, which means that the minimum income before tax is increased, from 6,693 EUR in 2000 up to 9,750 EUR in 2002
- The number of tax brackets is reduced, from 18 down to 17 in 2002 and band widths are made uniform to 1,650 EUR in 2002
- The maximum tax rate significantly decreases, from 46% to 38% in 2002

Additionally, for “class 1a” tax payers, the basis for complement calculation (see *supra*) is fixed to 38,671 EUR⁶² in 2001 (40,159 EUR in 2000) and 39,000 EUR in 2002. The proportional part for reduction jumps from 25% in 2000 to 50% in 2001 and 2002⁶³. These computations are still to be made insofar as the marginal tax rate does not exceed its maximum possible value (46% in 2000, 42% in 2001, 38% in 2002). Finally, the rules linked to the threshold for the “net” income resulting from the tax liability, henceforth useless, are dropped. It must also be noticed that the 2001-2002 tax reform leaves the rules prevailing for the composition of fiscal households unchanged.

Figure A.1 Impact of the 2001-2002 tax reform
on the average rate of tax on income, given the tax class



Source : CEPS/INSTEAD

Figure A.1 shows how taxes are changing through the reform, given the adjusted taxable income and the tax class to be considered. The gain for tax payers is rather high, about a 7 % drop in the average tax rate for all classes when an adjusted taxable income of 50,000 EUR / year (*idem* for “class 1” tax payers if an income of 30,000 EUR, 8% for “class 1a”, 5% for “class 2”).

ENDNOTES

- 3 Source : STATEC - National statistical institute of Luxembourg (through <http://www.statistiques.public.lu/>).
- 4 For a detailed presentation of social indicators, see Atkinson et al. (2002) and Marlier et al. (2006).
- 5 <http://www.iser.essex.ac.uk/msu/emod/>
- 6 For a comparison between outcomes from interview and register data, see also *e.g.* Nordberg (2003) and Nordberg and Penttälä (2001), for Finland.
- 7 “Panel Socio-Economique Liewen zu Lëtzebuerg” (see <http://www.ceps.lu/>).
- 8 EU-SILC is an instrument aiming at collecting timely and comparable cross-sectional and longitudinal multidimensional microdata on income, poverty, social exclusion and living conditions (see <http://epp.eurostat.ec.europa.eu/>).
- 9 See <http://www.statec.public.lu>
- 10 Inspection Générale de la Sécurité Sociale (see <http://www.mss.public.lu/>).
- 11 MSW = 1368.74 EUR / month as on 1st of January 2003.

A track for overcoming the problem would be to deal with postal addresses, after improvement in their normalization.

Either married all along the year, or married during the (civil) year, or divorced during the year.

If unmarried parents, the child goes to his mother's household, unless an explicit demand from the mother to link the child with his father concerning the family benefits. If born during the year, or when family benefits come to an end during the (civil) year, a child is still linked to his parents' household.

Information for non-residents is partially available in the Data Warehouse.

Total disposable income = (earnings – social contributions – taxes + social benefits) summed up over all members of the household.

$2,110 = 2,110 / 1.0$

$1,000 = 1,800 / 1.8$

Both the household disposable income (to be attributed to each member within the household) and the individual equivalent weight are unambiguously lower in a “fiscal” framework, compared to the “residence” one. But the impact on the individual ratio is qualitatively unknown *ex ante* (see example in Table 2.2), as well as the average evolution of the equivalised income throughout the population.

When the weighting of cases (designed for better fitting the Luxembourg population) is implemented / taken into account.

Of course, the adaptation/selection procedure just described may help. Moreover, the weighting process of the survey data is also based on administrative data sources partially overlapping our administrative-based dataset. Nevertheless, this was not at all *a priori* a guarantee for comparability for fiscal households.

Primary income = gross employment and self-employment income + gross investment and property income (excluded from results in Table 3.3, for comparability reasons) + maintenance payments + gross private pension benefits (low, on average, in Luxembourg) + apprentice income.

