

Taxing top income earners in the Czech Republic: An IDEA for reform

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Summary

- The study brings new facts about the distribution of top incomes and the taxation of top income earners in the Czech Republic, derives optimal marginal tax rates on the top incomes, and proposes a specific systemic reform.
- The top one percent of the highest paid persons in the Czech Republic include those employees and business owners whose gross incomes exceed CZK 1,230 million per year.
- By international comparison, the Czech Republic exhibits low inequality of gross incomes. The top 10% of the income distribution accounts for 25.7% of total income, whereas in all developed countries for which comparable data is available this figure is significantly higher, between 28.2% and 46.3%. When it comes to the top one percent of the income distribution, the discrepancy compared with other developed countries is less pronounced: The top one percent accounts for 6.8% of total income, while for comparable countries it is between 5.4% and 19.7%.
- The top one percent of the highest paid taxpayers account for only 6.5% of all taxes paid (income tax and insurance premiums), i.e. less than in proportion to their share

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in total income. The taxation of top incomes is one of the lowest in international comparisons, both in absolute levels and taxation of average incomes.

- Using realistically selected input parameter values, the optimal marginal tax rates imposed on the highest incomes range between 33–43%.
- Given a number of non-systemic changes in the past, it is desirable to consolidate changes in the taxation of top incomes. We propose a reform that would significantly simplify the taxation of top incomes and make it more transparent. The tax bases for health and social insurance for employees and self-employed persons would be consolidated, introducing a single ceiling on health and social insurance at the level of four times the average gross salary, while gross income exceeding this ceiling would be taxed at the top income tax rate of 40%.
- In consequence, the proposed reform brings the taxation system closer to a “flat tax” than any legislation which has been in effect in the Czech Republic since 1989.