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## TAX EXPENDITURES IN THE CIAT MEMBER COUNTRIES



**CIAT**

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**Fernando Peláez Longinotti**

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# S ummary

This document provides a general overview of tax expenditures in the CIAT member countries. The information sources used were: the member country tax expenditure reports, examination of the data in the CIAT Tax Expenditure Data Base (TEDLAC), as well as the responses to a specific survey carried out among all the member countries.

This subject is being considered from a qualitative as well as quantitative perspective. On the one hand, a review is made of the most relevant qualitative aspects arising from the contents of the country reports. The synthesis of this analysis will attempt to show the *elements* which these reports should include in order to become an accurate tool for the analysis and evaluation of the exceptions existing in the tax systems. At the same time, efforts will be devoted to identifying certain best practices found in the more advanced reports on this matter.

Following the classification, ordering and systematization of the results published, the second part of this document will show a quantitative analysis of the monetary valuations and estimates, comparing the results of the different countries, in relation to each country's national production and collection, and breaking down the results within the main collection instruments.

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# Introduction

An area wherein the Inter-American Center of Tax Administrations has been working for a long time is the study of tax expenditure identification and estimation practices. CIAT has provided direct counseling to the countries in this area, has developed a Manual of Best Practices for the presentation of Tax Expenditures<sup>1</sup>, trained member countries and created the Tax Expenditure Data Base (TEDLAC), in addition to carrying out several technical studies on this subject.

On this occasion, we are presenting this document whose objective is to analyze the practices dealing with the identification of exceptions, quantification of tax expenditures and the publication of reports on Tax Expenditures of the CIAT member countries.

The document is divided into two main sections. In the first section, there are the constitutive elements of tax expenditure reports which should be an effective tool for evaluating the exceptions that give way to tax expenditures.

The second section includes a synthesis of the empirical evidence. In other words, the analysis of all member country tax expenditure reports, plus complementary information. This section, in turn, is divided into two parts:

The first involves the review of the most relevant qualitative aspects, arising from the contents of the country reports. The synthesis of this analysis will endeavor to show the *elements* that these reports must include in order to become a precise tool for the analysis and evaluation of the exceptions existing in the tax systems. Likewise, it will include the best practices found in the most advanced reports on this subject.

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<sup>1</sup> Manual of Best Practices in the Measurement of Tax Expenditures. An Ibero-American experience. Inter-American Center of Tax Administrations – CIAT. 2011.

The second part of this section, following a classification, ordering and systematization of the results published, will show a quantitative analysis of the monetary valuations and estimations, comparing the results of the different countries, in relation to each country's GDP and disaggregating the results within the main collection instruments.

In order to consider the situation from these two perspectives, the main sources of information used were: the official and public tax expenditure reports prepared by the member countries, the micro-data of the CIAT Tax Expenditure Data Base (TEDLAC) and the response to a questionnaire that was sent to the tax administrations of the member countries.

The identification, quantification and publication of the tax expenditure reports is of great importance, inasmuch as it allows for determining the economic dimension of the phenomenon and the beneficiary individuals, sectors, regions or activities. It is also one of the components of the cost-benefit equation, which the officials in charge of policy must analyze to determine whether the benefit granted through this mechanism brought about the desired effect and if the latter justifies the associated tax sacrifice.



## **2** Elements constituting the Tax Expenditure reports

This first section will show the steps considered essential in order that the tax expenditure reports may become a useful tool for the assessment of the tax system and in particular, the exceptions that are part thereof.

As mentioned in previous discussions of this topic, the identification, quantification and publication of the tax expenditure reports is of great importance, inasmuch as it allows for determining the dimension of the phenomenon and the beneficiary individuals, sectors, regions or activities. It is also one of the components of the cost-benefit equation which the official in charge of policy must analyze to determine whether the benefit granted through this mechanism brought about the desired effect and if the latter justifies the associated tax sacrifice.

### **2.1 Definition of Tax Expenditures**

The TEs are the economic result of the exceptions to a referential tax or a referential tax system.

In general, the referential tax system includes the elements that constitute the nature of the tax: assessment of the taxable base, the structure of the rates, the accepted accounting practices, the form and conditions of the expenditure deductions made, specific rules for facilitating the administration of taxes, among others.

These exceptions that will give way to the TEs may adopt several forms: exemptions, subsidies, credits, preferential tax rates, tax deferrals, among others. The TE reports identify and measure the reductions in tax revenues resulting from these deviations according to a determined referential framework, a previous definition of the scope of the tax expenditure concept and the methodological definitions referring to the purpose of the estimate, the sources of information available, the type of estimate applied, among other elements.

## **The tax expenditure concept and the stipulations proposed in the CIAT Manual (2011):**

*“Based on the definitions used by the countries analyzed, it is clear that a provision is considered a tax expenditure when it generates a loss in collection and implies a deviation of some general tax provision. Likewise, the fact that it pursues an economic or social policy objective of the State, or increases the taxpayer’s economic availability are also characteristics of a tax expenditure.*

*The OECD (2002) defined tax expenditures as the estimated costs in tax revenues that result in the preferential treatment of specific activities. On his part, Kraan (2004) expanded this definition noting that a tax expenditure may be defined as a transfer of public resources that is achieved through the reduction of tax obligations with respect to a tax of reference, instead of a direct public expenditure.*

*The IMF’s Tax Transparency Manual defines tax expenditures as the sacrificed revenues as a result of certain provisions of the tax code, such as exemptions of the tax base, deductions from gross revenues, tax credits that are deducted from tax obligations, reductions of the tax rate and postponement of the payment of taxes (such as accelerated depreciation).*

*The same document’s glossary adds that tax expenditures are the concessions or exemptions of a “normal” tax structure which reduce the collection of government revenues and that, since the government’s policy objectives may be achieved in an alternate manner by means of subsidies or other direct disbursements, it is considered equivalent to a budgetary expenditure.*

*Having considered the countries’ practice and the proposals of the OECD and IMF, the TEMWG (Tax Expenditure Measurement Working Group) recommends that tax expenditure be defined as resources not collected by the State, due to the existence of incentives or benefits that reduce the direct or indirect tax burden of specific taxpayers in relation to a referential tax system, in order to achieve certain economic or social policy objectives”.*

From the definition it follows that TEs give way to losses in collection and every exception is the result of a policy objective that is executed through the latter. The scope of the concept is general; that is, it recognizes not only those benefits granted in direct taxation, but also those exceptions introduced in

indirect taxation, for which reason it includes exceptions in consumption taxes, although one cannot specifically and a priori identify the subset of individuals that will benefit therefrom.

The delimitation of the referential tax system is a key element in the initial process of this procedure and as we shall see, the different options of demarcation of this referential tax scheme will provide some more or less equivalent tax sacrifice results.

## **2.2 The referential tax system, as framework for determining tax expenditures**

The first step of the process for measuring tax expenditures is the definition of the reference framework. This moment of the process shall be determinant for the subsequent identification as well as the quantification of results. Its previous discussion, definition and formal documentation will assist the analysts in the research process. Its presentation in the TE report favors the interpretation by third parties, for which reason it is also a recommendable practice.

The selection of a referential tax system has a fundamental impact on the subsequent result of the TE measurements, since with a greater or lesser scope of what may be considered as the normal structure of the tax being analyzed, a lower or greater number of exceptions will be identified and the total dimension of the quantified tax expenditure will be lower or greater.

One of the main difficulties when it comes to identifying the TE within a particular tax lies in agreeing on a referential tax system or tax against which one may compare the provisions that establish taxation exceptions in the legislation. The TE quantifications will differ in accordance with the adopted definition, which goes hand in hand with, among other things, the difficulty for making comparisons of the global dimension of collection not rendered effective, as well as the list of exceptions identified as TE among different country reports.

The introduction to the discussion of this aspect in the CIAT Manual reads as follows: “...the measurement of the TEs requires their correct identification, for which purpose it is necessary to initially define a referential tax system. Undoubtedly this is the most complex task of the entire process

*and the one generating the most discussion. The referential tax system may result from reading the legislation or from a theoretical conceptual framework; that is, some option of an optimal tax system”.*

From the review of the most recent TE reports in the CIAT member countries, it may be seen that while some documents have very elaborate reference frameworks, other reports rather include very general definitions on this issue, while still others only include definitions of the TEs. Therefore, at most one could only deduct and not with all certainty, the reference framework implicit in that study. Since this is the previous step for the subsequent identification of the TEs, each country will have the option of determining how general or detailed the selected description of the referential tax system will be. As a matter of fact, the idea of the referential tax differs from one analyst to another and from country to country, especially when, as we shall see, the reference is a conceptual definition of the tax.

