INFORME

The Flat tax era: Evolution of Taxation in OCDE Countries

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"Friendly Warning":

If you'll allow me, I'd like to start with a friendly warning. First of all, I must say that perhaps in this presentation I am guilty of leaning into my background as an economist, particularly one specialized in public sector economics. Maybe the topic I am going to address isn't the most trendy, and it's certainly not about the latest ruling from the European Court of Justice or a specific case related to tax planning. What I want to propose today is that we all take a moment to reflect together on the historical evolution of tax systems in OECD countries over the past few decades.

Now, perhaps looking at History is not a fashionable or novel topic, but I consider it fundamental for understanding the present and the main trends that may shape the future of taxation in the countries around us. This topic is undoubtedly deep, and I have spent considerable time preparing for it, resulting in a ***document of almost 80 pages****. Naturally, I cannot present it all here, but* ***it is available through the LEA Vienna 2024 Conference App*** *for anyone who is interested in exploring it further.*

However, it's clear that what I'm about to present cannot be fully covered in just five PowerPoint slides. There are many graphs and tables, so I decided to condense it into a Word document. I apologize if it's not the most visually appealing presentation.

The idea for analyzing this topic came to me because recently, there has been a lot of talk in Italy—a country where we have many clients and work extensively—about the flat tax policy. It has been widely discussed in the press, and we have followed it closely. In Spain, we have also had a flat tax system for some time, and I personally began to wonder if it is a good system, if it is fair, and what results it has produced.

Additionally, Spain introduced a special tax regime some time ago, which has recently been modified. This regime is quite favorable, applying a flat tax of 24% on Spanish-source income while not taxing foreign-source income at all. This has made the system quite well-known globally and has attracted many qualified workers, entrepreneurs, and company directors to come and live in Spain and benefit from the regime. Portugal also has a similar system, perhaps even more advantageous, although the last Portuguese government, as some of you may know, has either eliminated or significantly limited it.

Finally, I want to apologize in advance if this subject, on top of being possibly boring or heavy, is presented in rather limited English, as mine is. I am a Catalan speaker and I already struggle to express myself in Spanish—imagine trying to present the history of taxation in English! I ask for your understanding and patience, and thank you very much for your attention in advance.

Index:

- ✓ Introduction
- ✓ Historical Analysis of Taxation in OECD Countries
- ✓ The Laffer Curve Doctrine
- ✓ Current Tax Rates in OECD Countries.
- ✓ Italy's Flat Tax System
- ✓ Spain's Recent Tax Policies and Flat Tax System (Régimen de Módulos)
- ✓ Spain: Beckham Law – Special Tax Regime for Inbound new workers/entrepreneurs
- ✓ Critical conclusion for Flat Rate Policies. Trends and Future Directions for Tax Policies: Flat Tax vs. Progressive Taxation

1. Introduction

The landscape of taxation in OECD countries has undergone significant transformations over the past several decades. From the post-war era of high progressive taxation to the recent trends favoring flat tax systems, tax policies have played a crucial role in shaping the economic and social structures of these nations. One of the most debated concepts in the realm of tax policy is the **Laffer Curve**, introduced by economist Arthur Laffer. His theory argues that there is an optimal tax rate that maximizes government revenue, and that reducing excessively high tax rates can, paradoxically, lead to an increase in tax receipts by incentivizing economic activity.

This report delves into the evolution of taxation systems across OECD countries, focusing on the rise of flat tax systems and the influence of supply-side economics. It will analyze the historical shifts in tax policies, from high marginal tax rates designed to fund growing welfare states to the tax reductions and reforms aimed at fostering competitiveness in a globalized economy. Special attention will be given to empirical evidence supporting or contradicting the Laffer Curve theory, particularly in the case studies of **Italy** and **Spain**.

The purpose of this report is to explore the implications of these tax policy changes on economic growth, revenue generation, and income inequality. By examining the experiences of countries that have adopted low or flat tax regimes, this study aims to provide a comprehensive understanding of the benefits and challenges associated with these reforms. In doing so, it will offer policy recommendations for OECD countries navigating the complex interplay between tax rates, economic performance, and fiscal sustainability.

2. Historical Analysis of Taxation in OECD Countries

Post-WWII Period (1945–1970s)

After World War II, OECD countries adopted progressive tax systems with high marginal tax rates to fund reconstruction and welfare programs. Personal income tax rates for the highest earners often exceeded 80%, and corporate tax rates were similarly high.

- Key Features:
  - High Marginal Tax Rates: The top personal income tax rate in the United States was 91% in the 1950s.
  - Expansion of Welfare States: Funding for healthcare, education, and infrastructure.
  - Economic Growth: Despite high taxes, economies grew rapidly due to industrialization and pent-up post-war demand.

1970s–1980s: Neoliberal Shifts

The oil crises of the 1970s led to stagflation, prompting a reevaluation of economic policies. Neoliberalism, advocating for reduced government intervention and lower taxes, gained prominence.

- Policies Implemented:
  - United States: President Reagan reduced the top marginal income tax rate from 70% to 28% in the 1980s.
  - United Kingdom: Prime Minister Thatcher lowered the top rate from 83% to 40% and reduced corporate taxes.
- Rationale:
  - Supply-Side Economics: Lowering taxes was believed to stimulate economic growth by increasing investment and work incentives.

1990s–2000s: Globalization and Tax Competition

The globalization era intensified tax competition among countries seeking to attract multinational corporations.

- Corporate Tax Rate Reductions:
  - Ireland: Reduced its corporate tax rate to 12.5%, attracting significant foreign direct investment (FDI).
  - OECD Average: Corporate tax rates fell from an average of 32.2% in 2000 to 25% in 2008.
- Personal Income Tax Adjustments:

    - Gradual reductions in top marginal rates but less pronounced than corporate tax cuts.

2008 Financial Crisis and Aftermath

The global financial crisis led to increased government deficits and a reevaluation of tax policies.

- Responses:
    - Stimulus Spending: Governments increased spending to boost economies.
    - Tax Policy Adjustments: Some countries raised taxes on high earners to address deficits.

2010s–Present: Digital Economy and Global Initiatives

- Digital Services Taxes: Implementation of taxes targeting digital giants (e.g., France's 3% DST).
- International Cooperation: OECD's BEPS project and proposals for a global minimum corporate tax rate.

Historical Analysis of Taxation in OECD Countries: Spain, Italy, and Portugal Case Studies

This expanded section will include a more detailed historical perspective on taxation in OECD countries, particularly focusing on Spain, Italy, and Portugal, and how these countries adapted their tax policies over time. Additionally, charts and tables will help illustrate key trends.

Post-WWII Period (1945–1970s)

After World War II, OECD countries adopted highly progressive tax systems with elevated marginal tax rates to fund post-war reconstruction and expanding welfare programs. Spain, Italy, and Portugal also followed this trend, although with some variations due to political differences.

Key Features:

- High Marginal Tax Rates: Top personal income tax rates often exceeded 80% in the post-war period.
  - Italy: Marginal tax rates peaked at 90% for the highest earners.
  - Spain and Portugal: While slightly lower, Spain had rates around 70% for top earners, while Portugal, after transitioning from dictatorship, raised taxes as well to fund modernization and public services.
- Expansion of Welfare States: These countries used tax revenue to fund growing welfare systems, such as universal healthcare, education, and pensions.
- Economic Growth: Despite high taxes, the economies of Spain, Italy, and Portugal grew rapidly due to post-war industrialization and labor reforms.

Table 1: Post-WWII Marginal Income Tax Rates in Selected Countries (1950s)

Country	Top Personal Income Tax Rate (%)	Corporate Tax Rate (%)
United States	91%	50%
United Kingdom	83%	45%
Italy	90%	48%
Spain	70%	45%
Portugal	65%	40%

1970s–1980s: Neoliberal Shifts

The global economic crises of the 1970s, including the oil shocks, brought stagflation (simultaneous high inflation and unemployment), which prompted many OECD countries to shift toward neoliberal economic policies. These policies were marked by lower taxes, deregulation, and reduced government intervention.

Policies Implemented:

- Italy: Italy began reducing taxes in the late 1980s as part of broader efforts to reform its stagnant economy.
- Spain: Following Franco's death in 1975 and the transition to democracy, Spain implemented economic reforms that included lowering marginal tax rates and introducing a progressive income tax system.
- Portugal: After the 1974 Carnation Revolution, Portugal modernized its economy and gradually lowered tax rates as it moved towards the European Community (now EU).

