Direct and Indirect Tax Revenues

Table 1

Tax structures in the OECD area

	1965	1975	1985	1995	2005
Personal income tax	26	30	30	27	25
Corporate income tax	9	8	8	8	10
Social security contributions	18	22	22	25	26
(employee)	*(6)*	*(7)*	*(7)*	*(8)*	*(8)*
(employer)	*(10)*	*(14)*	*(13)*	*(14)*	*(15)*
Payroll taxes	1	1	1	1	1
Property taxes	8	6	5	6	6
Taxes on goods and services	38	33	34	32	32
Other taxes	1	1	1	3	3
Total	100	100	100	100	100

Source: OECD (2007).

Governments are frequently encouraged to rely less on direct taxes and more on indirect taxes, an issue that has recently received considerable attention in politics and academia. It is argued that a greater reliance on indirect taxes is more efficient and that direct taxes have undesirable redistributive effects. The efficiency cost of taxation is lower with indirect taxation because the tax base is more broadly defined than with income taxes. Since indirect tax rates can be lower, they reduce the deadweight loss of taxation. Also, attempts by taxpayers to engage in tax avoidance or even tax evasion are less likely with indirect taxes. Thus, the consequent conclusion is that indirect taxes should finance a higher share of government expenditures. However, redistributive policy is less effective with indirect taxes since indirect taxes are levied anonymously and can only be indirectly adjusted to the income status of households.

A more detailed look at the government finances of OECD countries reveals that the share of indirect

Table 2

Taxes on goods and services as percentage of total taxation

	1965	1970	1975	1980	1985	1990	1995	2000	2005
Canada	40.5	31.7	32.0	32.6	31.8	25.8	25.4	24.2	25.4
Mexico				51.2	64.8	55.3	53.9	53.0	56.7
United States	22.8	20.0	19.5	17.6	18.8	17.4	18.0	16.1	17.4
Australia	34.7	32.0	29.3	31.1	32.8	27.8	29.0	28.7	27.8
Japan	26.2	22.4	17.3	16.3	14.0	13.7	15.8	19.3	19.4
Korea			61.1	62.7	59.5	46.7	43.1	38.3	34.3
New Zealand	27.9	27.2	24.2	22.3	23.1	33.6	33.4	34.7	32.1
Austria	37.4	37.4	34.5	31.5	32.6	31.5	28.0	28.2	28.4
Belgium	37.2	35.8	27.4	27.2	25.4	26.5	25.7	25.3	25.3
Czech Republic							32.2	31.6	31.3
Denmark	41.4	38.8	34.3	37.5	34.3	33.0	32.1	32.1	32.2
Finland	42.5	39.6	31.9	35.3	33.9	32.5	30.2	29.0	31.3
France	38.4	38.1	33.3	30.4	29.7	28.4	27.3	25.7	25.3
Germany	33.0	31.8	26.9	27.1	25.7	26.7	28.0	28.1	29.0
Greece	48.8	48.2	46.8	41.2	42.7	44.5	41.3	35.3	34.6
Hungary							40.6	40.5	39.7
Iceland	62.7	61.3	63.0	59.9	61.1	51.3	48.7	44.8	40.4
Ireland	52.6	52.4	46.5	43.7	44.4	42.3	39.8	38.3	37.8
Italy	39.5	38.7	29.4	26.5	25.4	28.0	27.3	27.9	26.4
Luxembourg	24.7	20.5	20.9	21.5	24.3	24.8	26.7	27.2	28.8
Netherlands	28.6	27.8	24.2	25.2	25.6	26.4	27.2	29.1	31.7
Norway	41.1	42.8	37.6	35.3	37.5	35.5	38.6	31.8	27.9
Poland							35.2	36.3	36.7
Portugal	47.6	47.2	42.6	46.5	43.7	44.2	40.8	37.5	39.3
Slovak Republic								36.1	39.7
Spain	40.8	35.9	24.2	20.7	28.7	28.4	28.6	29.6	28.0
Sweden	31.2	28.2	24.3	24.0	26.6	25.0	27.8	24.6	26.1
Switzerland	34.2	30.2	22.4	23.0	21.9	21.2	21.9	22.5	23.6
Turkey	53.9	49.4	41.3	25.6	36.0	27.9	37.6	42.0	49.3
United Kingdom	33.1	28.8	25.0	29.2	31.5	31.1	35.3	31.9	30.3
OECD Average	38.4	36.1	32.8	32.5	33.7	31.9	32.4	31.7	31.9

Source: OECD (2007).

taxes has decreased. Table 1 shows the share of different taxes in tax revenues from 1965 to 2005. Indirect taxes are taxes on goods and services. The share decreased from 38 percent in 1965 to 32 percent in 2005. The share of personal income and corporate income tax stayed roughly at the same level – approximately 35 percent. In contrast, social security contributions gained in fiscal importance. Their share rose from 18 percent to 26 percent over the reported time span. If social security contributions are excluded, the share of indirect taxes over direct taxes – defined as taxes on goods and services over personal and corporate income tax – increased.

Table 2 gives a more disaggregated view. The share of taxes on goods and services varies widely over countries. For instance, as of 2005 the US has had the lowest share (17.1 percent) whereas Mexico has the highest share (56.7 percent). From 1965 to 2005, the share decreased in almost all countries. Exceptions are New Zealand, Luxembourg and the Netherlands. Possible explanations for the divergence between the general policy discussion and the actual development of tax shares might be that income tax rates have indeed decreased over time (in particular capital income tax rates) and indirect tax rates have increased while income tax bases have become more broadly defined. This means that income taxes have not lost their fiscal importance as one might assume based on a comparison of statutory tax rates on income.

M.K.

Reference

OECD (2007), *Revenue Statistics* 1965–2006, 33–38.