## 2.3 Approaches for establishing the referential tax system

According to Craig and Allan (2001)<sup>2</sup> in order to determine their reference framework, the countries may choose one of three identified approaches: the *conceptual approach*, the *legal approach* and the *analogous subsidy approach*.

According to the conceptual approach, the reference framework should be what is known as “*the normal tax structure*”. The most notorious case of the application of this conceptual approach is the admission of Haig-Simons’ definition of income, conceptual reference framework which is quite recurrent in the studies, especially in the developed countries<sup>3</sup>.

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2 Craig, Jon; Allan, William. Fiscal Transparency, Tax Expenditures and Budget Processes: An International Perspective. IMF (2011)

3 Due (1968) in considering in his paper the allocation and distribution functions, on the taxation side, he proposes that the main step in the establishment of an income tax structure, is the definition of income. In a broad sense, income is every economic profit which a person obtained during the period under consideration. This author specifies in this definition according to Simons, that the revenue of a person during the period consists, in an economic sense, in the algebraic sum of: the value of consumption during the period, financed with revenues for use of productive factors or transfers which the person receives during the period or with the accumulated wealth (in this definition, to the amount of paid consumption one must add the value of the goods produced by the person for its own use -self-consumption- and the value of use of the durable consumption goods possessed); as well as the net increase of individual net worth during the period, either through accumulation of net savings during the period or increases in the value of the property.  $Y=C+\Delta W$

Some countries which in their TE studies are in favor of the conceptual approach for establishing the reference framework, base their analysis on this type of definition of income, although variations or adjustments are introduced whenever it is impossible to clearly introduce such concept.

Because of the great importance of collection of individual income taxes in the developed countries, the discussion regarding the tax base model and the referential tax in these countries has been focused on Income Tax. With respect to consumption taxes, a predominant collection figure in the Latin American countries and mainly with respect to Value Added Tax, a clearly dominant instrument in this type of taxation, one usually finds in the bibliography that a sound VAT should be established as reference that would be applicable through a single rate, to the entire final consumption without exceptions.

The second approach quoted by Craig and Allan is the one known as *Legal approach*. According to these authors, in this case one takes the tax law existing in a country as basis for determining the point of reference (taxpayer unit, types of income included, operations not considered in the tax sphere, etc.).

In general, in the design of the regulation that provides for the tax, first of all, one considers the general definitions regarding its nature, or what is juridically known as the taxable transaction or tax generating event. The taxable transaction will be the hypothesis provided in the law (or the regulation for establishing a tax) which, if it takes place, it gives way to the tax and accordingly the tax obligation which links the taxpayer to the creditor entity, that is, the State.

These hypotheses defined in the regulation, delimit the scope of the tax to specific objective economic events (the sale of goods, obtaining income, the possession of net worth, etc.), when specific individuals are the ones intervening (individuals, enterprises, etc.), in a specific spatial (delimitation of income tax within the national territory, for example) and temporary sphere (income obtained in periods of enforcement of the tax, for example). These elements are known as aspects of the taxable event (objective aspect, subjective aspect, spatial aspect and temporary aspect) and their joint occurrence verifies the hypothesis provided in the legislation for configuring the tax.

When the normal structure of a tax is then based on a legal approach, an economic event will be considered tax expenditure when, having complied with the hypotheses for configuring the tax, the very regulation of the tax, or some other, excludes that specific event from the application thereof. Following the legal approach then, we shall find in the very regulation of the tax or else in other regulations with tax effects, the exceptions to the normal structure of the tax in an explicit manner.

The tax regulation itself will provide us the other parameters that will comprise the normal structure of the tax, such as the scales, rates, the demarcation of the space wherein the taxable event takes place, among others.

**Those who are in favor of the legal approach state that the objective of this study in a manner coherent with the presentation of budgetary expenditures should be, how much is not collected according to the provisions of the current tax regime, from which revenues are reported and not what would be collected if a conceptual taxation model were adopted.**

The third approach, of the analogous subsidy, following Craig and Allan's classification, identifies as TE only those concessions that show a direct analogy with a grant via expenditure. According to Villela et al (2011) in practice, this approach leads to an identification of the TEs which is very similar to the legal approach.

The determination of a very abstract reference framework, that would be closer to the conceptual framework of the tax, could include many of the provisions of the tax legislation identified as TEs. On the other hand, a more processed point of reference, or one adapted to the nature of the tax according to the internal legal provisions, could include within the reference framework some of these same types of provisions, for which reason they would not be considered TEs.

The adoption of the conceptual or else the legal approach, will guide the researcher in determining the taxable amount of the tax being analyzed; that is, what is (would be) the scope of the tax. In any case, the tax instruments have an entire series of features that go beyond the determination of the tax base and which must necessarily be defined in order to conclude the reference framework.

Anyway, and even with these definitions, each of these elements allows great freedom of judgment and when examining the practice country by country, each one is in some way unique. The truth is

that a technique should be proposed in advance, which must be consistent with the objectives of the estimate and be clearly explained for purposes of improving understanding of the identification of the items liable to be estimated, as well as the amount of the TEs found.

With respect to the referential tax system, in the analysis carried out by the CIAT Manual it is stated that the countries included in its study identify the TEs according to a referential tax system based on the legislation, whether of a tax nature or not. Only a few countries consider the referential tax system based on a theoretical conceptual framework, in some special cases.

The CIAT Manual recommends the legal approach to delimit the referential tax system to be used for identifying the TEs. In this way, the lower tax burden would be verified by comparing the one actually borne by the taxpayer with the one he would have had to bear if the general legislation would have been applied. In its recommendation it adds that when the internal legislation is significantly deviated from the internationally accepted doctrine, one should evaluate the use of a referential tax system based on a theoretical conceptual framework.

The difficulties in *comparability* that occur between countries lie in the differences in legislations regarding similar taxes. These differences are more clearly evidenced in income taxes, both individual and corporate, where the different countries adopt different definitions for income. That is, legislations that establish gross income as basis for calculating the tax, before deducting any expenditure and those who admit a generality of disbursements as deductions in order to determine it. The scope of the definitions and parameters established in the legal regulation will affect the result to a greater or lesser extent.

Heady & Mansour (2019)<sup>4</sup> consider that the selection of the reference point will be a determinant factor in relation to the amount of general tax expenditures that will be reported. At times, these may be substantial. For example, the United States estimates tax expenditures in relation to income taxes only at approximately 6 per cent of GDP (OECD 2010, 138). However, the critical role in the

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4 Heady, Christopher; Mansour, Mario. Tax Expenditure Reporting and Its Use in Fiscal Management. A Guide for Developing Economies. Fiscal Affairs Department. International Monetary Fund. 2019

selection of the referential index implies that such aggregate number is not the main value of the tax expenditure. Rather, it is the transparency with respect to the cost of each tax provision what makes the tax expenditure estimate useful, on allowing a sound cost-benefit evaluation. This is an essential statement for inclusion in the text, in order to lower the pressure in the comparison of the results.

## **2.4 Identification of items that will result in tax expenditure.**

### **The Exception Files and the Tax Expenditure Inventory**

The identification of TEs is a complex process that requires a detailed analysis of the tax provisions; that is, those included in the tax regulation as well as exceptions disseminated in other laws. In some cases, there are constitutional provisions that exempt certain economic activities, as is the case of education in some countries, for example. This identification goes beyond the mere verification of the loss in collection.

In each period for updating the estimates, it will be necessary to review the exceptions existing in the system, by identifying the changes and the new exceptions that may have been introduced.

For this purpose, it is of great help to systematize the information analyzed and collected, in relation to the exceptions found. Tax systems usually include hundreds of exceptions, for which reason this part of the process is fundamental in order to integrally visualize the exceptions map, the individual valuation and the joint cost thereof.

In this stage it will be essential to prepare Individual Exceptions Files, and to consolidate them in a Tax Expenditure Inventory, or tax expenditure matrix.

The Individual Files will be a form for registering the most relevant elements of identification of the exception. In this way, every exception identified will be represented with its main characteristics:



name; description of the exception, referential tax, type of tax expenditure, regulatory source of origin, date of enforcement, date of expiration, among others.

The consolidation of the individual files, will result in the tax expenditure inventory.

It is a recommended practice to keep an inventory of TEs, identifying the tax, the type of exception, the regulatory source, the period of enforcement and the description thereof, to then complete it with the information sources used for the estimate and the methodology applied. The inventory format suggested is the one provided in our Tax Expenditure Data Base (TEDLAC), which considers the registration of all these elements.

