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TAXATION AND MORE REPRESENTATION? ON FISCAL POLICY, SOCIAL MOBILITY AND DEMOCRACY IN LATIN AMERICA

by

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PREFACE

The way taxes are levied and resources allocated is at the heart of the social contract between citizens and the state. For developing countries, frequently characterised by low levels of public revenues, pressing social policy needs and tenuous democracies, this issue may be even more important than in OECD countries. Fiscal policies to support investments in nutrition, health, education, infrastructure and unexploited comparative advantages are not only technical challenges; they are also political challenges. Fiscal legitimacy is often low, as citizens in developing countries frequently do not trust that tax revenues are well spent, making them less willing to pay taxes in the first place.

This paper by Christian Daude and Ángel Melguizo, economists of the OECD Development Centre, sheds useful light on the debate in Latin America. Latin Americans that are part of the social contract and have higher levels of education are more willing to pay taxes, and accept higher levels of taxation. The more they perceive a good quality of public services (in particular education and health), the more they are willing to pay taxes. Finally, those that think to have climbed up the social ladder, and/or expect their children to rise further still, agree that good citizens should pay taxes, and reject that current tax rates are too high.

This is good news. Nevertheless, in several countries in Latin America, low observed levels of tax revenues mean that tax hikes are needed, but low fiscal legitimacy might render the best-designed tax reform unenforceable. So, the best way to build confidence in reforms is by increasing the efficiency and transparency of expenditure and by improving life conditions of important shares of the population at present excluded from the social contract. This would create a broader constituency that supports improvements in public expenditure and would be more willing to finance them.

This paper has been elaborated as part of the LAC-OECD Initiative, and in particular as part of that Initiative's pillar entitled “Fiscal Policy: Improving Taxation and Public Expenditure”, which is a joint project of the OECD Centre for Tax Policy and Administration and the OECD Development Centre. This work is generously supported by Spain, Chile and Mexico, that we thank. We hope it will contribute to a better informed debate on fiscal policy, helping ultimately to improve the well-being of the people in Latin America and the Caribbean.

Mario Pezzini
Director
OECD Development Centre
September 2010

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RÉSUMÉ

Le contrat social est-il brisé (en crise) en Amérique latine ? C'est ce que de nombreux auteurs laissent entendre, qui s'appuient sur les fortes inégalités, le faible niveau de taxation et le manque de qualité des services publics de la région. Cet article analyse de façon empirique la relation entre la politique budgétaire, la mobilité sociale et la consolidation démocratique en Amérique latine et dans les Caraïbes, en utilisant les enquêtes régionales *Latinobarómetro* pour 2007 et 2008. D'une façon générale, nos résultats ne confortent pas complètement l'hypothèse de perspectives de mobilité sociale ascendante (POUM), et montrent l'influence de la perception de la qualité des services publics, entre autres choses, sur la disposition des contribuables à s'acquitter de leurs taxes et impôts. Bien qu'un long chemin reste encore à parcourir, nos résultats semblent globalement indiquer qu'il existe une base pour un renforcement du contrat social en Amérique Latine.

Classification JEL: E62, I38, P16

Mots clé: Démocratie, mobilité sociale, politique budgétaire, Amérique Latine

ABSTRACT

Is the social contract in Latin America broken? Many authors have suggested this is the case, given the high levels of inequality, the low levels of taxation and the low quality of public services observed in the region. This paper analyses empirically the relationship between fiscal policy, social mobility and democratic consolidation in Latin America and the Caribbean, using the 2007 and 2008 rounds of the regional *Latinobarómetro* survey. In general, our results do not firmly support the prospect of upward mobility hypothesis, and show that the perception about the quality of public services, among others, matters for the willingness to pay taxes. All in all, we interpret our results as an indication of that – although there is still a long way to go – the potential basis for a stronger social contract in Latin America exists.

JEL Classification: E62, I38, P16

Keywords: democracy, social mobility, fiscal policy, Latin America

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I. INTRODUCTION

In the second half of the 18th century, the population of the British colonies in North America rallied behind the demand ´no taxation without representation!´ Indeed, citizens in the colonies were taxed by Britain, but had no direct representation in the British parliament, a state of affairs they considered an illegal denial of their rights as Englishmen. This movement was especially popular in Boston, where protest movements culminated in December 1773. The *Boston Tea Party*, as it became known, arose when a dispute about whether to accept three shiploads of tea – and pay the British taxes on them – escalated into direct action. A group of colonists boarded the ships and destroyed their cargo by throwing it into the Boston Harbour. Historians point to the incident as the spark that ultimately led to the war of independence and the establishment of the United States of America, founded on the principles of democracy and fiscal legitimacy.[1] Clearly, this event highlights how fiscal policy is at the very heart of the social contract between citizens and the state.

While it is undeniable that public finance and democracy do not always go hand-in-hand, democracy is the political regime under which social preferences have the greatest potential to be reflected, via fiscal policy, in resource allocation, income redistribution, and economic stabilisation. In this framework, more than a century ago Wicksell raised the 'voluntary exchange theory of revenue-expenditures', in which taxes appear as voluntary payments by individuals in exchange of public services (see Musgrave, 1939 for a critical discussion).

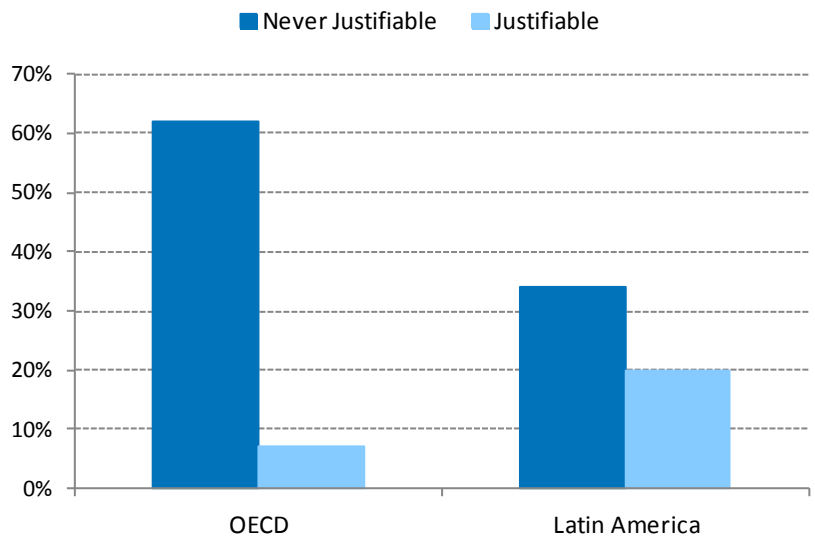
This paper analyses a particular dimension of this issue, namely the relationship between citizens´ perceptions regarding social mobility, the functioning of democracy, and their attitudes towards fiscal policy. We focus on Latin America and the Caribbean. This is a particularly interesting region, characterised by very high levels of income inequality (the highest in the world), and relatively low levels of fiscal revenues and redistribution.[2] This picture has led some authors to ask whether the social contract is broken (or at least extremely weak) in Latin America. Figure 1 shows one aspect of this weak social contract compared to OECD countries: low tax morale. On average, citizens in Latin America are almost three times more likely to justify tax evasion (20% versus 7% in OECD countries) and only 34% of respondents in Latin America consider tax evasion always wrong compared to an average of 62% in OECD countries.

1 http://en.wikipedia.org/wiki/No_taxation_without_representation (last accessed August 31, 2010).

2 For previous analyses on the relationship between fiscal policy and the political economy in Latin America, see OECD (2008) and the references therein.

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Figure 1. **Tax morale in Latin America and OECD countries (´Do you think cheating on taxes is justifiable?´)**



Source: Authors' calculations based on *Latinobarómetro* survey 2008 and *Values Survey database*.

Notes: The average for Latin America includes data from 18 countries: Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Dominican Republic, Ecuador, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, Panama, Paraguay, Peru, Uruguay, and Venezuela for 2008. For the OECD, it includes data from 20 countries: Australia [2005], Canada [2006], Finland [2005], France [2006], Germany [2006], United Kingdom [2006], Italy [2005], Japan [2005], Mexico [2005], Netherlands [2006], New Zealand [2004], Norway [2007], Poland [2005], Slovenia [2005], South Korea [2005], Spain [2007], Sweden [2006], Switzerland [2007], Turkey [2007], United States [2006]. The specific question asked is: Please tell me for each of the following statements whether you think it can always be justified, never be justified, or something in between, using this card. (Read out statements. Code one answer for each statement). Cheating on taxes if you have a chance: 1 – Never Justifiable, 2, 3, … 10 – Always Justifiable. 'Never Justifiable' refers to the percentage of answers that reply 1; 'Justifiable' is the fraction of answers between 5 and 10.

