A lack of transparency

Do you know about the taxes your government does NOT collect?

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All over the planet, governments are desperate for funds to finance social policies, public infrastructure and development projects. Yet, the very same governments routinely forego huge amounts of tax revenues by granting tax incentives to investors, setting lower value added tax rates for the consumption of specific goods or services, exempting specific groups from paying energy taxes, and so on. These mechanisms are called “tax expenditures”: departures from the normal tax structure, designed to favour a particular industry, activity, or group of persons.

This is not a minor issue. In the United States alone, the federal government is estimated to have foregone more than 1.5 trillion USD in 2017. This equals 37 per cent of its direct federal spending and roughly 6 per cent of the country’s GDP (according to figures provided by the US Department of the Treasury). Existing estimates, though limited in scope, show that tax expenditures range from 0.7 per cent to 6.6 per cent of GDP in Latin America and from 0.6 per cent to 7.8 per cent of GDP in Africa.

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The actual figures may well be considerably higher, because hardly any government provides an encompassing picture of its tax expenditure provisions and their costs. Governments sometimes cite noble causes to justify tax expenditures. These include attracting investment capital from abroad, promoting innovation and employment, or facilitating access to basic goods. In most cases, however, governments simply do not know how effective these provisions are in reaching their stated goals and, more importantly, if their benefits outweigh their costs.

A 2018 assessment of the 43 G20 and OECD economies shows that eight countries have not reported any tax expenditures over the last ten years. 26 have published a basic report, and only nine governments have published detailed and comprehensive reports on a regular basis. The picture is even bleaker in Africa, the region with the highest number of low- and lower-middle-income countries. Out of 53 African countries recently reviewed by the Global Tax Expenditures Database (GTED) team, only 19 have released public reports at least once between 2000 and 2019. The remaining 34 countries did not publish any reports during this period. The GTED is a joint effort of think tanks and research institutions from Europe, Asia, Africa and Latin America led by the Council on Economic Policies (CEP) and the German Development Institute (DIE). The main goal of the project is to increase transparency, generate trustworthy information and expand research in the field of tax expenditures. The GTED is set up with official data published by governments worldwide in a consistent format to increase the level of international comparability.

The reports provided by the group of 19 African countries vary hugely in quality and scope. Morocco and Ivory Coast stand out thanks to the breadth of the information their reports offer. Apart from these two cases, most of the countries with tax expenditure reports provide aggregate estimates of the foregone revenue, either at the tax base or at the budgetary category level. They do not provide specific information at the level of individual provisions, which would be needed to perform cost-benefit evaluations and assess the effectiveness and efficiency of these provisions. Moreover, no country presents consistent data on the number of beneficiaries of each provision. Less than half of the countries specify the budgetary category, reveal a policy objective, specify the targeted beneficiaries, or include a detailed description for each provision. This kind of information is not only crucial for policy-makers. It is also important for increasing transparency and accountability towards the society.

For the purposes of transparency and political debate, tax expenditure reports have to be public. Ideally, they should be linked to the budget or found on open and easily accessible government websites or repositories. References to such reports in official government statements should include information on where to find them. Since a vast majority of governments do not fully report their tax expenditures, the public cannot discuss whether these mechanisms make sense. Academic research cannot assess their impact in terms of distribution, investment or market distortions, and parliamentarians cannot decide to get rid of those tax expenditures that clearly fail to generate the desired effect. It is therefore paramount that international tax cooperation discusses common standards for tax expenditure reporting, and encourages governments worldwide to apply them, as envisioned, for instance, by the Think20 Task Force on Trade, Investment and Tax in 2018.

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