Domestic Resource Mobilization and Tax Expenditures

By

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1.Why Focus on DRM in LICs?

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- First, (domestic resource mobilization) or DRM is critical for financing the SDGs--on average, by 2030 LICs need to mobilize additional 5 percentage points of GDP from domestic sources to finance the SDGs in 5 key areas
- Second, DRM would help improve debt sustainability
- Third, it would help deal with COVD effects on revenues and expenditures
- Finally, it would contribute to fiscal consolidation going forward

2. What have LICs achieved in the past 20 years?

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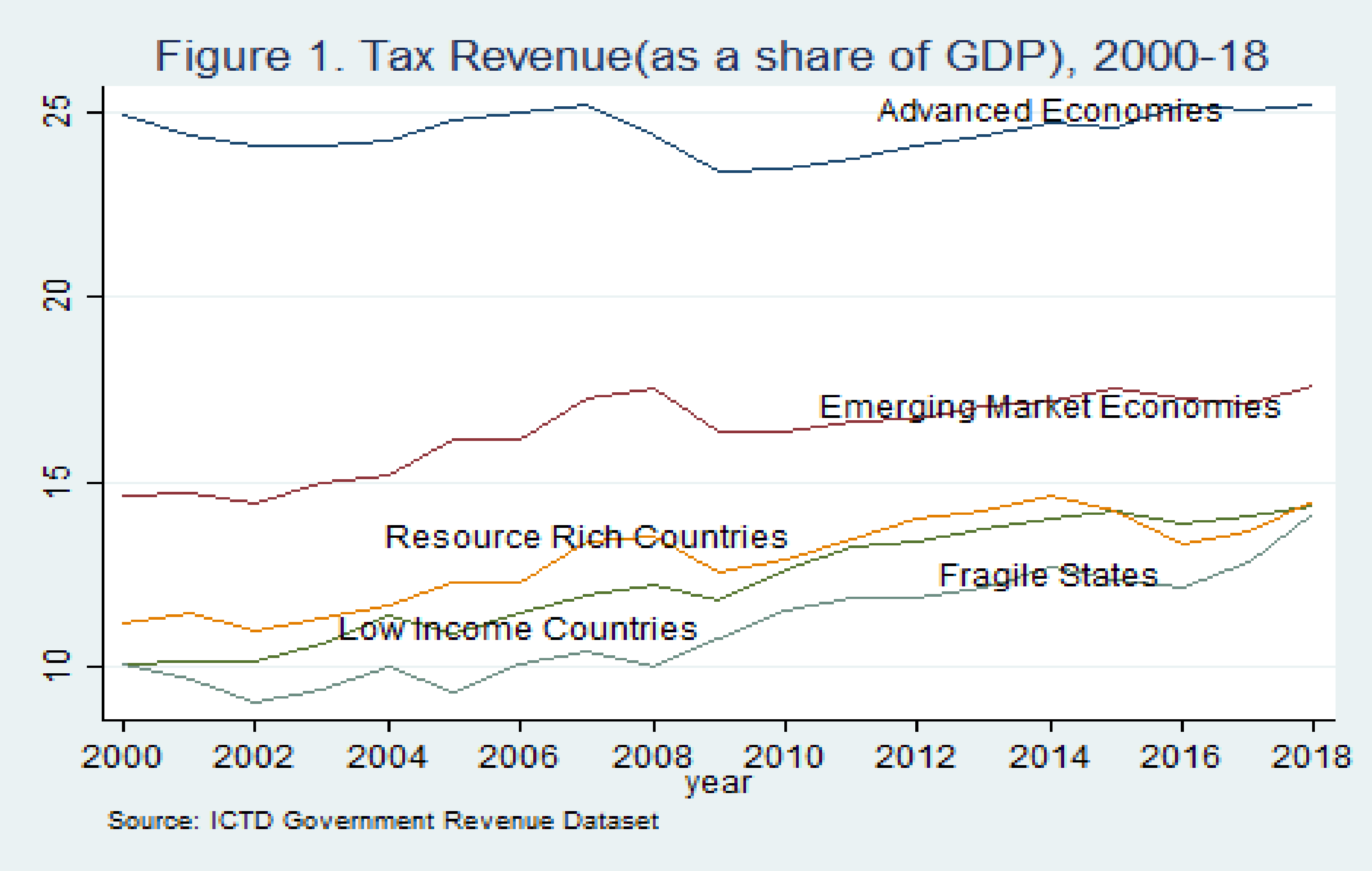
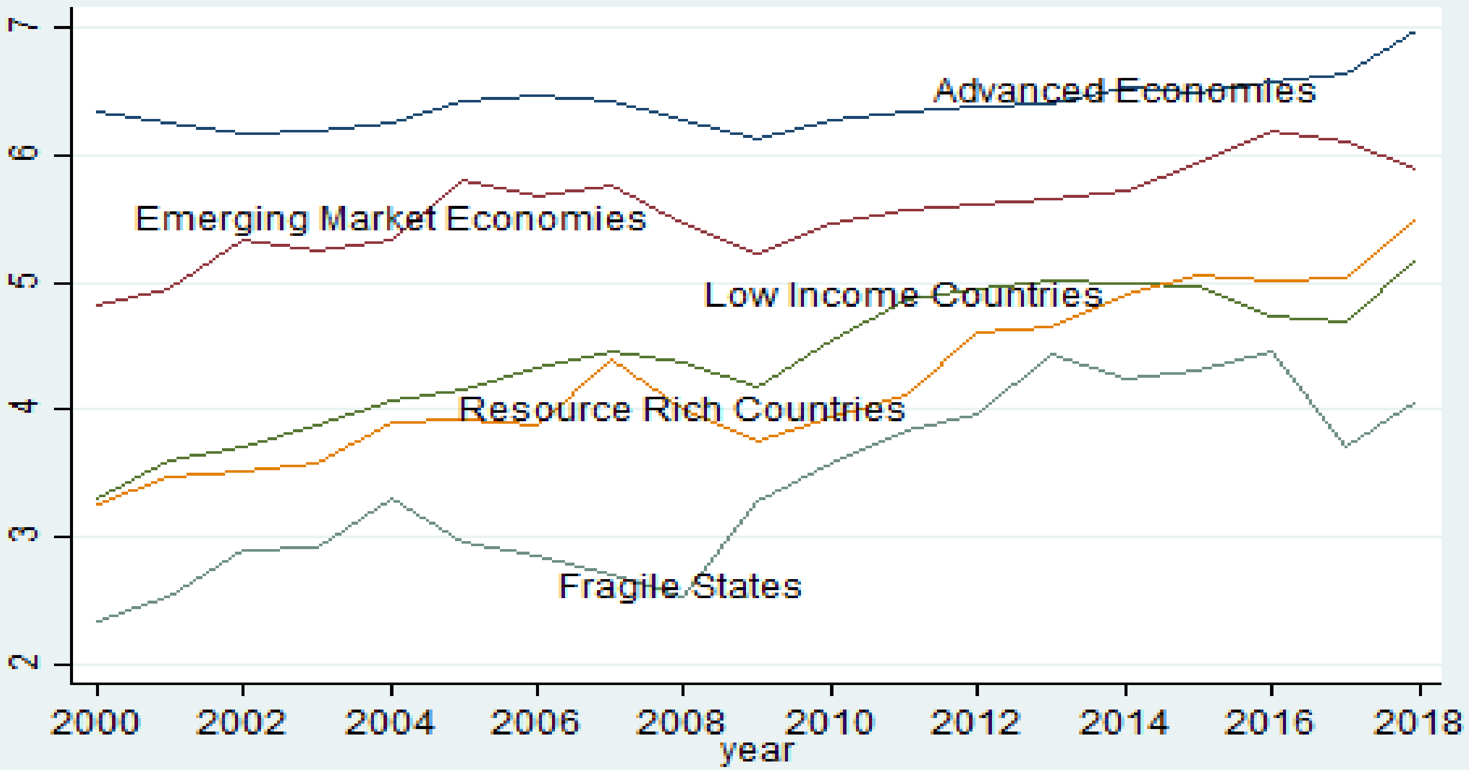
- On average, tax-to-GDP rose by 4 percentage points of GDP in LICs



2. What have LICs achieved in the past 20 years?

- A significant portion of the increase in LIC revenue has come from growing VAT collections