This paper explores empirically the relationship between fiscal policy, social mobility and democratic consolidation in Latin America and the Caribbean, based on two recent rounds (2007 and 2008) of the regional *Latinobarómetro* survey. In the second section we briefly summarise the theoretical and empirical literature. The third section reports the basic trends in the consolidation of democratic regimes in Latin America, consolidation and the level of support expressed for democracy among different income groups. In the fourth section we ask whether perceptions of the possibility of social mobility, and of the quality of public services condition the role of fiscal policy in the social contract, and for the level of taxation and redistribution; that is, do people's views about appropriate levels of taxation and their willingness to pay taxes change when governments provide public goods of reasonable quality and there are avenues for social advancement? Within this simple framework, we particularly focus on the behaviour and beliefs of citizens in the middle range of the income distribution, often considered ´net payers´. Section five summarises, and highlights the main policy implications of the analysis.

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II. A BRIEF LITERATURE REVIEW

From a theoretical point of view, the median voter model (see for instance Down, 1957) suggests that if *ex ante* inequality (*i.e.* before taxes and government transfers and other public expenditure) is high, as it is in Latin America, democracy should lead governments to raise revenues and effect significant redistribution. Simply put, the median voter is likely to benefit from progressive income taxation (which will fall more heavily upon voters with higher incomes than his) and progressive transfers and spending (which will disproportionately favour him). However, even in a theoretical framework, democracy may be a necessary, but not sufficient condition for a bigger government and more redistribution. As surveyed in Alesina and Giuliano (2009) preferences for redistribution stem from numerous sources, from the individual history (mobility experiences affect political attitudes toward redistribution; Piketty, 1995) and the organisation of the family, to nation- and region-wide cultural and social values.

In a seminal paper, Meltzer and Richards (1981) argue that the demand for redistribution results from a balance between the aspirations of the middle and poor classes, and the economy-wide disincentives they expect from a higher level of taxation. In particular, if poor and middle-income voters (potential beneficiaries from redistribution) take into account the effects of taxation on labour-leisure decisions of their fellow citizens when voting, this will limit the size of government and the degree of redistribution.

Alesina and Angeletos (2005a) stress the relevance of social beliefs about the degree of fairness in social competition. According to these authors, if a society believes that they live under a ´meritocracy´ (in which individual effort determines income), and that all have a right and opportunity to enjoy the fruits of their effort, it will choose low redistribution and low taxes. Consequently, in equilibrium effort would be high, and the role of luck, birth, connections or corruption limited.[3] In fact, as Benabou and Ok (2001) formalise, even the poor may vote for low levels of redistribution if they think that in the future, they or their offspring could progress (becoming a net payer and not benefiting from higher tax rates and redistribution). Thus, societies with high mobility, or more precisely where people there is high mobility, may therefore opt for low levels of redistribution; this is the so-called ´prospect of upward mobility´

3 These authors add a second and opposite equilibrium. If society beliefs that luck, birth, connections or corruption determine wealth, it will levy high taxes, and social beliefs will be self-fulfilling as well. In a parallel paper, Alesina and Angeletos (2005b) develop the last argument. 'Big governments raise the possibilities of corruption; more corruption may in turn raise the support for redistributive policies to intend to correct the inequality and injustice generated by corruption'. We are not so convinced on the latter point. Alternatively, citizens may start avoiding paying taxes, ending up, again, with a small(er) government and low redistribution.

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(POUM) hypothesis. Conversely, in societies where mobility is perceived to be low, the median voter theorem will rule and the poorer would vote for more redistribution.[4] Additionally, Corneo and Grüner (2000) highlight the role of social incentives. Even if the middle-class households may benefit from larger redistribution, the fear of losing social status in favour of the poor may align them to the conservatives.

It is important to note, though, that for the POUM to hold, some premises should be in place: policies should be expected to persist, agents should not be very risk-averse, and those poorer than the average should expect to become richer than the average (Benabou and Ok, 2001). All of these factors may be temporary. As illustrated by the ´tunnel effect' of Hirschman (1973), poor and middle class individuals may be willing to accept and support high (or even increasing) levels of inequality during the early stages of development (staying in the slow lane of the traffic jam in the tunnel, according to his evocative metaphor). But they will do so, as long as they keep their hope in progressing (*i.e.* that their lane starts to advance faster as well). Government credibility, risk aversion and expectations therefore play a crucial role.

Przeworski (2007) generalises the case, pointing out that those without property, even if they constitute a vast majority, either do not want to or cannot use their political rights to equalise property, incomes, or even opportunities. This may be due not only to the expectation to become rich, but also to ideological domination since the media is owned by the elite, or to difficulties of the poor to co-ordinate political action when they have heterogeneous preferences over aspects of life not immediately related to the economy. In a somewhat related vein, Chong and Olivera (2008) show empirically that those countries with compulsory voting exhibit less income inequality. Therefore, since poorer countries also have relatively more unequal distributions of income, the authors support the promotion of such voting schemes in developing countries.

However, Przeworski (2007) adds an additional and challenging dimension. Even in situations when governments are elected with the support of the poor to equalise income and then try to do so, they may fail. Modern redistribution policies mainly aim at equalising human capital by investing in health and education (in contrast to a focus on redistribution of land or industrial capital in the past). Such redistribution may not result in an equalisation of outcomes as before, since the same educational system may produce different outcomes depending on the socioeconomic background of pupils. In other words, the equalisation of opportunities may not be enough to reduce inequality. Furthermore, if the people are aware of these weak effects of publicly provided services, they will attach low value to these services and hence have low willingness to fund them through taxes.

In contrast to this rich narrative literature, there are relatively few rigorous empirical studies regarding the topics outlines above. Among them, Issaksson and Lindskog (2009) confirm, for a sample of 25 countries, that self-interest and meritocracy reduce the demand for redistribution between and within countries, respectively. However, the authors point out that heterogeneity across countries is very high, being the Latin American ones where these effects

4 Rodriguez (2004) proposes a reassessment of the POUM effect, by which in societies where the rich can influence politics such as they do not pay taxes, the median voter will prefer low levels of taxation to reduce the incentives of rent seekers.

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are among the lowest. Corneo and Grüner (2002) add to them the aforementioned social status, as a relevant variable for a sample of 12 countries. Focusing on tax policy, Profeta and Scabrosetti (2008) find that democracy in Latin America has no significant effect on either the level of taxation or on its progressivity. This is due to low institutional capacity (especially, in the tax administration), a low quality of democracy (vulnerable to populisms, ´termites´ which erode the tax bases, and ´devoradores´ who capture social expenditure, as Elizondo and Santiso, 2009 put it for Mexico and Brazil, respectively), and inefficiencies in the budgetary and tax systems (in the sense that expenditure and tax benefits tend to benefit the high-income population; see Breceda *et al*., 2008, and OECD, 2008).

Focusing on the analysis of perceptions, Torgler (2005) highlights the significantly lower 'tax morale' (*i.e.* the values and attitudes regarding the paying of taxes) in Latin America. Among its determinants, and using the surveys *Latinobarómetro* 1998, and *World Values Survey* 1981-1997, the author points to the tax burden, but also to the lack of honesty, and corruption. Taxpayers perceive their relationship with the state not only as a relationship of coercion, but also as one of exchange. When they feel they are treated fairly, they are more willing to pay taxes. So, 'there are alternative tax policy strategies to those assuming that people are knaves who must be controlled'. Gaviria (2007), based on *Latinobarómetro* 1996 and 2000, argues that the high demand for redistribution and the weak support for market outcomes in Latin America in the late 1990s and early 2000s stem from pessimistic views on social justice and equality of opportunities, as well as on past and expected mobility. Differences in expressed attitudes between rich and poor are substantial (in fact, larger than in other regions), and the poor are more likely to demand redistributive policies. While these two papers are closely related to ours, there are some important differences. First, in addition to the determinants explored by Torgler (2005) we consider perceptions of social mobility, which in theory are a key determinant of the desired amount of taxation, as discussed above. Second, Gaviria (2007) considers only the expenditure side of redistribution while we explore both revenues and expenditures as equally critical parts of the social contract embedded in public finance. Finally, we explore also the link between the quality of public services and the willingness to pay taxes, and more general the perception of how democracy works in the region, an issue not addressed by any of these papers.

