Reform of Business Taxation. Is Germany Moving Towards a Dual Income Tax System?

Germany's governing coalition has put forward a bill that would reduce tax rates and reform business taxation. This far-reaching reform bill is currently proceeding through the legislative process. Some elements of the reform have already been implemented within the framework of the Tax Relief Law 1999/2000/2001. From 2002 on, tax rates are to be cut rigorously and the structure of business taxation – the interaction between income tax, corporation tax and trading tax (*Gewerbesteuer* – a local tax on business) – is to be fundamentally reformed.

As far as the internal coherence of the tax system is concerned, the reform marks a radical change. Profits retained by incorporated companies will in future be taxed at just 25%, a far lower rate than that applying to distributed profits, as the latter are also subject to the income tax paid by shareholders. Unincorporated companies are to be given the option of paying tax on the same basis as incorporated companies, enabling them too to benefit from the tax cuts (option model); alternatively they are to be permitted to set off part of their trading tax payments against their income tax dues. Small shareholders will pay more tax than currently as the full imputation system of corporation tax (corporation tax paid can be set off against income tax dues) is to be replaced by the so-called 'half-income system' (income tax must be paid on half of distributed profits). The option model renders the taxation system significantly more complicated, and it is difficult to make out an economic argument in favour of the privileged treatment offered to retained profits. It must therefore be doubted whether the federal government's reform concept has a future. If the top rate of income tax is not to be reduced beyond the 45% currently under discussion, in the longer run there is likely to be pressure to tax dividends and interest earnings at the same low level as retained profits (flat-rate final withholding tax, dual income tax). It would make more sense to retain the present integration of corporation and income tax, to avoid an excessive differentiation of tax rates, and to fundamentally reform trading tax.

The government's aim in reforming business taxation is to improve incentives and thus the fiscal parameters for investment, growth and employment, to simplify the implementation of tax laws and make the tax system more just. An additional goal is to make German business taxation compatible with European requirements.

The bill envisages the following measures, to come into effect at the start of 2001

- Corporation tax is to be reduced to a uniform rate of 25%, applying to both retained and distributed profits.
- The current system of full imputation, whereby domestic corporation tax can be set off in full against the corporation or income tax paid by residents of Germany, is to be abolished. In order to avoid double tax burdens, only 50% of the profits distributed by incorporated companies to their shareholders are subject to income tax (half-income system); this is subject to the exemption with progression method (*Progressionsvorbehalt*),[1] however.
- In order to avoid double taxation within the business sector, dividend income of incorporated companies is not subject to tax (general exemption of dividends). This applies equally to dividends from home and abroad.
- Capital gains from the sale of shares that one incorporated company holds in another are exempt from tax.
- On the other hand, for those paying income tax the ceiling for taxable capital gains of shares in incorporated companies that are subject to tax is reduced to 1 per cent of equity capital owned by the shareholders. The aim is to prevent the retained profits of incorporated companies being realised without paying (income) tax when shareholders sell their shares.
- Unincorporated firms (sole proprietors and partnerships) – which represent around 85% of all firms in Germany – are to be allowed to choose whether to pay tax in the same way as an incorporated company ('option model'), or whether to set off their trading tax against their income tax dues up to a level equal to twice the calculation base for trading tax.[2]

In order to counter-finance these reforms the following measures are planned:

- The degressive depreciation rate for machinery and equipment is to be reduced from 30% to 20%.
- The linear depreciation rate for commercial buildings is to be reduced from 4% to 3%.

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[1] Under the 'exemption with progression method' the average tax rate, allowing for tax-free income (i.e. in this case including the tax-free half of the income from distributed profits), is determined and applied to taxable income.

[2] The trade tax calculation base amounts 5% of the tax base (profits plus half of interest payments, a basic allowance and lower rates are provided to small and medium-sized unincorporated firms) on which local government applies their own local rate (390% on average in 1998).

- Special depreciation allowances and savings-related depreciation allowances for small and medium-sized enterprises are to be abolished.
- The periods of time over which machinery and equipment depreciate are to be increased substantially.
- The rules on external financing by partners (under § 8a of corporation tax law) are to be tightened.

