



Background paper prepared by

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The views expressed are those of the author and do not necessarily reflect the views of UNCTAD.

**Domestic resource mobilization in Latin America and the Caribbean:  
fiscal policy challenges<sup>1</sup>**

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## Introduction

Proposals for mobilizing domestic resources to achieve the Sustainable Development Goals by 2030 are a key pillar of the development model put forth by the United Nations and the Economic Commission for Latin America and the Caribbean (ECLAC). In the region these measures are being developed and adopted in a period characterized by very modest growth, which contrasts sharply with that experienced prior to the global economic and financial crisis. The erosion of the fiscal space occasioned by the current macroeconomic context will require comprehensive and sustained reforms to public finances to ensure public sector solvency, protect investment, safeguard achievements on the social front and broaden tax resources.

Domestic resource mobilization, however, cannot be analyzed as simply a means by which sustainable development is financed; rather it must be viewed as endogenous to the development process itself. Raising resources, especially from the public ambit, is not neutral in terms of its impact on society or on the subsequent evolution of the economy. In that respect, the region is hindered by a tax structure that is skewed towards regressive indirect taxes, elevated levels of tax evasion, and a high dependency on revenues deriving from the exploitation of non-renewable natural resources.

Tackling these challenges, especially in a low growth environment, is further complicated by significant obstacles of political economy. Nevertheless, a number of policies tools are available to boost public revenues and support sustainable and inclusive growth. Countries in the region are adopting innovative measures to tackle tax evasion and avoidance as well as to improve the administration of their tax systems. These efforts have been supported by increasing regional and international cooperation in fiscal and financial affairs.

The aim of this report is to provide an overview of the current state of domestic resource mobilization in Latin America and the Caribbean as well as to examine some of the key challenges the region's countries face to boosting public revenues to finance sustainable and inclusive development. To that end, Chapter 1 examines current trends in domestic resource mobilization in the region and how they have been shaped by change in the economic cycle after the crisis.

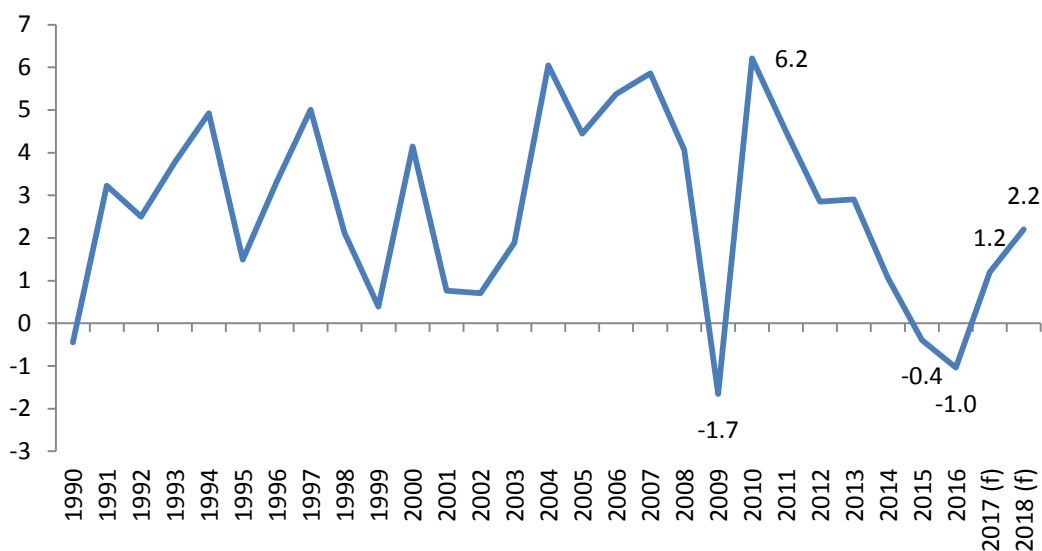
Chapter 2 then examines a number of key domestic resource mobilization challenges for the region and for developing countries more generally, including: weak direct taxation, rampant tax evasion, elevated dependence on revenues from non-renewable natural resource revenues and harmful tax competition.