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III. DEMOCRATIC CONSOLIDATION IN LATIN AMERICA: FROM DATA TO PERCEPTIONS

The strength of the link between social mobility and fiscal policy relies on the degree to which citizens can chose freely between alternative political parties or candidates to express their preferences regarding taxation and public expenditures. In this sense, Figure 2 shows that the region has been steadily moving towards democratic regimes since the mid-1980s, according to the *Polity IV* ranking. [5] Out of 23 countries in the region that are included in the *Polity* database, 18 countries were ranked as democracies in 2008, with only one country (Cuba) being an autocracy, compared with only 7 democracies and 8 autocracies in 1980.

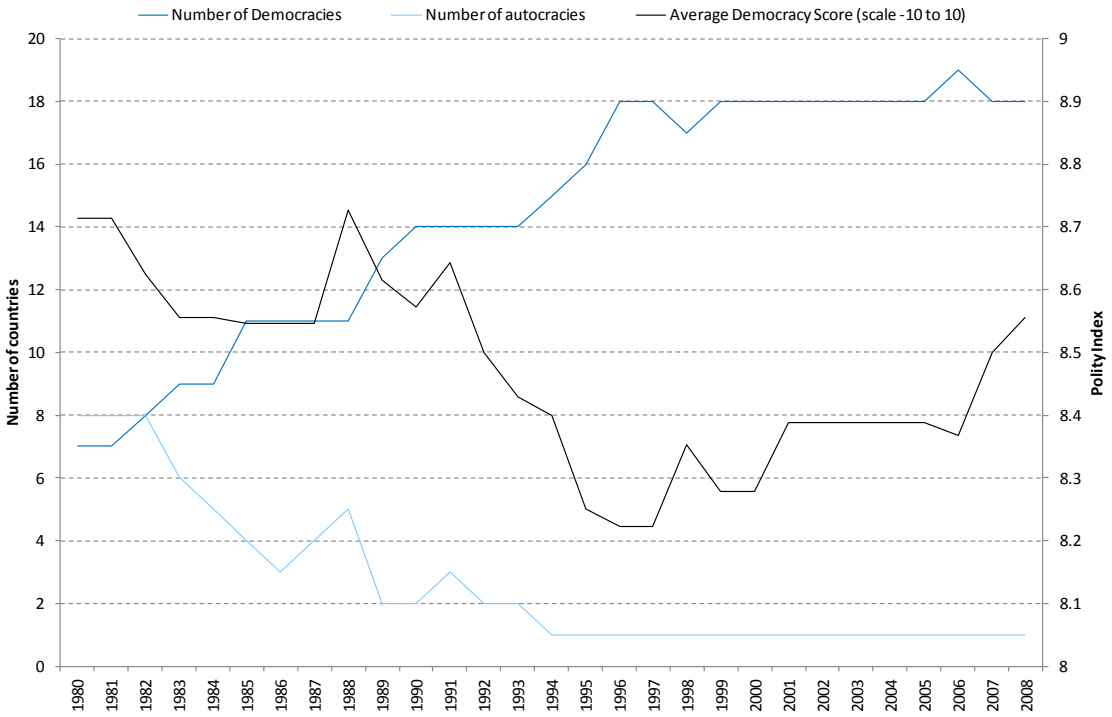
At the same time, as shown in the figure, in the early 1990s the expansion in the number of democracies was accompanied by a decline in the average ´quality´ of democracy, given the relatively imperfect nature of the new democracies in the region. However, since the mid-1990s, there has been a fairly steady democratic consolidation in the region, although the index of almost 8.6 for Latin America and the Caribbean in 2008 is still below the average of 9.6 for OECD member countries (maximum score 10). Needless to say that there is also a lot of variation within the region, which includes consolidated democracies like Costa Rica, Chile and Uruguay (with a *Polity* score of 10, like most OECD countries), but also countries like Ecuador and Venezuela where democratic consolidation is considerably weaker, according to this indicator.

What do citizens in Latin America think about their democracies? Does democracy have an intrinsic value for Latin Americans? Is it perceived as a useful tool to solve social conflicts effectively? How do perceptions about social mobility and relative status relate to the perceptions regarding democracy? These are some of the questions we try to tackle using *Latinobarómetro* results for 18 countries of the region.

5 The Polity democracy score relies on experts' assessments along six dimensions which include qualities of executive recruitment, constraints on the executive, and the degree of openness of polities and political competition. See the website of the Polity IV project (www.systemicpeace.org/polity/polity4.htm) for more details.

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Figure 2. **Democratic consolidation in Latin America**



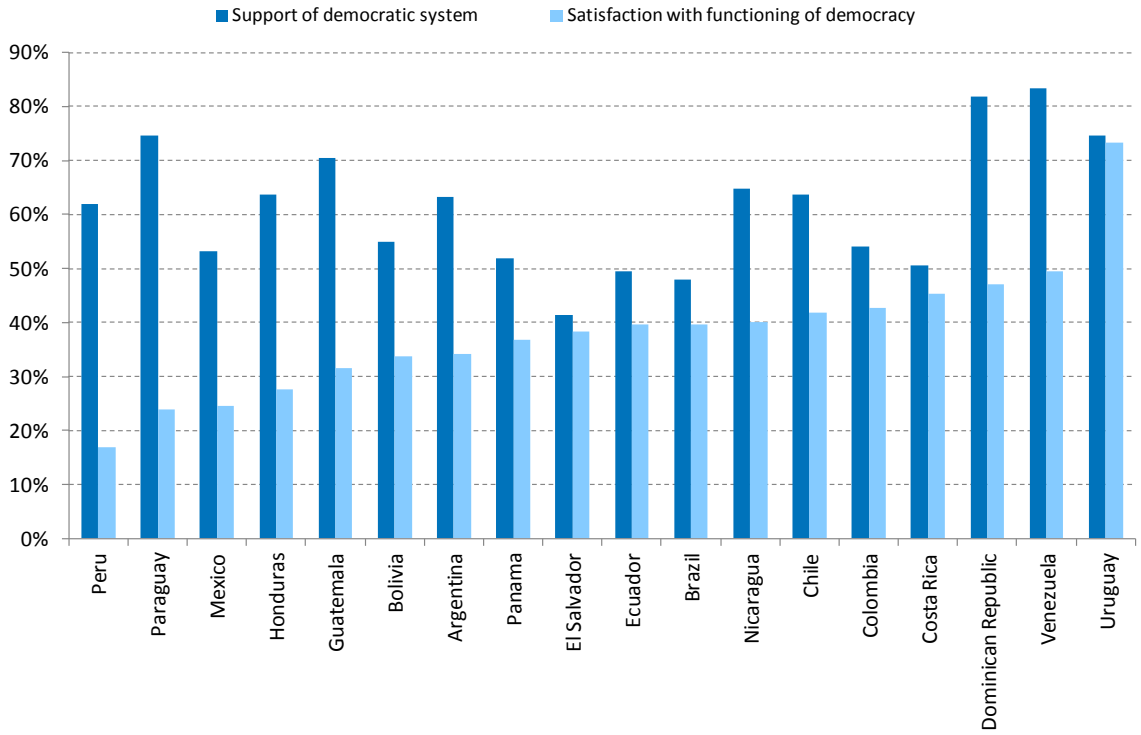
Source: Authors' calculations based on Polity IV database.

Notes: Following the criteria of Marshall and Cole (2009) countries are classified as a democracy if the polity score is greater or equal to 6. See http://www.systemicpeace.org/polity/polity4.htm for more details.

In Figure 3, we present two key perception indicators by country: the support for democracy as the best system to organise the society, and the degree of satisfaction with the way democracy functions in each country. The picture that emerges is one of a preference for democracy in principle, but a very low degree of satisfaction with how democracy is working. With the sole exception of Uruguay (where over 70% of the population is satisfied), the majority of people in every country in the region are not satisfied with the current functioning of their democracies. This does not reflect disillusionment with democracy itself, since the support for democracy as system of organisation of their societies is very high in most countries. In Venezuela, Dominican Republic, Uruguay, Paraguay and Guatemala, more than 70% of the population support democracy. In a second group, while support is lower, democracy nevertheless still enjoys the support of the majority. This group includes Nicaragua, Chile, Honduras, Argentina, and Peru. In the rear, a third group of countries (Bolivia, Colombia, Mexico, Panama, Costa Rica, Ecuador, Brazil and El Salvador) shows relatively low levels of support (just around 50% of the population) – a group that contains the largest countries in the region in terms of population (Brazil and Mexico). Overall, this shows that democracy is far from having consolidated its support and satisfaction across the region.