Uniform business taxation conducive to profit retention

With its concept for a uniform system of business taxation, the federal government has departed from the principle that the top rate of income tax should be as close as possible to the rate of corporation tax on retained profits. Corporation tax is to be cut to the low rate of 25% so as to make Germany more attractive as a production location, against the background of international tax competition. Yet ultimately it is only the profits retained within the firm that benefit from the lower tax rate. The tax burden on retained profits is final, applying irrespective of the way the profits are utilised. On those profits distributed to private, domestic shareholders, by contrast, income tax must also be paid under the half-income system.

In macroeconomic terms there is little justification for treating retained profits more favourably than distributed profits. It may prevent the allocative function of the capital market from working properly. For it is not only via 'self-financing', i.e. using retained profits, that firms invest and create jobs; firms also – and indeed primarily – finance investment using loan and equity capital. It may be that special programmes (such as equity capital support, the provision of venture capital) or specific tax subsidies (allowances such as savings depreciation) are called for where small firms lack finance for investment or in support of high-risk and innovative investment. However, it cannot be the task of the taxation system 'generally to strengthen the internal financing of firms so as to overcome the poor equity capital structure typical of the German economy and the resulting vulnerability of firms in times of crisis', as set out by the government in justifying its bill.

The fact that in future both the interest on loan capital and distributed profits will be subject to a significantly higher tax rate than retained profits means, all other things being equal, that more funds will be 'locked up' within firms. This does not necessarily mean that investment funds will be inefficiently deployed. After all, even now firms choose, in the light of expected yields, between investment in real capital, shareholdings and financial investment. Within the circle of incorporated companies (including those partnerships and one-person firms opting for the incorporated firm model) profit distribution is not disadvantaged in tax terms. Consequently, private investors will, in administering their portfolios, make greater use of investment funds and other financial intermediaries which then, as incorporated companies, invest these funds in a tax-neutral fashion on the capital market. This is likely to render the relationship between private investors and corporate management more indirect. It also means that greater attention will be paid to shareholder value in investment decisions. Yet as other countries – particularly the USA and Switzerland – show significant problems of taxation distorting financing and saving decisions do not result.

What does constitute a problem, however, is the fact that savings out of profit income are uniquely privileged. This contravenes the principle of equality of taxation and is also problematic in terms of its impact on income distribution. For private investors – unlike firms – do not benefit from the lower tax rates for investive uses of money when they save income derived from distributed profits, interest, earnings from self-employment or, and above all, from paid employment. Nor is there any guarantee that the favourable treatment accorded to retained profits will stimulate job creation in Germany, all the more so as depreciation allowances have been tightened.

Difficult implementation in unincorporated firms

The proposed uniform system of business taxation is likely to be rejected by many unincorporated companies because the option of being treated as an incorporated company is not attractive to all partners; the option requires the agreement of all partners. Moreover, firms must carefully weigh up the advantages against the possible disadvantages. Alongside the lower tax rates for retained profits, the most important positive element is the fact that salaries and pension provisions for owner-executives can be deducted from the profits on which tax is to be paid. On the other hand, those taking the option must expect a substantial increase in the paperwork involved in tax declarations. This is because treating such firms for tax purposes as quasi-incorporated companies requires a bookkeeping distinction between the firm as an independent economic entity and the personal sphere of the owner/partner.[3] In the case of special business assets, reserves may become apparent and subject to tax. The inheritance tax laws are also more restrictive in the case of incorporated companies, so that significantly higher inheritance taxes may become due.

All in all, the option model is unlikely to attract the majority of the one-person firms and small unincorporated companies. If they do not opt to be treated as incorporated companies, they do not benefit from the lower corporation tax on retained profits. On the other hand, their tax burden is reduced by the fact that they can set off part of their trading tax dues against income tax. Moreover, many people in this group do not pay the top rate of income tax, so that the effective additional tax burden compared with an incorporated company is likely to be relatively minor.