Chapter 3 reviews recent policy measures in the region to boost domestic resource mobilization as well as some potential areas for future work. Finally, Chapter 4 argues for the strengthening of international partnerships to provide support for domestic resource mobilization efforts in the developing world. The concluding section provides some final thoughts on domestic resource mobilization in the context of renewing fiscal pacts in Latin America and the Caribbean.

## **1. Domestic resource mobilization in Latin America and the Caribbean**

Domestic resource mobilization cannot be understood outside the overall macroeconomic context, as it necessarily conditions the available policy space, creating opportunities as well as imposing limits on policymakers. In the context of Latin America and the Caribbean, after roaring back to growth after the global economic and financial crisis in 2008-2009, the economies of the region entered into a prolonged period of deceleration (figure 1). Between 2011 and 2016, real year-on-year growth fell with little or no respite from 6.2% to -1.0%, led in particular by significant declines in some of the region's largest economies such as Argentina and Brazil. Nevertheless, this regional average belies significant heterogeneity of results at the country level, with significantly stronger and more consistent growth in Central America.

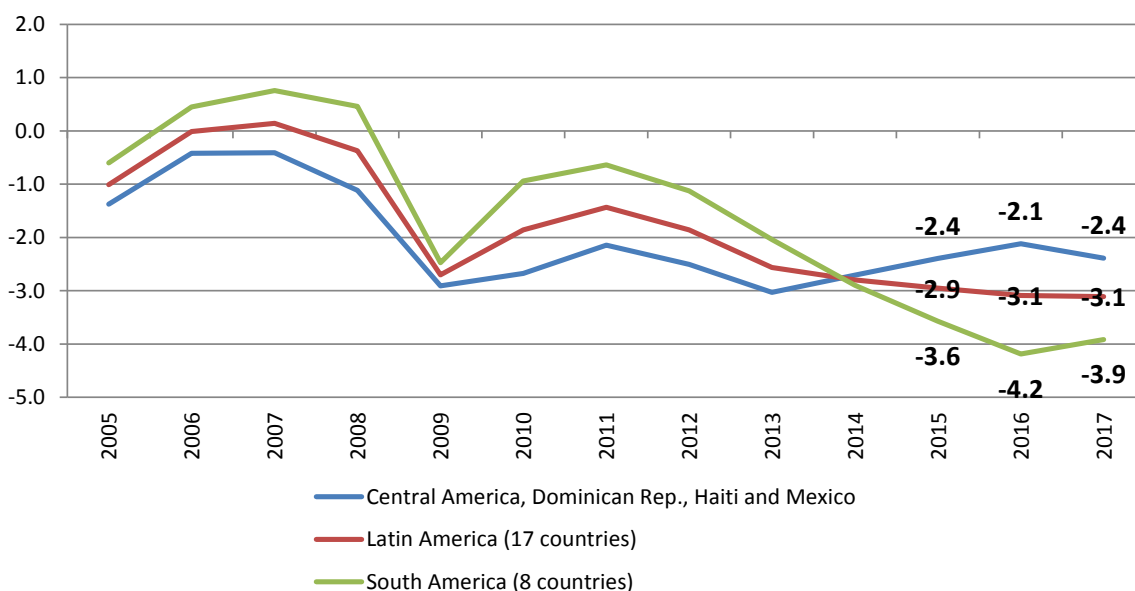
Figure 1  
**LATIN AMERICA AND THE CARIBBEAN: YEAR-ON-YEAR REAL VARIATION OF GROSS DOMESTIC PRODUCT, 1990-2018 <sup>a</sup>**  
*(Percentages on the basis of constant 2010 US dollars)*



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official information.