Rationale: The neoliberal push was driven by supply-side economics, which argued that lowering taxes would encourage investment, productivity, and ultimately economic growth.

Table 2: Tax Reforms in Spain, Italy, and Portugal (1970s–1980s)

Country	Top Income Tax Rate Before	Top Income Tax Rate After	Corporate Tax Rate Reduction
Italy	85%	65%	From 48% to 42%
Spain	70%	56%	From 45% to 35%
Portugal	65%	58%	From 40% to 35%

1990s–2000s: Globalization and Tax Competition

By the 1990s, globalization had intensified competition among countries to attract multinational corporations. This led to corporate tax rate reductions across OECD countries, including Spain, Italy, and Portugal.

Corporate Tax Rate Reductions:

- Spain: Reduced its corporate tax rate from 35% to 25% over the 1990s and early 2000s, to remain competitive within the European Union.
- Italy: Cut its corporate tax rate from 43% to 27.5% by the mid-2000s.
- Portugal: Reduced its corporate tax rate from 40% to 25% to attract foreign investment.

2008 Financial Crisis and Aftermath

The global financial crisis of 2008 led to significant economic contractions, particularly in southern European countries. Governments faced growing budget deficits and responded by raising taxes, cutting spending, and implementing austerity measures.

Responses:

- Spain: Spain raised taxes on high earners and increased the value-added tax (VAT) to 21% to counter large deficits.
- Italy: Italy also raised taxes, including a solidarity tax on high incomes, to reduce public debt.
- Portugal: Portugal implemented strict austerity measures after receiving a bailout from the European Union.

Table 3: Tax Adjustments in Spain, Italy, and Portugal (2008–2015)

Country	Top Income Tax Rate Increase	Corporate Tax Rate	VAT Increase
Spain	From 43% to 47%	30%	From 18% to 21%
Italy	From 43% to 48%	27.5%	From 20% to 22%
Portugal	From 42% to 45%	25%	From 19% to 23%

2010s–Present: Digital Economy and Global Initiatives

The rise of the digital economy has presented new challenges for taxation in OECD countries. Countries like Spain, Italy, and Portugal have introduced digital services taxes (DSTs) to tax large multinational tech companies that were previously paying minimal taxes in these countries.

Digital Services Taxes:

- Spain: Introduced a 3% tax on revenues from digital services provided by companies like Google and Amazon in 2020.
- Italy: Implemented a similar 3% digital tax in 2020.
- Portugal: Has explored the introduction of a DST but has yet to fully implement one.

International Cooperation:

These countries are also part of the OECD's Base Erosion and Profit Shifting (BEPS) initiative, which seeks to close tax loopholes exploited by multinationals. The OECD is pushing for a global minimum corporate tax rate of 15% to prevent tax base erosion.

Chart 2: Evolution of Corporate Tax Rates in Spain, Italy, and Portugal (1990–2021)

Corporate Tax Rates in Spain, Italy, and Portugal (1990–2021)

Here is the chart showing the Corporate Tax Rates in Spain, Italy, and Portugal from 1990 to 2021. This visualizes the trend of declining corporate tax rates in these countries, reflecting their efforts to remain competitive in the global economy.

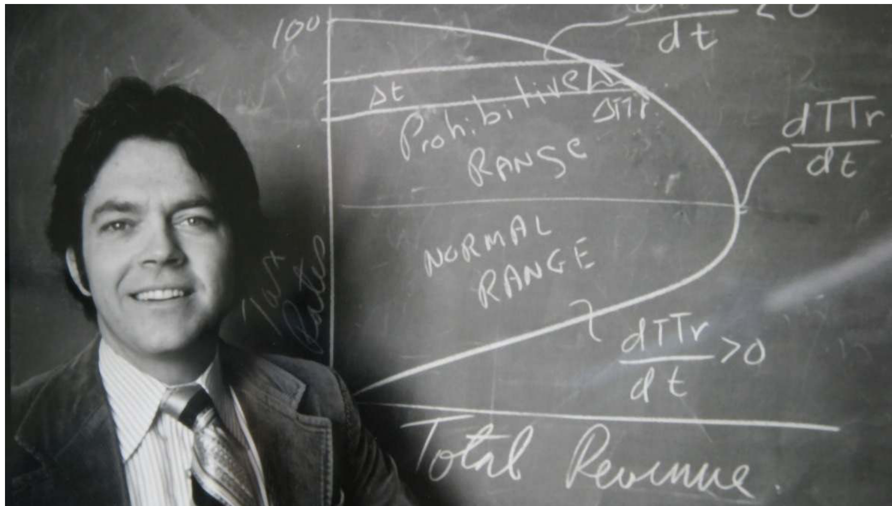
- Spain: Gradually reduced its corporate tax rate from 35% to 25%.
- Italy: Reduced its rate from 43% to 24%.
- Portugal: Saw a decline from 40% to 21%.

OBSERVATIONS:

- All three countries have consistently lowered corporate tax rates over the past three decades to attract foreign investment and encourage economic growth.
- Portugal, in particular, implemented one of the most aggressive reductions, dropping to 21%.

3. Laffer Doctrine

1. Laffer Curve. Overview



Arthur Laffer junto a su famosa curva. Foto de Laffer Center.

Arthur B. Laffer is an American economist best known for his development of the **Laffer Curve**, a theoretical representation of the relationship between tax rates and tax revenue. Born on **August 14, 1940**, in **Youngstown, Ohio**, Laffer became a prominent figure in the field of supply-side economics during the 1970s and 1980s.

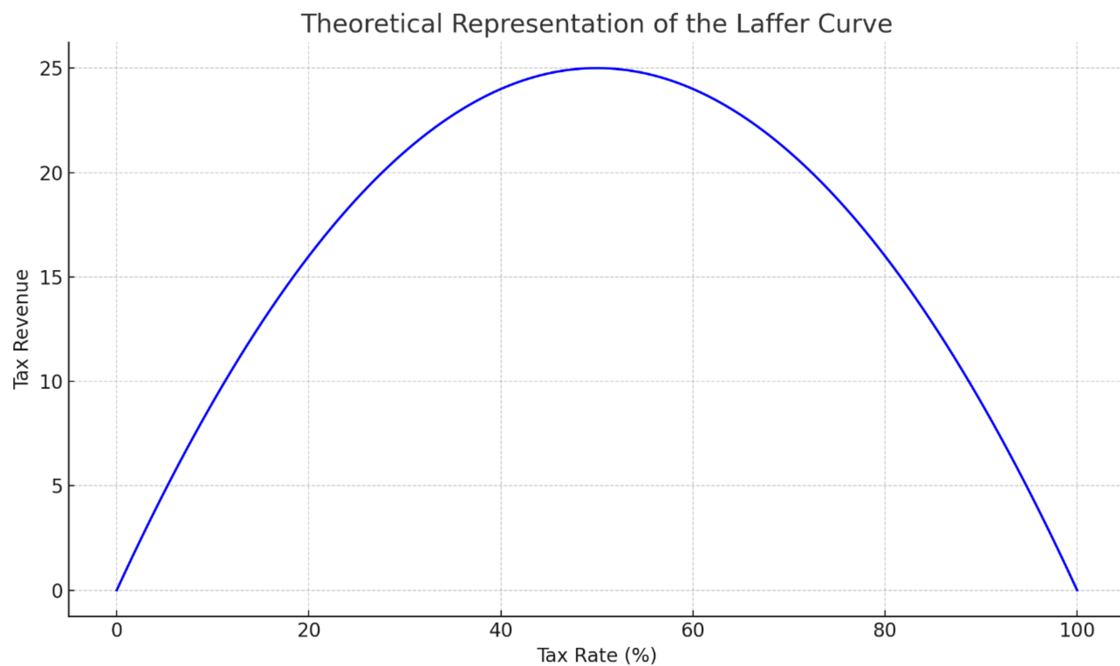
Laffer earned a **B.A. in Economics** from Yale University in 1963, followed by an **M.B.A.** and a **Ph.D. in Economics** from Stanford University. His work in the field of economics brought him into political circles, where he became a key advisor to President **Ronald Reagan** during the 1980s. His economic philosophy centered around the belief that reducing tax rates could spur economic growth by incentivizing investment, work, and production, which would in turn increase overall tax revenues—a concept encapsulated by the Laffer Curve.

The Laffer Curve wanted to demostrate that there is an optimal tax rate that maximizes government revenue. If tax rates are too high, they may discourage work, investment, and production, leading to decreased revenue. Laffer's ideas heavily influenced Reagan's economic policies, particularly the **Economic Recovery Tax Act of 1981**, which enacted substantial tax cuts.

