FLAT TAX REFORM AND HOUSEHOLDS’ DISPOSABLE INCOME IN ITALY: A DYNAMIC SAM-BASED CGE MODEL

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The Italian Government is working over a fiscal policy reform to tackle the inequality and allow an increase in household disposable income to stimulate the level of final consumption and production. The reform proposed by the Italian Government concerns the replacement of the current progressive tax system with a flat one, introducing a flattened households’ income tax based on two tax rates.

The analysis proposed, respond to the exigency of providing an ex-ante quantification of how such a policy affects the economic system both in aggregate and disaggregate terms. In particular, the study develops a dynamic Computable General Equilibrium model based on the Italian Social Accounting Matrix where the all the flows related to the Households are broken down by income deciles. The data from Households’ income and wealth conducted by the Bank of Italy and Households’ consumption made by the ISTAT are matched using the propensity score matching technique. However, to break down the flows related to primary and secondary income distribution according to income deciles, the SHIW is integrated with the taxes database of the Ministry of Economy and Finance. The dynamic CGE model is calibrated on the SAM and the policy scenarios are designed in order to simulate the change in the income tax rates to replicate the Italian Government fiscal policy proposal. The policy outcome might be twofold: on the one hand, after the implementation of the policy, the so-called fiscal multipliers would find greater application. In other words, through an increase in disposable income, there should be an increase in consumption and thus, an increase in overall income, triggering, over time, a process of increasing State budget. On the other hand, the new taxation system could reduce the tax burden especially for higher incomes, thus affecting inequality, unless the allowances system is modified accordingly.

References
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