In this respect, we will comment in greater detail the contents of TEDLAC. It includes the following variables:

## CHART 1

### Dictionary of Variables included in the TEDLAC

VARIABLE NAME	DESCRIPTION	TYPE
Country	Name of country under analysis	Categorical (16 types)
Tax category	Categorisation according to CIAT extended manual	Categorical (9 types)
Tax name	Name of the tax in the country concerned	Alphanumeric
Type of Tax Expenditure	CIAT handbook categorization	Categorical (7 types)
Tax incentive	Mark I if it is an Incentive or B if Tax Benefit	Categorical (2 types)
Normative source	Law and regulations giving rise to the exception	Alphanumeric
Name of the measure	Colloquial name of the measure in the country	Alphanumeric
Description of the measure	Describe in more detail how the measure operates	Alphanumeric
Validity from	Year since the first application of the measure	Alphanumeric
Effective until	Year of expiry of the measure (if any)	Alphanumeric
Associated budget Sector	Budget sector most associated with the measure	Categorical (16 types)
Specific geographical area	Territorial area where the benefit is applied	Alphanumeric
Exercise	Year in which the tax expenditure is being reported	Categorical
Measurement method	Describes the measurement method applied in the study	Alphanumeric
Information sources	Describes the sources of information used for the estimation	Alphanumeric
Amount of tax expenditure	Amount in national currency of tax expenditure	Numerical
Source	Tax expenditure report accounted for	Alphanumeric
Upgrade	Update year of the analysed TE database	Alphanumeric

The registration rules consider the existence of various types of classification variables: categorical, qualitative, in addition to the quantitative variable per se, which is the amount of Tax Expenditure of said measure in particular.

Among the categorical variables one may find: a general classification of incentives in 2 types, 9 classes of taxes, 7 types of tax expenditures, 16 associated budgetary Sectors and an opening, depending on the economic exercise being analyzed. These codifications allow for carrying out multiple analyses and describe the information at the level of hundreds of sub-categories formed by certain combinations of said variables.

The qualitative variables describe in greater detail some characteristics of the register such as: name of the measure, description, legal and regulatory source, the measurement method, the sources of information for the estimate, the report which originates every register, etc. This allows for considering the individual detail and getting to know in particular the measure that is being analyzed.

The accounting and characterization of the various items follow the recommendations included in the CIAT Manual of Best Practices for the Measurement of Tax Expenditures.

## **2.5 Estimation of the Tax Expenditure of each of the identified exceptions**

Much in the same way as in the process of identification of exceptions, where we are faced with alternatives for the election of the approach to be adopted for delimiting the referential tax (conceptual approach, legal approach or analogous subsidy approach), in this stage we are considering now, the countries must choose among various methodological alternatives for undertaking the measurement. These are related with the selection among various estimation methods, the investigation with respect to which ones are the most appropriate sources of information for the estimation and selection of the specific estimation technique. These sub-stages take place prior to the specific estimation of each one of the exceptions, for which reason it must be borne in mind that the methodological decisions taken will determine the amounts which we will definitely report as tax expenditures.

In order to assess each item, it is necessary to resort to various techniques which, to a great extent are conditioned by the availability and quality of the information found and the sources thereof. In each case one tries to determine the equivalent economic value of the tax expenditure resulting from the exception, for which purpose, in general, it will be necessary to know the amount of the economic

event that originated it. The sources per se, their origin, the institutional character of the issuer, and the level of disaggregation or detail of the basic information shall provide some more or less technically reliable estimates. In some cases, the lack of referential information on which to make the estimates, may lead to non-estimation.

In this process, the previous discussion within the estimation team, the explicit definition of the methodologies adopted and their presentation in the document, as well as the preparation and preservation of the working documents on the estimates, are fundamental for the analysis and review of the results and afford greater transparency to the entire process. The clear presentation with an appropriate level of openness of the results in the TE reports, favor the interpretation by the interested parties, and the subsequent analyses that could be undertaken, for which reason it is also a recommendable practice.

The process for estimating tax expenditures requires the definition of a general estimation method, which will serve as guide in the case by case estimation of tax expenditures. Dirk-Jan Kraan (2004)<sup>5</sup> presents three main methods for estimating tax expenditures: the revenue foregone or loss of revenues *method*, the *revenue gain method* and the *outlay equivalence method*.

These are three methods of different interpretation and application that will report different results. The literature, in general, does not consider the different methods in greater depth or the alternatives for overcoming the difficulties which each one may bring with it, as well as the differences which each methodology may produce. Nevertheless, we shall include herein the main characteristics of each of them.

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5 Dirk-Jan Kraan. Off-budget and Tax Expenditures. OECD JOURNAL ON BUDGETING– VOLUME 4 – NO. 1 – ISSN 1608-7143 – © OECD 2004. Previous studies on estimation methods (OECD, 1984; OECD, 1996)

## CHART 2

### The three estimation methods suggested by Dirk-Jan Kraan

REVENUE FOREGONE METHOD	REVENUE GAIN METHOD	OUTLAY EQUIVALENCE METHOD
The method determines a loss of collection occurring in a past period when the exemption was in force.	Endeavors to estimate the additional collection that would be obtained with the repeal of the exception that allows for the tax expenditure.	It is presented in such a way as to render comparable the tax expenditure with the budgetary expenditure.
The application of this method does not consider the changes in taxpayer behavior, since actually one seeks to determine the amount of tax not collected following the registration of the return.	The main difference with the previous method is that the estimates consider the taxpayers' behavioral changes.	It endeavors to estimate the equivalent transfer which the state should make to the taxpayer so that his available revenue, following deduction of the tax may be similar to that obtained with the existence of the tax exception.

**Source:** Based on Dirk-Jan Kraan's proposed estimation methods.

For an adequate evaluation and control of tax expenditures it is essential to count on their individualized estimates, for which purpose the previous identification process is fundamental. Together with the identification of the exceptions, we should analyze which are the information sources available and which will be the most appropriate technique for making the estimate. For such purpose we should consider the type of exception and the referential tax; however, it will be a determinant factor to be aware of the availability of the information for the estimate; that is, the types and reliability of the information sources to be used.

The most appropriate and reliable source for making estimates are the tax data bases, disaggregated case by case or taxpayer by taxpayer. Although such openness may not be determinant for estimating the tax expenditure -for example, the case of taxes with proportional rates where we could estimate the collection impact on the basis of certain aggregated statistics of the returns-, the case by case

analysis or estimation with microsimulation provides additional richness since it allows us to make additional evaluations of the fiscal cost. Some examples are: the distribution of revenue following the tax expenditure, the utilization level according to the taxpayers' economic dimension, the breakdown of the tax sacrifice according to different dimensions -economic activity sectors, or else, its geographical distribution-.

That is, beginning with the tax micro-data, the information may be added in the most diverse manners for carrying out the pertinent cost analyses. In the case of taxes with progressive rates, the estimation based on microsimulation becomes obligatory in order to have a precise estimate of the economic impact of specific benefits.