Nordberg (2003) gets for Finland a level of « earned income » (close to our « primary income ») lower for register data in 1995 but higher in 1999.

If a confidence level of 99%, the conclusion does not change.

For example, as a proxy for “institutional households”, all individuals more than 75 years old and mentioned as “single without dependent” are dropped from both the administrative-based dataset (“institutional households” included in initial data) and survey-based data (for symmetry reasons).

The mean primary income goes from 1,384 up to 1,464 on the administrative-side, from 1,493 up to 1,539 on the survey-side, with, for the latter, a confidence interval changing to [1,459 - 1,619].

This information is partially available in the input datasets. While simulating through EUROMOD, we avoid the question of non-take-ups and, on top of that, dissimilarities due to differing levels of non-take-ups that might be observed in administrative-based and survey-based data.

The Atkinson inequality index can be expressed as $A(\varepsilon) = 1 - \left[\frac{1}{n} * \sum_i \left(\frac{x_i}{\mu} \right)^{1-\varepsilon} \right]^{\frac{1}{1-\varepsilon}}$, where n is the number of individuals, x_i is the income level, μ the average income and ε the inequality aversion coefficient. It takes a value between 0 (minimum inequality) and 1 and can be interpreted in terms of social welfare : it shows that part of total income which might be saved, while keeping the social welfare (associated to the Atkinson index) unchanged and distributing the remaining disposable income equally. See Essama (2000) and Lambert (1993).

The Gini coefficient takes a value between 0 (minimum inequality) and 1. If we define the social welfare as $W(x) = \frac{1}{n^2} \sum_i \sum_j \min\{x_i, x_j\}$, then it can be shown that $W(x) = \mu * (1 - G)$, where n is the number of individuals, $x_{i/j}$ is the income level, μ the average income and G the Gini inequality index. See Essama (2000) and Lambert (1993).

These would be fully compatible in all cases if a 99% confidence interval.

A decomposition of inequality indices by population sub-group could also enlighten the question.

The 95% confidence interval for the average poverty rate through survey-based data is [8.4% - 10.7%].

Only couples with 3 dependents or more are signaled less at-risk-of-poverty through survey-based than administrative-based data.

Table 3.5 helps in understanding the reason why, concerning the whole population. With ratio of mean income between the first decile (nearby the poverty line) and the fifth one (close to median income) of 0.55 (= 47% / 85%) in administrative-based data, to be compared with 0.46 for the survey-based data, we can expect that fewer members of the first decile in the administrative-based data are to be trapped below the poverty line.

The Foster-Greer-Thorbecke poverty index with parameter 1, which is the product of the poverty rate and the income gap ratio, is shown to be 0.027 through survey-based data (*resp.* 0.013 through administrative-based data), leading to an income gap ratio of $0.027/0.096 = 28\%$ (*resp.* 18%). The income gap ratio = $1 - (\text{Mean income of the "poor"}/\text{Poverty line})$: it refers to the extent to which the incomes of the poor lie below the poverty line.

A "Single with dependent(s)" is most often a single parent with dependent child(ren). See Table 3.1.

See Callan and Walsh (2006) for a proposal of alternative benchmarks, including a "distributional neutral policy", mainly appropriate when a comparison between countries.

As it is presently designed, neither feedback effects through prices or budget constraints, nor behavioral answers. Moreover, EUROMOD is static which means that the time dimension (hence links through time) is not included in the model.

See section 3.3.

Vertical redistribution consists in reducing inequalities of equivalised income between households who have the same structure, but a different income level.

Horizontal redistribution consists in reducing inequalities of equivalised income between households who have the same income level, but a different structure.

The increase in progressivity can be explained by an enlargement of the first tax bracket (tax rate = 0%) which overcomes, regarding the measurement of progressivity through the Kakwani index, the effect of reducing the marginal tax rates for higher income levels.