Laffer continues to be an influential figure in economic policy debates. In 2019, he was awarded the **Presidential Medal of Freedom** by President Donald Trump, further cementing his legacy as a significant contributor to American economic policy.

A cloth napkin from the Two Continents restaurant in Washington (with Donald Rumsfield, Dick Chaney and a WP journalist) *with his famous curve, not knowing that this piece of fabric would end up changing the economy through its influence on the thinking of Ronald Reagan and Margaret Thatcher, and having its own showcase in* ***the Museum of American History****.*

2. Theoretical Framework



Core Idea of the Laffer Curve

- Too Low a Tax Rate: Insufficient tax revenue because the government is not collecting enough from the economic activity.
- Too High a Tax Rate: Reduced incentives for work and investment lead to decreased economic activity, shrinking the tax base and lowering total revenue.
- Optimal Point: The point where tax rates balance with the highest possible tax revenue.

Justifications According to Supply-Side Economics:

- Increased Economic Activity: By lowering taxes, individuals have more disposable income, which can incentivize work, productivity, and investment.
- Increased Investment: Lower corporate taxes encourage businesses to expand and innovate, fostering overall economic growth.
- Tax Revenue Growth: The argument suggests that a lower tax rate can expand the tax base by boosting the economy, potentially leading to higher total revenue.

3. Historical Application: Reaganomics and Thatcherism

Reaganomics (United States, 1980s)

The Laffer Curve heavily influenced President Ronald Reagan's economic policies. Reagan's administration implemented significant tax cuts:

- Reduction of Top Marginal Tax Rate: In 1981, Reagan reduced the top marginal tax rate from 70% to 50%, and further down to 28% by 1986.
- Goal: The goal was to stimulate economic growth by increasing disposable income and investment.
- Result: The U.S. economy saw growth during the 1980s, but federal deficits increased, and critics argued that the tax cuts disproportionately benefited the wealthy.

Thatcherism (United Kingdom, 1980s)

Margaret Thatcher's government in the UK also applied principles of the Laffer Curve:

- Reduction of Top Marginal Tax Rate: The top rate of personal income tax was reduced from 83% to 60% in 1979, and to 40% by 1988.
- Goal: To promote business investment, reduce government intervention, and encourage private enterprise.
- Result: While economic growth and investment improved, inequality increased, and public spending remained a challenge.

Curve-inspired tax policies in different economic contexts.

Curve-inspired tax policies in different economic contexts.

- **United States: Reaganomics and the 2017 Tax Cuts**
  - Reaganomics (1980s)Policy Overview: In the 1980s, President Ronald Reagan
  - The Tax Cuts and Jobs Act (2017)

- **United Kingdom: Thatcherism and Austerity**

✓ Example: Thatcher's Tax Cuts (1980s)

- **Russia: Flat Tax Revolution**

✓ Example: Russia's Flat Tax (2001)

- **Estonia: Flat Tax and Economic Growth**

✓ Example: Estonia's Flat Tax (1994)

- **France: Tax Cuts and Revenue Shortfalls (2007-2012)**

✓ Example: Sarkozy's Tax Cuts (2007)

4. Empirical Evidence and Criticisms

Supporting Evidence

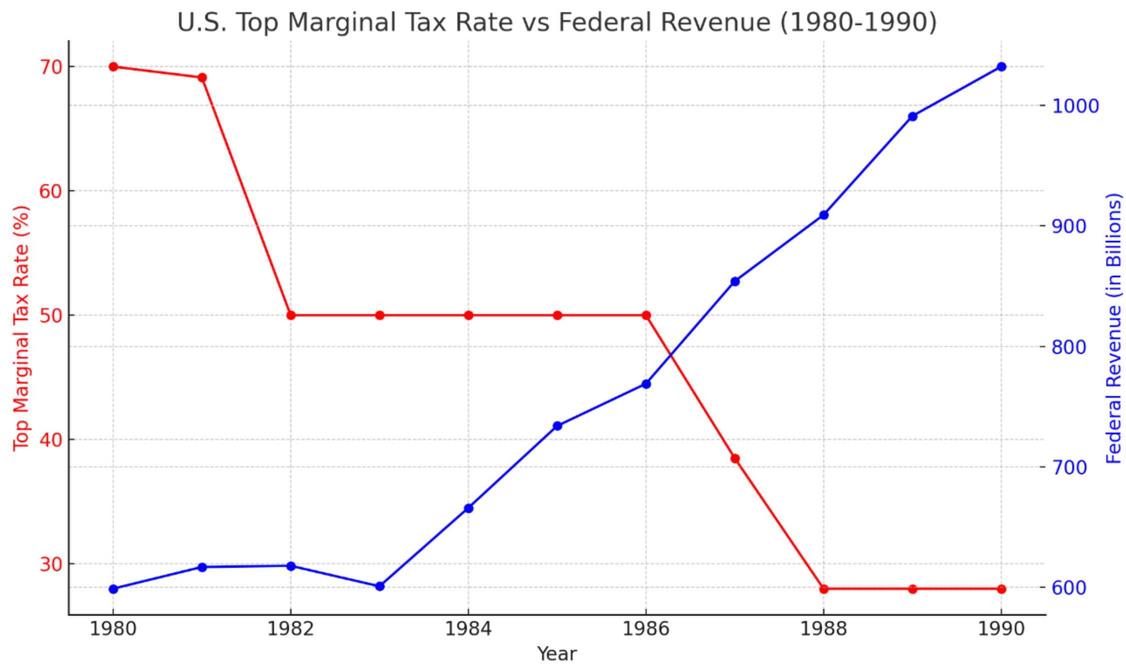
- Economic Growth: Following tax cuts in the U.S. and the U.K., both countries experienced periods of economic growth and expansion of corporate investment. Proponents argue that this demonstrates the validity of the Laffer Curve in practice.

Criticisms and Contradictions

- Revenue Shortfalls: In both the U.S. and the U.K., tax cuts led to increased deficits, challenging the idea that lower tax rates would automatically generate enough growth to offset the reduction in tax revenue.
- Rising Inequality: Tax cuts primarily benefited wealthier individuals and corporations, leading to a widening wealth gap in both countries.
- Context Dependency: Critics argue that the effectiveness of the Laffer Curve depends on the initial tax rate. If tax rates are already low, further reductions may not stimulate additional growth or revenue.

5. Visual Representations and Data

Chart comparing the U.S. top marginal tax rates and federal revenue growth during the 1980s under Reagan's tax cuts to illustrate how this doctrine was applied in practice.



Here is the chart comparing the U.S. top marginal tax rates with federal revenue growth during the 1980s under President Reagan. The red line represents the significant reduction in the top marginal tax rate, while the blue line shows federal revenue in billions of dollars. Despite the reduction in tax rates, federal revenue did continue to grow, although critics note that deficits also increased during this period.

This visualization demonstrates the complex relationship between tax rates and revenue, illustrating a key point in the debate around the real-world application of the Laffer Curve.

6. Critics

The Laffer Curve, while a compelling theoretical model in supply-side economics, has faced significant criticism. These critiques primarily focus on the oversimplification of real-world economics, empirical inconsistencies, and the broader social and economic impacts of policies inspired by the Laffer Curve. Below is an analysis of the major criticisms, supported by data and practical examples.

1. Oversimplification of Economic Dynamics

One of the main criticisms of the Laffer Curve is that it oversimplifies the complex relationship between tax rates and government revenue. The curve assumes a direct correlation between tax rates and economic behavior, such as work and investment decisions. However, real-

world economies are influenced by a wide range of factors, including government spending, monetary policy, global market conditions, and income distribution.

- Example: Economic growth in the 1980s following Reagan's tax cuts is often cited as proof of the Laffer Curve's effectiveness. However, other factors such as deregulation, monetary policy, and technological advancements also played crucial roles. Focusing solely on tax rates does not account for these broader influences.

CONCLUSION:

The simplicity of the Laffer Curve makes it appealing to policymakers, but it does not fully capture the complexity of economic systems. In practice, revenue and growth depend on more than just tax rates.