## **3** The practice of reporting tax expenditures in CIAT member countries

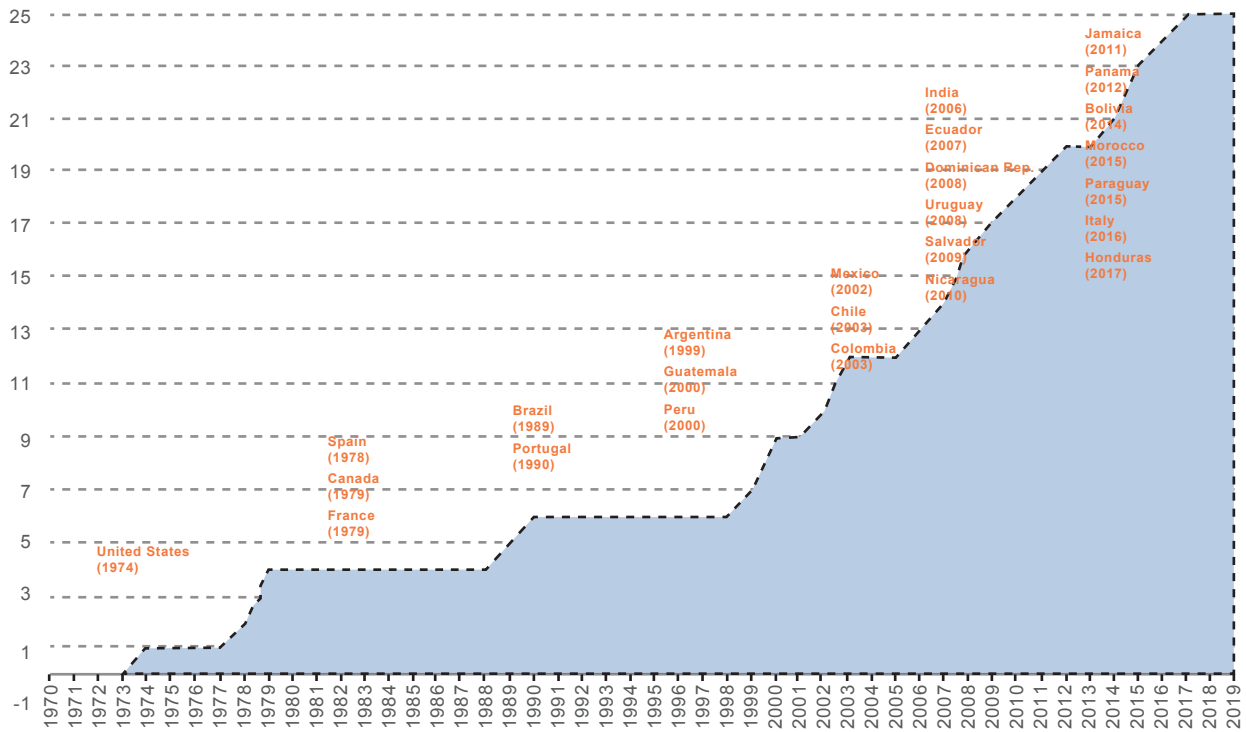
The goal of this work is to study practices related to the identification of exceptions, the quantification of tax expenditures and the publication of reports on Tax Expenditures of CIAT member countries, from both a qualitative and a quantitative perspective. To this end, each of the member countries' public reports was accessed, the information contained in CIAT's Tax Expenditure Database (TEDLAC) was explored, and in addition, as a complement to these two sources of information, a questionnaire was disseminated among the member countries with the objective of systematizing some of the elements considered relevant to collect.

### **3.1 Evolution of the Tax Expenditure reports practice in CIAT member countries**

Currently, from more than 40 CIAT member countries, 26 of them publish their tax expenditure studies. Since the early 1970s, the number of countries that joined those that estimate and report periodically on this topic has been increasing.

GRAPH 1

## Number of CIAT countries that publish reports 1970 - 2018



**Source:** Prepared by the authors based on the legislation attached to the countries' tax expenditure reports and response to the CIAT 2019 survey.

The figure shows the gradual appearance of more reports over the years, with the United States being the pioneer, followed by Spain, France and Canada. From the years 2000, there has been a surge of first reports. The last group to be integrated according to the information used for this analysis were: Jamaica, Panama, Bolivia, Morocco, Paraguay and Honduras. In any case, there are still a good number of countries that must incorporate this practice.

In addition to being able to identify since when each country submits these reports, we investigate who are responsible for preparing them.



Following Heady & Mansour (op.cit.), institutional arrangements for reporting tax expenditures should prioritize the integrity of estimates by improving transparency in tax management and providing relevant analysis to inform not only the legislative authority but also other potential stakeholders. This paper presents what its authors call “minimum requirements” to ensure this transparency. For these authors, the preparation of tax expenditure reports should be centralized in the Ministry of Finance and not in each of the executing units that have responsibility for that exception. In this way the criteria and definitions of the scope of the work are centralized. In particular, they propose that this work should be carried out by the fiscal policy units of these secretaries. In turn, this body should oversee legislation that involves the introduction, suppression or modification of tax expenditures and should be the only government institution to raise and exchange on these exceptions with parliament. For their part, Tax Administrations must be effective data providers and must have the necessary power to request additional information from taxpayers on their activities that benefit from tax expenditures. They will also be information providers, other ministries, national statistical institutions, etc.

Our work investigated who is responsible for the preparation of these reports. In order to do so, the reports themselves were analyzed, as well as the legal provisions that require them to be submitted, and the response to the questionnaire sent to the Tax Administrations. In contrast to the suggestion of the authors cited above, in a number of countries the responsibility for tracking tax expenditures rests with the Tax Administrations themselves, so they do not officiate only as suppliers of inputs for estimation. In a large number of countries, the Ministries of Finance are responsible for following up this study.

The following table identifies, for each CIAT member country that publishes tax expenditure reports, which agency or bodies are responsible for this work. In most cases, the work of preparing these studies is carried out by the Finance Ministries of the countries, the Tax Administrations or both acting jointly<sup>6</sup>.

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6 A particular case is that of the United States, where the estimates of tax expenditures are made by the Office of Tax Analysis, within the Department of the Treasury, in conjunction with the Joint Committee on Taxation, a nonpartisan committee of the U.S. Congress. Fiscal expenditures are published by the Office of Management and Budget in the U.S. Government Budget.

### CHART 3

#### Agency responsible for the estimates and publication of the report

COOUNTRY	FIRST PUBLICATION	AGENCY RESPONSIBLE FOR THE ESTIMATES AND PUBLICATION OF THE REPORT
Argentina	1999	National Directorate for Tax Research and analysis / Ministry of Finance
Bolivia	2014	Ministry of Economy and Public Finance
Brazil	1989	The Federal Revenue of Brazil (Receita Federal do Brasil - RFB)
Canada	1979	Department of Finance Canada
Chile	2003	The internal Tax Service, + Budget Directorate of the Ministry of Finance
Colombia	2003	Special Administrative unit Directorate of Taxes and National Customs – DIAN, / Ministry of Finance and Public Credit
Ecuador	2007	The Internal Revenue Service, Tax Administration in Ecuador.
Salvador	2009	Unit of Tax Studies /General Directorate of Internal revenue / Ministry of Finance
Spain	1978	State Secretariat for budgets and Expenditure - Ministry of Finance
United States	1970 or 1974	The Office of Tax Analysis, within the Department of the Treasury, and the Joint Committee on Taxation
France	1979	Ministères de l'économie et des Finances
Guatemala	2000	Superintendence of Tax Administration
Netherlands		The Netherlands Ministry of Finance
Honduras	2017	Secretary of Finance * The Revenue Administration Service (SAR)
India	2006	Ministry of Finance Department of Economic Affairs
Italy	2016	Commission appointed by decree of the Economy and Finance Ministry
Jamaica	2011	The Ministry of Finance and the Public Service; / Ministry's Taxation Policy Division
Morocco	2015	Ministères de l'économie et des Finances
Mexico	2002	The Secretariat of Finance and Public Credit
Nicaragua	2010	Ministry of Finance and Public Credit-Directorate for Economic Studies
Panama	2012	Ministry of Economy and Finance Directorate General of Income Tax Studies
Paraguay	2015	Ministry of Finance, State Secretariat of Taxation
Peru	2000	Superintendency for National Customs and Tax Administration (SUNAT)
Portugal	1990	Ministry of Finance
Dominican Rep.	2008	The Ministry of Finance in coordination with its dependencies: The Directorate General of Internal Taxes (DGII) and The General Directorate of Customs (DGA)
Uruguay	2008	General Taxation Directorate - Uruguay. / Ministry of Economy and Finance.

**Source:** Prepared by the authors based on legislation attached to the countries' Tax Expenditure reports and response to the CIAT 2019 survey.

We must bear in mind that it is normally the government, through the Ministry of Finance of each country, who submits to the parliament the laws of accountability for the budgetary expenditure each year. When Tax Expenditure reports are incorporated into these accounting laws, they are treated as such, so it is natural that the body responsible for this report is the Ministry of Finance, even when this body is not responsible for the process of identifying items and estimating tax expenditures.

Frequently, it is the Tax Administrations who have the technical responsibility of carrying out the entire process of maintaining the inventory of tax expenditures and making the estimates, submitting the report to the Ministry of Finance who sends it to Parliament. This practice occurs in a large number of CIAT member countries, and is mainly the result of the high specialization in tax revenues of the administrations, their proximity to the main sources of information (tax returns, and diversity of tax-related reports).

### **3.2 Best practices identified in the reports**

From the comparative review of these reports, both by countries with experience in their preparation and by those who have most recently adopted this practice, we see that there is no consistency with the elements that they should include. We can also mention those most commonly found in these documents: a general definition of tax expenditure, a description of the reference framework for each of the taxes under analysis, a description of each of the items identified as tax expenditure, a compilation of the tax rules that give rise to each benefit, the results found, as well as the projection of the tax expenditures for future periods. The latter component is mainly included in those reports that are integrated into the budget and accountability laws.