We could also compare mean income for deciles determined from the income distribution when no tax reform, on one side, to deciles determined with the tax reform implemented, on the other side (the result is not reported in the paper but available on demand). We preferred the above presentation which leaves the members of the deciles unchanged.

There is no gain for first two deciles of more-than-65-years-old singles, which means that the members of those categories are taxed neither with nor without the reform. As can be seen from Table 3.5, the mean equivalised income (which is simply disposable income, for singles) for second decile is about 1,300 EUR / month or 15,600 EUR / year for more-than-65-years-old singles, which is below the threshold for taxable income for "class 1a" tax payers (15,865 EUR in 2000, above later on).

One counterexample is to be found for 2-workers' households, between first and second deciles, in survey-data only.

For example, singles with dependent(s) and households where nobody or one person only is working show an equivalised income more concentrated on the first deciles, compared to average (see Table 3.4), a first condition for lower taxation.

For example, more-than-65-years-old singles are benefitting from the advantageous "class 1a" taxation when non-married (see appendix). The Luxembourg tax-benefit system is also exhibiting an important "family advantage" (Berger *et al.*, 2002).

Due to the tax reform, the poverty line is increasing from 1,188 EUR (see Table 3.3) to 1,254 EUR (+ 5.6%) when survey-based data, from 1,138 EUR to 1,199 EUR (+ 5.4%) when administrative-based data.

See also Immervoll *et al.* (2006).

See Figari *et al.* (2007).

Which implies that working on categories is easier than with survey-based data where an appropriate procedure for the weighting of cases may be necessary.

It may be important to know, as far as the tax-benefit system is concerned, how the value of a variable evolves during the year (*e.g.* in Luxembourg : the marital status).

Out of the income characteristic, we have chosen to focus our attention on typologies based on the age (<18, >= 60, others), the gender, the number of workers within the (fiscal) household and the type of household (single < 65, single 65+, single with dependents, couples with 0/1-2/3 dependents).

54 Several determinants play indeed a role when categories are compared and cannot always be easily
disentangled : the overall distribution of disposable income, the composition of households and the
characteristics of the tax-benefit system. This complexity explains why impacts on categories of
populations, in terms of relative gain and ranking, may depend on the criteria shown up.

55 A residence household is defined as all persons “living together” at the same address.

56 To the nearest lower multiple of EUR 50, from 2002 on.

57 Example : In 2002, a married couple with adjusted taxable income = 30,000 EUR will be attributed a
tax liability of 1,074 EUR = $2 * 537$ EUR (tax liability for an income of 15,000 EUR when “single”
without children).

58 1,620,000 LUF (1 EUR = 40.3399 LUF).

59 Example : a lone parent with children whose taxable income is 30,000 EUR is attributed a tax
liability of 4,970 EUR [tax liability when a “class 1” tax payer whose income is 30,000 – 25% *
(40,159 – 30,000) = 27,460 EUR]. *NB : the “complement” calculation is performed only if the adjusted
taxable income is less than the basis (40,159 EUR). Moreover, if leading to a negative outcome, the
value is set to “0”.*

60 Formally, this means that when an increase of income by 1000 EUR, the supplement in tax liability
can never exceed, in 2000, 460 EUR for “class 1a” tax payers.

61 360,000 LUF.

62 640,000 LUF.

63 Example : a young single without children (hence « class 1 ») whose adjusted tax income is 9,000
EUR in 2000 should have paid, given the schedule for his class, a tax of 161 EUR. Nevertheless, this
would result in a “net” income of 9,000 – 161 = 8,839 EUR, which is below the threshold of 8,924
EUR, hence leading to a reduction of the tax down to 76 EUR and a net of 8,924 EUR.

64 1,560,000 LUF.

65 Example : a lone parent (with children) whose taxable income is 30,000 EUR in 2002 is now
attributed a tax liability of 1,125 EUR [tax liability when a “class 1” tax payer whose income is
30,000 – 50% * (39,000 – 30,000) = 25,500 EUR].