Although incorporated companies will also benefit from a simplification of their tax declarations, primarily because the credit of corporation against income tax will be dropped, a number of complicated transitional regulations must be observed. In the longer term capital investors will adopt new avoidance and arbitrage strategies: because profit distribution will become relatively unattractive, incorporated companies may buy back their shares; alternative ways of distributing profits will also be sought, for example by firms granting loans to their shareholders. Employees will have an incentive to redefine earned income – on which a higher rate of tax has to be paid – as retained profits, e.g. by way of profit participation schemes.

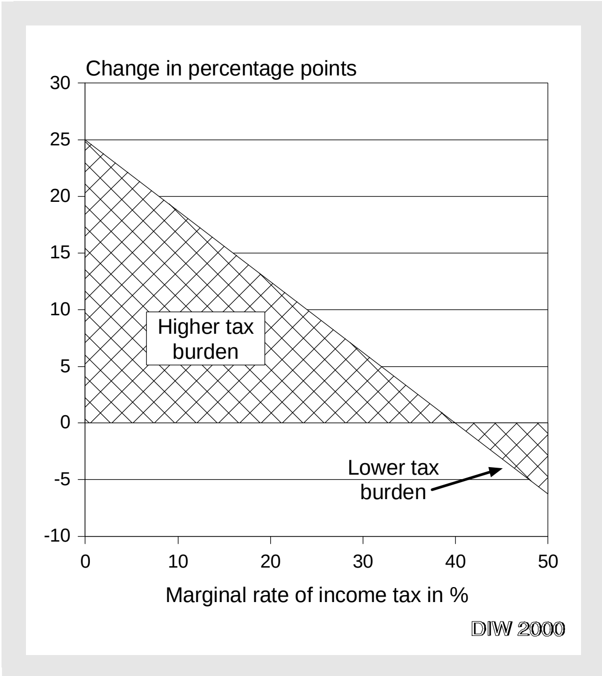
The ability to deduct trading tax from income tax dues, which is foreseen as a way of reducing the tax burden on the self-employed and unincorporated companies, is unconvincing in terms of the coherence of the overall taxation system, as the deduction is to apply only to a specific group of firms. It would have been better to embark on a fundamental reform of trading tax, widening the circle of those paying the tax, broadening the tax base, and reducing tax rates. However, no attempt is to be made to reform trading tax until towards the end of the government's term of office.

Small shareholders at a disadvantage

One of the drawbacks of the proposed reform is that the half-income system works to the disadvantage of small shareholders. Shareholders whose capital earnings remain below the tax-free allowance on income from savings – i.e. those who currently pay no income tax on

Figure 1

How Will Shareholders' Tax Burden[1] be Affected by the Reform of Business Taxation?



1 Change in the tax burden (income and corporation tax) on gross dividends resulting from the reform of business taxation for different marginal tax rates.
Source: DIW calculations.

such earnings and who are reimbursed for the corporation tax paid on the dividends – will in future have to pay at least the business tax of 25%. Yet even for those investors paying tax on their dividends, the tax burden will increase insofar as they pay income tax at a rate of less than 40%. For a person paying an individual rate of tax of 20%, for example, the tax burden on the gross dividend rises, compared with the current system, by 12.5 percentage points to 32.5% (cf. figure 1). Those taxpayers paying tax at a rate of 40% or higher, on the other hand, benefit from the half-income system.

Germany's tax system can be made 'Europe-compatible' in other ways

It cannot be disputed that a classical corporation tax system, together with the half-income system, is simpler, less subject to fraud, and more compatible with European rules than Germany's prevailing tax system. The question is whether these advantages are sufficient to offset the disadvantages compared with the current system based on complete deduction of corporation from income tax. One alternative would be to simplify the

[3] Self-employed persons or members of a partnership opting to pay corporation tax are effectively treated for tax purposes as if they held shares in an incorporated company. They are then in a position to conclude contracts, subject to tax, of employment, rental etc. of various forms. The tax authorities must examine whether these are appropriate or whether they constitute a hidden form of profit distribution. The private income is taxed, along with other private withdrawals under the private income tax rules, on the basis of the half-income system.

prevailing system; there is certainly no shortage of proposals to this end.