The turn of the economic cycle has also left an indelible mark on the region's fiscal accounts. The average fiscal deficit in Latin America increase significantly as a result of the global economic and financial crisis in 2009, falling from -0.4% of GDP in 2008 to -2.7% of GDP (figure 2). In the immediate aftermath of the crisis, as economic activity in the region returned to high rates of growth, fiscal accounts began to show signs of improvement, reaching a deficit of -1.4% of GDP in 2011. However, since that point deficits began increasing again, in line with the continual deceleration of the economy.

Figure 2  
**LATIN AMERICA (SELECTED SUBREGIONS): OVERALL FISCAL BALANCE OF THE CENTRAL GOVERNMENT, 2005-2017 <sup>a</sup>**  
*(Percentages of GDP)*



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official information.

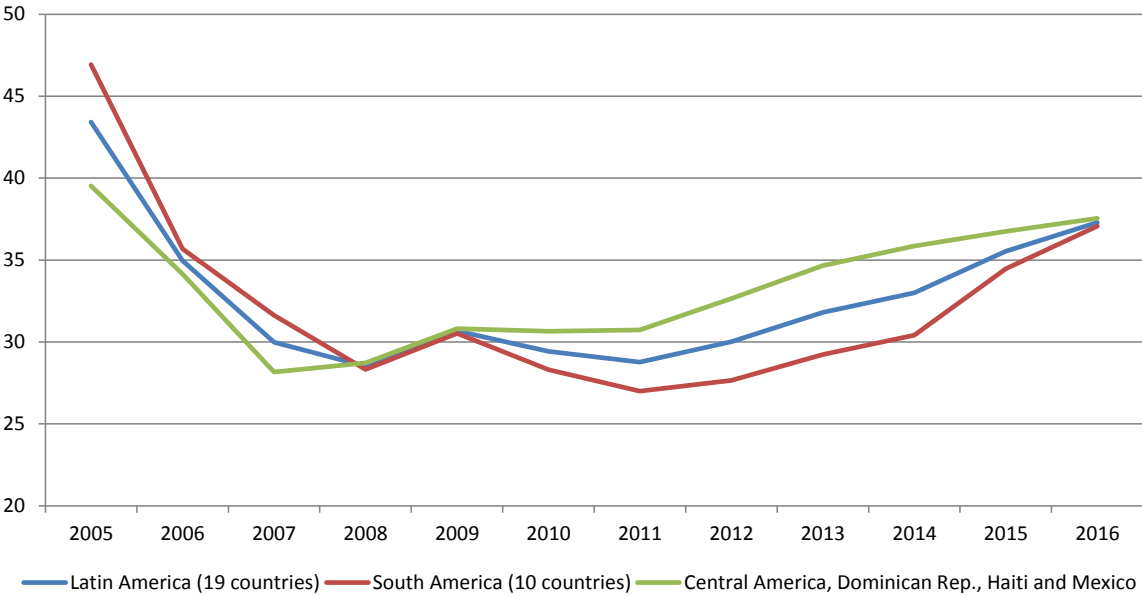
<sup>a</sup> Simple averages. Data for Mexico refer to the federal public sector and data for Peru refer to the general government.

Beginning in 2014 there was a shift in the trajectories of fiscal deficits at the sub regional level reflecting differing macroeconomic situations. In the north of the region – Central America, Dominican Republic, Haiti and Mexico – there was an improvement in the average deficit, which returned to its 2011 level (-2.1% of GDP). In contrast, mounting fiscal deficits in South America pulled the average fiscal deficit to -4.2% of GDP in 2016. Interestingly, these shifting trajectories resulted in a near steady average deficit at the central government level for Latin America as a whole, which has hovered around -2.8% of GDP and 3.1% of GDP between 2014 and 2017.

