Do taxpayers really want a simple tax system? Evidence on preferences towards income tax simplification

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Abstract
There seemingly is a consensus in the academic literature and the public debate that modern tax systems are too complex and should be simplified. However, one can also derive economic arguments in favor of a certain degree of tax complexity and it is puzzling why tax systems seem to get even more complex over time despite the seemingly consensus for more simplification. In this paper, we present the results from a detailed survey with a representative sample of the German population which sheds light on preferences for tax simplification. We find that generally people are in favor of a more simpler tax system. If we make survey respondents aware of the potential benefits of tax complexity, the preferences for simplicity are reduced. For example, a large share respondents think that taxpayers who have to bear the costs of commuting to work or taking care of elderly family members should pay less in taxes than comparable taxpayers who do not have to bear these costs. That is, participants implicitly favor to add complexity to the tax system by allowing to deduct these costs from the tax base. The survey also includes two randomized experiments in which we present different arguments in favor and against simplification. The experimental results also show that the support for tax simplification is elastic to information in favor of tax complexity.

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1 Introduction

Should tax systems be more simple? The seemingly correct answer to this question is: yes. For example, recent literature shows that the self-employed value tax simplicity and leave money on the table because of complex tax schedules (Aghion et al. 2017), that taxpayers underreact to complex tax incentives (Abeler and Jaeger 2014), that the existence of complexity-adding tax expenditures facilitates tax evasion (Paetzold and Winner 2016), and that tax simplicity increases the take up of tax refunds by firms (Zwick 2018). The debate among policy makers and the general public also appears to be clear in this regard: there seems to be a consensus that simplifying tax systems is generally desirable; for example through lower rates and broader bases.

However, there are also arguments in favor of a certain degree of tax complexity. For example, a fairly complex tax system with a certain amount of expenditures i) makes it possible to tailor taxes to individual situations and to use ‘tagging’ components, ii) allows to tax highly elastic goods at effectively lower rates, and iii) enables to include Pigouivian elements into the tax system (Hines 2017). These elements of a complex tax system can contribute to making the tax system efficient. Complex components of the tax system potentially also have redistributive purposes – think for example of deducting the costs of elderly care of family members – and might therefore be viewed as equity enhancing and fair. There also is a political economy component to the debate, namely that special interest groups and lobbyists can use deductions and expenditures to achieve beneficial tax treatment of the groups they represent. The general support of simple tax systems might miss out some of these arguments about efficiency, redistribution and political economy.

In addition, the data show that there is an upward sloping trend in growth of tax expenditures in the US – see Figure 1 – and other countries. It is thus a puzzle why most tax systems remain so complex although the majority of voters seems to be in favor of substantial tax simplification. One potential explanation is that, while most people generally support simple tax systems, they wish to keep those complexity components of the system from which they benefit.

In this paper, we study preferences for tax simplicity among the general population. We included a wide set of questions in the context of tax simplification into the German Internet Panel, a representative survey of the German population (N =2464). Our question block surveys attitudes towards tax simplicity and includes two randomized components which allow us to test if the support for tax simplicity depends on information about the consequences and pros/cons of tax complexity. To the best of our knowledge, we set up the first detailed survey of tax-simplicity preferences.

The concept of tax complexity is complex in itself, and for the purpose of the survey we decided to focus on a special dimension of tax complexity: the amount of tax expen-
ditures and deductions. While there are clearly more dimensions of tax complexity (e.g., documentation requirements, etc.), expenditures and deductions are a main component of tax complexity and a major subject in the debate about complexity. Moving to a system without any expenditures and deductions would clearly make any existing tax system more simple, easier and more comprehensible. We further focus on the case of personal income tax systems which seems to us to be the natural choice for a survey on tax questions among the general public.

Germany is a sensible choice to run a survey about tax-simplicity preferences. The public debate about the topic keeps popping up at regular intervals. One prominent example of this debate is the proposal of representatives of the conservative party to simplify the tax system in a way that makes it possible to file the income-tax return on a sheet of paper that is not larger than a usual German beer coaster. Studying complexity through its dimension of expenditures and deductions is also sensible in the case of Germany; the country presumably has more than 500 deduction possibilities (Kirchhof 2011).

Our survey reveals the following main results. First, more than 90% of the participants indeed think that the tax system should be simplified. We survey this question a scale from 1 to 6 where 6 means strong support for tax simplicity and find an average of 5.2 (see Figure 2). In line with this general support for a simpler tax system, 50% of the participants perceive the filing of a tax return to be considerably difficult (see Figure 3).