Figure 2. VAT Revenues (as a share of GDP), 2000-18



Source: ICTD Government Revenue Dataset

2. What have LICs achieved in the past 20 years?

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- Revenues from corporate income tax increased somewhat despite falling tax rates
- Revenues from personal income tax also increased; however, revenues substantially lower than in advanced economies
- Very little collected from property taxes
- Overall, little change in the ratio of revenues from direct to indirect taxes; on the other hand, this ratio has improved in SSA with greater growth in direct taxes during the past 20 years
- Personal income tax reforms and strengthened tax revenue administration in LICs and EMEs have helped improve income distribution

3. Where would LICs be in 2030 if the current tax system and past growth prevailed?

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- Illustrated with tax buoyancy in SSA, which is slightly above one

Table 1. Buoyancy of Total Tax Revenue Across Different Country Groups

	Long-term buoyancy	Short-term buoyancy
All countries	1.088	1.004
Fragile	1.067	0.892
Foreign-aid dependent	1.089	1.043
Natural-resource rich	1.069	0.969

Source: Gupta, Jalles and Liu (2021).

3. Where would LICs be in 2030 if the current tax system and past growth prevailed?

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- Domestic tax revenues generated by 2030 will not be adequate to cover spending needed to achieve the SDGs (e.g., Benin, Rwanda, and SSA as a whole)

Table 2. Projected Increases in Tax-to-GDP Ratio by 2030 in SSA, Benin and Rwanda

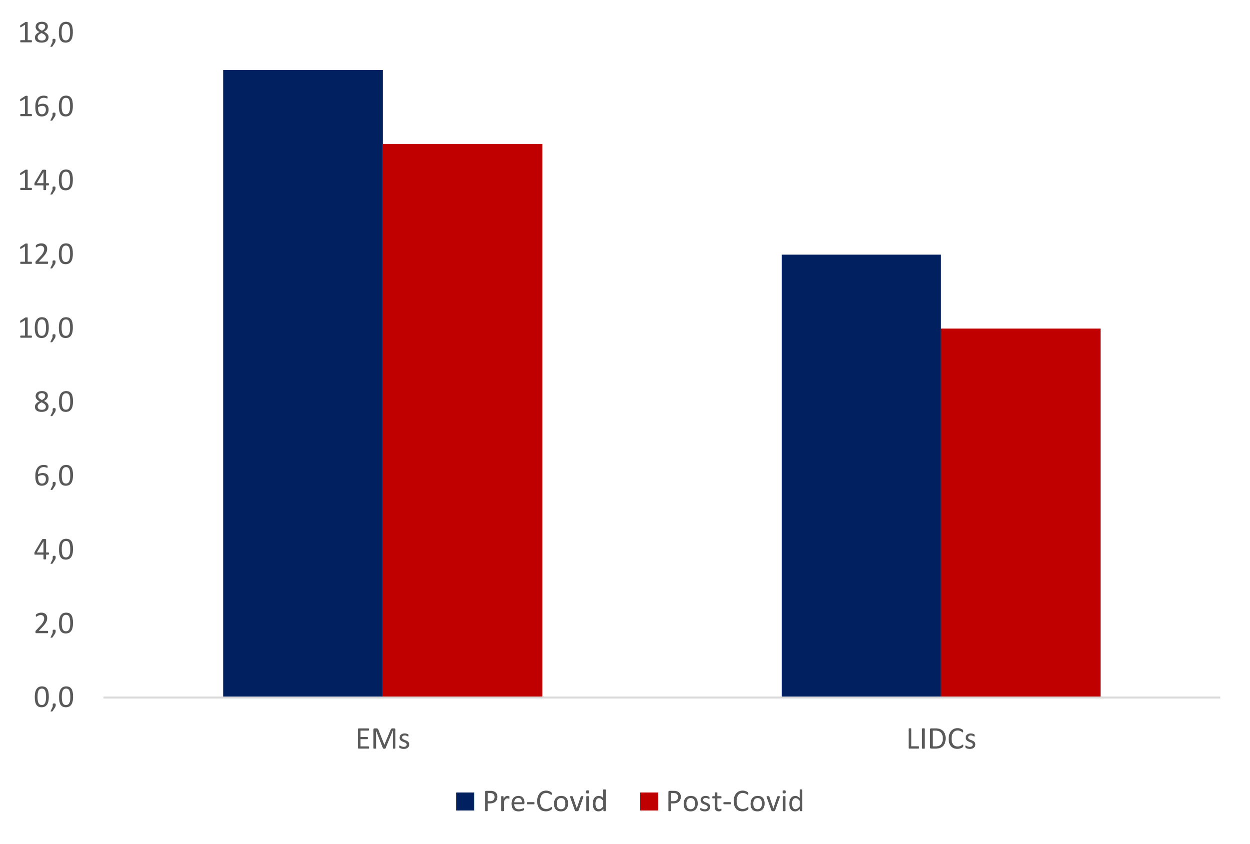
	Tax-to-GDP Ratio, 2016 (in percent)	Estimated Tax Buoyancy	Projected Tax-to-GDP Ratio in 2030 (in percent)	Increase in Tax-to-GDP Ratio
SSA	15.8	1.08	16.6	0.8
Benin	9.2	1.18	10.6	1.4
Rwanda	15.5	1.13	18.7	3.2

