DUAL PROGRESSIVE INCOME TAX (DPIT)

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BETTER POLICIES FOR BETTER LIVES

Countries have moved away from (semi-) comprehensive income tax systems……

- **Comprehensive income tax system** – taxes all or most income less deductions (net income) under the same rate schedule. Wage and capital income are taxed at the same rates, usually according to a progressive rate schedule; the value to the taxpayers of the tax allowances increases with income.
  - Typically no integration between corporate and personal level capital income taxes
  - No country implements a full comprehensive income tax system:
    - Very difficult to tax changes in wealth on accrual (the recent proposal in Chile is very interesting)
    - Imputed income from owner-occupied housing in often taxed at lower rates
    - Fringe benefits are typically taxed at lower rates than other labour income
    - Particular form of savings are usually tax-favoured (e.g. pension savings)
  - Typically results in a very high tax burden on labour and capital income, leading reduced work incentives and saving.
  - Tax-arbitrage behaviour as a result of the many tax expenditures
  - Are comprehensive income tax systems compatible with individual taxation (individual as tax unit) or rather imply that the family is the tax unit?

…..towards (semi-) dual income tax systems

- **Dual income tax system** – levies a proportional tax rate on all net income (capital, wage and pension income less deductions) combined with progressive rates on gross labour and pension income. This implies that labour income is taxed at higher rates than capital income, and that the value of the tax allowances is independent of the income level.
  - Double taxation of dividends and sometimes capital gains would typically be prevented through an imputation system
  - Why a proportional (and usually lower) rate on capital income:
    - The loss of vertical equity might be largely offset by efficiency gains
    - The lower tax rate offsets the impact of the taxation of the nominal rate of return to capital, even though the inflation premium just compensates for the erosion of the real value of the assets
    - To tackle tax evasion as capital is more mobile than labour income.
  - In order to ensure an equal tax treatment of wage earners and the self-employed, the income of the self-employed might has to be split into a labour and a capital income component. This is necessary also to prevent self employed to incorporate.
  - Particular types of capital often continue to be taxed favourably (pensions)
  - Imputation tax credits are typically not available for foreign shares.

Does AEIO allow countries to move towards Dual Progressive Income Tax systems?

- **Automatic Exchange of Information for Tax Purposes** might become a game changer which allows countries to tax capital income at slightly higher and more progressive rates.

- Statutory CIT rate cuts imply that the burden on capital income is shifted from the corporate towards the personal level. Such a shift entails efficiency and equity gains, but requires that tax evasion can be prevented.

- From DIT towards a **Dual Progressive Income Tax system**?
  - Tax capital income separately from labour income (schedular tax treatment)
  - Capital income can be taxed at modestly progressive tax rates – shift some of the SSCs from labour towards capital income
  - Basic allowance in the capital income "box" could exempt a minimum amount of capital income (inclusiveness) – possibly replacing other capital income tax privileges?
  - Top tax burden on capital income (taking CIT and capital income taxes at personal shareholder level into account) can be aligned with top tax burden on labour income.
  - What about the owner-occupied house and other immovable property?

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