2. Empirical Inconsistencies: Tax Cuts and Revenue Shortfalls

A major empirical criticism is that the Laffer Curve does not consistently predict revenue growth following tax cuts. Historical evidence suggests that while tax cuts can stimulate economic activity, they often lead to deficits and revenue shortfalls, especially when the starting tax rates are already moderate. (**less than 70% of Fiscal Pressure on global GDP)**

- U.S. Example (Reaganomics): During the Reagan administration, tax cuts did stimulate economic growth, but they also led to significant increases in the national deficit. Federal debt tripled from $900 billion in 1980 to over $2.7 trillion by 1988. While revenues grew, they did not grow enough to offset the cuts, and government spending on defense and social programs contributed to rising deficits.
- UK Example (Thatcherism): Margaret Thatcher's tax cuts also led to economic recovery, but they exacerbated income inequality. While corporate investment increased, public revenue shortfalls forced the government to cut public services, leading to political and social unrest.

CONCLUSION:

The empirical evidence suggests that tax cuts often lead to deficits when starting from moderate tax rates. The assumption that all tax cuts will pay for themselves through increased revenue has not held up in many real-world scenarios, especially when the cuts favor the wealthy.

3. Effect on Income Inequality

Tax cuts driven by the Laffer Curve tend to disproportionately benefit high-income earners and corporations. By reducing top marginal tax rates, these policies often widen the gap between the rich and the poor, contributing to income inequality.

- Reagan's Tax Cuts: The top marginal tax rate in the U.S. was reduced from 70% to 28%, which primarily benefited the wealthiest Americans. Middle- and lower-income

earners saw less dramatic changes in their tax burdens, and the wealth gap in the U.S. widened significantly during this period. Wealth accumulation at the top was also driven by financial deregulation, stock market gains, and capital investments—benefiting the wealthy more than workers.

- UK Example: In the UK, Thatcher's tax cuts reduced the top income tax rate from 83% to 40%. While this encouraged investment, it also led to significant reductions in welfare spending and public services. The result was increased inequality, with wealth concentrated among the upper class and corporate sectors.

4. Revenue Recovery Depends on Starting Tax Rate

The effectiveness of the Laffer Curve in increasing revenue hinges on the starting tax rate. If tax rates are already very high (as they were in the U.S. before the Reagan cuts), there is more room for revenue increases after cuts. However, in cases where tax rates are moderate or low, further reductions are less likely to stimulate significant revenue growth.

- Example: Countries like Estonia and Hungary, which adopted flat tax systems with low rates (around 20% or lower), did not experience substantial revenue growth. While these systems simplified tax administration, they did not expand the tax base enough to generate significant additional revenue. This shows that cutting already moderate rates is less likely to produce the desired Laffer Curve effect.

5. Neglect of Government Spending Needs

The Laffer Curve focuses solely on tax revenue, neglecting the spending side of government finances. In reality, tax cuts reduce the government's ability to fund public services, infrastructure, education, and welfare programs. If tax cuts reduce revenue without a corresponding reduction in spending, deficits grow, and critical public services may suffer.

- Example: The Reagan administration's tax cuts were paired with increased military spending, resulting in record deficits. In the UK, Thatcher's tax cuts led to reduced funding for public housing, healthcare, and welfare programs, which disproportionately affected the working class and unemployed.

6. Tax Evasion and Loopholes

The Laffer Curve assumes that lower tax rates will automatically increase compliance and reduce tax evasion, but evidence suggests this is not always the case. Even with lower rates, individuals and corporations may seek ways to avoid taxes through loopholes, offshore accounts, and tax shelters.

- Example: In the U.S., despite lower tax rates, tax avoidance strategies (such as the use of offshore tax havens) became more sophisticated after the Reagan tax cuts. High-income earners and multinational corporations have the resources to exploit legal loopholes, reducing the overall effectiveness of the tax system.

7. Summary of Criticisms

Criticism	**Key Point**
Oversimplification	The curve ignores economic complexity and other influences on growth.
Empirical Inconsistencies	Tax cuts often lead to deficits, especially if starting tax rates are moderate.
Exacerbates Inequality	Wealthier individuals benefit more from tax cuts, leading to wider income gaps.
Starting Tax Rate Dependency	The Laffer Curve works better with very high starting tax rates, not moderate ones.
Neglects Government Spending Needs	Lower tax revenue affects funding for public services, leading to cuts in crucial sectors.
Tax Evasion	Lower rates don’t automatically reduce evasion without closing loopholes.

4. Current Tax Rates in OECD Countries.

Overview

The current landscape of taxation in OECD countries reflects a general trend toward lower corporate tax rates, driven by globalization and tax competition, while personal income tax rates have seen more varied approaches depending on the country's fiscal policy and economic needs

Average Corporate Tax Rate in OECD Countries (1980–2021)

Here is the chart showing the Average Corporate Tax Rate in OECD Countries from 1980 to 2021, illustrating the steady decline from approximately 47% to 23%. This trend reflects the global shift toward lower corporate taxation to promote competitiveness and attract investment.

Corporate Tax Rates in OECD Countries

1. Top OECD Countries by Corporate Tax Rates (2023)
    - France: 25%
    - Germany: 30% (including local trade tax)
    - Japan: 30.62%
    - United States: 21%
    - United Kingdom: 19% (recent changes proposed)
    - Ireland: 12.5% (a standout low corporate tax rate)
    - Hungary: 9% (one of the lowest in the OECD)

As of recent years, Hungary and Ireland continue to have some of the lowest corporate tax rates, which has made them attractive destinations for multinational companies. On the other hand, countries like France and Germany maintain relatively higher corporate tax rates but offer various incentives for businesses.

Country	Corporate Tax Rate (%)
Hungary	9
Ireland	12.5
Switzerland	~15*
United Kingdom	19
Spain	25
Netherlands	25
Germany	29.9**
France	28
Japan	30.62

* Varies by canton in Switzerland.
** Includes federal and municipal taxes in Germany.

Corporate Tax Rates in Selected OECD Countries (2021)

2. Average OECD Corporate Tax Rate (2023) The average corporate tax rate in OECD countries has declined to around 23.5%, continuing the downward trend that has been evident since the 1990s. Countries like Ireland have used their low corporate tax rates as a cornerstone of their economic strategy, attracting significant foreign direct investment (FDI) from multinational companies.

3. Tax Competition in the OECD

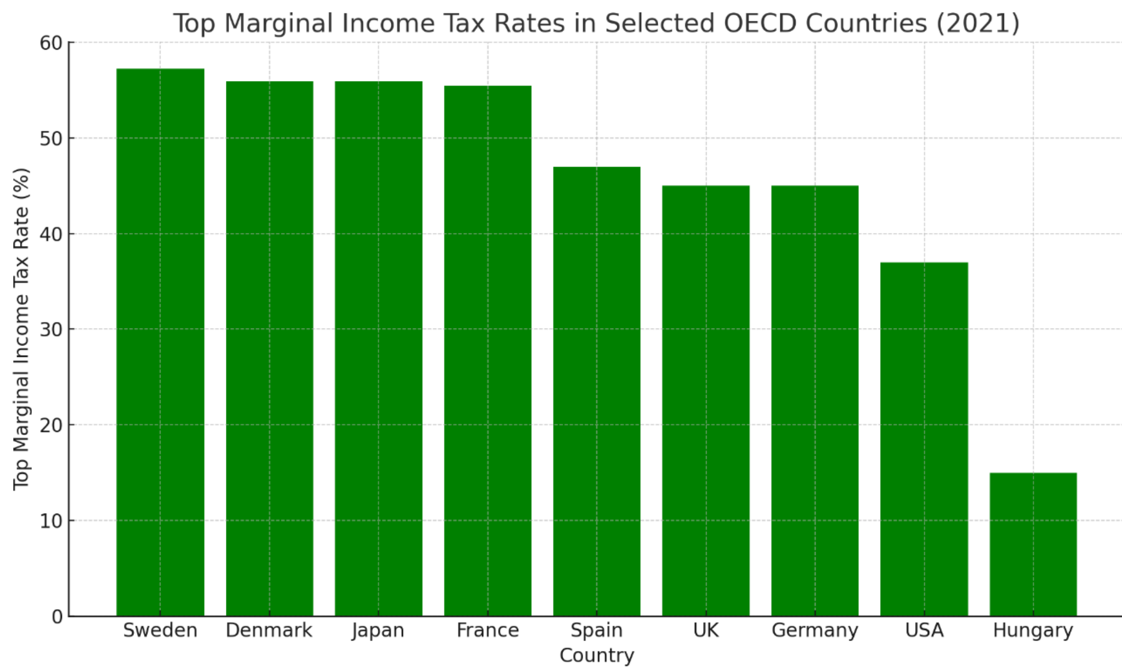
   - The trend of lower corporate tax rates has led to significant tax competition among OECD countries, particularly in Europe. Countries such as Ireland, Luxembourg, and Hungary have become popular for companies looking to reduce their tax burden, prompting other countries to follow suit with their own rate reductions.
   - This "race to the bottom" has been both praised for increasing competitiveness and criticized for undermining governments' ability to raise revenue.