Source: Gupta, Jalles and Liu (2021).

4. Impact of COVID on revenues and spending

- COVID-19 pandemic has affected tax compliance and the taxation base—and may have a permanent impact on the LIC revenue position

Tax revenue projection pre- and post COVID for 2020 (% GDP)



IMF Fiscal Monitor Database

4. Impact of COVID on revenues and spending

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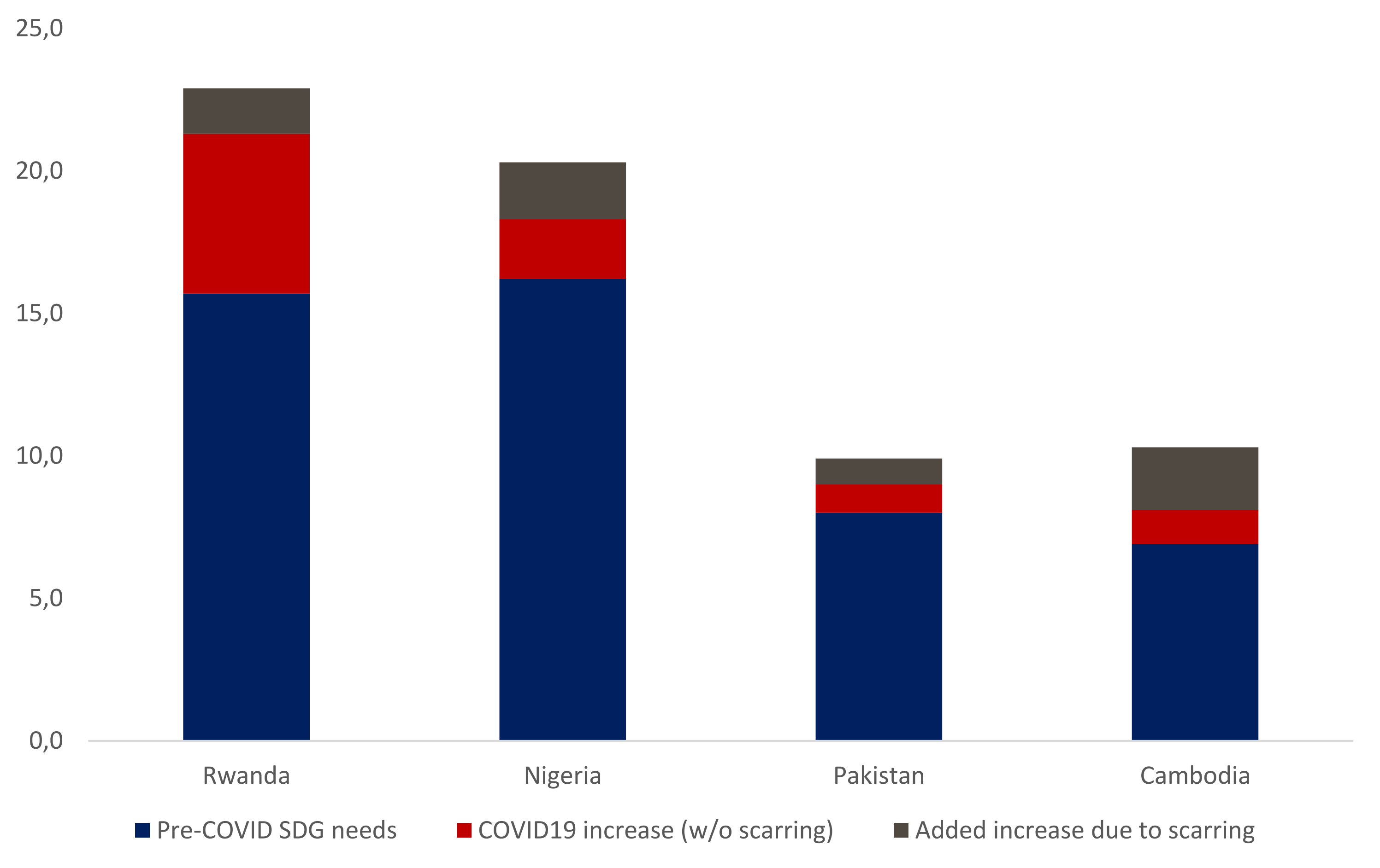
- **Additional spending needs pre- and post COVID-19 (% GDP)**