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Figure 3. **Satisfaction and support for democracy by country in 2008**



Source: Authors' calculations based on *Latinobarómetro* survey 2008.

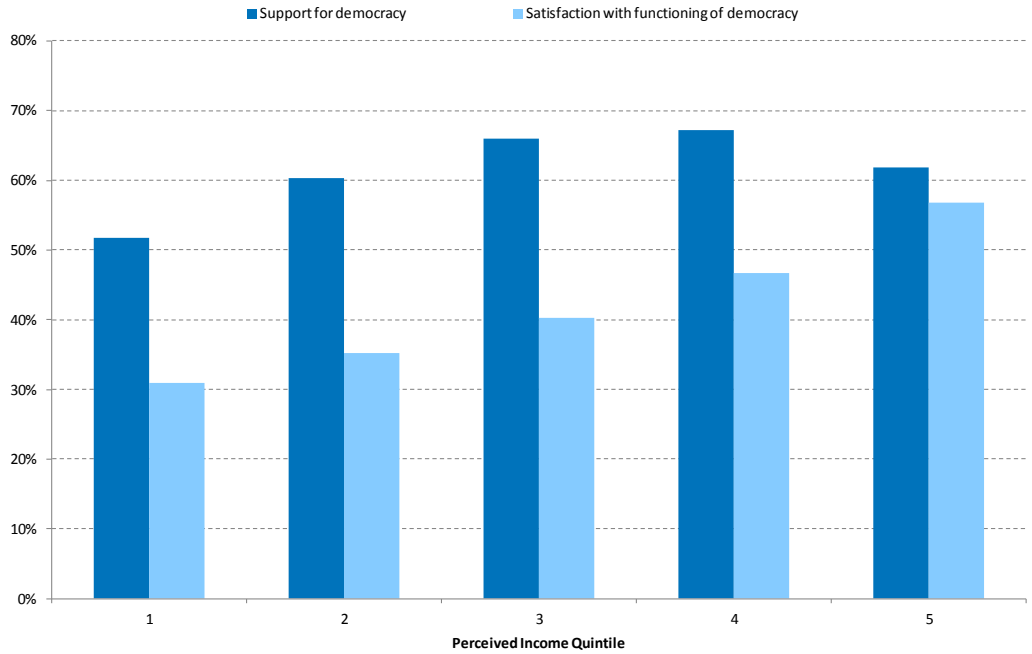
Notes: Satisfaction with the functioning of democracy refers to answers (very and fairly satisfied) to the question: 'In general, would you say you are very satisfied, fairly satisfied, not very satisfied or not satisfied at all with the way democracy works in your country?'. Support for the democratic system refers to the proportion of persons that answered agreed with the statement that 'Democracy is preferable to any other kind of government'.

Figure 4, shows how the support for democracy and satisfaction with its functioning is distributed across self-perceived income quintiles in the region. Satisfaction with democracy increases monotonically with the perception people have regarding their economic status. For example, a person who puts himself in the highest quintile is almost twice as likely to be satisfied with the way the democratic system works than a person in the first quintile (57 versus 31%, respectively).[6] Furthermore, the differences between the different quintiles are significant at conventional levels of confidence. With respect to the support of democracy, there seems to be a non-monotonic relationship with people perceiving themselves as part of the middle quintiles (2 to 4) being significantly more prone to value democracy.

6 It is important to point out that perceived positions in the income distribution differ significantly from the objective positions, with relatively rich individuals self-classifying themselves at lower income quintiles and the poor considering themselves relatively less deprived (see Fajardo and Lora, 2010). However, it can be argued that in political views and actions it is the perceived position, rather than the objective one, that matters most.

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Figure 4. **Attitudes towards democracy by perceived income quintiles in Latin America**

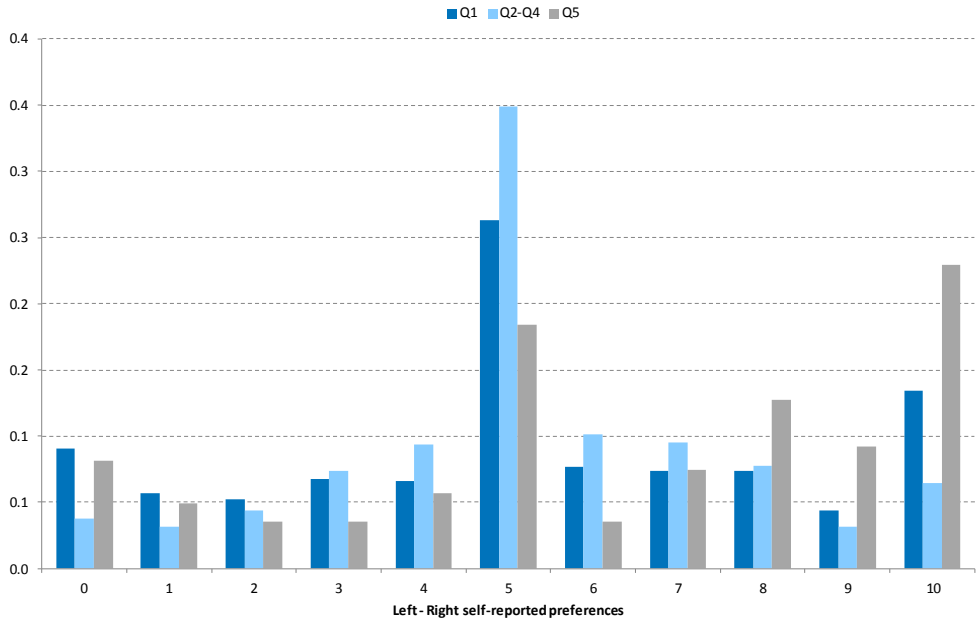


Source: Authors' calculations based on *Latinobarómetro* survey 2008.

Figure 5 shows the distribution in terms of left-right ideology that people report about themselves in Latin America by the same self-reported income quintile. There are two interesting results. First, people that perceive themselves as belonging to the middle quintiles (2 to 4) consider themselves also more in centre of the political preference distribution. For example, over 54% of these citizens report scores between 4 and 6 (the political centre), while for the lower quintile it descends to 41%, and to 28% among the upper one. Second, the percentage of the population in these middle quintiles who considers itself at the extremes (either left or right) is lower than among the poorer or the richer (on both sides of the distribution). This is reflected also by a lower dispersion in political preferences for the middle quintiles *vis-à-vis* the other groups.[7]

7 The coefficient of variation for those in the middle of the income distribution is 0.44, compared with 0.52 for the upper part and 0.57 for the low-income groups.

Figure 5. **Distribution of political preferences by income quintiles**



Source: Authors' calculations based on *Latinobarómetro* survey 2008.

Thus far, we have focused on aggregate data by country or quintile. However, many personal characteristics beyond income have a strong influence on perceptions and social preferences (*e.g.* see Inter-American Development Bank, 2009). Therefore, in what follows we analyse the same issues showed in Figures 3 – 5, including the perceptions on social mobility and meritocracy. Table 1 reports the main result from estimating a PROBIT model for the dichotomic outcomes (support of democracy, as well as satisfaction with democracy), and ordered PROBIT regressions for the left-right classification. In addition to country dummies, we include ethnicity dummies, and marital and employment status dummies.[8] Additional controls include: gender (female dummy), a dummy for households that report economic problems (to be precise, those who are not able to cover needs in a satisfactory manner), age, a head of household dummy, the years of education of the respondent, the degree of religiosity, and a dummy for whether the respondent is citizen of the country where the interview was performed. Our main variables of interest are dummies for each self-reported income quintile, as well as the perception with respect to future and past mobility (according to whether the respondent ranks himself in the income distribution compared to where he thinks his parents were and offspring will be).

8 For ethnicity, we introduced dummies for each self-reported ethnicity: Asian, black, indigenous, mestizo, mulato, white, and other race. Marital status dummies include: married/living with partner, single, and separated/divorced/widow. Employment status includes: self-employed, salaried employee in a state company, salaried employee in a private company, temporarily out of work, retired/pensioner, don't work/responsible for shopping and housework, and student.