2. Personal Income Tax Rates in Selected OECD Countries (2021)

The following table provides the top marginal income tax rates for individuals in selected OECD countries. These rates show the highest percentage of income that the government takes from the highest earners.

Country	Top Marginal Rate (%)
Sweden	57.2
Denmark	55.9
Japan	55.9
France	55.4
Spain	47*
United Kingdom	45
Germany	45
United States	37
Hungary	15 (flat tax)

Top Marginal Income Tax Rates in Selected OECD Countries (2021)



5. Italy's Flat Tax System

In recent years, Italy has adopted elements of a flat tax system as part of broader efforts to reform its tax structure and attract foreign investment. The flat tax in Italy has two main components: a flat tax for new high-net-worth residents and a flat tax for small businesses and self-employed individuals.

Key Features of Italy's Flat Tax

1. **Flat Tax for High-Net-Worth Individuals:**
    - Introduced in 2017, this flat tax targets wealthy foreign individuals who choose to relocate to Italy.
    - The €100,000 annual flat tax applies to all foreign-sourced income, regardless of the amount. This rate is designed to attract high-net-worth individuals, including retirees, entrepreneurs, and investors, by offering tax certainty and simplicity.
    - This scheme also allows the individual's family members to benefit, with each additional family member taxed at a flat rate of €25,000 per year.

2. **Flat Tax for Self-Employed and Small Businesses:**
    - In 2019, Italy introduced a flat tax of 15% for self-employed workers and small businesses with annual revenues below €65,000.
    - This initiative was designed to reduce tax complexity for smaller enterprises and encourage entrepreneurial activity. The flat tax significantly simplifies the filing process for small businesses, eliminating many deductions and complex reporting requirements.
    - For businesses with revenues between €65,000 and €100,000, the tax rate increases to 20%, but the flat tax system remains in place, allowing these businesses to maintain simpler tax compliance.

Table: Italy's Flat Tax Breakdown

Category	Tax Rate	Criteria
High-Net-Worth Individuals (foreign income)	€100,000/year	Foreign-sourced income
Self-Employed / Small Businesses	15%	Revenues below €65,000/year
Medium-Sized Businesses	20%	Revenues between €65,000 - €100,000
Additional Family Members	€25,000/year	Applies to family members of HNWIs

3. Flat Tax for Pensioners Moving to Southern Italy

- Launched in 2019 to revitalize underpopulated regions.
- Key Features:
  - 7% flat tax on all foreign income, including pensions.
  - Applicable for up to 9 years.
- Eligibility:
  - Retirees moving to municipalities with fewer than 20,000 inhabitants in southern regions.
- Impact:
  - Attracted foreign retirees.
  - Stimulated local economies in designated areas.

6. Spain's Recent Tax Policies

Spain's approach to taxation has traditionally been more conventional, maintaining a progressive tax system while also attempting to balance competitiveness and social equity.

Over the years, Spain has implemented various tax reforms, including moderate reductions in personal and corporate taxes, particularly during the Zapatero administration **("Bajar impuestos es de Izquierdas**": lower taxes is being leftie). However, Spain has faced ongoing challenges, including tax revenue shortfalls, tax evasion, and the need to fund significant public spending, particularly in pensions and healthcare.

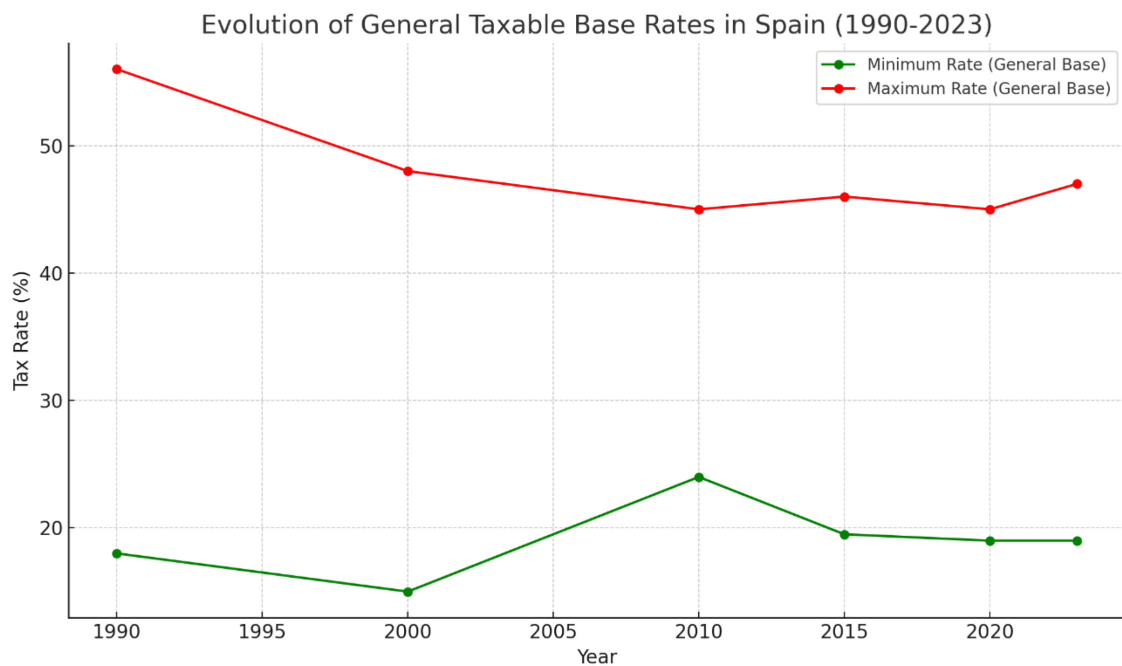
Table: Historical Tax Rates on General Taxable Base in Spain (1990-2023)

Year	Minimum Rate (General)	Maximum Rate (General)	Top Marginal Income Bracket (€)
1990	18%	56%	65,000
2000	15%	48%	60,101
2010	24%	45%	53,407
2015	19.5%	46%	60,000
2020	19%	45%	60,000
2023	19%	47%	300,000+

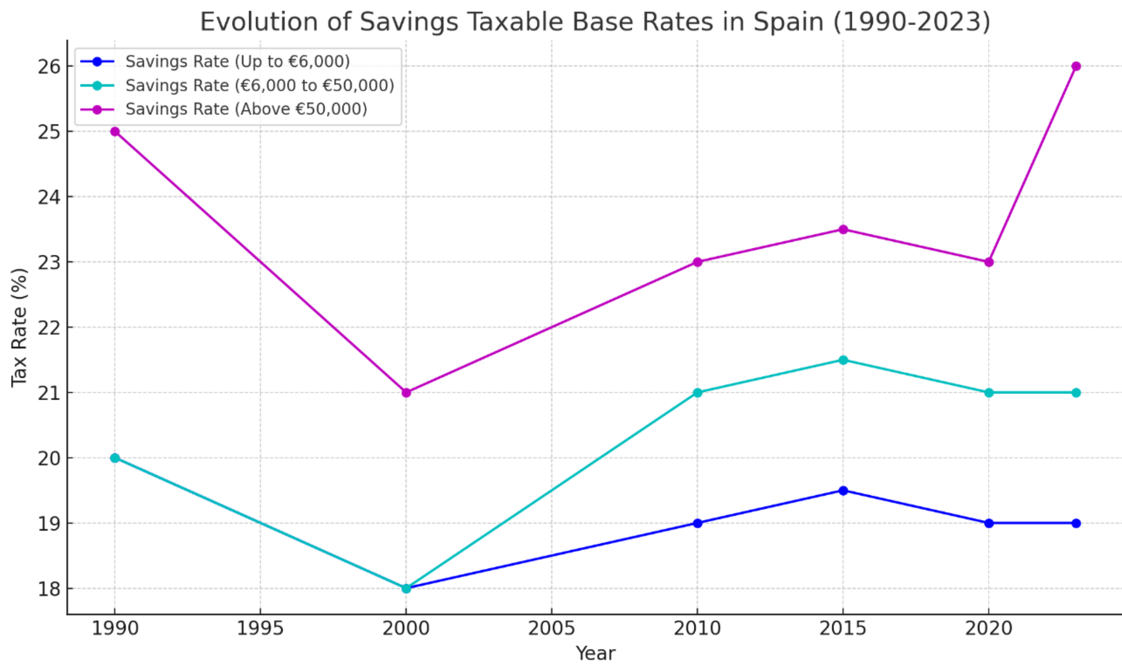
Table: Historical Tax Rates on Savings Taxable Base in Spain (1990-2023)

