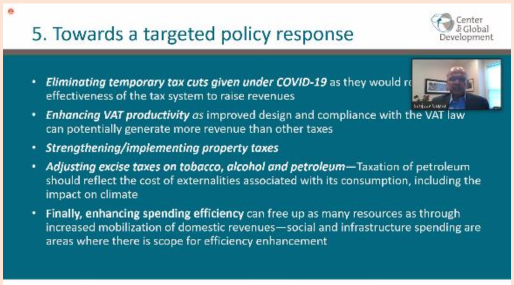
VIRTUAL SEMINAR

TAX INCENTIVES IN DEVELOPING ECONOMIES IN TIMES OF COVID19

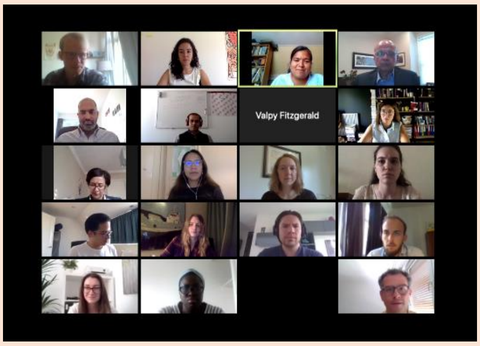
-SUMMARY-

On June 24, 60 participants from all over the world gathered for a virtual webinar on “Tax Incentives in Developing Economies in Times of COVID-19”. After an introduction by Irma Mosquera, Agustín Redonda discussed the implications of economic downturn due to COVID-19. While the impact on GDP might not be stronger in developing economies than in advanced economies, the consequences of GDP loss will be stronger in developing countries, as poverty might increase. Therefore, countries need to support their economies. However, tax expenditures might not be the best way to do so. Moreover, negative effects (e.g. redundancy, impact on environment) are well documented. Especially, the large informal sector of developing economies which by definition is outside the tax system and which is particularly affected by the crisis would not profit from tax expenditures. Although not all tax incentives are equal (e.g. cost-based are profitable to profit-based), they should always be used with care. If enacted, they need to be targeted and transparent. Three key takeaways for policy makers are: a) to make an estimation of the cost to be incurred when enacting a specific policy; b) look for ways to track and trace the impact of the tax incentive; and c) keep in mind the desired objective when adopting a given incentive in order to target it specifically to assist the sector that can leverage from it.



In the next presentation, Sanjeev Gupta argued that the crisis might present an opportunity for countries to improve tax systems. He noted that, while tax incentives used to be industrial policy measures in the past, many of them had transformed into tools to protect the politically connected. The crisis might enable governments to undertake reforms that previously were politically difficult and reverse inefficient tax policy choices. Mr Gupta raised awareness about the importance of determining correctly the expenses to be incurred by the governments during the COVID19 pandemic (e.g. usual expenditures that should be correctly assesses refer to education, health, roads, electricity, water and sanitation). Having a proper estimation of the resources that the country has and the portion of such that will be consume in expenditures is not only beneficial for creating a better suited tax policy but also for transparency reasons (e.g. IMG emergency assistance is connected with higher transparency of public spending). Some reforms to be considered might be the abolition of tax holidays, enhancing VAT productivity, or implementing property taxes. In the discussion, it was mentioned that reductions in VAT rate were reversed in some places.

Valpy Fitzgerald mentioned that to alleviate the economic consequences of the COVID19 crisis, developed economies' governments have been able to incur debt. As this is less feasible in developing economies, increments in the tax-to-GDP ratio are necessary in the latter. In that context, he warned against corporate income tax cuts, since corporate income tax is potentially the only form to effectively tax wealth in developing economies. He noted that for developing economies, international cooperation is necessary to raise revenue from multinational enterprises, especially in digitalized sectors. He therefore regretted the recent choice of the US to withdraw support from ongoing discussions around digital taxation at the OECD.



Finally, Alexandra Readhead considered the specific case of mining sector: She pointed out that the mining sector is not more affected by the COVID-19 crisis than others. Indeed, it is necessary to differentiate among different minerals: While the price of certain minerals decreased (such as aluminium and nickel), the price of gold increased significantly. Therefore, governments need to be very careful when providing support to mining industries (tying support to conditions, for example). Moreover, governments with revenue losses in other areas might consider profitable mining companies for prepayments of royalties and taxes. She noted that already before the crisis, many tax incentives in the mining sector were redundant and opaque.

Irma Mosquera closed the discussion. She noted the variations of policy responses among countries. While some governments were trying to raise more revenues, others went into other directions: The Philippines, for example sped up an already planned reform consisting in a decrease of the corporate income tax rate. She pleaded for more transparency in the policy choices taken by countries.