The accumulation of fiscal deficits in the region has led to an increase in public debt levels (figure 3). In the immediate aftermath of the global economic and financial crisis public debt levels oscillated, reflecting the sharp increase of the deficit in 2009 and the improvement in the economic situation in a number of countries between 2010 and 2011. However, beginning in 2012 gross public debt of the central government in the region began to rise notably, with a particularly

sharp increase in 2015 (from 33.0% of GDP in 2014 to 35.5% in 2015). In general debt levels rose higher in the north of the region, reflecting higher deficits pre-2014, compared to the south. Data for 2016 show that the subregional averages have nearly converged again. Preliminary figures for 2017 suggest that the rate of growth of public debt has slowed, potentially pointing to a lower overall deficit than currently projected.

Figure 3  
**LATIN AMERICA (SELECTED SUBREGIONS): GROSS PUBLIC DEBT OF THE CENTRAL GOVERNMENT, 2005-2016<sup>a</sup>**  
*(Percentages of GDP)*



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official information.

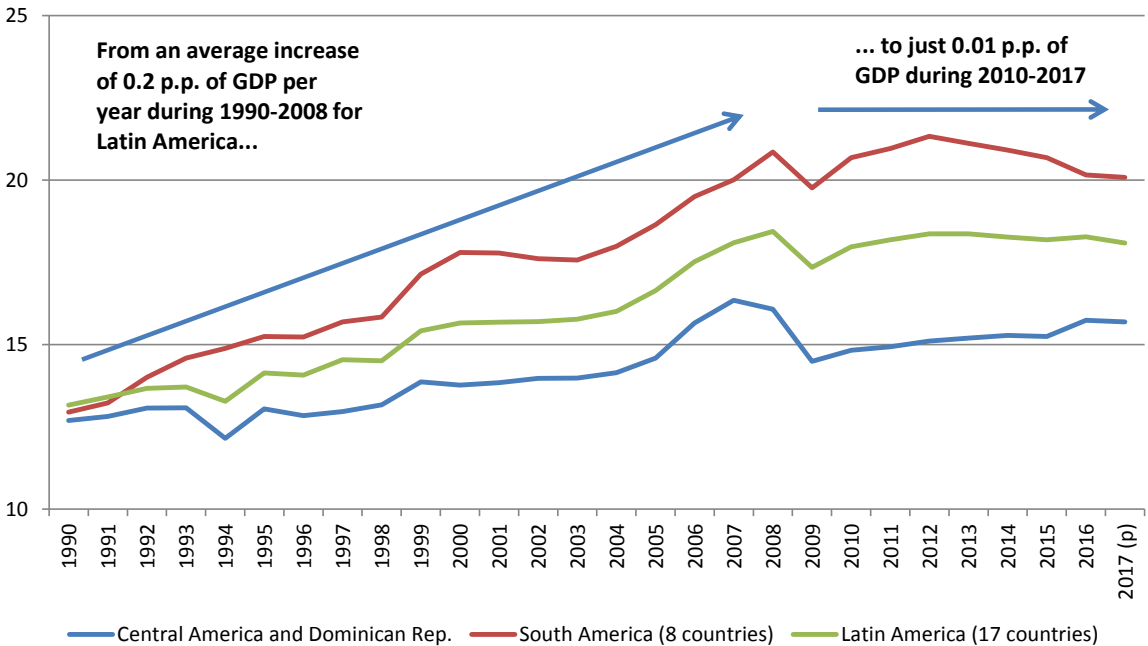
<sup>a</sup> Simple averages.

Economic deceleration, and outright recession, significantly impacted public revenues in the region in the post crisis period. While central government revenues in Latin America rose on average 0.2 percentage points of GDP per year between 1990 and 2008, in the period after the crisis (2010-2017) they have averaged a 0.01 percentage point increase per year (figure 4). Additionally, the regional average obscures significant variations between the north and the south of the region, with a significant slip in revenues registered in South America starting in 2012. In



contrast, revenues in the north of the region have continued to grow after falling sharply in the immediate aftermath of the crisis.