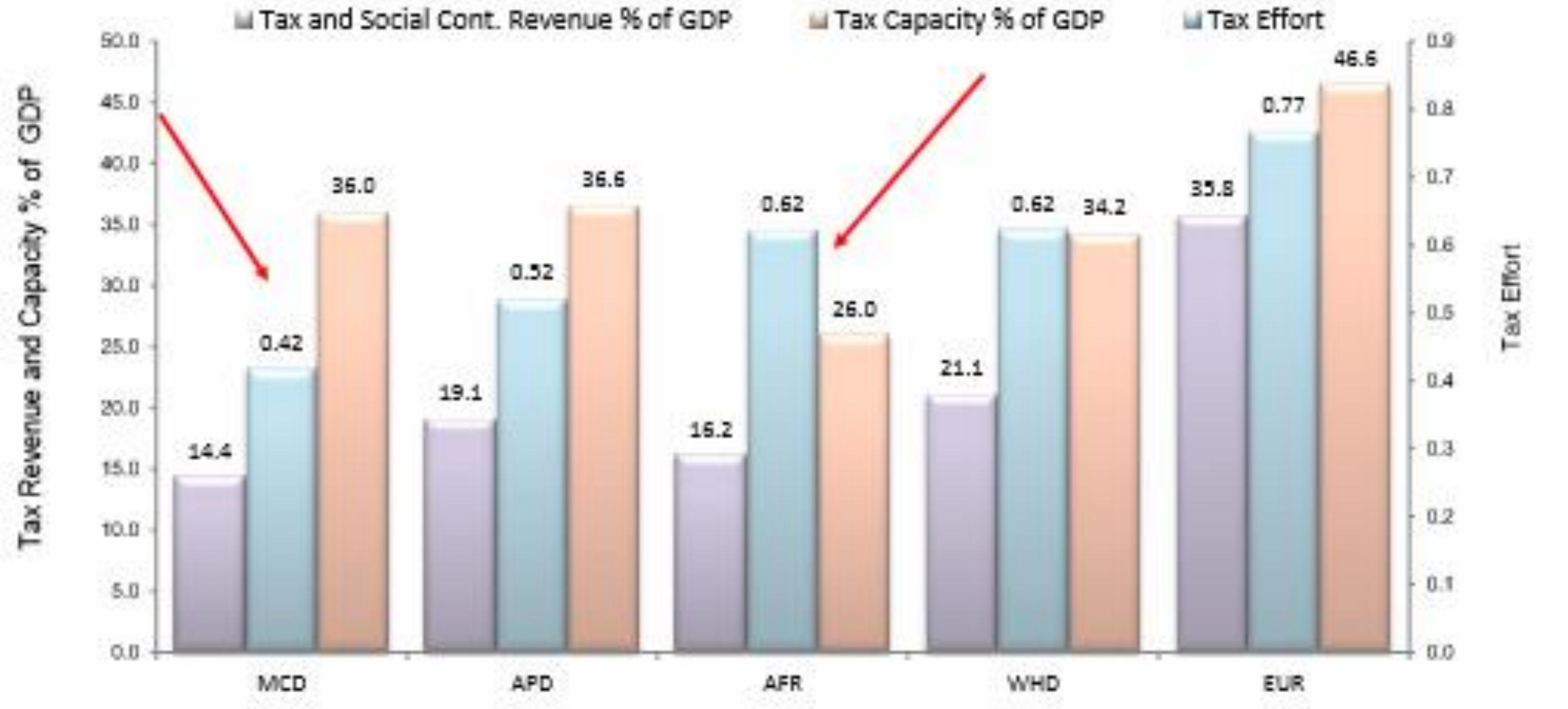


IMF Staff Discussion Note: A Post-Pandemic Assessment of the Sustainable Development Goals, April 2021

5. But considerable revenue potential exists

African, Asian and Middle Eastern Countries