Second, we then dig deeper into preferences for tax simplicity and study if this large support holds as we ask for the desired tax treatment in particular contexts. We have a series of questions in which we present participants with the living situations of two fictitious taxpayers, and then survey if these two taxpayers should pay the same amount of taxes or if any of the two should pay less than the other person. We designed the questions in a way where the two fictitious persons are similar in all tax-relevant means except for one particular circumstance in their living situation. In particular, the two fictitious taxpayers were different with respect to i) the distance between their home and work place, ii) the amount of charitable giving, iii) the requirement to spend money on the elderly care of a family member. The results show that in all three cases (i to iii) a large fraction of respondents indicate that the two persons should not pay the same amount of taxes. Specifically, i) almost 40% of the respondents believe that commuting to work should reduce the tax burden, ii) more than 30% of the participants think that charitable donations should result in a lower tax burden, and iii) roughly 60% of the respondents indicate that the costs for elderly care should be deductible and reduce the tax burden (see Figures 4, 5 and 6). Of course, these differential treatments of two otherwise identical taxpayers can only be achieved through expenditures and deductions, and thus through a substantial degree of tax complexity. We are able to show that the
answers to these questions are not driven by self interest; the results are qualitatively the same if we condition on not benefiting of the respective tax expenditure (see Figures 7 and 8). These results are thus evidence that the preferences for tax simplicity become weaker as people are made aware of the possibility to treat different taxpayers differently through a certain layer of complexity.

Third, we implement two randomized survey experiments to study the causal link between information about the implications of tax simplification and preferences for tax simplicity. To maximize power, we have one experimental intervention at the beginning of the survey, and one experimental intervention towards the end (with separate randomization for the two experimental components).

The first experiment includes three randomly assigned groups. A control group where we make a neutral statement about the fact that there is an ongoing debate about whether the tax system is too complex because of various deduction possibilities and allowances. The second group is confronted with a statement highlighting that tax deductions can be used to reduce the tax burden for taxpayers which are disadvantaged by circumstances. This hence is a potential argument against tax simplification. We label this group the *Redistribution* group. A third experimental group is presented an argument in favor of tax simplification, namely that a complex system with many deductions offers possibilities to avoid taxation and manipulate taxable income, e.g., through claiming unjustified deductions or simply due to better knowledge of the tax code. We label this group the *Avoidance* group.

The *Redistribution treatment* significantly reduced the general support of tax simplification relative to the control group. This is additional evidence that preferences for tax simplicity are elastic to information about the implications of tax simplicity. The *Avoidance* treatment did not have any significant effects. This is probably not surprising because support for simplification is already very high in the control group and there is not much room to further increase this support (see Table 1). The *Avoidance* treatment, however, affected how people think about the beneficiaries of tax complexity; the treatment increased agreement with the statement that deductions and tax exceptions work in favor of the rich (see Table 2).

The second experiment also included three groups (with a new randomization, so that there is no correlation between treatment-group status in the two experiments). We again have a control group with no particular information. We then have a group in which we highlight that a system with deductions and exemptions ‘provides opportunities to tax someone according to his personal abilities and is thus more efficient in economic terms’. We label this group the *Efficiency* group. We then have a treatment where we make participants in this group aware that deductions and expenditures are potentially used by lobby and special interest groups to bargain tax exemptions for their clients. We
label this group the *Special Interest Group* group.

The results of our second experiment show that the *Efficiency* argument considerably lowered the support for tax simplification, relative to the control group. This suggests that participants are not aware of the potential efficiency implications of tax complexity when they exhibit their strong preference for tax simplification. The *Special Interest Group* treatment did not have an effect, relative to the control group (see Table 3).

Fourth, we aimed at eliciting which type of revenue-neutral tax reforms people would prefer. This exercise shows that about 35% of favor a tax schedule that is more progressive but comes with less deductions (see Figure 9). The policy choices were not affected by our experimental treatments.

## 2 The Survey

**German Internet Panel** We collected survey data through the German Internet Panel (GIP). The GIP is a longitudinal survey that is operated and administered at the University of Mannheim in Germany. The main purpose of the panel survey is to collect "data on individual attitudes and preferences relevant in political and economic decision making processes". GIP data are collected online on a bi-monthly basis. The survey is representative for the German population aged 16 to 75. (These information about the survey are taken from Doerrenberg and Peichl (2018)).