Figure 4  
**LATIN AMERICA (SELECTED SUBREGIONS): CENTRAL GOVERNMENT TOTAL REVENUES, 1990-2017**  
*(In percentages of GDP)*

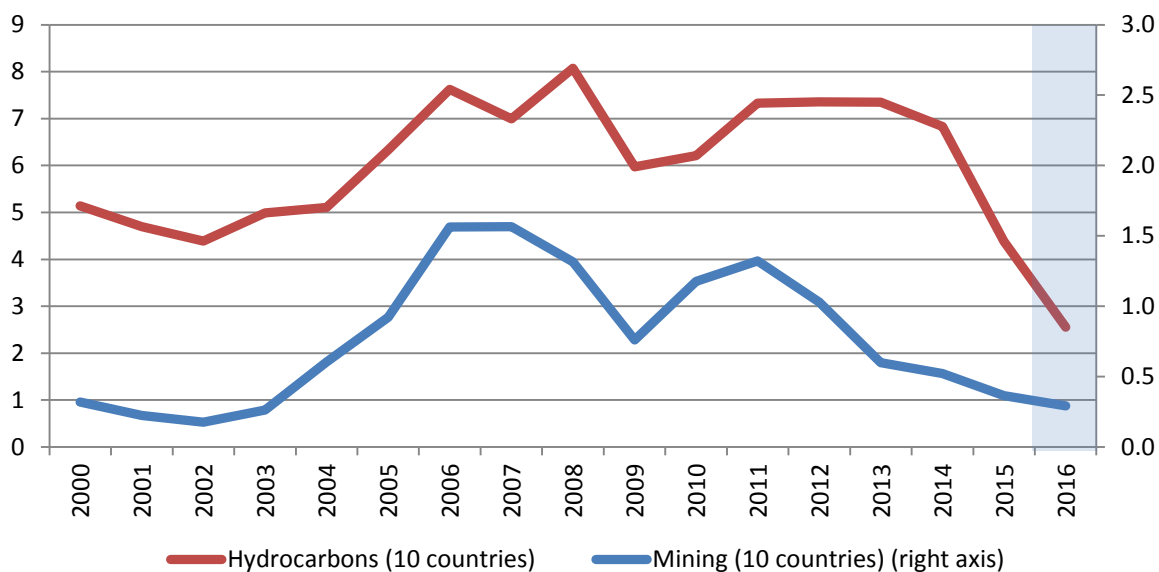


Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official information.

<sup>a</sup> Simple averages.

The evolution in total public revenues in the region, especially in South America, has been strongly influenced by the rise and fall in commodities prices. As seen in figure 5, between 2003 and 2008 (2007 in the case of mining) fiscal revenues – from tax and non-tax instruments – grew rapidly in Latin America and the Caribbean. Hydrocarbons revenues rose from an average of 5.0% of GDP in 2003 to a maximum of 8.1% of GDP in 2008 (a 62% increase). In contrast, mining-related revenues increased from 0.3% of GDP in 2003 to a peak of 1.6% of GDP in 2007, which represented a more than a quintupling over the period.

Figure 5  
**LATIN AMERICA AND THE CARIBBEAN: FISCAL REVENUES FROM NON-RENEWABLE NATURAL RESOURCES, 2000-2016<sup>a</sup>**  
*(In percentages of GDP)*



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official information.

Note: Mining includes: Argentina, Bolivia (Plurinational State of), Brazil, Chile, Colombia, Dominican Republic, Jamaica, Mexico, Peru and Suriname. Hydrocarbons include: Argentina, Bolivia (Plurinational State of), Brazil, Colombia, Ecuador, Mexico, Peru, Suriname, Trinidad and Tobago and Venezuela (Bolivarian Republic of). Values for 2016 are based on official government estimates from 2017 budget documents or from preliminary annual figures. When figures for 2016 were not available they were estimated using monthly data (typically for the first three quarters of the year). When monthly data was not available revenues were estimated by applying the year-on-year change in the price for the most representative product – or basket of products in the case of mining – for the country, expressed in national currency terms, to 2015 revenues.