This review allows us to highlight some reports as models. Canada's report, for example<sup>7</sup>. The work of this country has a very clear demarcation of the reference tax system, defining for each tax: the unit of taxation, the period of taxation, the tax base, the aliquots and scales, the treatment of inflation, the treatment of exceptions introduced to avoid double taxation, among others.

This work highlights the presence of the exceptions descriptions, a good practice that we have mentioned in previous points, which is of great help to the policy maker to have in hand all the elements that matter to each particular exception in their review.

The following figure presents a clipping of the Canada Tax Expenditure report where we can view the format of the identification file characterization and presentation of the individual results of each estimate.

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7 Report on Federal Tax Expenditures. Concepts, estimates and evaluations. Department of Finance, Ministry of Finances. Canada. 2018

**FIGURE 1**

**Excerpt of exception files. Tax Expenditure Report Canada**

Exemption from GST for ferry, road and bridge tolls									
Description	Ferry services and road and bridge tolls are generally exempt from GST. The exemption does not include international ferry services, which are zero-rated, consistent with other international transportation services.								
Tax	Goods and Services Tax								
Beneficiaries	Households								
Type of measure	Exemption								
Legal reference	Part VIII of Schedule V and section 14 of Part VII of Schedule VI to the Excise Tax Act								
Implementation and recent history	<ul style="list-style-type: none"><li>This measure has been in effect since the inception of the GST in 1991.</li></ul>								
Objective – category	To achieve a social objective								
Objective	This measure ensures that the use of Canada's highway systems and related infrastructure will not be subject to tax (Goods and Services Tax: Technical Paper, August 1989).								
Category	Non-structural tax measure								
Reason why this measure is not part of benchmark tax system	GST exemptions are deviations from a broadly defined value-added tax base.								
Subject	Social								
CCOPOG 2014 code	70451 - Economic affairs - Transport - Road transport								
Other relevant government programs	Programs within the mandates of Canadian Heritage, Immigration, Refugees and Citizenship Canada, Transport Canada and Public Safety Canada (among other departments) also support various other social objectives. Additional information on the relevant Government programs is provided in the table at the end of Part 3.								
Source of data	Statistics Canada, Supply and Use Tables and National Income and Expenditure Accounts								
Estimation method	Goods and Services Tax model								
Projection method	Goods and Services Tax model								
Number of beneficiaries	No data is available.								

Cost information:

Millions of dollars	2012	2013	2014	2015	2016 (P)	2017 (P)	2018 (P)	2019 (P)
Goods and Services Tax	10	10	10	15	15	15	15	15

**Source:** Report on Federal Tax Expenditures. Concepts, estimates and evaluations. Department of Finance, Ministère des Finances. Canada. 2018. Page 133 exemption from sales tax on goods and services (GST), for ferry, road and bridge tolls

On the other hand, the work of Brazil is also remarkable for its rigor in the presentation of the frame of reference and the methodology as well as for its very good presentation of the results. In addition to having a broad expression of the concept of tax expenditure and the reference tax system, it has a very wide display of the estimated results at the level of diversity of dimensions: by budgetary function, by region, by mode of expenditure, by type of tax.

### **3.3 Quantitative evaluation of tax expenditures**

In this section we will present the tax expenditures results of CIAT member countries.

On previous occasions we have addressed this issue but only reaching the countries of Latin America and the Caribbean. This work therefore constitutes a leap in the scope of the number of countries analyzed. Valuable work was incorporated, especially from countries that are pioneers worldwide in the identification, estimation and reporting of this phenomenon. The countries that are included in this analysis in relation to our previous delivery are: United States, Canada, France, Italy, Spain, India, Morocco and Portugal, and we also update the information of the other 16 countries that make up our Tax Expenditure database.

Access to quantitative information on each country's tax expenditures was made by directly analyzing the most recent official reports. In turn, this information was supplemented by the exploitation of the information contained in the CIAT tax expenditure database (TEDLAC). TEDLAC is formulated from the systematic recording of the information contained in the reports, with openness to the highest level of disaggregation permitted in each report. In total our database has registered 6046 items of tax expenditures included in the latest reports of the countries analyzed.

The exploitation of TEDLAC data allows us to know the relationship between tax expenditure and GDP of each country, their evolution over the periods included in the analysis, as well as the distribution of the data according to the most relevant tax categories, where exceptions were found (value added taxes, personal and business income taxes, selective taxes, tax on Foreign Trade, property, etc.). It is

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8 Demonstrativo dos Gastos Governamentais Indiretos de Natureza Tributária Bases Efetivas. Centro de Estudos Tributários e Aduaneiros. Receita Federal

also possible to know the amount and cumulative amounts of collection losses attributable to each type of tax expenditure (exonerations, reduced aliquots, deductions, credits, etc.).

The information, as provided for in the database, enables tax expenditure to be distributed according to the budgetary sectors most associated with the measure under analysis, which is classified according to the proposal included in the CIAT Manual (Education; Health and Sanity; Housing; Development and decentralization; agricultural and industrial activities; energy and mining; etc.). In the process of registration each item of tax expenditure was classified as a tax benefit or as a tax incentive. Among the first are all tax expenditures associated with public social spending, while those tax expenditures that are presented for the purpose of promoting a specific economic activity were classified as tax incentives.

### **3.4 Weight of tax expenditures on the economy of CIAT member countries**

The reading of the reports of the countries that we had not reached in the past opportunities, allows us to appreciate that the information is able to be registered in the same model of the TEDLAC, so they may be incorporated in the next updates of this database.

Below are the results of each country's total tax expenditure relative to the Gross Domestic Product. It is important to note that the presentation of the results in this way and the contrast of the results between the countries is by way of reference since the different works differ in the scope of their study, both as regards the amount of taxes included in the analysis as well as the greater or lesser extent of the referred tax and its correlate with a lesser or greater basis for estimating the tax expenditures.

On the other hand, the total tax expenditure on the GDP would imply that all exceptions would be "lifted" at the same time and that in turn there would be no overlapping effect between the different measures. In turn, reading several of the country reports, it can be seen that it is common for countries not to add up tax expenditures but simply to expose them one by one by identifying them. For example, Canada, the United States or Uruguay.

# CHART 4

## Tax expenditures on Gross Domestic Product, CIAT member countries

COUNTRY	LAST ACCOUNTING YEAR	T-2	T-1	T
Argentina	2017	2.6%	2.7%	3.0%
Bolivia	2013	1.0%	1.3%	1.3%
Brazil	2016	4.5%	4.5%	4.2%
Canada	2018	6.2%	6.2%	6.3%
Chile	2018	3.4%	3.4%	3.0%
Colombia	2018	8.2%	8.0%	8.0%
Costa Rica	2016	5.0%	4.9%	5.3%
Ecuador	2017	4.7%	4.6%	4.7%
Salvador	2017	3.8%	3.7%	3.5%
Spain	2018	3.1%	2.7%	2.9%
United States	2018	7.6%	7.6%	6.7%
France	2018	3.9%	4.1%	4.2%
Guatemala	2016	2.5%	2.5%	2.3%
Honduras	2017	6.6%	6.9%	6.8%
India	2018	2.1%	1.8%	1.6%
Italy	2018	3.2%	3.1%	3.0%
Jamaica	2016	4.4%	4.4%	3.6%
Morocco	2018	3.2%	2.7%	2.6%
Mexico	2018	3.3%	3.7%	3.7%
Nicaragua	2013	4.6%	5.0%	5.4%
Panama	2016	4.2%	4.1%	3.5%
Paraguay	2016	1.5%	1.3%	1.3%
Peru	2017	2.3%	2.1%	2.2%
Portugal	2018	5.9%	6.7%	6.5%
Dominican Republic	2018	6.5%	6.1%	5.9%
Uruguay	2017	6.5%	6.4%	6.4%
<b>Overall Average</b>		<b>4.3%</b>	<b>4.2%</b>	<b>4.2%</b>
<b>Latin America and the Caribbean (LAC)</b>		<b>4.2%</b>	<b>4.2%</b>	<b>4.1%</b>
<b>North America and Europe -selected countries (NAEsc)</b>		<b>5.0%</b>	<b>5.1%</b>	<b>4.9%</b>

**Source:** Own elaboration on the basis of: 1) tax Expenditures: a Database of Tax Expenditures, CIAT + Tax Expenditures Reports of the member Countries; 2) GDP: GDP Statistics of each country, drawn from the collection of the WEO/IMF.