Year	Savings Rate (Up to €6,000)	Savings Rate (From €6,000 to €50,000)	Savings Rate (Above €50,000)
1990	20%	20%	25%
2000	18%	18%	21%
2010	19%	21%	23%
2015	19.5%	21.5%	23.5%
2020	19%	21%	23%
2023	19%	21%	26%

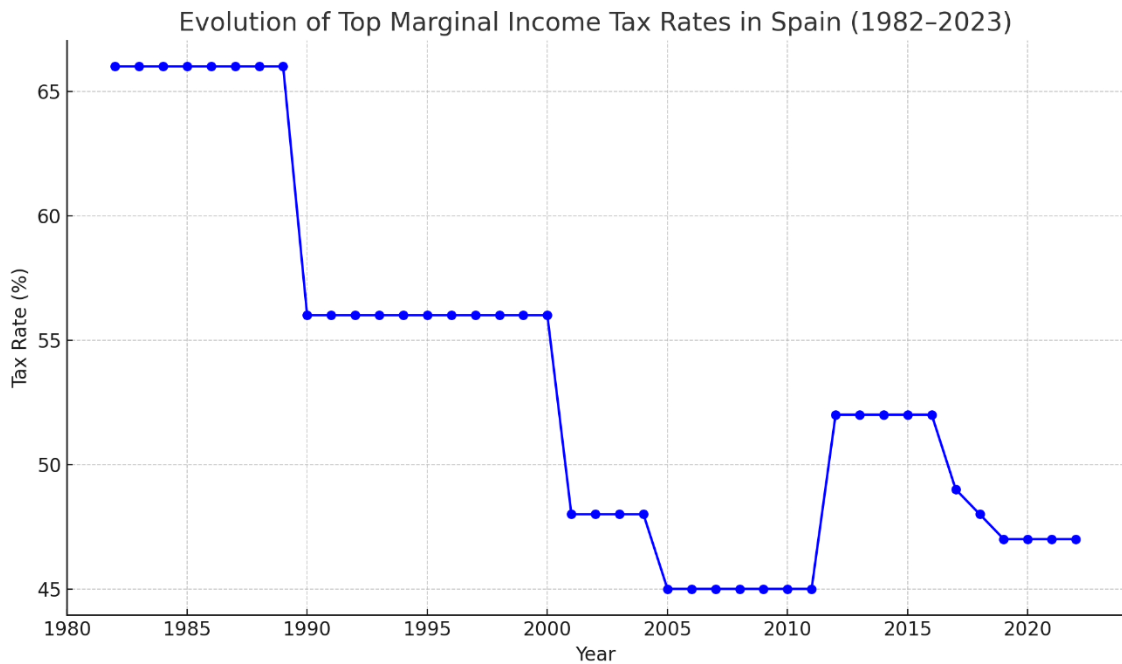
Evolution of General Taxable Base Rates in Spain (1990-2023)



Evolution of Capital Taxable Base Rates in Spain (1990-2023)



Evolution of Top Marginal Income Tax Rates in Spain (1982–2023)

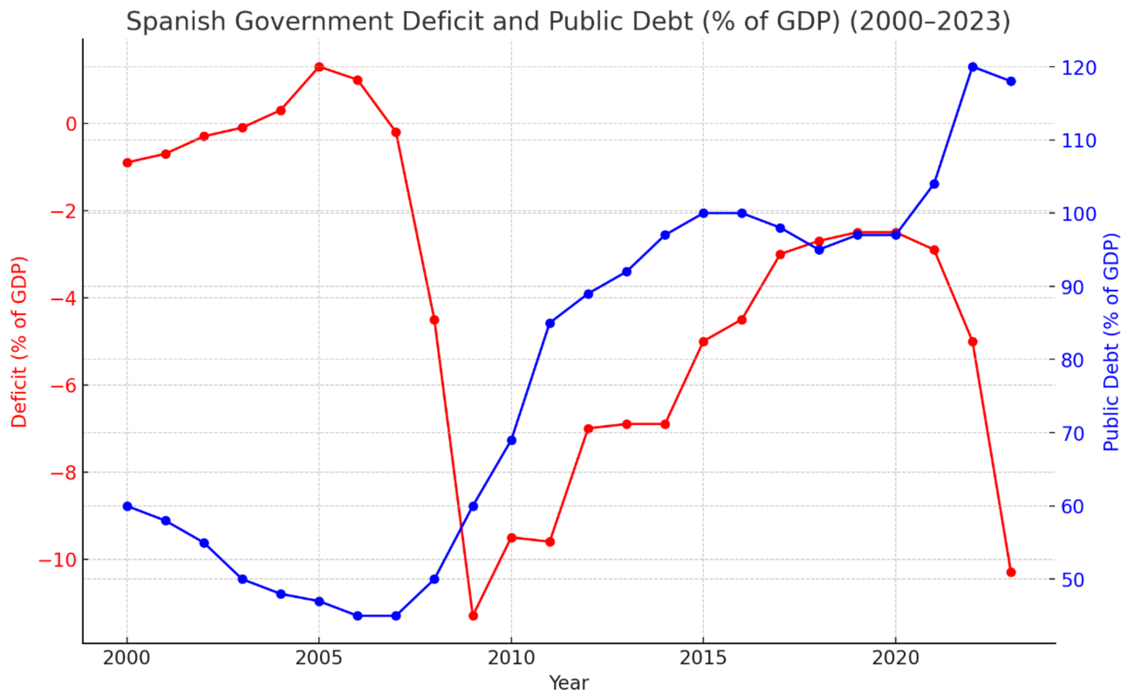


Here is the chart showing the evolution of top marginal income tax rates in Spain from 1982 to 2023. It reflects the significant tax cuts under Aznar, increases during Rajoy's austerity measures, and recent adjustments under Pedro Sánchez.

Evolution of Corporate Tax Rates in Spain (1982–2023)

Here is the chart showing the evolution of corporate tax rates in Spain from 1982 to 2023. The corporate tax rate decreased significantly during the Aznar era and remained relatively stable afterward, with a slight reduction during recent years to 25%.

Spanish Government Deficit and Public Debt (% of GDP) (2000–2023)



Here is the chart showing Spain's government deficit and public debt as a percentage of GDP from 2000 to 2023. It highlights the sharp increase in both deficit and debt following the 2008 financial crisis and again during the COVID-19 pandemic. The chart also illustrates Spain's struggle to reduce its deficit during the years of austerity under Mariano Rajoy and its ongoing challenges with public debt.

Recent Modifications (2018–Present): Balancing Taxation with Social Priorities

Spain's more recent tax policy, particularly under Prime Minister Pedro Sánchez (since 2018), has focused on raising taxes on the wealthy to address inequality, while also attempting to balance fiscal responsibility.

- Tax on High Incomes: The Sánchez government has raised the top marginal tax rate back up to 47%, particularly targeting high-income earners and large corporations. The corporate tax rate remains at 25%, with reduced rates for small businesses. /23%). First two profitable years 15%.

- Wealth and Digital Taxes: Spain has also introduced taxes on wealth and digital services to adapt to a more modern economy. In 2021, a digital services tax (often referred to as the "Google tax") was introduced, targeting large tech companies operating in Spain. Tax on “High Patrimonies” (Impuesto a la riqueza): Wealth tax for net assets up to 3 Mio euro.

- Green Taxes: In line with European Union environmental goals, Spain has introduced new green taxes aimed at reducing carbon emissions and promoting sustainability. (Impuesto sobre el Plastico, etc)

- Fiscal Outcome: The COVID-19 pandemic has caused a significant drop in tax revenue and increased government spending, pushing Spain’s budget deficit back up to over 10% of GDP in 2020. Recovery plans funded by the European Union’s recovery fund have provided some fiscal breathing room, but long-term challenges remain.

Estimation Objective Taxation Regime (Módulos) in Spain – Flat Tax

The Estimation Objective Regime, also known as the "Módulos" system, is a simplified taxation model for self-employed individuals and small businesses in Spain. This regime calculates tax liability based on specific objective factors, rather than actual profits or revenues. It applies to sectors where business activity can be standardized and quantified through measurable elements.

