Building Tax Capacity in Developing Countries

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SDN/2023/006

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2023 SEP







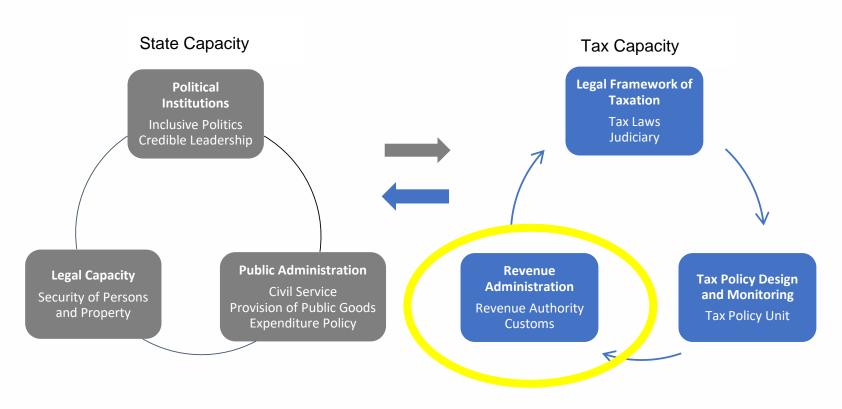
Building Tax Capacity for Revenue Mobilization

APRIL 2024

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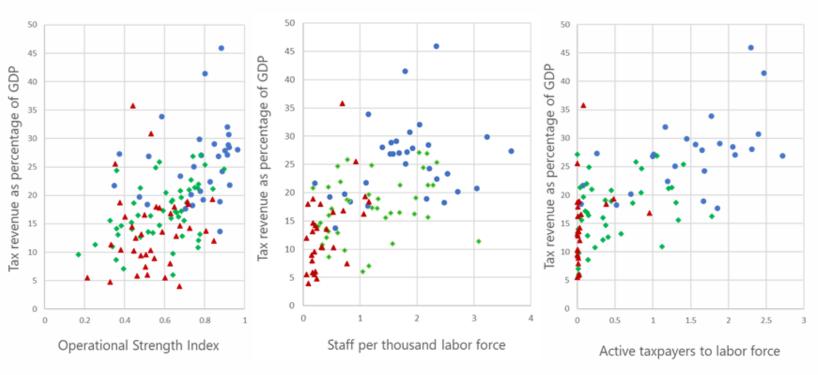
Tax capacity defines the essence of a state that relies on taxation to play its role effectively

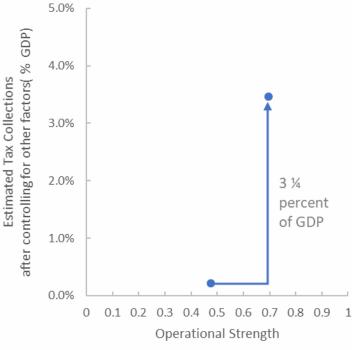


Source: IMF staff.

Growing tax revenue through building revenue administration capacity

- Advanced Economies
- Emerging Markets
- ▲ Low Income Developing Countries



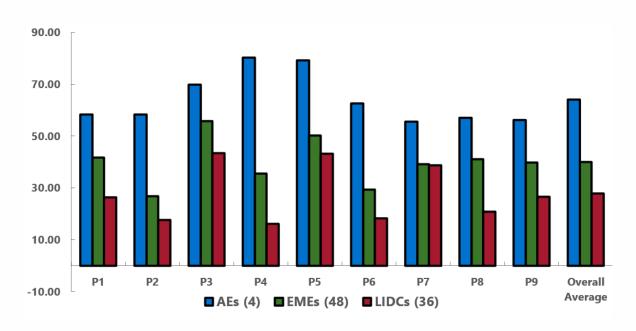


Countries with a stronger tax operational capacity collect more tax, after controlling for tax policy and macro-economic factors

The role of tax institutions: modernizing revenue administrations

- Well-funded, well managed, and autonomous revenue administrations are central to tax capacity
- Digitalization is critical for regular functions, data driven decision making and compliance management: (digital tools help calculate and reduce VAT compliance gaps)

LIDCs lag, in some cases significantly, on key characteristics of effective revenue administrations