We can see that the relationship between tax expenditure and GDP is relevant, if we consider that this is income that is being renounced as a result of the total diversity of policies implemented through exceptions introduced in the tax system of each country. The simple average for all countries is in about 4.2%. That is to say, on average the countries waive some amounts equivalent to that percentage of the product to execute certain policies through this instrument.

If we consider only the countries of Latin America and the Caribbean, the average tax expenditure on GDP is similar to the overall average. The values found for this region alone are above those determined in the previous update of this information by CIAT<sup>9</sup>.

This change in the average results of the region is a consequence of the replacement, in this update, of previous reports with new ones, which resulted in changes in their results. This is the case, for example, of Colombia, a country that in its new report shows a tax expenditure with a greater scope regarding the taxes it analyses and a result much higher than it showed in previous reports<sup>10</sup>.

On the other hand, the selected countries of North America and Europe comprise Canada, Spain, the United States, France, Italy and Portugal and show tax expenditures results in relation to GDP in the order of 5%<sup>11</sup>.

In the following chart we present, for a better visualization, the main descriptive statistics of the distribution resulting from the TE/GDP ratio for the average of the last three years of the countries analyzed and the histogram of absolute frequencies of cases according to frequency intervals.

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9 Overview of Tax Expenditures in Latin America: Main statistics of the CIAT Database. CIAT 2018

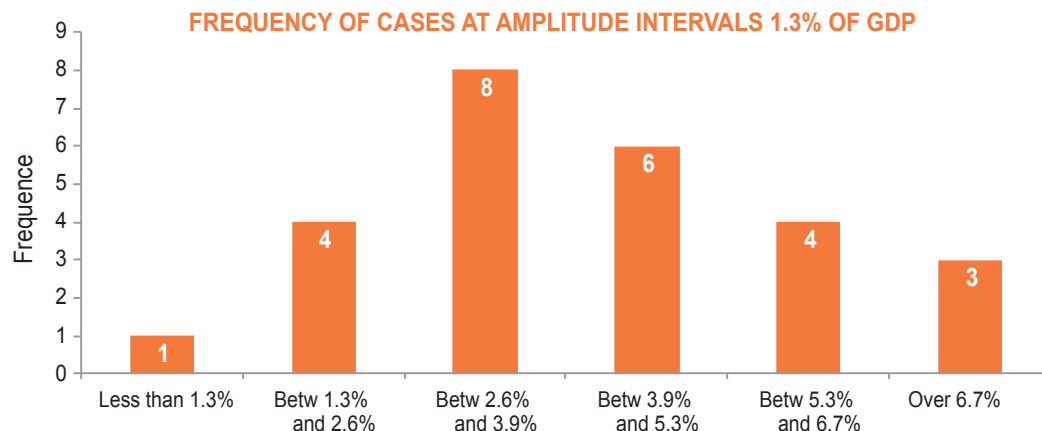
10 Previous report from Colombia included in the TEDLAC: tax expenditure in Colombia. Benefits in the income tax and CREE –legal persons taxable Years 2013 - 2014 - Coordination of Economic Studies sub-Directorate of Management Analysis Operational Direction of Organizational Management. Report used in this report: **medium-term fiscal framework 2019. Ministry of Finance and Public Credit.**

11 As it is exposed to the classification of countries into two groups (Latin America and the Caribbean, and North America and Europe), Mexico was deliberately left in the Category Latin America and the Caribbean in order to maintain the comparability with the previous reports on Tax Expenditures, covering the region of Latin America and the Caribbean and including Mexico.

## GRAPH 2

### Descriptive statistics and tax expenditure frequency histogram on GDP in CIAT member countries

GT PROM	
Average	0,0422
Typical Error	0,0037
Median	0,0400
Mode	
Standard deviation	0,0188
Sample variance	0,0004
Curtosis	0,7734
Asymmetry coefficiente	0,3246
Range	0,0684
Minimum	0,0121
Maximum	0,0805



It can be seen that the minimum value (average of the last 3 years exposed) is 1.2% and corresponds to Bolivia for the average 2011-2013 period (source: TEDLAC)<sup>12</sup>. For its part, the highest value found reaches 8.1% of GDP on average for the 2016-2018 three-year period, comes from the *Medium-Term Fiscal Framework report* of the Ministry of Finance and Public Credit of Colombia and was corroborated by the response to the survey sent by that country.

<sup>12</sup> At the time of completion of this work, Bolivia's New Tax Expenditure Report was accessed, which in the latest TEDLAC update had not been considered because it was not available. This country updated its study until 2016. For that year the Tax Expenditure on the GDP stood at a value equivalent to that exposed here (1.2%).

We can observe that the most frequent interval is between 2.6% and 3.9% of the product (the result of 8 countries is located in that interval), observing an asymmetric distribution to the right, which explains the fact that the average is located in the interval following the mode.

From the observation of the last three records, we appreciate that this relationship is quite stable, with no major ups and downs at the level of each country, which can make us think that much of the tax expenditure is structural, or rather rigid, in terms of their revision. The most important observable decreases are: United States, last record decreases by 0.9% of GDP; Jamaica, by 0.8% of GDP; Panama, by 0.6% of GDP. On the side of the increases in the TE relative to production we can highlight: Argentina, last record shows increase of 0.3% of GDP; Costa Rica, 0.4% of GDP; Nicaragua 0.4% of GDP.

The opening up of the tax figures considered in each report allows us to visualize how tax expenditure is distributed in the countries. First of all, it is important to note that some countries only record tax expenditures corresponding to the central government, or in the case of the Federations of states, only to the exceptions that impact on the collection of the Federation. It is the case of the United States that does not report for the exceptions that states may even introduce into the retail sales (Sales Tax). Brazil, for its part, does not register exceptions in the tax on the circulation of goods and services (ICMS). Both taxes would be classified as general taxes on consumption and, as shown in the table below, have little relative weight in both countries.

When we look within the tax expenditure, we can see that, especially in Latin American countries, which are highly dependent on VAT on their tax revenues, there is a significant amount of tax expenditure in this instrument. The average of the Tax Expenditure on GDP only for the countries of Latin America is above the overall average of tax expenditures (2.3%, 2.1%), while for the selected countries of North America and Europe this value came in at 1.5%, in the reports corresponding to the last financial year. This relationship is reversed when we analyze tax expenditure on the personal income taxes.

The Tax Expenditure on VAT represent on average almost 50% of all the Tax Expenditure of the countries, with some cases well above this average, such as Colombia with a 6.6% of GDP or Nicaragua, with a 4.2%. Portugal also shows a high TE for VAT register, reaching 3.9% of GDP.

After VAT, the second one is the tax waiver for the existing exceptions in taxes on the income of individuals. Here we highlight the cases of the United States, Canada, France and Italy. As far as we can say that, just as in Latin America, VAT has a greater weight and a greater Tax Expenditure, in the more developed countries, there is an inverse relationship, the collection of taxes that tax income, and especially individuals, have a greater weight in the collection and there is also a greater incidence of tax expenditure on the product. In fact, the average PIT Tax Expenditure on GDP for the countries of Latin America is 0.5%, whereas this ratio reaches to 2.8 points of GDP for selected countries in North America and Europe.

