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# Do Lower Taxes Reduce Informality? Evidence from Brazil\*

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## Abstract

We exploit a unique, large-scale formalization program in Brazil to estimate the effects of reducing the costs of formality on firm formalization. We rely on both firm-level administrative data and individual panel data to show that reducing taxes once registration costs have already been eliminated reduces firm informality. This effect comes from the formalization of existing informal firms, and not from the creation of new formal businesses nor greater formal firm survival. The implied formalization elasticity is otherwise low, and our cost-benefit analysis indicates that the program led to net losses in tax revenues.

**Key words:** Taxes, informality, firm creation.

**JEL code:** O17, H32, H26.

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