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Table 1. **Determinants of attitudes towards democracy in Latin America (2008)**

	(1)	(2)	(3)	(4)	(5)	(6)
Dependent Variable	Support for democracy	Support for democracy	Satisfaction with democracy	Satisfaction with democracy	Left-Right	Left-Right
Estimation Method	Probit	Probit	Probit	Probit	Ordered Probit	Ordered Probit
Female Dummy	-0.092	-0.092	-0.065	-0.065	-0.021	-0.022
	(0.030)***	(0.030)***	(0.030)**	(0.030)**	(0.025)	(0.025)
Economic Problems Dummy	-0.103	-0.102	-0.182	-0.180	-0.011	-0.007
	(0.027)***	(0.027)***	(0.027)***	(0.027)***	(0.022)	(0.022)
Age	0.006	0.006	0.001	0.001	0.004	0.004
	(0.001)***	(0.001)***	(0.001)	(0.001)	(0.001)***	(0.001)***
Head of household	-0.010	-0.009	0.055	0.055	-0.009	-0.010
	(0.033)	(0.033)	(0.034)	(0.034)	(0.027)	(0.027)
Years of Education	0.031	0.032	-0.014	-0.014	-0.008	-0.008
	(0.003)***	(0.003)***	(0.003)***	(0.003)***	(0.003)***	(0.003)***
Religiosity	0.090	0.090	0.137	0.137	0.089	0.089
	(0.026)***	(0.026)***	(0.026)***	(0.026)***	(0.022)***	(0.022)***
Citizen dummy	0.057	0.056	-0.137	-0.136	-0.047	-0.046
	(0.091)	(0.092)	(0.092)	(0.092)	(0.068)	(0.068)
Quintile 2	0.212	0.208	0.070	0.074	0.079	0.089
	(0.038)***	(0.038)***	(0.040)*	(0.040)*	(0.036)**	(0.036)**
Quintile 3	0.262	0.256	0.179	0.187	0.139	0.162
	(0.038)***	(0.039)***	(0.040)***	(0.041)***	(0.037)***	(0.037)***
Quintile 4	0.213	0.202	0.280	0.295	0.174	0.215
	(0.051)***	(0.053)***	(0.053)***	(0.055)***	(0.046)***	(0.048)***
Quintile 5	0.203	0.193	0.505	0.532	0.223	0.287
	(0.097)**	(0.099)*	(0.100)***	(0.102)***	(0.099)**	(0.102)***
Perceived past mobility		0.018		-0.002		-0.014
		(0.009)**		(0.009)		(0.008)*
Perceived future mobility		0.012		0.014		0.025
		(0.008)		(0.008)*		(0.007)***
Constant	-0.158	-0.168	0.094	0.057		
	(0.372)	(0.370)	(0.353)	(0.347)		
Observations	13141	13141	12697	12697	10996	10996
Pseudo-R2:	0.08	0.08	0.07	0.07	0.01	0.01

Notes: Robust standard errors in parenthesis. * significant at 10%, ** significant at 5%, *** significant at 1%. All regressions include country, ethnicity, marital status and employment status dummies not reported due to space limitations. The dummy for the first income quintile is omitted in the regressions.

Column 1 shows that the result of a higher support of democracy within the middle quintiles continues to hold when controlling for individual socio-economic conditions. However, now the upper quintile also appears as significantly supporting democracy more than the lowest one (and the difference with respect to the middle quintiles is only significant for the third one). This result also holds when we include the perceived social mobility indicators. Interestingly,

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people who think that they advanced with respect to their parents significantly support democracy more (column 2). With respect to the degree of satisfaction with the functioning of democracy, column 3 shows a positive association between the level of satisfaction and the perceived position in the distribution of income continues to hold (as suggested in Figure 2). Furthermore, there is some evidence that people who perceive more prospects of upward mobility in the future, also tend to be more satisfied with democracy today in their country of residence (column 4).

Finally, columns 5 and 6 analyse the issue of how people rank themselves in terms of left-right political preferences. The regressions confirm a higher tendency towards the right at higher levels in the perceived income distribution. If, as in the literature (Alesina and Giuliano, 2009; Gaviria, 2007), we interpret these preferences over the political spectrum as preferences over redistribution (the left taken to be more prone to redistribute than the right), two interesting results emerge. First, preferences for redistribution are decreasing with the self-perceived income status. This seems to be rational, given that the richer you are the more likely you are to be a net payer. Second, the results in column 6 imply that people, who think that their children will move up, tend to support less redistribution, while those who experienced themselves upward mobility in the past tend to support more redistribution.[9] Thus, while the first result clearly is in line with the POUM hypothesis, interpretation of the second is more complicated. The second result could indicate that people who experienced successful upward mobility believe that their mobility was aided by redistributive public finance, and therefore continue to support redistribution nowadays. Of course, political preferences are much more complex than just attitudes regarding fiscal policy, and therefore the left-right preferences might be an imperfect proxy for preferences over redistribution. We explore related issues in detail in the next section.

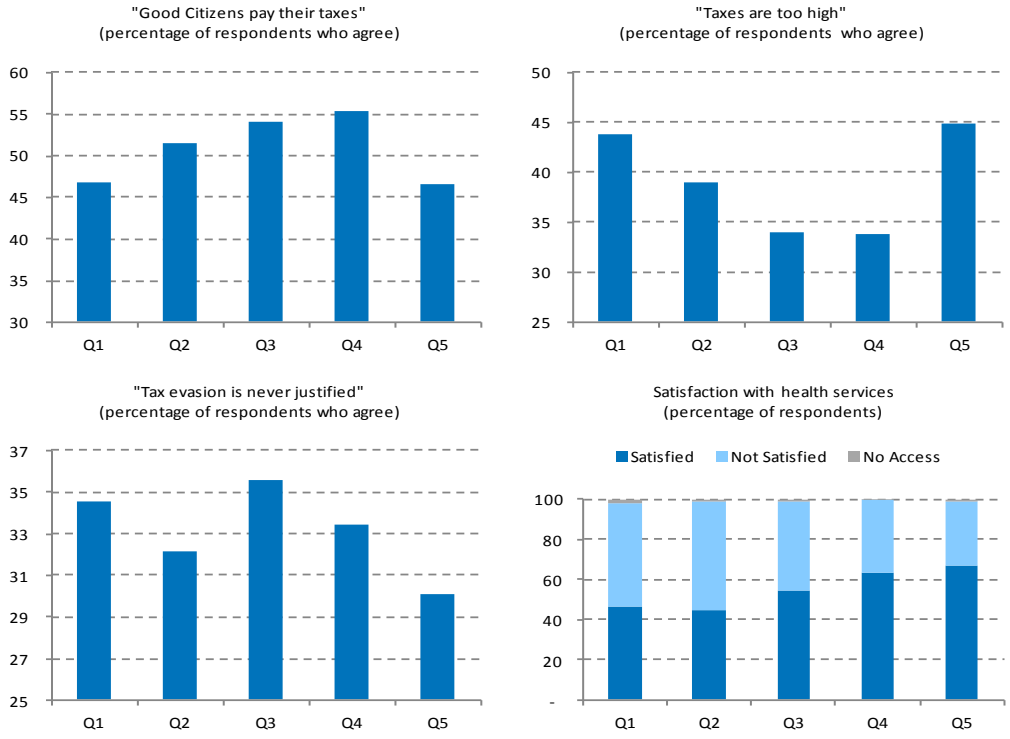
9 This result is not driven by collinearity between both measures of mobility, given that the correlation between future and past mobility is just – 0.21. Furthermore, if included separately the result holds.

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IV. DEMOCRACY, SOCIAL MOBILITY AND FISCAL POLICY IN LATIN AMERICA: EMPIRICAL ANALYSIS

The evidence presented in the previous section shows that the middle sectors of the income distribution in Latin America are in principle a supporter of democracy and have rather moderate views on politics. Yet, they remain unsatisfied with how democracy actually functions in the region. Is this dissatisfaction evident in their views on taxation and public services? Figure 6 synthesises the main descriptive statistics in this regard. Clearly, those who consider themselves in the middle display higher 'tax morale' than other members of society: members of the middle quintiles are more likely to consider that citizens should pay their taxes, less likely to consider that taxes are too high, and less likely to justify tax evasion. However, they are also less satisfied with the provision of public services, compared to the affluent. In short members of the middle quintiles have a 'dissatisfied customer' relationship with the state: while relatively supportive of taxation, they are not satisfied with the services they receive.

Figure 6. **Taxation and Satisfaction with Public Services by self-reported income quintiles**



Source: Authors' calculations based on *Latinobarómetro* 2007 and 2008.