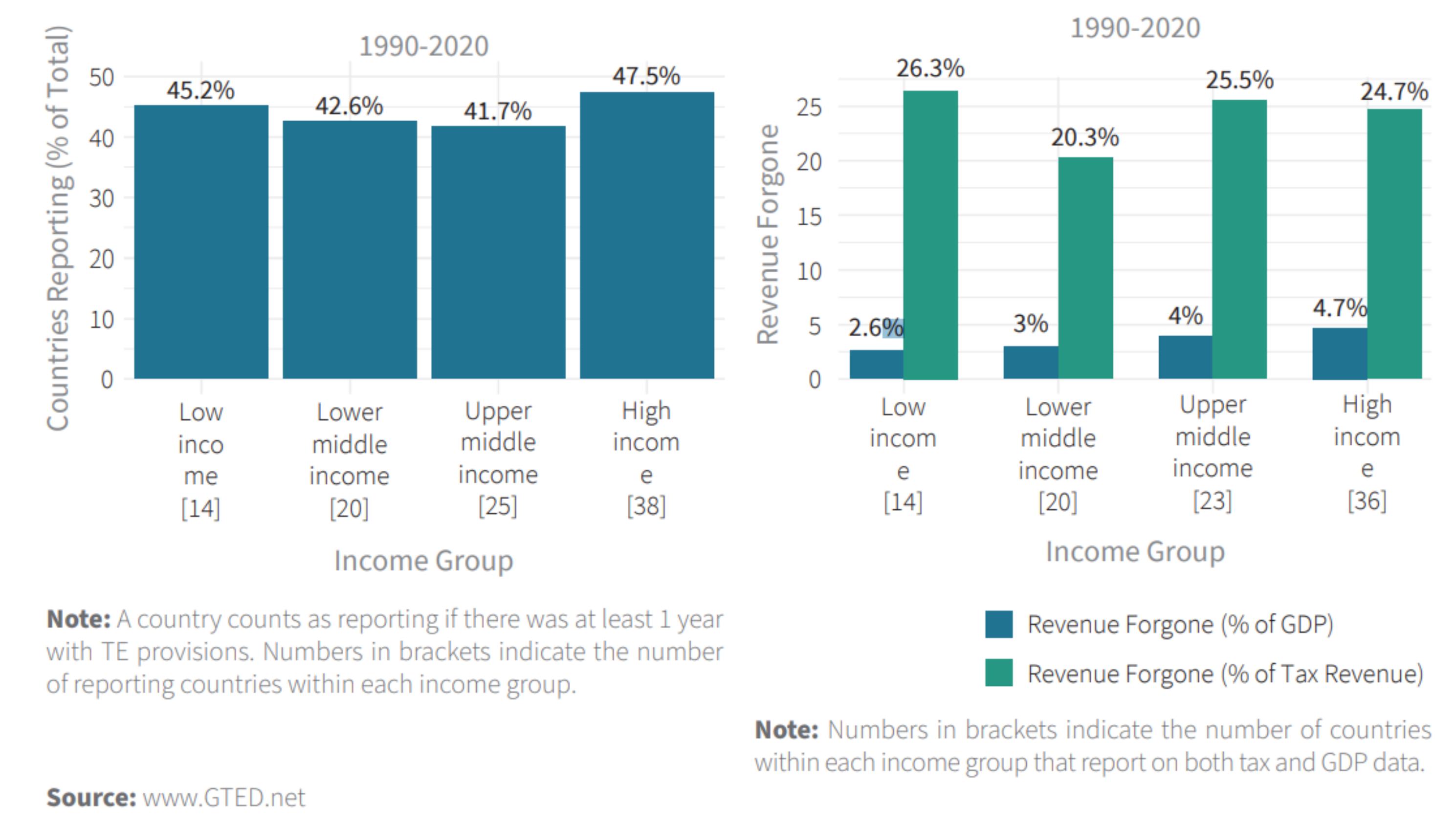
- Considerable potential exists for raising domestic revenues—that is, the tax capacity in these countries is substantially more than actual tax collections