CHART 5

Tax expenditures by tax category, last period of each country

COUNTRY	GENERAL CONSUMPTION TAXES	PERSONAL INCOME TAX	CORPORATE INCOME TAXES	EXCISE TAXES	PROPERTY TAXES	OTHER	TOTAL
Argentina	1.4%	0.3%	0.4%	0.4%	0.1%	0.4%	3.0%
Bolivia	1.0%	s/e	0.1%	s/e	s/e	0.2%	1.3%
Brasil	1.5%	0.7%	0.9%	0.0%	0.0%	1.2%	4.2%
Canadá	1.0%	4.4%	0.8%	s/e	s/e	s/e	6.3%
Chile	0.8%	1.2%	1.0%	0.0%	s/e	s/e	3.0%
Colombia	6.6%	0.6%	0.7%	0.0%	s/e	s/e	8.0%
Costa Rica	3.1%	1.1%	0.9%	0.1%	s/e	0.1%	5.3%
Ecuador	2.4%	0.7%	1.3%	0.2%	0.1%	0.1%	4.7%
Salvador	1.8%	1.7%	s/e	s/e	s/e	s/e	3.5%
Spain	1.7%	0.8%	0.3%	0.1%	0.0%	0.1%	2.9%
United States	s/e	5.9%	0.8%	s/e	s/e	s/e	6.7%
France	0.9%	2.7%	0.2%	0.3%	0.1%	0.1%	4.2%
Guatemala	1.4%	0.1%	0.7%	0.0%	0.0%	0.0%	2.3%
Honduras	3.7%	0.7%	1.9%	0.5%	s/e	s/e	6.8%
India	s/e	0.4%	0.5%	0.4%	s/e	0.4%	1.7%
Italy	0.1%	2.2%	0.2%	0.2%	s/e	0.4%	3.0%
Jamaica	1.9%	0.0%	0.1%	0.3%	s/e	1.2%	3.6%
Morocco	1.4%	0.4%	0.4%	0.0%	s/e	0.4%	2.6%
Mexico	1.4%	1.0%	0.5%	0.0%	s/e	0.8%	3.7%
Nicaragua	4.2%	0.0%	0.3%	0.0%	s/e	0.9%	5.4%
Panama	2.2%	0.1%	1.2%	s/e	s/e	s/e	3.5%
Paraguay	0.9%	0.1%	0.2%	s/e	s/e	0.2%	1.3%
Peru	1.7%	0.2%	0.2%	0.0%	s/e	0.1%	2.2%
Portugal	3.9%	0.6%	0.6%	0.5%	0.4%	0.5%	6.5%
Dominican Republic	2.8%	0.1%	0.5%	0.9%	0.8%	0.7%	5.9%
Uruguay	3.7%	0.4%	1.1%	0.1%	1.1%	s/e	6.4%
<b>Overall Average</b>	<b>2.1%</b>	<b>1.1%</b>	<b>0.6%</b>	<b>0.2%</b>	<b>0.3%</b>	<b>0.4%</b>	<b>4.2%</b>
<b>Average LAC</b>	<b>2.3%</b>	<b>0.5%</b>	<b>0.7%</b>	<b>0.2%</b>	<b>0.4%</b>	<b>0.5%</b>	<b>4.1%</b>
<b>Average NAECsc</b>	<b>1.5%</b>	<b>2.8%</b>	<b>0.5%</b>	<b>0.3%</b>	<b>0.2%</b>	<b>0.2%</b>	<b>4.9%</b>

**Source:** Own elaboration on the basis of: 1) tax Expenditures: Database of Tax Expenditures, CIAT + Tax Expenditures Reports of member Countries;  
2) GDP: GDP Statistics of each country, drawn from the collection of the WEO/IMF.

Between the VAT and the two forms of taxation of the income we accumulate 90% of the value of the Tax Expenditure total average for the last exercise of analysis of each country. According to the greater or lesser extent of the reports, and of course the existence or not of other tax figures in each country, we observe that the Tax Expenditures appear with lesser relative weight in the selective taxes and in the property taxation, among others.

Another fact to note from the reading of the tax expenditure reports, is that most countries do not report tax expenditures in the taxes that Finance Social Security (in the table under the heading others), and those who do so include mainly national taxes that complement the collection of Social Security contributions.

This may be a consequence of that the taxes that have as purpose to fund this activity are collected by the entities of the social security itself, often independent from the scope of the Ministry of Finance. But the truth is that these taxes have a weight that is relevant in the total revenues of the countries, and deficits of the social security systems are a source of concern and very probably in all cases there are exceptions in these systems of taxation that should be relayed for their consideration.

### **3.5 Weight of tax expenditure in relation to the collection in CIAT member countries**

The aim of the tax system is to obtain sufficient income to finance public expenditures, guaranteeing a fair distribution of the tax burden, minimizing the negative effects on the economic efficiency that taxes produce, as well as the costs of administration and compliance with tax rules.

It is also an objective to consider *transparency*. According to Mirrlees (2011)<sup>13</sup> this objective has two dimensions: on the one hand the certainty, or absence of arbitrariness in the determination of the tax obligation and on the other the intelligibility of the tax rules. The introduction of exceptions in the tax system, alters the pre-existing balance, reduces tax collection capacity, and can positively or negatively transform its redistributive impact. Produces economic inefficiencies, due to the introduction of an exception disturbs the neutrality of the system, it affects the equity, placing some taxpayers into a privileged position and produces an increase of the compliance costs to the extent that it complicates the tax system, reducing its transparency.

Much of the countries under analysis, especially those in Latin America, should improve their income/expenditure ratios in order to reduce their deficits. Among the factors that influence the improvement of the fiscal position, the collection capacity as well as the degree and effectiveness of public spending are a priority. In this context and focused on the point that interests us, it is good to ask ourselves: *how much can our countries improve their tax collection capacity?* In addition to quantifying, tracking and projections of tax revenues, it is essential to estimate, quantify and forecast both the tax evasion and tax expenditures. The knowledge of the dimension of each one of these elements will allow us to infer what may be the tax *revenue increase*, both by the reduction in non-compliance and of the existing exceptions in the system.

This section shows the relationship between the Tax Expenditure Statistics we have previously presented and the collection statistics of the countries analyzed. Accepting that the sum of tax expenditures is a reference to what would be collected in the absence of these exceptions, the sum of these two concepts gives us an idea of what potential tax revenues countries could dispose of in the absence of tax expenditures.

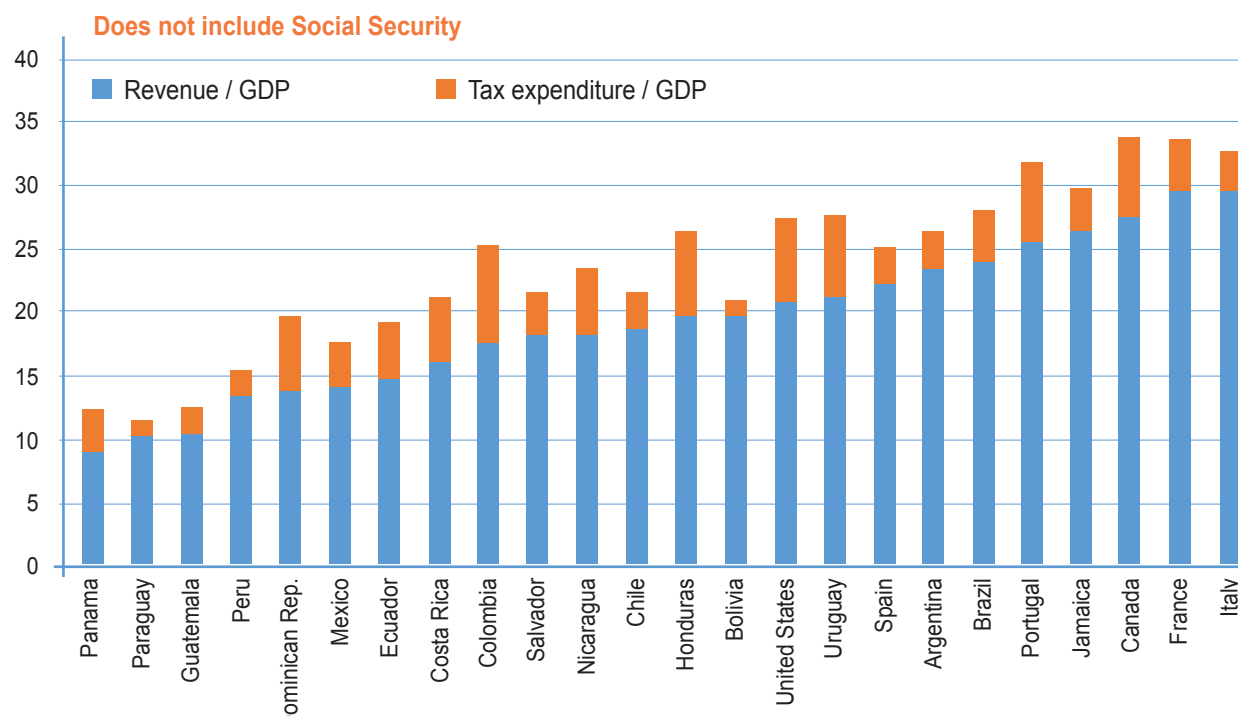
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13 Mirrlees, James, Adam, Stuart; Besley, Timothy; Blundell, Richard; Bond, Stephen; Chote, Robert; Grammie Malcolm; Johnson, Paul; Myles, Gareth & Poterba, James. Tax by Design. Institute of Fiscal Studies. 2011. This work seeks to present an optimal tax design, for which it identifies as basic principles or objectives of the tax system, the collection objectives, redistributive objectives, those related to economic efficiency, those related to equity, in the sense of fair sharing of the tax burden, those related to the costs of administration and compliance and the objectives related to transparency. (pp.XXVI-XXVII). For the authors, the first two principles deal with value judgments, while the others deal with economic considerations.