In this section, we explore more systematically the links between tax morale, perceptions of social mobility and the quality of democracy, as well as the POUM hypothesis. Therefore, we use two recent rounds (2007 and 2008) of the regional survey *Latinobarómetro*. *Latinobarómetro* is an annual public opinion survey with data from around 20 000 interviews, covering 18 Latin American countries (Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Dominican Republic, Ecuador, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, Panama, Paraguay, Peru, Uruguay and Venezuela), *i.e.* around 1 000 – 1 200 interviews per country. For most of the analysis, such as the regression analysis performed in the previous section, this limited coverage per country does not allow detailed national level analysis, so results will be obtained for the region as a whole.[10]

IV.1. Empirical approach

We focus on the role of taxation and fiscal policy with respect to the social contract between the citizens and the state. In particular, we analyse empirically the determinants of the perceptions regarding tax morale, the level of taxes, and the demand for fiscal redistribution. We proxy tax morale by two of the questions included in the survey: whether people think that good citizens should pay taxes, and whether they think that evasion may be justified. *Latinobarómetro* directly asks whether people consider that taxes in their country are too high, which allows us to tackle whether Latin Americans prefer lower or higher taxes.[11] Finally, although the demand for redistribution is one of the central policy questions in the region, no question in the survey deals directly with it. Therefore, and following other authors (Alesina and Giuliano, 2009; Gaviria, 2007), we use the response to the question 'should the state intervene more in health assistance, education, or pensions' as proxy for demand of redistribution. Additionally, we also consider the preferences over whether the market (or the government) should solve all society's problems.

Control variables can be grouped in three classes, in line with the literature surveyed in the first section. As a first group of independent variables, we include several socio-economic identifiers: sex, age, citizenship, family composition, race, religion, political preferences (left-right), level of savings, number of years of education, and the (self-reported) economic quintile. We pay special attention to the role of education, and the behaviour of those in the middle quintiles. Focusing on the latter, the middle quintiles represent a very interesting case, since they are often said to be the net payers (being basically composed by dependent workers with no options to avoid taxation, but with too many resources to benefit from targeted social benefits).

The second group of variables serve to test the ´meritocracy hypothesis´ (if a society believes that individual effort determines income, and that all have a right to enjoy the fruits of their effort, it will choose low redistribution and low taxes), and the ´POUM hypothesis´ (people who anticipate an upward mobility would not vote for a higher redistribution, even if they are

10 As in the previous section, regressions include country dummies to capture the differences in perceptions that exist across countries. Furthermore, we include a series of controls (age, gender, occupation, among others) that influence also perceptions and opinions.

11 We have also tried to test the drivers of the opposite response, ´are taxes too low?´, since it may represent a demand for redistribution, but there are few people in Latin America who actually think that taxes are too low, and should be raised.

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poor at present, since in the future they will be net payers). In order to do so, we include both the perceptions on past (vs. parents) and future (vs. offspring) mobility, and explicit questions about whether success depends on hard work rather than connections, and if a poor person in the country can become rich if she works hard

Thirdly, taxation cannot be analysed separately from public expenditures. Households and firms may be willing to pay higher taxes if they (perceive that they) receive more/better public services. Therefore, we will test this issue, considering both specific questions on the level of satisfaction with health care, education and pensions, as well as more general aspects like the satisfaction with democratic system, and the perception of corruption in the country.[12]

Before showing the results, some caveats are needed. First, due to the very nature of the *Latinobarómetro* database, it should be stressed that the analysis is based on perceptions, which may differ from reality. This is evident, for instance, in the classification of respondents by quintiles. If the survey sample is representative, each of the self-reported quintiles should comprise 20% of responses. However, people tend to concentrate in the fourth quintile.[13] Nevertheless, perceptions are precisely what drive political decisions. Second, despite the existence of some theoretical modelling, causality is in many of the cases very difficult to establish. Therefore, results should be interpreted mainly as correlations. Finally, due to the different scales of the variables, our interpretation of results is mainly based on the signs rather than the magnitudes of the coefficients.

IV.2. Main results

Among the socioeconomic controls, the level of education plays a significant role in both the willingness to pay taxes and the level that people may accept. More years of education increases the likelihood of thinking that good citizens should pay taxes (Table 2, columns 1-8) and considering that evasion is not justified (Table 3, columns 1-5). Furthermore, respondents with more education also consider less frequently that taxes in their country are too high (Table 4, columns 1-7, and Table 5, columns 1-4). This result is in line with Torgler (2005), and overall, it highlights the potentially important role for education in fostering social responsibility among citizens.

Our results also suggest that the people who perceive a higher past mobility, and forecast a higher future mobility agree that good citizens should pay taxes (Table 2, columns 6-7),[14] and

12 Additionally, we have analysed a group of variables that may serve to test whether political participation and the media play a role in the weak social contract in Latin America (as suggested in Przeworski, 2007). However, the preliminary analysis on the political participation on the confidence in the media and the level of information are not particularly different between the rich and the poor (both groups exhibiting in general terms, lower levels that the middle quintiles).

13 For this reason, oftentimes research on social classes, and in particular the so-called middle class, relies on data on consumption patterns (especially in durables) or on investment decisions (housing, access to credit, and education for the offspring). Latinobarómetro includes information about some of these issues, but the absence of a generally accepted definition also entails significant caveats.

14 However, when controlling for corruption perceptions, these results are less robust (column 8 in Table 2).

do not think that current taxes are too high (Table 4, columns 6-7; Table 5, columns 1-4). They also tend to disagree with tax evasion (Table 3, columns 3 and 5), although coefficients are not significant at conventional levels.

Focusing on the questions regarding on meritocracy, the majority of those who think that success depends on hard work rather than connections, and those who believe that a poor person in their country can become rich by working hard, also think that taxes are not too high (Table 5, columns 1-4). As a consequence, these results do not support with the POUM and meritocracy hypothesis put forward by Gaviria (2007) for the region. This author, using *Latinobarómetro* 1996 and 2000, argued that the high demand for redistribution and the weak support for market outcomes in Latin America in the late 1990s and early 2000s stemmed from pessimistic views on social justice and equality of opportunities, as well as on past and expected mobility. In contrast, our findings support the argument of Benabou and Ok (2001), suggesting that risk aversion and the demand for social insurance against the risks of downward mobility or stagnation may dominate the POUM effect.

Our results support the role of a link between better public services, better institutions, and higher tax morale, in line again with Torgler (2005). Satisfaction with health care and education – though not with pensions – reinforce the belief that good citizens should pay taxes (Table 2, columns 1-7), and, in general terms, reduce the share of the population that thinks that taxes are too high (Tables 4 and 5). A lower level of perceived corruption also reduces the percentage of citizens who consider taxes too high (Table 2, column 8), and those who justify evasion (Table 3, columns 4 and 5). Similarly, a high degree of satisfaction with the functioning of democracy increases the number of citizens who think that good citizens should pay taxes (Table 2, columns 2 and 7) and reduces those who think that taxes are too high (Table 4, columns 2 and 7; Table 5, columns 1-4). However, somewhat at odds with the latter finding, the same satisfaction with democracy seems to increase the share of people who justify tax evasion (Table 3, columns 2 and 5).

Unfortunately, no clear result was obtained from the analysis of the determinants of the proxies for preferences for redistribution (Table 6). Most coefficients of interest are not significant, and within those which are, results are not easy to interpret. For instance, households who have recently suffered economic problems seem to trust neither the government, nor the market (see columns 1-4). A similar contrasting picture emerges from individuals who are confident about future mobility.

Finally, on the role of income levels, even leaving aside the mentioned caveats stemming from the self-classification, we do not find a clear result, once we controlled for the other variables. For instance, population classified in the upper-middle quintiles (3 and 4) significantly think that good citizens should pay taxes (Table 2, columns 1-8), but at the same time, quintiles 4 and 5 justify evasion (Table 3, columns 1-5). For the remaining issues, income groups *per se* do not seem to play an important role.