Germany's tax laws are currently at odds with European law because the tax authorities only permit domestic corporation tax to be deducted from income tax dues. This puts foreign shares at a disadvantage on the German capital market. It must be recognised, however, that other EU countries also use full or partial imputation in their tax systems. Ultimately this problem must be solved through international agreement. Within bilateral agreements on double taxation or a multilateral scheme applying throughout the EU it would be possible to provide for the general principle that foreign corporation tax can be deducted from income tax in the country of residence; it would also be conceivable to set up a clearing system to divide up tax revenue between the participating countries.

Significant tightening of depreciation allowances

In principle the degressive depreciation system is justified by the fact that many investment goods are subject to rapid technical or economic devaluation and the risks of tying up funds in real capital are greater than is the case with financial investment. Compared with other countries, the degressive depreciation rate in Germany at 30% is rather generous. Reducing it to 20%, as planned by the government in order to finance the reform of business taxation, on the other hand, would appear to be going too far. The advantage vis-à-vis a linear depreciation for investment goods with a short or medium useful life-span – which constitute the majority of investment goods purchased – would then be marginal. A degressive rate of 25% would seem more appropriate.

Also problematic is the generalised increase in depreciation periods for mobile investment goods. In principle the normal useful life of the goods within the firm should be used as the basis for setting the depreciation period, as required by current German tax law. For the vast majority of investment goods purchased by firms this is appropriate, because the investment goods can no longer be effectively used by others once they have been decommissioned, and the firm merely recoups their scrap value. Extending the depreciation period in the direction of a good's *technical* useful life would only seem to be acceptable in those cases where significant revenue can normally be derived from their subsequent sale once they are no longer used by the firm; this suggests the need for an effective market for the used good, such as that for used cars. This is the idea behind the recent judgement by the federal tax court. The new depreciation tables, which were drawn up with reference to this judgement have extended depreciation periods for many mobile investment goods beyond what is required by this principle.

Commercially used buildings are depreciated in linear fashion; the depreciation rate is to be reduced from 4% to 3%. Yet it can be argued that allowing all commercial buildings to depreciate over a period of 33 years is too undifferentiated. Office buildings, hotels, department stores, airports and railway stations, for instance, can normally be assumed to remain in use for considerably longer than 25 or 33 years, whereas the economic value of factories and storage facilities can be drastically reduced within a short space of time. Other areas of German tax law – such as the value attributed to real estate for tax purposes – has always based its depreciation allowances on significantly longer periods and differentiated criteria. Moreover, it must be borne in mind that factories and storage facilities account for only a relatively small proportion of commercial building investment (around 15%, excluding housing rental). For these reasons investment in buildings is an area of the changes in depreciation allowances that needs to be reconsidered.

What effect will the planned reform have on the tax burden?

Incorporated companies

For the firm as such, the implications of the reform for tax burdens can be determined relatively easily. The picture becomes more equivocal, however, if the position of the shareholders is also considered. The impact of the half-income system and the planned exemption with progression method are difficult to estimate in advance. For the purposes of the following analysis it is assumed that profits are distributed to middle-income shareholders. In the new system the tax burden on firms is independent of the distribution rate (proportion of profits distributed). By contrast, the overall tax burden borne by profits – corporation plus income tax – depends on both the distribution rate and the income level of shareholders. The tax burden is reduced, compared with existing legislation, the reduction increasing as the distribution rate becomes lower. In most of the cases considered here shareholders do not benefit from a reduction in taxation, because the calculation base is to be broadened, raising taxable profits,[4] and corporation tax

[4] The planned broadening of the tax base is represented in the following tax-burden calculations by a flat-rate increase of 5% in pre-tax profits.