Key Features

- Tax Calculation: Determined by fixed parameters (such as number of employees, area of premises, or energy consumption), not based on actual income or expenses.
- Target Audience: Mostly small businesses or self-employed individuals in certain sectors.
- Simplified Reporting: Reduced administrative burden compared to the general tax regime.
- Eligibility: Only applicable to specific sectors and businesses below certain revenue thresholds.

1. Who Can Use the Módulos Regime?

Criteria	**Details**
Type of Businesses	Self-employed (freelancers) in agriculture, transport, retail, etc.
Annual Revenue Cap	€250,000 for most activities (lower in some sectors)
Business Activity	Limited to sectors defined by the government, such as transport, small retail, hospitality, etc.
Number of Employees	Maximum 5 employees (depends on sector)

2. Tax Parameters in the Módulos Regime

Parameter	**Example**
Square Meters	Premises area in businesses like retail or hospitality
Number of Vehicles	Transport businesses calculate tax based on fleet size
Employees	For certain businesses, the number of employees impacts taxation
Energy Consumption	Manufacturing or agriculture activities use energy as a parameter

3. Key Tax Components

Component	Details
Personal Income Tax (IRPF)	Calculated based on modules, not real income
Value Added Tax (VAT)	VAT is also calculated on predefined modules, simplifying reporting
Social Security Contributions	Self-employed contribute based on income bracket, separate from Módulos calculations

4. Advantages and Disadvantages

Advantages	Disadvantages
Simplified Reporting	Not suitable for businesses with fluctuating income
Predictable Tax Payments	Non-eligibility for businesses exceeding thresholds
Lower Administrative Burden	No flexibility in calculating based on real income

5. Sectors that Commonly Use Módulos

Sector	Common Business Types
Retail	Small stores, kiosks
Hospitality	Bars, restaurants
Transportation	Small freight carriers, taxi drivers
Agriculture	Farmers, small-scale agricultural producers

6. Recent Developments & Reform Trends in Modulos Regime

The government has been considering reforms to the Módulos regime, aiming to:

- Adjust thresholds and eligible sectors.
- Encourage transition to the direct estimation regime (based on actual income).
- Ensure that businesses not exceeding the new limits continue to benefit from simplified taxation.

7. Conclusion

The Módulos regime offers a practical solution for small businesses in Spain to reduce administrative work and predict tax liabilities. However, it is not suitable for every business, particularly those with fluctuating revenues. Understanding the eligibility criteria and the tax parameters is essential for effectively navigating this regime.
Conclude many times to Inequality against Income from Salaries and Professional Activities.

7. The Beckham Law – Special Tax Regime for Inbound new workers/entepreneurs

The "Ley Beckham", or Beckham Law, is a special tax regime introduced in Spain in 2005, primarily aimed at attracting skilled foreign workers and professionals. The law was named after footballer David Beckham, who benefited from this regime when he moved to play for Real Madrid. Under this regime, foreign workers, entempreneurs, shareholders of new companies, relocating to Spain could opt to be taxed as non-residents, allowing them to pay a flat tax rate on their income instead of progressive rates.

Key Features of the Beckham Law:

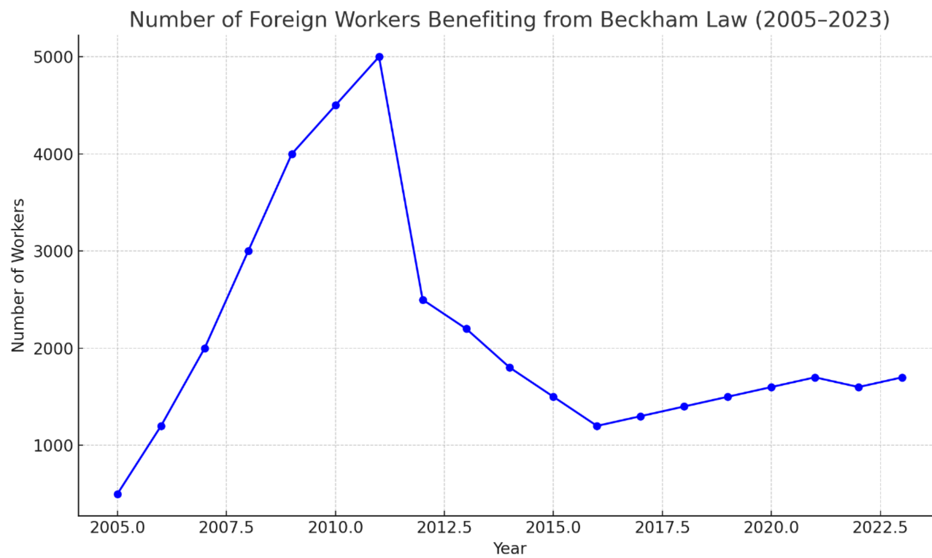
- Flat Tax Rate: The special tax regime originally allowed qualifying foreign workers to be taxed at a 24% flat rateon their Spanish income (up to €600,000). Any income above that threshold was taxed at 45% (the regular progressive rate at that time).
- Duration: The regime initially lasted for 6 years, allowing new residents to benefit from the lower tax rate during their stay in Spain.
- Non-Spanish Income Exempt: One of the significant advantages of the regime was that it allowed foreign residents to exclude income earned outside of Spain from Spanish taxation.

Reform in 2010:

In 2010, due to criticisms about the law favoring wealthy foreign workers, especially high-profile athletes, the Spanish government reformed the Beckham Law:

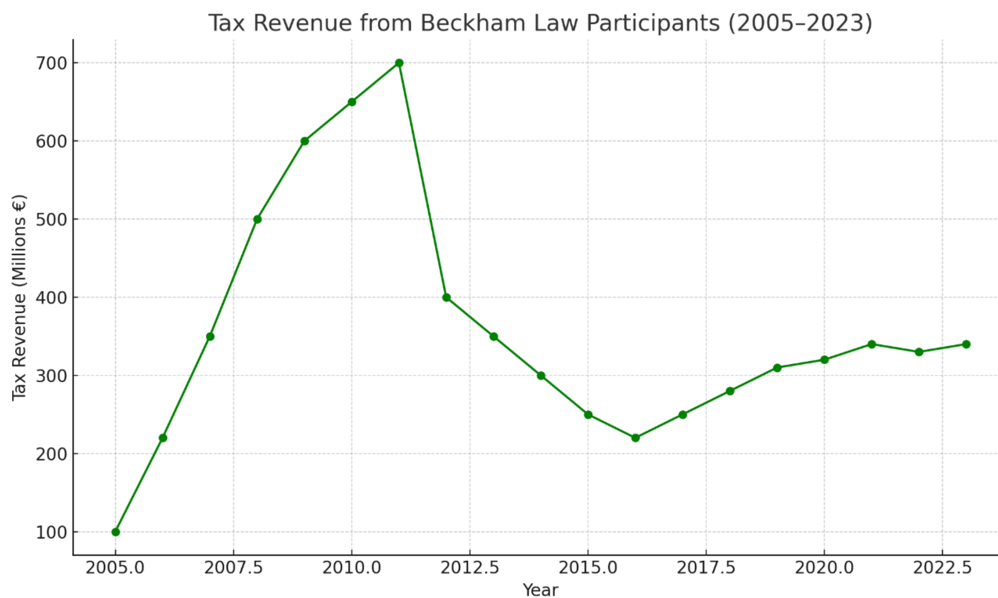
- Limit on Eligibility: Professional athletes were excluded from the regime, which meant they could no longer benefit from the special tax rate.
- Income Threshold: The regime applied to those earning under €600,000 annually, with those earning above that subject to Spain's regular progressive rates.

Number of Foreign Workers Benefiting from Beckham Law (2005–2023)



Here is the chart showing the number of foreign workers who benefited from the Beckham Law from 2005 to 2023. The chart illustrates a significant increase in the number of workers opting for the special tax regime after its introduction in 2005, followed by a decline after the 2010 reform, which excluded athletes and set income limits.

Tax Revenue from Beckham Law Participants (2005–2023)



8. Critical conclusion for Flat Rate Policies. Trends and Future Directions for Tax Policies: Flat Tax vs. Progressive Taxation

In the global context, we observe two dominant trends:

1. Flat Taxes: Countries like Estonia, Russia, and Hungary have embraced flat tax systems, offering simplicity and a more predictable tax burden for individuals and businesses. The flat tax model is particularly appealing to countries seeking to reduce tax evasion and simplify compliance.
2. Progressive Taxation: In contrast, many OECD countries, such as Germany, France, and the Nordic nations, maintain highly progressive tax systems. These systems aim to balance income inequality by imposing higher taxes on top earners while maintaining strong social safety nets.