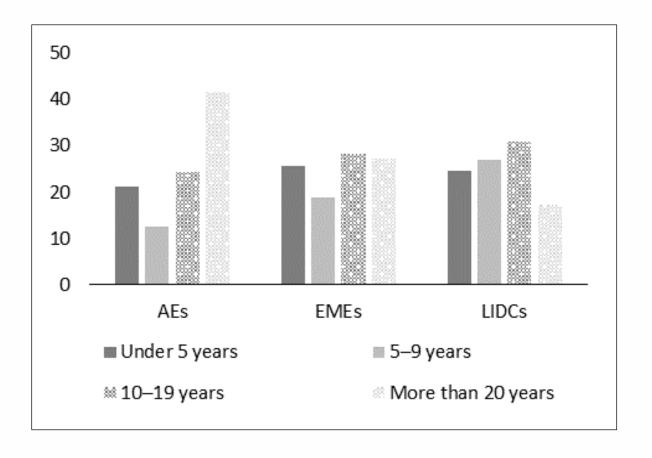
Source: IMF staff calculations based on reports provided by the TADAT secretariat. P1: Integrity of the Registered Taxpayer Base; P2: Effective Risk Management; P3: Supporting Voluntary Compliance; P4: Timely Filing of Tax Declarations; P5: Timely Payment of Taxes; P6: Accurate Reporting in Declarations; P7: Effective Tax Dispute Resolution; P8: Efficient Revenue Administration; P9: Accountability and Transparency.

Administrative reform vs policy choices?

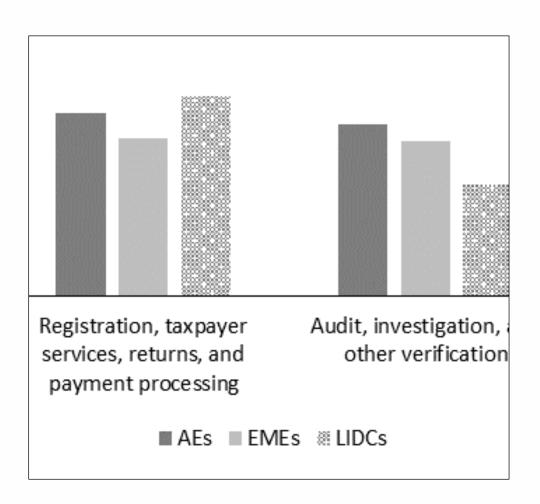
- When mobilizing additional revenue, the choice between improvements in tax administration practices or interventions and policy changes is important, and likely deserves more attention than given.
- In countries where there is low capacity and low compliance, more revenue would likely be realized with increased administrative capacity. Increased capacity would then permit improved impact of tax policy changes.
- An example:
 - Country X has very low filing and payment compliance and therefore increasing the VAT rate will likely result in marginal returns.
 - However, investing in administrative capacity to increase filing and payment compliance would increase revenue and ensure that future tax rate increases achieve the revenue projected.

Long staff tenure in specialized roles contributes to capacity

- AEs benefit from experienced staff (with long tenure and specialization)
- The share of experienced staff is smaller in EME and LIDCs suggesting room for improvement



Allocation of staff by function also matters



- There is a longstanding difference between the percentage of staff allocated to enforcement in AEs and LIDCs (with EMEs in the middle):
- For AEs this exceeds 30 percent, while for LIDCs it is about 20 percent.
- Up-to-date IT systems are also essential to enhance staff productivity and effectiveness, including to cater to multinational enterprises that have access to the latest technologies and to support digitization.

Leveraging tax and customs collaboration to strengthen compliance

- Strengthening cooperation between tax and customs administrations could leverage data use and improve efficiency and effectiveness in revenue collection.
- With appropriate governance and management arrangements, separate revenue agencies can work cooperatively.
- Non-compliance in customs may signal tax non-compliance, and viceversa. There are several strategies to improve detection.
- Of the 166 countries that provided data to the 2021 International Survey on Revenue Administration (ISORA), 40 percent have integrated tax and customs administration (34 percent of LIDCs, 44 percent of AEs). Even with organizational integration there is significant opportunity to improve sharing.

Effective tax administration includes

- Operating at arm's length to reduce opportunities for rent-seeking behavior.
- Autonomy, but accountability, and transparency to build and maintain public trust in a fair tax system.
- Effective oversight, including internal and external auditing.
- A strong focus on maximizing voluntary compliance with an integrated, approach combining preventive, detective, and corrective actions.
- Robust taxpayer service strategies that include measures to lower compliance costs for taxpayers and operational costs for the administration.