Table 1

Impact of the Reform of Business Taxation on Incorporated Companies and Shareholders

For different distribution rates
and different marginal tax rates for shareholders

Assumption: Distribution rate = 0%		
Position	DM	in %
Prevailing tax legislation (2000)		
Pre-tax profits	100 000	100.0
Trading tax (local rate = 400%)	16 666	16.7
Corporation tax	33 334	33.3
Solidarity surcharge	1 833	1.8
Business tax burden	51 833	51.8
Income tax on dividends[1]	0	0.0
Solidarity surcharge	0	0.0
Total tax burden	51 833	51.8
Proposed tax laws (2001)		
Pre-tax profits[2]	105 000	100.0
Trading tax (local rate = 400%)	17 500	16.7
Corporation tax (25%)	21 875	20.8
Solidarity surcharge	1 203	1.1
Business tax burden	40 578	38.6
Income tax on dividends[1]	0	0.0
Solidarity surcharge	0	0.0
Total tax burden	40 578	38.6
Decrease (–) or increase (+) in tax burden compared with 2000		
Burden of business taxes	–11 255	–21.7
Income tax on dividends	0	–
Total tax burden	–11 255	–21.7

1 Assuming that all shareholders face the average marginal tax burden. —
2 The calculation base rises by 5% due to the tightening of depreciation allowances.
Source: DIW calculations.

can no longer be set off against income tax. The lower their individual marginal tax rate, the greater the increase in the tax burden borne by shareholders (cf. table 1).

Unincorporated companies

A number of firm-specific factors determine whether it is advisable for unincorporated companies to take up the option of being taxed as incorporated companies. In order to calculate the impact of the reform of business taxation on unincorporated companies it is necessary to make assumptions on the extent to which the tax base is broadened, on the owner's 'wage' in the firm taking the option, and on the level of pension provisions.

In the model calculations presented here it is assumed that an individual firm opts for the corporation model. Profits up to DM 200 000 are deducted from total profits as the wages of entrepreneurship; the owner pays private income tax on this sum. Profits in excess of this sum are subject to the income tax following the half-income system to the extent that they are distributed. Unlike the calculation models for incorporated companies, the profits distributed by unincorporated firms are subject to the exemption with progression method.

Generally the option model is attractive only for firms earning a profit of DM 50 000 and above. For a firm earning profits of DM 1 million and a distribution rate of zero, the firm pays DM 143 759 less in tax compared with existing legislation, a reduction of 28.2%. If the firm were not to opt for the corporation model, on the other hand, the tax reduction would amount to just DM 49 651 or 9.7%. A different picture emerges, however, if the profits are distributed in full. In such a case an entrepreneur should look very carefully at the two taxation forms before deciding. Allowing for the entrepreneurial 'wage' assumed here, the option model is only more favourable for profits of up to DM 200 000. In all other cases an unincorporated firm does better by rejecting the option. For a firm making a profit of DM 1 million, the option model actually leads to an increase of DM 1 829 in the overall tax burden. If, on the other hand, such a firm sticks to the income tax option, allowing for the possibility of deducting trading tax, the tax burden is reduced by DM 49 561 (–9.7%) compared with prevailing tax legislation.

Income tax rates also to be reduced

At the end of 1999 the government announced amendments to its original proposal for business tax reform, the main effect of which is to reduce income tax rates faster and more significantly than originally envisaged. The main aim is to reduce the tax burden of, alongside private households, those single-person firms and small partnerships that cannot benefit from the option model and who also scarcely benefit from the possibility of deducting trading tax. The proposals are as follows:

- The final stage of the already adopted tax reform 1999/2000/2002 is to be brought forward to the year 2001. The initial rate of income tax is to fall to 19.9%, the top rate to 48.5%; the basic tax-free allowance is to rise to just over DM 14 000.
- In 2003 the initial rate of tax is to be cut further to 17% and the top rate to 47%; the basic tax-free allowance will rise to DM 14 500.

– For 2005 it is envisaged that the initial rate of tax will be reduced to 15%, the top rate to 45%; the basic allowance rises to DM 15 000 (cf. figures 2 and 3).