IMF Staff Discussion Note: A Post-Pandemic Assessment of the Sustainable Development Goals, April 2021 (background note)

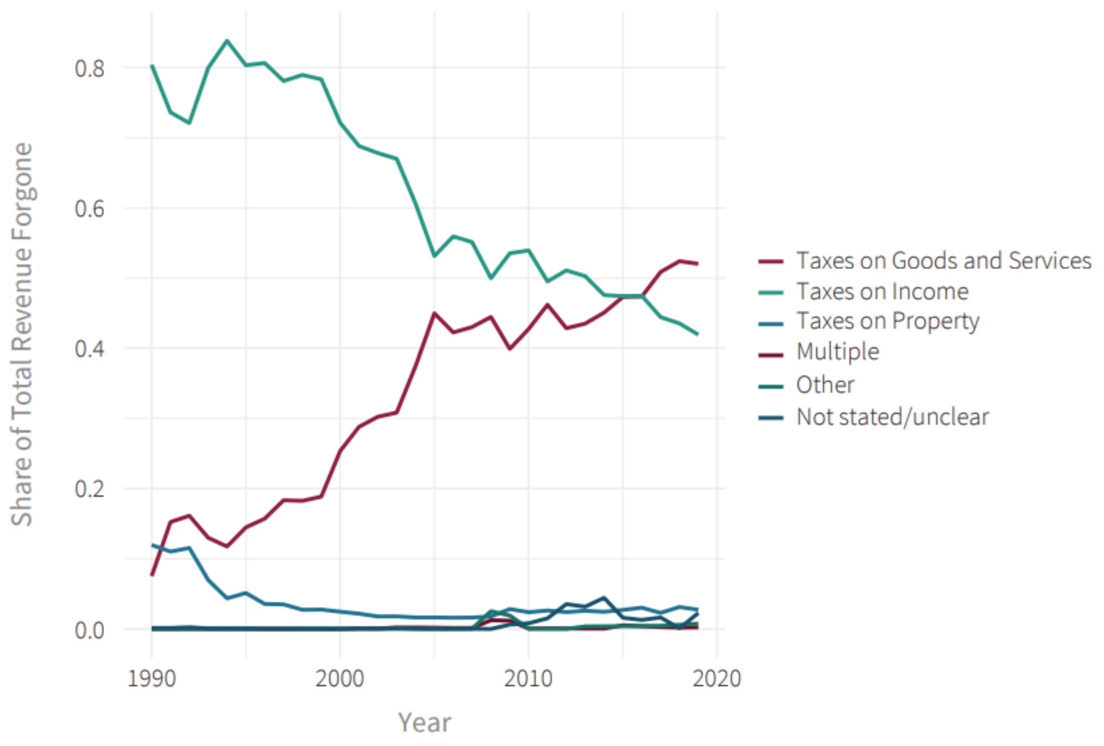
6. One area of revenue leakage is tax expenditures

Average of Countries Reporting & Revenue Forgone by Country Income Group



6. Growing exemptions………

Figure X. Global Unweighted Evolution of Revenue Forgone by Tax Base



Note: Only provisions with a revenue forgone estimate are included.

Source: www.GTED.net

7. Other tax areas need strengthening as well

- Other policy actions that can potentially yield revenues going forward
  - Improving VAT efficiency through enhanced compliance and policy design particularly in construction and trade sector
  - Adjusting excise taxes
  - Strengthening progressive taxation, through personal income tax and property tax
  - Strengthening international taxation and tax- avoidance measures
  - Considering environmental taxes
  - Reviewing non-tax revenues

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