Building tax capacity: a sound legal framework & robust HR practices

Legal Framework

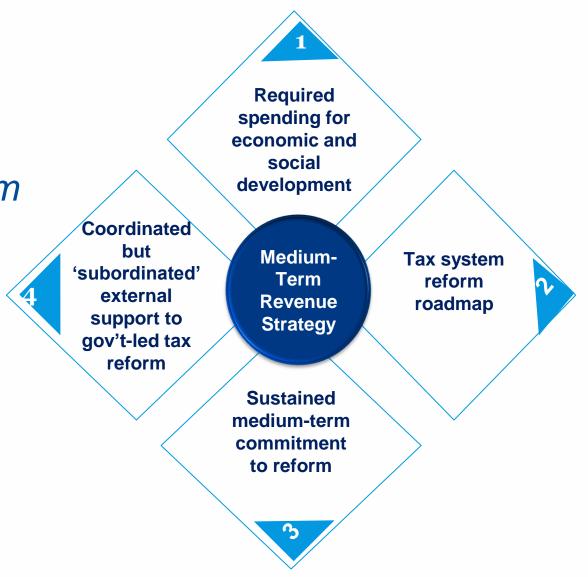
- Simple and effective taxing legislation
- Simple and flexible procedures legislation and regulations (tax procedures code)
- Up-to date procedures laws balance simplicity and comprehensiveness, stability and transparency.
- Legal framework is a key component of tax certainty, which can impact economic growth

HR Practices

- Skilled sustainable workforce
- Gender balanced
- Appropriately remunerated to minimize wrongdoing
- Sanctions for wrongdoing
- Skills based recruitment
- Performance based promotion

Improving taxation with MTRS

A comprehensive strategy—a
Medium-Term Revenue Strategy
(MTRS)—can help identify tax reform
measures and facilitate their
implementation.



IMF approach for building tax capacity



DIAGNOSTIC ASSESSMENT

Using assessment tools to benchmark, identify current state and gaps between current state and good practice



REFORM STRATEGY ELABORATION

Consultations
with authorities,
development
partners, and within
IMF to prioritize
topics and elaborate
reform strategy



SEQUENCED IMPLEMENTATION OF DIVERSE CD INTERVENTIONS

Supported by IMF staff and short- and long-term experts with quality control from IMF HQ staff using variety of delivery modalities, inerson, virtual, hybrid and training



EVALUATION AND RE-PRIORITIZATION

Assessment of outcomes and systematic evaluation of performance provide feedback to help prioritize resource allocation

Using different channels, we share knowledge and give advice through:

- Country-specific work: missions, desk reviews, and workshops
- Cross-country work: training and regional & global conferences
- Massive open online courses on <u>PFM</u>, <u>RA-GAP</u>, <u>VITARA</u> and revenue forecasting
- Social media presence: <u>Podcasts</u>, IMF <u>Blogs</u>, <u>PFM Blog</u>, <u>Twitter</u>, <u>Facebook</u>
- <u>How To Notes</u> on specific fiscal topics, <u>working papers</u>, and <u>other analytical work</u>.
- Revenue portal: https://www.imf.org/en/Topics/fiscal-policies/Revenue-Portal

Our work starts with a diagnostic assessment, and our CD intervention is carefully sequenced and constantly evaluated.

Takeaways

- LIDCs need significant additional revenue to pursue SDGs, ensure debt sustainability, and finance other priorities
- There is scope to increase tax capacity in LIDCs, centering on reforms of core domestic taxes and improving revenue administrations' performance
 - ▶ At about 13.3 percent of GDP on average, tax revenues (excluding SSCs) in LIDCs are well below their estimated 22.2 percent potential
 - Quality of tax systems matters—administrative simplicity, legal certainty, transparency, equity and efficiency
- Tax capacity development should increasingly focus on building fiscal institutions
- A holistic approach to building tax capacity, such as MTRSs, could facilitate coordination across institutions, and achieve a better balance between revenue and other objectives

Thank you!

Dive into the world of tax and customs with the help of the new IMF portal

IMF.org/RevenuePortal