The impact of these proposals would be to reduce the tax burden most significantly among low- and medium-income brackets. For instance, in 2001 an unmarried taxpayer with an annual taxable income of DM 60 000 would enjoy a reduction of DM 1000; on top of this come DM 309 and DM 602 in 2003 and 2005, respectively. Summing these reductions, the person in question would be paying 14% less in tax compared with the year 2000.

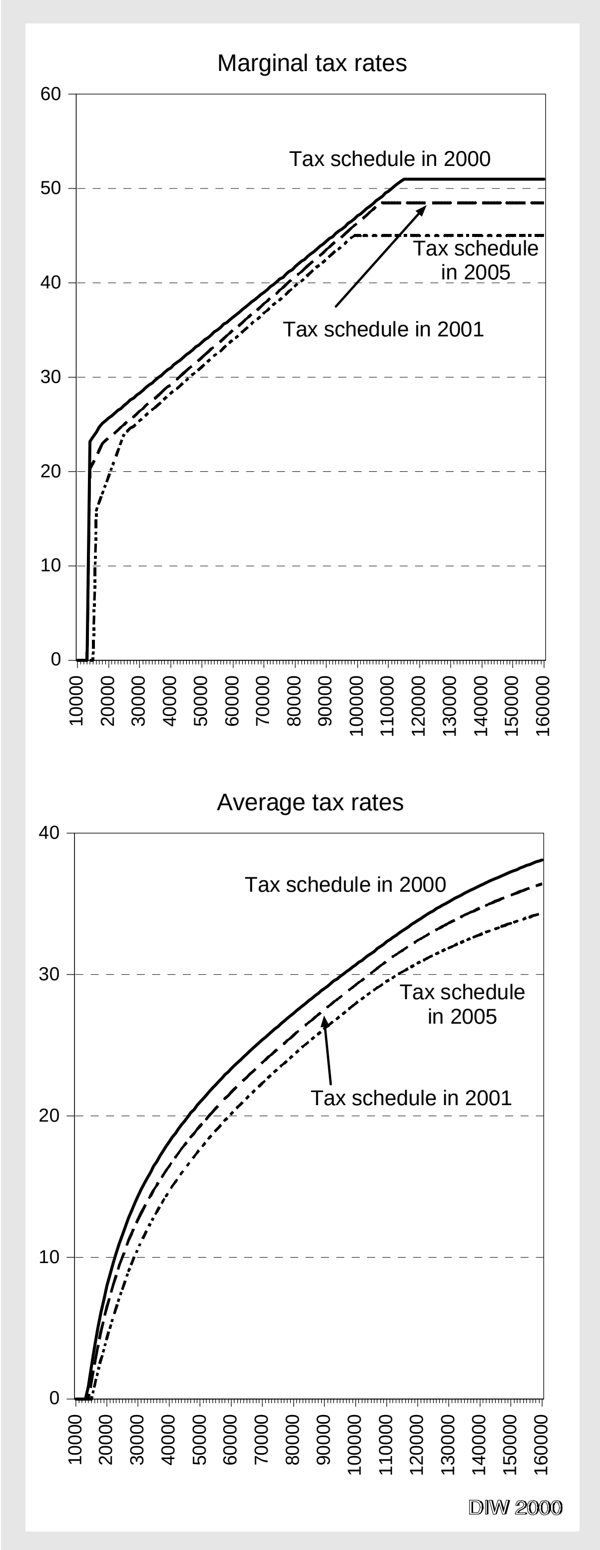
Positive macroeconomic effects

Overall the package of business tax reform measures is expected to have a positive impact on the German economy, as it will reduce the overall burden of taxation on profits (cf. table 2). Any positive impulse for investment is likely to be limited, however. Indeed, at the microeconomic level the effect on investment, growth and employment may initially actually be negative. Although a marked reduction in tax rates improves the incentives for foreign direct investment, for domestic investors, whose earnings on both national and international financial investment are subject to German taxation – i.e. those firms and private investors that do not evade tax on their capital earnings – even the cut in (marginal) tax rates makes investment in domestic real capital less attractive compared with financial investment (tax paradox): it reduces the value of the items that can be deducted from pre-tax profits. This effect is all the more pronounced when the scope for claiming deductions is further reduced by measures to broaden the tax base (such as the planned restrictions on the depreciation allowances).