Conclusion: Will More Countries Adopt Flat Taxes?

The flat tax model is gaining popularity among countries looking to simplify their tax codes and boost compliance. However, the long-term sustainability of flat taxes remains debated, particularly in countries with significant public spending needs. Countries with progressive taxation are likely to maintain their systems to address wealth inequality, but we may see more hybrid models combining elements of flat taxes with traditional progressive structures

As countries continue to compete for investment in a globalized economy, the trend toward lower corporate tax rates and simplified tax systems, like flat taxes, is likely to persist. However, these policies are not without controversy, and there are several factors to consider as governments balance the need for revenue with the desire to attract business.

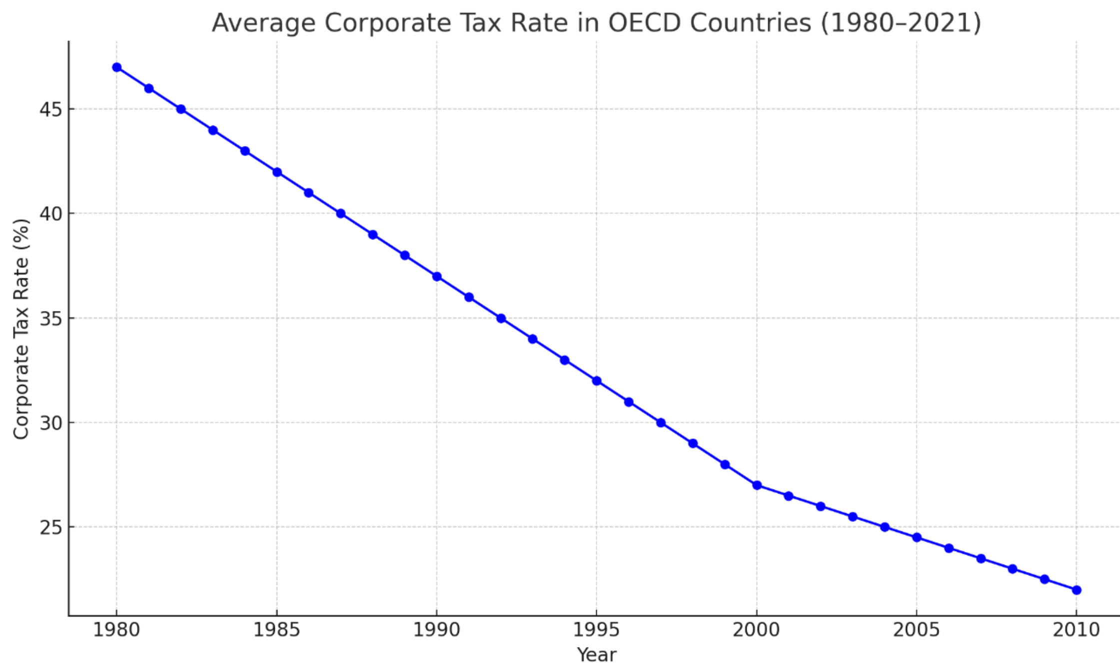
Key Trends in Taxation:

1. Global Tax Competition: The pressure on countries to lower their corporate tax rates is unlikely to abate, particularly as digitalization makes it easier for companies to shift profits across borders.
2. Adoption of Flat Taxes: Countries like Estonia, Hungary, and Russia have adopted flat tax systems, and others may follow suit as they look for ways to simplify their tax codes and attract investment.

3. International Coordination: The rise of tax avoidance schemes has led to increased international cooperation, with organizations like the OECD and EU pushing for more coordinated tax policies, including the global minimum tax.

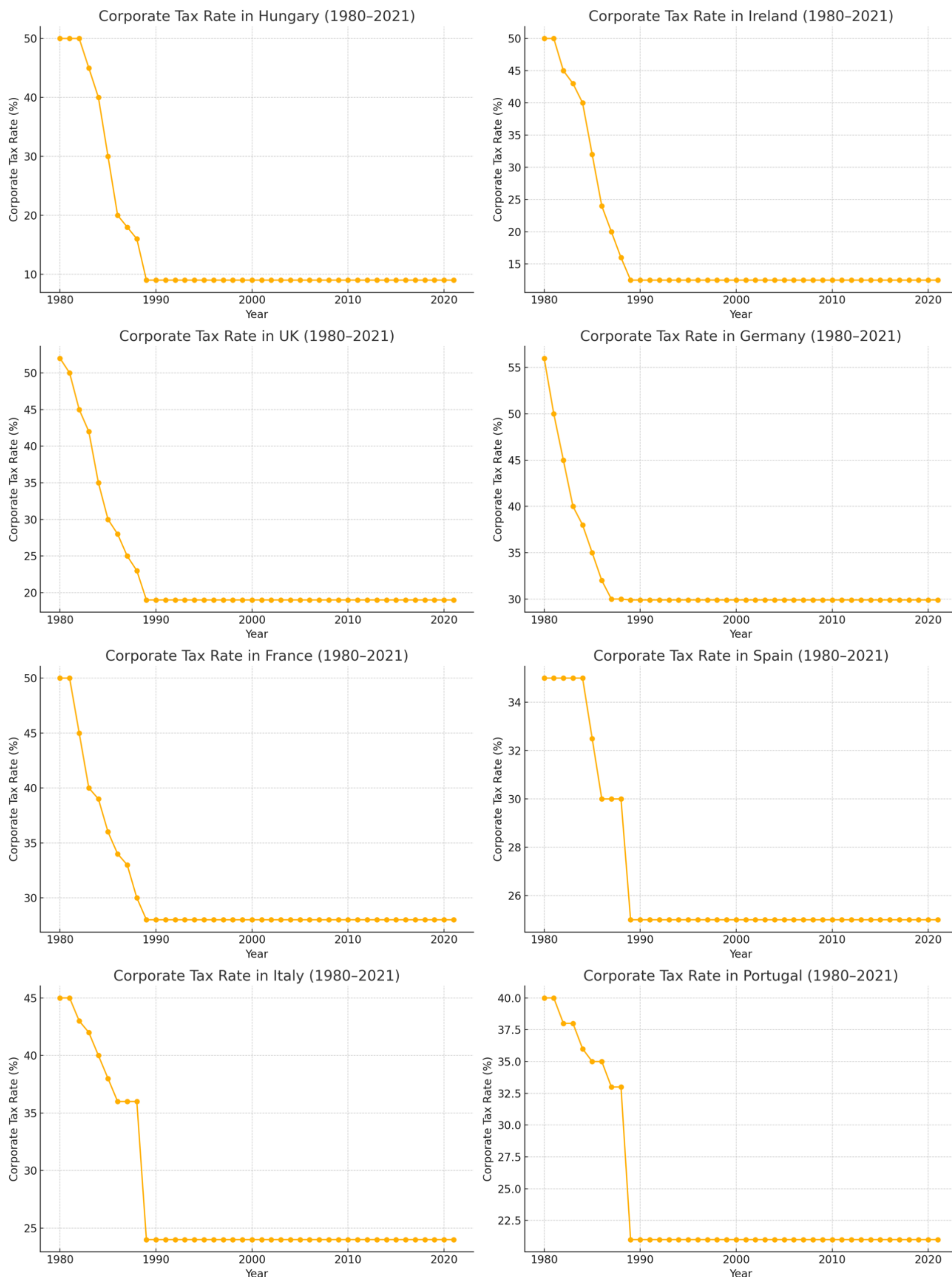
Final Charts

Average Corporate Tax Rate in OECD Countries (1980–2021)



Here is the chart showing the Average Corporate Tax Rate in OECD Countries (1980–2021). The chart highlights the steady decline in corporate tax rates across OECD countries, dropping from approximately 47% in 1980 to 22% in 2021. This reflects the ongoing trend toward lower corporate taxes to attract business investment.

Corporate Tax Rate in Serveral Countries (1980–2021)



Here is a series of charts showing the Corporate Tax Rate Evolution from 1980 to 2021 for selected OECD countries: Hungary, Ireland, UK, Germany, France, Spain, Italy, and Portugal. These charts illustrate the trend of declining corporate tax rates in these countries, reflecting global tax competition and efforts to attract investment.