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Taxes as determinants of firm competitiveness - micro and macroeconomic perspectives

Project objectives/Research hypothesis

The objective of this project is to understand better the link between taxation and performance of the economy. The optimal tax rates permit maximizing the fiscal revenue without reducing excessively the business activity. Naturally, tax avoidance as well as shadow economy emerge as counter-parts of taxation, but without behavioral foundations economic models are relatively inapt to address such questions comprehensively. In fact, this has been a problem in majority of economic analyses including a recent DSGE take on optimal taxation by Trabandt & Uhlig (2009). It has received already nearly 200 citations in less than 3 years despite two oversimplifying assumptions of one sector economy and no tax avoidance. This project seeks to alleviate these two shortcomings. We will develop a macroeconomic model of optimal taxation founded on microeconomic patterns of firm behavior. We formulate the following hypotheses:

H1: firms survival and performance depend not only on structural factors, competition and business cycle but also on the form and parameters of the tax system [microeconomic]

H2: tax optimization raises survival probability and improves firm performance

H3: despite firm heterogeneity optimal tax rate exists but is different from baseline those with homogenous firms [macroeconomic]

H4: tax avoidance varies with tax rate (higher tax rates lead to bigger tax evasion) and business cycle [macroeconomic]

All hypotheses will be tested with reference to the Polish economy, but the econometric analysis will comprise other countries for comparison.