Positive effects on the macroeconomy are to be expected above all else because the reform of business taxation forms part of a comprehensive package of reforms. Along with the cuts in income tax rates, the overall burden of taxes and contributions will be reduced substantially. Consequently, it is not only the profits retained within firms, but income in general that will benefit. In 2001 firms and private households will have to pay around DM 45 billion less tax. Merely the fact of bringing forward the 2002 tax schedule to 2001 reduces the tax burden by DM 28.5 billion. This can be expected to improve the conditions for strengthening of supply and demand. The income tax measures are therefore to be welcomed.

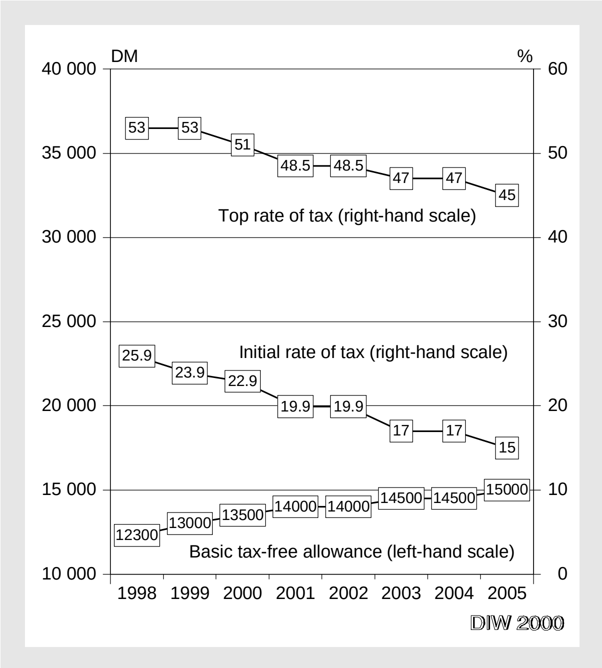
Figure 2

Income Tax Schedule in 2000 and Planned Tax Schedules for 2001 and 2005



Sources: Federal Ministry of Finance; DIW calculations.

Figure 3
Basic Tax-free Allowance, Initial Tax Rate and Top Rate, 1998 to 2005



Source: Federal Ministry of Finance.

Conclusion

Although a positive macroeconomic effect is to be expected from the tax reform as a whole, the fact remains that the proposed business taxation reform suffers from conceptual deficiencies. Both the privileged treatment of retained profits and the abandonment of full imputation in favour of the half-income system in taxing dividends contravene the principles of equal and economically neutral taxation. The fact that the option model renders the tax system yet more complex is a cause for concern. Nor is the partial crediting of trading tax against income tax for single-person firms and partnerships coherent and convincing. If the aim is to reduce the burden of trading tax, then this tax should be reformed directly.

Irrespective of the taxation of retained profits, the system of full imputation should be retained for distributed profits. This concept was and is convincing in terms of both consistency of tax system and its effects on wealth distribution. Specifically, it is appropriate to the principle of taxation according to ability to pay.

Particularly problematic is the planned introduction of a differential between the rate of corporation and the top rate of income tax; from 2005 this is to amount to 20 percentage points. If international competition is held to require a marked reduction in corporate tax rates, while at the same time retaining the present system, the dilemma arises that a corresponding cut in the top rate of income tax would be required; for this should not be at a level that is significantly higher than the rate of corporation tax on retained profits (the differential to business income subject to income tax is currently 3 percentage points). The greater the difference, the greater becomes the pressure to introduce the option model, i.e. to permit sole proprietors and partnerships, too, to benefit from the lower rate of tax on retained profits.

From 2005 the top rate of income tax is to be 45%. A cut to significantly below 40%, as called for by the opposition parties, is currently not only scarcely practicable for fiscal reasons, it is also problematic in terms of income distribution.