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Table 2. **Do you think that good citizens should pay taxes? (Probit estimates, 2007 data)**

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Female	-0.021	-0.020	-0.021	-0.020	-0.021	-0.021	-0.019	-0.047
	(0.026)	(0.026)	(0.026)	(0.026)	(0.026)	(0.026)	(0.026)	(0.031)
Economic problems	-0.065	-0.061	-0.059	-0.058	-0.064	-0.062	-0.051	-0.095
	(0.023)***	(0.024)***	(0.024)**	(0.024)**	(0.024)***	(0.024)***	(0.024)**	(0.027)***
Age	0.006	0.006	0.006	0.006	0.006	0.006	0.006	0.007
	(0.001)***	(0.001)***	(0.001)***	(0.001)***	(0.001)***	(0.001)***	(0.001)***	(0.001)***
Head of household	-0.019	-0.021	-0.019	-0.018	-0.019	-0.019	-0.019	0.016
	(0.029)	(0.029)	(0.029)	(0.029)	(0.029)	(0.029)	(0.029)	(0.034)
Years of education	0.021	0.021	0.021	0.021	0.021	0.022	0.022	0.02
	(0.003)***	(0.003)***	(0.003)***	(0.003)***	(0.003)***	(0.003)***	(0.003)***	(0.003)***
Religious	0.057	0.053	0.055	0.054	0.056	0.056	0.051	-0.003
	(0.023)**	(0.023)**	(0.023)**	(0.023)**	(0.023)**	(0.023)**	(0.023)**	(0.026)
Citizen	-0.056	-0.057	-0.056	-0.056	-0.056	-0.053	-0.055	-0.038
	(0.072)	(0.072)	(0.072)	(0.072)	(0.072)	(0.072)	(0.072)	(0.096)
Quintile 2	0.050	0.047	0.051	0.050	0.050	0.049	0.045	0.089
	(0.038)	(0.038)	(0.038)	(0.038)	(0.038)	(0.038)	(0.038)	(0.041)**
Quintile 3	0.079	0.070	0.076	0.075	0.078	0.074	0.062	0.181
	(0.037)**	(0.037)*	(0.037)**	(0.037)**	(0.037)**	(0.038)*	(0.039)	(0.041)***
Quintile 4	0.103	0.091	0.097	0.095	0.102	0.097	0.078	0.202
	(0.048)**	(0.048)*	(0.048)**	(0.048)**	(0.048)**	(0.050)*	(0.050)	(0.056)***
Quintile 5	-0.045	-0.052	-0.053	-0.053	-0.046	-0.048	-0.066	0.084
	(0.089)	(0.089)	(0.089)	(0.089)	(0.089)	(0.092)	(0.092)	(0.110)
Satisfaction with democracy		0.069					0.058	
		(0.023)***					(0.024)**	
Satisfaction with health care			0.047				0.019	
			(0.022)**				(0.026)	
Satisfaction with education				0.064			0.053	
				(0.022)***			(0.025)**	
Satisfaction with pension system					0.013		-0.013	
					(0.021)		(0.023)	
Past mobility						0.015	0.015	-0.019
						(0.006)**	(0.006)**	(0.009)**
Future mobility						0.014	0.012	0.011
						(0.006)**	(0.006)**	(0.008)
Corruption								-0.001
								(0.000)***
Constant	0.214	0.184	0.145	0.118	0.194	0.192	0.083	-0.619
	(0.157)	(0.157)	(0.160)	(0.160)	(0.160)	(0.158)	(0.164)	(0.336)*
Observations	14116	14116	14116	14116	14116	14116	14116	11486
Pseudo-R2:	0.03	0.03	0.03	0.03	0.03	0.03	0.03	0.05

Notes: Robust standard errors in parenthesis. * significant at 10%, ** significant at 5%, *** significant at 1%. All regressions include country, ethnicity, marital status and employment status dummies not reported due to space limitations. The dummy for the first income quintile is omitted in the regressions. Column 8 uses the 2008 survey data, while the remaining regressions use the 2007 survey.

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Table 3. **Tax evasion is justified (Ordered Probit estimates, 2008)**

	(1)	(2)	(3)	(4)	(5)
Female	0.033	0.035	0.033	0.029	0.031
	(0.029)	(0.029)	(0.028)	(0.029)	(0.029)
Economic problems	0.018	0.022	0.017	0.015	0.019
	(0.026)	(0.026)	(0.026)	(0.026)	(0.026)
Age	-0.004	-0.004	-0.004	-0.004	-0.004
	(0.001)***	(0.001)***	(0.001)***	(0.001)***	(0.001)***
Head of household	0.052	0.052	0.052	0.052	0.052
	(0.031)*	(0.031)*	(0.031)*	(0.031)*	(0.031)*
Years of education	-0.028	-0.027	-0.028	-0.028	-0.027
	(0.003)***	(0.003)***	(0.003)***	(0.003)***	(0.003)***
Religious	0.045	0.042	0.045	0.049	0.046
	(0.024)*	(0.024)*	(0.024)*	(0.024)**	(0.024)*
Citizen	-0.045	-0.042	-0.045	-0.048	-0.046
	(0.084)	(0.084)	(0.084)	(0.084)	(0.084)
Quintile 2	0.049	0.049	0.050	0.052	0.053
	(0.041)	(0.041)	(0.042)	(0.041)	(0.042)
Quintile 3	0.017	0.014	0.019	0.018	0.016
	(0.041)	(0.041)	(0.042)	(0.041)	(0.042)
Quintile 4	0.185	0.180	0.188	0.187	0.183
	(0.052)***	(0.052)***	(0.054)***	(0.052)***	(0.054)***
Quintile 5	0.328	0.317	0.328	0.327	0.312
	(0.094)***	(0.094)***	(0.097)***	(0.094)***	(0.097)***
Satisfaction with democracy		0.067			0.081
		(0.025)***			(0.025)***
Past mobility			-0.011		-0.010
			(0.009)		(0.009)
Future mobility			-0.010		-0.010
			(0.008)		(0.008)
Corruption				0.002	0.002
				(0.000)***	(0.000)***
Observations	9620	9620	9620	9620	9620
Pseudo-R2:	0.02	0.02	0.02	0.02	0.02

Notes: Robust standard errors in parenthesis. * significant at 10%, ** significant at 5%, *** significant at 1%. All regressions include country, ethnicity, marital status and employment status dummies not reported due to space limitations. The dummy for the first income quintile is omitted in the regressions. The dependent variable ranges from never (0) to always justified (10).

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Table 4. **Do you think taxes are too high? (Probit estimates, 2007)**

	(1)	(2)	(3)	(4)	(5)	(6)	(7)
Female	0.041	0.040	0.040	0.039	0.039	0.041	0.036
	(0.032)	(0.032)	(0.032)	(0.032)	(0.032)	(0.032)	(0.032)
Economic problems	0.196	0.187	0.180	0.183	0.189	0.191	0.165
	(0.029)***	(0.029)***	(0.029)***	(0.029)***	(0.029)***	(0.029)***	(0.029)***
Age	0.000	0.000	0.000	0.000	0.000	0.000	0.000
	(0.001)	(0.001)	(0.001)	(0.001)	(0.001)	(0.001)	(0.001)
Head of household	-0.063	-0.060	-0.064	-0.066	-0.064	-0.063	-0.063
	(0.036)*	(0.036)*	(0.036)*	(0.036)*	(0.036)*	(0.036)*	(0.036)*
Years of education	-0.009	-0.009	-0.009	-0.009	-0.009	-0.010	-0.010
	(0.004)**	(0.004)**	(0.004)**	(0.004)**	(0.004)***	(0.004)***	(0.004)***
Religious	0.013	0.022	0.018	0.018	0.016	0.014	0.028
	(0.028)	(0.028)	(0.028)	(0.028)	(0.028)	(0.028)	(0.028)
Citizen	-0.004	-0.003	-0.004	-0.006	-0.007	-0.011	-0.011
	(0.087)	(0.087)	(0.087)	(0.087)	(0.087)	(0.087)	(0.087)
Quintile 2	0.007	0.017	0.004	0.008	0.006	0.014	0.022
	(0.049)	(0.049)	(0.049)	(0.049)	(0.049)	(0.050)	(0.049)
Quintile 3	-0.091	-0.070	-0.087	-0.087	-0.090	-0.076	-0.050
	(0.048)*	(0.048)	(0.048)*	(0.048)*	(0.048)*	(0.049)	(0.049)
Quintile 4	-0.104	-0.078	-0.091	-0.091	-0.098	-0.081	-0.041
	(0.059)*	(0.059)	(0.059)	(0.059)	(0.059)*	(0.061)	(0.062)
Quintile 5	-0.063	-0.046	-0.045	-0.050	-0.054	-0.036	0.005
	(0.108)	(0.108)	(0.108)	(0.108)	(0.108)	(0.112)	(0.113)
Satisfaction with democracy		-0.155					-0.134
		(0.029)***					(0.029)***
Satisfaction with health care			-0.115				-0.066
			(0.027)***				(0.031)**
Satisfaction with education				-0.109			-0.054
				(0.027)***			(0.031)*
Satisfaction with pension system					-0.081		-0.038
					(0.026)***		(0.027)
Past mobility						-0.029	-0.028
						(0.008)***	(0.008)***
Future mobility						-0.021	-0.018
						(0.008)***	(0.008)**
Constant	0.748	0.810	0.915	0.917	0.876	0.773	1.058
	(0.185)***	(0.186)***	(0.189)***	(0.189)***	(0.189)***	(0.187)***	(0.194)***
Observations	13460	13460	13460	13460	13460	13460	13460
Pseudo-R2:	0.08	0.08	0.08	0.08	0.08	0.08	0.08

Notes: Robust standard errors in parenthesis. * significant at 10%, ** significant at 5%, *** significant at 1%. All regressions include country, ethnicity, marital status and employment status dummies not reported due to space limitations. The dummy for the first income quintile is omitted in the regressions.

