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Session 6: Communication of TEs

Follow-up Technical Meeting on
Tax Expenditures

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September 2023

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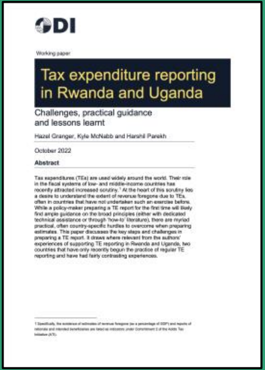
Lesson #7: Communication becomes the key bridge between the technical exercise and the TE report’s objectives around greater transparency and informing policy. In this process, preventing certain misconceptions is paramount.


ODI

Working paper

Tax expenditure reporting in Rwanda and Uganda

Challenges, practical guidance and lessons learnt

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October 2022

Abstract

Tax expenditures (TEs) are used widely around the world. Their role in the fiscal systems of low- and middle-income countries has recently attracted increased scrutiny.[1] At the heart of this scrutiny lies a desire to understand the extent of revenue foregone due to TEs, often in countries that have not undertaken such an exercise before. While a policy-maker preparing a TE report for the first time will likely find ample guidance on the broad principles (either with dedicated technical assistance or through 'how-to' literature), there are myriad practical, often country-specific hurdles to overcome when preparing estimates. This paper discusses the key steps and challenges in preparing a TE report. It draws where relevant from the authors' experiences of supporting TE reporting in Rwanda and Uganda, two countries that have only recently begun the practice of regular TE reporting and have had fairly contrasting experiences.

ODI Working Paper: Tax expenditure reporting in Rwanda and Uganda

Role of TE Report

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Transparency / Accountability to public (taxpayers) on how public money is spent → Accessible & understandable to citizens

Basis for efficient budget allocations between policy/development objectives → In terms that relate to other public spending (e.g. budget sectors/recipients)

Basis for evaluation of effectiveness, an input to better policymaking → Detailed costing by provision, tax type, beneficiary etc

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How TE is communicated and to whom

- Internal report

- Speech / account to Parliament

- Report publication (with budget or separate)

- Public announcements, media engagement, presentation to stakeholders etc.

Interested Parties:

- MoF and RA (technical)
- Ministers (political)
- Legislature/Parliament
- Development partners
- Civil society
- Private sector
- Public

3 Common Misconceptions

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- **1. Tax Expenditure = Tax Exemption**
  - Tax 'expenditure’ comes in many forms and serves a variety of purposes.
  - The intended beneficiaries of some expenditures *may* be foreign investors, but many could also be targeted at domestic businesses, SMEs, low-income households, disabled individuals or targeted emerging sectors, for example
  - In many jurisdictions, the phrase ‘tax exemption’ is – probably rightly – associated with negative connotations and the authors of a TE report must meet the challenge to carefully communicate that not all TEs meet the definition of a tax exemption.

3 Common Misconceptions

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- **2. Tax expenditures are wasteful**

- Research has provided a strong challenge to the need for investment tax incentives (such as investor motivation surveys), e.g., **simply stating the estimated revenue foregone from TEs in a report does not imply that this revenue represents a net loss.**

  - Only an evaluation of costs and benefits of each TE measure would provide that evidence.

- The TE Report is, in essence, the first part of a Cost-Benefit-Analysis…

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3 Common Misconceptions

- **3. “Revenue foregone” is equal to “revenue gain”**
- A common misconception is that the estimated revenue foregone can be read as the amount that government would receive if the tax reliefs were removed.
  - Particularly pertinent when governments are under pressure to mobilise revenue.
  - **But revenue gained from removing an expenditure does not equal revenue foregone**
    - **Behavioural factors**
    - **Limitations on govt’s ability to remove provisions (e.g. some are structural)**
    - May be cases where a tax expenditure is in place as it provides support to a key sector, industry or group of taxpayers in the least administratively costly manner.
      - If TE removed, maybe government continues to provide support (e.g. subsidy).

Common misconceptions:

From govt perspective – challenge to overcome these misconceptions!

"Over the last 40 years, tax incentives, although a deviation from the tax system, have since doubled from 40 to 80 per cent, despite their relevance coming under intense scrutiny.

…the design of Uganda's tax incentive regime impacts overall effectiveness, which in the end might force government to put in place regressive tax measures "to make ends meet"."

DAILY MONITOR WEDNESDAY, OCTOBER 13, 2021

www.monitor.co.ug

Shs5 trillion lost in tax exemptions, incentives

According to the government tax expenditure report, incentives, reliefs and exemptions were more visible in international trade taxes, value added tax and income tax.

BY ISMAIL MUSA LADU

KAMPALA. More than Shs5 trillion in taxable revenue is foregone due to exemptions and related incentives, according to the government tax expenditure report.

The report, the first to be published despite being a mandatory annualised document, indicates that during the 2019/20 financial year, a total of Shs5.03 trillion was foregone due to tax expenditures incurred on exemptions, reliefs and incentives.

Exemptions and reliefs related to international trade taxes, which stood at more than Shs2.1 trillion, according to the report, contributed the largest share of foregone tax followed by val-

MAKING INFORMED DECISIONS

Experts have argued that the government tax expenditure report should inform decision making processes in regard to tax incentives with the need to understand if indeed they have been important in attracting foreign direct investment and priority sector investment.

Others argue that instead of focusing on tax incentive, which are in most cases abused, government should focus on provision of skilled and cheap labour, access to raw material and predictable political environment to attract investments.

Framing / Language can also be key!

1. Expenditure?
2. Provision?
3. Relief?
4. Support?

Further Considerations

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1. To be meaningful, consider audience & their interests:
   - Salience e.g. express in terms of budget sectors, target group(s) and objectives
   - Explain what report does and does not measure (e.g. <u>not effectiveness</u>)
   - Access is appropriate e.g. website, TV, radio and/or hard copy, local languages if needed
2. Proactive engagement & education to explain what the results mean, avoid misinterpretation & misconceptions
3. Be prepared for scrutiny and demand for further analysis

What can governments & their partners do?

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- Improve quality of report & how it is presented
- Strengthen stakeholder engagement and communications
- Clarify and amplify key messages from TE reports
- Coordination with development partners on the above
- Dialogue with peers and international agenda/networks e.g. ATI, ATAF

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