Rates of business taxation in the OECD countries range from around 30% to 40%. Against this background it must be asked whether corporation tax rates really have to fall as far as is planned by the German government. A less pronounced reduction would permit a solution in which corporation and income tax rates would remain relatively close.

The cornerstones of an alternative reform concept could be as follows:

- Reduction in the rate of corporation tax on retained profits to 35% and for distributed profits to 25%, which – as is currently the case – can be set off in full against the shareholder's income tax (full imputation system of corporation tax).
- Reduction in the calculation rate for trading tax to around 2.5% of profits, implying a halving of the burden of trading tax; the financial effects can be partially offset by broadening the tax base and the number of firms paying the tax; to the extent that local authorities suffer a loss of revenue, they should receive a higher share of value added tax receipts or should be required to transfer less of their trading tax receipts to other tiers of government.
- The top rate of income tax should then be reduced to the region of 40%. The loss of revenue could be offset by a further broadening of the tax base. In this context the system of splitting married couples' income for tax purposes should be reconsidered.

If the federal government implements the package of business tax reforms as envisaged in the bill presented to parliament, pressure could arise in the longer run to apply the new lower rates of tax not only to retained profits but also to distributed profits and other capital income. A large number of countries have already substantially reduced the tax burden on income from capital and entrepreneurial activity, while leaving other types of income, most notably earned income from employment, subject to the progressive income tax. In

Table 2

Financial Impact of the Planned Reform of Business Taxation and the Cut in Income Tax Rates

Increase (+)/decrease (–) in tax revenue in DM millions

Measure	Year of introduction[1]	Year of impact[2]			
		2001	2002	2003	2004
Reform of business taxation	–8 965	–16 455	–20 905	–17 340	–16 645
Incorporated firms: cuts in tax rates and reform measures as a whole	–20 110	–18 765	–28 260	–28 390	–26 635
Cut in corporation tax rate to 25%	–15 945	–16 600	–19 315	–19 170	–20 320
Replacing the imputation system by the half-income system in taxing dividends	+4 985	–	+3 905	+5 080	+5 585
Exempting tax corporations' capital gains	–4 220	–2 110	–3 800	–4 220	–4 220
Transitional rules for corporations' existing equity capital	–4 115	–	–5 425	–6 830	–6 055
Other measures	–815	–55	–3 625	–3 250	–1 625
Unincorporated firms: cuts in tax rates and reform measures as a whole	–7 545	–4 075	–7 445	–11 245	–14 315
Reduction in income tax equal to twice the calculation basis for trading tax	–10 025	–7 015	–8 360	–10 495	–10 045
Option to be taxed as a corporation	–2 680	–670	–3 885	–7 405	–11 035
Abolishing the limit on the tax schedule for business earnings	+5 160	+3 610	+4 800	+6 655	+6 765
Counter-financing measures to broaden the tax base (especially reducing depreciation rates)	+15 240	+5 675	+12 145	+17 125	+17 285
Extending depreciation periods	+3 450	+710	+2 655	+5 170	+7 020
Reform of income tax schedule 2001 to 2005	–27 600	–28 515	+1 395	–13 985	–13 260
Bringing forward the 2002 tax schedule to 2001	–27 600	–28 515	+1 395	–475	–
Introduction of 2003 tax schedule	–(13 300)	–	–	–13 510	–13 260
Introduction of 2005 tax schedule	–(35 200)	–	–	–	–
Tax reform package, total	–36 565	–44 970	–19 510	–31 325	–29 905

1 Effects of a full period of tax assessment, which can carry on for some years. — 2 Cash effects during the calendar year.
Source: Federal Ministry of Finance.

many cases the tax on capital income is withheld at a final flat rate, implying a dual system of income taxation.[5]

[5] Such systems have already been introduced by Norway, Sweden and Finland, and these are likely to be followed by Austria and the Netherlands.

There is thus a very real danger that the planned reform of business taxation in Germany marks the first step down the road towards a dual income tax system. It should not be automatically assumed that the implications of this for income and asset distribution will be politically acceptable.

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