The revenue statistics used for this contrast come from two main sources. On one side of the Tax Revenue Database built by the IDB and CIAT<sup>14</sup>. According to this publication these statistics consider the taxes collected by central, national or federal governments, as well as the ones collected by sub-national governments and Social Security contributions. They are available up to and including 2018 and cover nearly all countries in Latin America and the Caribbean. In addition, in order to contrast past records and incorporate countries that are not included in these statistics, the OECD tax statistics series was used<sup>15</sup>.

**GRAPH 3**

**Collection and tax expenditures relative to GDP**



14 <https://www.ciat.org/base-de-datos-de-recaudacion-bid-ciat/>

15 <http://www.oecd.org/tax/tax-policy/tax-database/>



The graph describes all countries under analysis according to the tax burden relative to current GDP (blue bars). This includes all tax collection concepts with the exception of the social security contributions. This exclusion is a consequence, as previously mentioned, that the greater part of the tax expenditure reports does not contain estimates of loss of revenue in social security contributions. For this reason, they are excluded from the tax collection base in order to improve the conditions of comparability between the total collection and the total tax expenditure.

It can be seen, first of all, that in all countries, tax expenditure has a significant weight in relation to the total revenue observed. For its part, if we consider as *potential revenue* the simple sum of tax expenditure and revenue, we would find that several countries would considerably improve their current relative position. For example, Colombia, Honduras, the United States or Uruguay would have considerable higher records if there were no exceptions in their tax system, while Canada would be the country with the highest tax burden under the same hypothesis.

Within the main taxes the conclusions are similar, and we will see that according to the countries, those figures that are most relevant in their collection are also relevant in relation to their Tax Expenditures. The following table (Table 6) aims to compare the overall weight of tax collection against GDP and the weight of tax expenditure against the same macroeconomic variable.

The first column “**Revenue/GDP**” presents the fiscal pressure, collected from the two sources of information mentioned, as well as the ratio of the collection on GDP of the two main sets of taxes that form part of the tax systems of the countries under analysis: on the one hand the general taxes on consumption (mainly value added taxes and taxes on retail sales) and on the other the taxes on income (mainly tax on the income of natural and legal entities).

As can be seen, the sum of these two concepts (general consumption taxes + income taxes) is lower than the value of the total fiscal pressure column. This is a consequence of the exclusion of all other tax instruments, in order to contrast only the most relevant concepts (VAT and income). That is to say, the difference with the Total fiscal pressure that appears in the table is equal to the weight of the other taxes that each country collects, according to these statistics. The collection amounts related to social security contributions were excluded.

This is a consequence of the fact that, as noted above, most countries do not estimate or report tax expenditures for these tax figures, so their exclusion serves to improve the comparability between tax collection and tax expenditure.

After the settings mentioned above the selected countries from Europe and North America have an average fiscal pressure of 25.8%, while for the countries of Latin America and the Caribbean it is 17.1%.

The second column, “**Tax Expenditures / Revenue Potential**”, presents the result of the quotient between the concepts of tax expenditure associated with each collection item, exposed in the previous quadrant, divided the revenue plus tax expenditure. *Revenue Potential* to these effects is the sum of the collection plus the tax expenditure. This measure allows us to appreciate how much eroded are the bases of each set of taxes and of the total collection for the exceptions existing in each tax system. At the general level (simple average), the tax expenditure reaches 17.3% of potential revenue.

**CHART 6**

**Current fiscal pressure, impact of tax expenditures  
on potential tax collection and equivalent fiscal pressure  
in the absence of tax expenditures. CIAT member countries**

COUNTRY	REVENUE / GDP*			TAX EXPENDITURES/ REVENUE POTENTIAL*			FISCAL PRESSURE IN ABSENCE OF TAX EXPENDITURES	
	GENERAL CONSUMPTION TAXES	INCOME TAXES	TOTAL FISCAL PRESSURE*	GENERAL CONSUMPTION TAXES	INCOME TAXES	TOTAL TAX EXPENDITURES	POTENTIAL TAX PRESSURE	INCREASE OF FISCAL PRESSURE*
Argentina	14.5	5.3	23.4	9%	11%	11%	26.4	13%
Bolivia	13.1	4.1	19.7	7%	2%	6%	21.0	7%
Brazil	13.1	7.0	23.9	10%	18%	15%	28.1	18%
Canada	7.7	15.4	27.6	12%	5%	18%	33.9	23%
Chile	11.0	7.0	18.7	7%	24%	14%	21.7	16%
Colombia	7.7	6.2	17.4	46%	18%	31%	25.4	46%
Costa Rica	8.8	4.8	16.0	26%	29%	25%	21.3	33%
Ecuador	10.4	4.0	14.7	19%	33%	24%	19.4	32%
Salvador	10.3	7.0	18.1	15%	20%	16%	21.6	19%
Spain	9.8	9.7	22.2	15%	10%	12%	25.1	13%
United States	4.3	12.4	20.8	0%	35%	24%	27.5	32%
France	11.3	10.9	29.4	7%	21%	13%	33.6	14%
Guatemala	6.4	3.7	10.3	18%	18%	18%	12.6	22%
Honduras	11.7	6.1	19.6	24%	30%	26%	26.4	35%
Italy	12.0	13.4	29.5	1%	15%	9%	32.5	10%
Jamaica	16.7	8.2	26.3	10%	2%	12%	29.9	14%
Mexico	6.4	7.2	14.1	17%	17%	21%	17.8	26%
Nicaragua	10.7	6.9	18.1	18%	5%	23%	23.5	30%
Panama	4.2	4.0	8.9	35%	24%	28%	12.4	39%
Paraguay	7.6	2.3	10.2	10%	11%	11%	11.5	13%
Peru	7.2	5.7	13.3	19%	7%	14%	15.5	17%
Portugal	13.8	9.8	25.4	22%	11%	20%	31.9	26%
Dominican Rep.	8.9	4.3	13.8	24%	13%	30%	19.7	42%
Uruguay	11.5	7.5	21.2	24%	17%	23%	27.6	30%
<b>Average</b>	<b>10.0</b>	<b>7.2</b>	<b>19.3</b>	<b>16.9%</b>	<b>17.3%</b>	<b>18.6%</b>	<b>23.6</b>	<b>23.7%</b>
<b>Average LA</b>	<b>10.0</b>	<b>5.6</b>	<b>17.1</b>	<b>19.3%</b>	<b>16.5%</b>	<b>19.4%</b>	<b>21.2</b>	<b>25.1%</b>
<b>Average NAEsc</b>	<b>9.8</b>	<b>11.9</b>	<b>25.8</b>	<b>9.4%</b>	<b>19.5%</b>	<b>16.1%</b>	<b>30.8</b>	<b>19.7%</b>

**Source:** Own elaboration on the basis of: 1) Database of Tax Expenditures, CIAT + Tax Expenditures Reports of the member Countries; 2) Database of Fund-IDB-CIAT; 3) statistics of tax in the OECD.

The **last column** of Chart 6 - “**Fiscal pressure in the absence of tax expenditures**” shows what the fiscal pressure would be if all tax expenditures were abolished (column: “Potential fiscal pressure”).

This allows us to determine an *increase in fiscal pressure* (column: “Increase of fiscal pressure”), as the variation in fiscal pressure under this hypothesis. This is a theoretical exercise, since on the one hand the exceptions would not all be lifted together, and if this were to happen it would not necessarily result in the levels of collection equivalent to the reported loss, because of the generalization in the use of the revenue foregone method for the estimates, as well as the fact that the estimates are made individually and many of the exceptions have some degree of redundancy among themselves.

The Fiscal pressure of the countries of Latin America (excluding SSCC), under the assumption that all the exceptions that give rise to tax expenditure would be eliminated and that this elimination would imply an increase in the equivalent collection, would go from 17.1% to 21.2%, which would imply an increase of 25.1%. For its part, the fiscal pressure of the selected countries of North America and Europe would increase by 19.7% from 25.8% to 30.8% of GDP.

While the tax expenditures in relation to the product, in selected countries of North America and Europe are higher than in the Latin America and the Caribbean countries (Chart 4), the loss of revenue from those relating to the potential collection are lesser than those observed in the countries of Latin America and the Caribbean (Chart 6). This can give us the pattern that the countries of North America and Europe have a better monitoring of the exceptions that integrate their tax systems, to some extent due to their greater experience in the follow-up of this topic (Graph 1).

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