The survey includes repeated questions (included in every wave) as well as questions only included in single waves. We included a block of questions about tax simplicity in wave 36. This wave went to the field in July 2018 and included 2464 participants.

**Randomized Survey Experiments** In the following, we show how we framed the information that we randomly varied across experimental groups.

**Experiment 1:**

- Introduction text for all groups

  In Germany there is an ongoing debate on whether the income tax system is too
complicated because of the many deduction possibilities and allowances.

- Redistribution treatment
  
  However, some argue that a tax system with many deduction possibilities and allowances has a social and redistributive effect. For example, tax deductions can be used to reduce the tax burden on tax payers which are disadvantaged by circumstances.

- Avoidance treatment
  
  Some argue that a tax system with many deductions and allowances gives more scope to avoid taxation and manipulate income. For example, tax deductions can be used to reduce one’s own tax burden due to better knowledge of the tax code or due to the claiming of unjustified deductions.

- Control group
  
  No further information other than Introduction text

Experiment 2:

- Introduction text
  
  We would like to mention again the ongoing debate on whether the income tax system is too complicated because of the many deductions and allowances.

- Efficiency treatment
  
  One argument against tax simplification that has not been brought forward so far is that a tax system with many tax deductions and allowances provides better opportunities to tax someone according to his personal abilities and is thus more efficient in economic terms.

- Special interest group treatment
  
  One argument in favor of tax simplification that has not been brought forward so far is that a tax system with many tax deductions and allowances gives special interest groups more possibilities to bargain exemptions for their clients.

- Control group
  
  No further information other than Intro text

3 Figures and Tables
U.S. Tax Expenditure Growth

Source: James Hines

Figure 2: Preferences for Tax Simplification.

Source: Own calculations based on German Internet Panel
Table 1: Should the tax system be simplified?

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<td>-0.123**</td>
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<td>-0.130**</td>
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<td><strong>Constant</strong></td>
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Demographics No Yes Yes Yes Yes
Tax difficulty No No Yes Yes Yes
Household Income No No No Yes Yes
Political Preference No No No No Yes

Scale of 1 (absolutely not) to 6 (absolutely). Robust standard errors in parentheses *** p<0.01, ** p<0.05, * p<0.1.
Table 2: Do deductions work in favor of the rich?

<table>
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Experimental Group Reference category: Control

Demographics No Yes Yes Yes Yes
Tax difficulty No No Yes Yes Yes
Household Income No No No Yes Yes
Political Preference No No No No Yes

Scale from 1 (add to a fair income distribution) to 6 (higher incomes benefit). Robust standard errors in parentheses *** p<0.01, ** p<0.05, * p<0.1.
Table 3: Should the tax system be simplified?

<table>
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<td>(0.176)</td>
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N 2187 2134 2114 1969 1969

Demographics No Yes Yes Yes Yes
Tax difficulty No No Yes Yes Yes
Household Income No No No Yes Yes
Political Preference No No No No Yes

Scale of 1 (absolutely not) to 6 (absolutely). Robust standard errors in parentheses *** p<0.01, ** p<0.05, * p<0.1.
Figure 3: Is filing a tax return difficult?

Source: Own calculations based on German Internet Panel
Person A has a considerable travel distance to work. Person B lives very close to work. Both Person A and B have the same gross income and are very similar by all other means. Source: Own calculations based on German Internet Panel
Figure 5: Who should pay more taxes? Donations

Person A spends a considerable amount of her income for charitable giving. Person B does no such thing. Both Person A and B have the same gross income and are very similar by all other means.

Source: Own calculations based on German Internet Panel
In contrast to Person B, Person A has a poor mother in need for elderly care and has to spend a considerable amount of her income for the care of her mother. Person A and B have the same gross income and are very similar by all other means. Source: Own calculations based on German Internet Panel
By people claiming the deduction. In contrast to Person B, Person A has a poor mother in need for elderly care and has to spend a considerable amount of her income for the care of her mother. Person A and B have the same gross income and are very similar by all other means. Source: Own calculations based on German Internet Panel.
By people claiming the deduction. *In contrast to Person B, Person A has a poor mother in need for elderly care and has to spend a considerable amount of her income for the care of her mother. Person A and B have the same gross income and are very similar by all other means.* Source: Own calculations based on German Internet Panel
Figure 9: Which revenue-constant reform?

Answer categories: Same rate for all no deductions; Same rate for all same deductions as in status quo; More progression no deductions; Prefilled income tax declaration; No change. Source: Own calculations based on German Internet Panel
References


Appendix

Additional Figures