

Demographic Change and Tax Revenues - Results from a Large Microsimulation Model for Germany

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Paper Abstract: Similarly to many other European countries, Germany has experienced a considerable demographic shift since the 1970s: higher life expectancy and diminishing birth rates, only partly balanced by immigration, have led to an altered population structure with an increasing share of elderly people. In the next decades, population aging in Germany will accelerate and also induce a decline of the total population. These demographic changes can be expected to have a profound impact on the governmental budget. While changes in public expenditures have been forecasted regularly since 2005, the revenue side has received less attention to date. We study the long-term (2015-2060) changes in tax revenues induced by demographic change. We focus on the development of income tax revenues given a shrinking workforce. Our aim is to quantify possible fiscal effects of demographic change using microsimulation and to identify elements of the income tax code particularly affected by demographic change. We find the expected demographic changes to have a clear negative impact on income tax revenues. Population aging increases the impact of various deductibility rules on total income tax revenues, in particular the impact of the deductibility of old-age and health insurance provisions. The impact of the deductibility of exceptional expenses such as expenses for caregiving also increases but remains small overall. Due to expected increases in real incomes, demographic change does not imply an absolute drop in income tax revenues in the next decades, however.