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Table 5. **Meritocracy and perception regarding excessive taxation (Probit estimates, 2007)**

	(1)	(2)	(3)	(4)
Female	0.035	0.034	0.028	0.033
	(0.033)	(0.033)	(0.033)	(0.033)
Economic problems	0.155	0.155	0.156	0.149
	(0.030)***	(0.030)***	(0.030)***	(0.030)***
Age	0.000	-0.001	-0.001	0.000
	(0.001)	(0.001)	(0.001)	(0.001)
Head of household	-0.063	-0.059	-0.058	-0.062
	(0.037)*	(0.037)	(0.037)	(0.037)*
Years of education	-0.010	-0.010	-0.011	-0.010
	(0.004)***	(0.004)***	(0.004)***	(0.004)***
Religious	0.028	0.027	0.030	0.032
	(0.029)	(0.029)	(0.029)	(0.029)
Citizen	-0.044	-0.049	-0.059	-0.057
	(0.091)	(0.092)	(0.092)	(0.091)
Quintile 2	0.032	0.032	0.029	0.031
	(0.052)	(0.052)	(0.052)	(0.052)
Quintile 3	-0.037	-0.036	-0.039	-0.032
	(0.052)	(0.052)	(0.052)	(0.052)
Quintile 4	-0.035	-0.032	-0.034	-0.024
	(0.064)	(0.064)	(0.064)	(0.065)
Quintile 5	-0.027	-0.020	-0.019	-0.009
	(0.117)	(0.117)	(0.117)	(0.117)
Satisfaction with democracy	-0.142	-0.140	-0.127	-0.122
	(0.030)***	(0.030)***	(0.030)***	(0.030)***
Satisfaction with health care	-0.034	-0.033	-0.030	-0.028
	(0.032)	(0.032)	(0.032)	(0.032)
Satisfaction with education	-0.064	-0.063	-0.058	-0.057
	(0.032)**	(0.032)**	(0.032)*	(0.032)*
Satisfaction with pension system	-0.042	-0.038	-0.032	-0.034
	(0.028)	(0.028)	(0.028)	(0.028)
Past mobility	-0.028	-0.027	-0.027	-0.027
	(0.009)***	(0.009)***	(0.009)***	(0.009)***
Future mobility	-0.019	-0.017	-0.017	-0.016
	(0.008)**	(0.008)**	(0.008)**	(0.008)**
Success depends on hard work rather than connections	-0.098			-0.098
	(0.028)***			(0.028)***
A poor person in my country can become rich if she works hard		-0.051		-0.041
		(0.030)*		(0.030)
Life Chances are independent of origin			-0.153	-0.152
			(0.029)***	(0.029)***
Constant	1.039	1.109	1.125	1.067
	(0.205)***	(0.205)***	(0.204)***	(0.205)***
Observations	12445	12445	12445	12445
Pseudo-R2	0.08	0.08	0.08	0.09

Notes: Robust standard errors in parenthesis. * significant at 10%, ** significant at 5%, *** significant at 1%. All regressions include country, ethnicity, marital status and employment status dummies not reported due to space limitations. The dummy for the first income quintile is omitted in the regressions. Dependent variable is dummy which take value one if the individual considers that taxes are too high.

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Table 6. **Demand for redistribution (Probit estimates, 2007)**

	(1)	(2)	(3)	(4)
Dependent Variable	State should intervene in health	State should intervene in education	State should intervene in pension	Market should solve all problems
Female	0.031	0.023	0.008	0.021
	(0.029)	(0.029)	(0.029)	(0.028)
Economic Problems	-0.085	-0.109	-0.043	-0.054
	(0.027)***	(0.027)***	(0.027)	(0.025)**
Age	-0.002	-0.002	-0.001	-0.001
	(0.001)**	(0.001)**	(0.001)	(0.001)
Head of household	-0.014	-0.025	-0.042	0.004
	(0.032)	(0.032)	(0.033)	(0.031)
Years of education	0.004	0.005	0.002	0.006
	(0.003)	(0.003)	(0.003)	(0.003)**
Religious	0.126	0.121	0.105	0.000
	(0.025)***	(0.025)***	(0.026)***	(0.023)
Citizen	0.046	-0.09	-0.008	-0.072
	(0.086)	(0.086)	(0.088)	(0.072)
Left-Right	0.037	0.033	0.03	0.002
	(0.005)***	(0.005)***	(0.005)***	(0.005)
Quintile 2	-0.047	-0.146	-0.123	0.092
	(0.043)	(0.043)***	(0.044)***	(0.041)**
Quintile 3	-0.052	-0.129	-0.089	0.088
	(0.043)	(0.043)***	(0.044)**	(0.042)**
Quintile 4	-0.049	-0.149	-0.085	0.156
	(0.056)	(0.056)***	(0.056)	(0.054)***
Quintile 5	0.215	0.154	0.3	0.005
	(0.107)**	(0.105)	(0.107)***	(0.107)
Distribution of income is fair	0.144	0.143	0.115	
	(0.030)***	(0.030)***	(0.031)***	
Satisfaction with health care	0.197			
	(0.025)***			
Satisfaction with education		0.124		
		(0.025)***		
Satisfaction with pension system			0.145	
			(0.024)***	
Past mobility	-0.014	-0.007	-0.007	0.01
	(0.007)*	(0.007)	(0.007)	(0.009)
Future mobility	-0.011	-0.011	-0.022	-0.019
	(0.007)	(0.007)	(0.007)***	(0.008)**
Opportunities independent of origin	0.049	0.074	0.106	
	(0.026)*	(0.026)***	(0.026)***	
A poor person can become rich	0.069	0.059	0.029	
	(0.026)***	(0.027)**	(0.027)	
Corruption				-0.001
				(0.000)***
Constant	-1.526	-1.082	-1.354	
	(0.195)***	(0.196)***	(0.201)***	
Observations	11688	11579	11412	9621
Pseudo-R2:	0.05	0.05	0.05	0.01

Notes: Robust standard errors in parenthesis. * significant at 10%, ** significant at 5%, *** significant at 1%. All regressions include country, ethnicity, marital status and employment status dummies not reported due to space limitations. The dummy for the first income quintile is omitted in the regressions.

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V. CONCLUSIONS AND POLICY IMPLICATIONS

Is the social contract broken in Latin America? Many authors have suggested this is the case, given the high levels of inequality, the low levels of taxation and the low quality of public services prevalent in the region.

This paper has analysed empirically the relationship between fiscal policy, social mobility and democratic consolidation in Latin America and the Caribbean, using the 2007 and 2008 rounds of the regional *Latinobarómetro* survey. Our results in general do not support the POUM hypothesis (the greater the mobility and the perception of meritocracy, the less citizens think taxes are too high), but they confirm that perceptions regarding the quality of public services (from the more global ones, to the more specific) matter for the willingness to pay taxes.

Therefore, we interpret our results as evidence that the social contract might be weak, but could and should be reinforced. The way forward may be, in fact, suggested by the analytical results themselves. The failure of POUM hypothesis is a great opportunity. Even those citizens who are confident about their future mobility seem to be demanding stronger social insurance programmes. Improvement in the quality of public services could provide a catalyst for such reforms, and in so doing foster more satisfaction with the functioning of democracy. Improvements in those areas may henceforth allow for higher levels of taxation in return by strengthening tax morale, or the willingness to pay taxes. In line with Torgler (2005), the relationship of citizens with their government is not just a matter of coercion, but also of trust. Finally, once again, this virtuous circle may be consolidated by higher levels of education, which affect positively support for all these reforms.

These results can be calibrated against the analysis in Marcel (2008), based on the survey *ECosociAL 2007*. As the author showed, only a minority of Latin Americans believes the low and middle income population will progress (*e.g.* access the university, own a house, or establish their own business) with high probability. Additionally, households in the region were found to be subject to many of the risks that may break the social contract and undermine social integration, such as crime, job insecurity, and poor or absent health-care cover. However, at the same time, Latin American citizens have strong beliefs in the value of effort, in the benefits of education, and in a the shared responsibility of the state and the individual, backed by a willingness to pay more taxes to finance social insurance.

All in all, we interpret our results as an indication of a potential basis for a stronger social contract in Latin America.

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