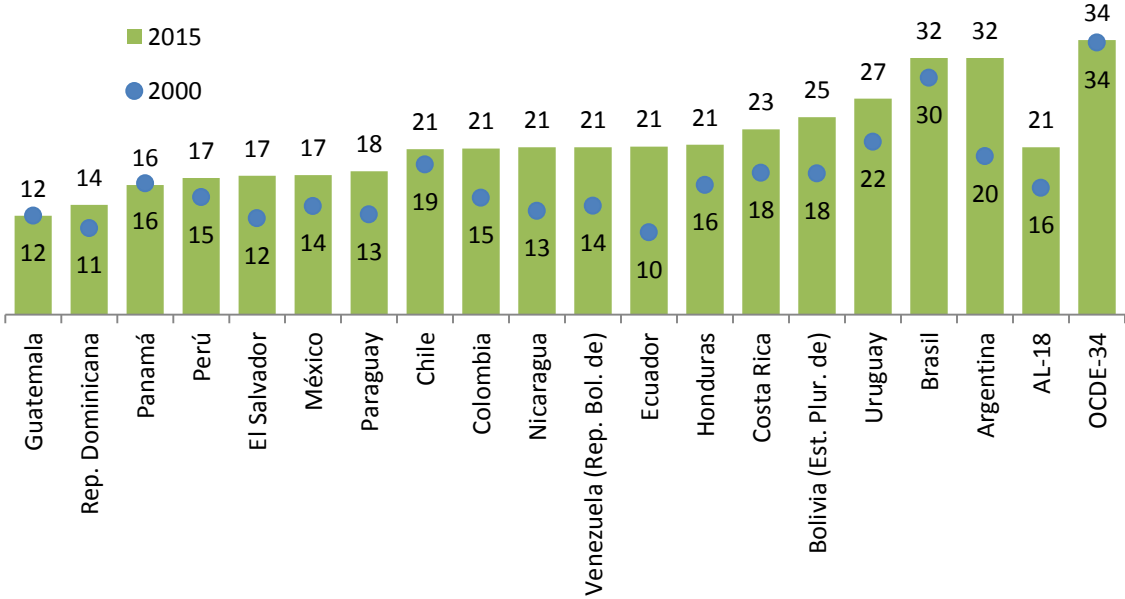
<sup>a</sup> Simple averages.

The recovery of prices in the post crisis period supported revenues from the exploitation of these non-renewable natural resources, but in recent years that impulse has faded significantly. Prices of minerals and metals began to dip in 2012 and continued to fall through 2016. In contrast, oil prices held relatively stable between 2011 and the first half of 2014. However, beginning in second half of 2014 there was a significant downward correction in prices that was reflected in a nearly immediate decline in hydrocarbons related revenues among Latin America’s major producers.

These trends in total public revenues notwithstanding, there has been a significant increase in tax revenues in the last decade, thanks in large part to improvements in the design of tax systems and their administration, the incorporation of new tax instruments (such as those on financial

transactions), and to macroeconomic policies that favored the reduction of fiscal deficits and public debt and fostered monetary stabilization (Gómez Sabaini and Morán 2013). As a result, between 2000 and 2015 tax revenues in Latin America rose 5 percentage points of GDP on average, from 15.9% of GDP to 20.9% of GDP (figure 6). A number of countries registered greater than averages increases such as Argentina (12 percentage points of GDP), Ecuador (11 percentage points of GDP), Nicaragua (8 percentage points of GDP), Venezuela (7 percentage points of GDP), Bolivia (7 percentage points of GDP) and Colombia (6 percentage points of GDP).<sup>2</sup>

Figure 6  
**LATIN AMERICA AND OECD: GENERAL GOVERNMENT TAX REVENUES, 2000 AND 2015**  
*(Percentages of GDP)*



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of OECD/ECLAC/CIAT/IDB (2017).

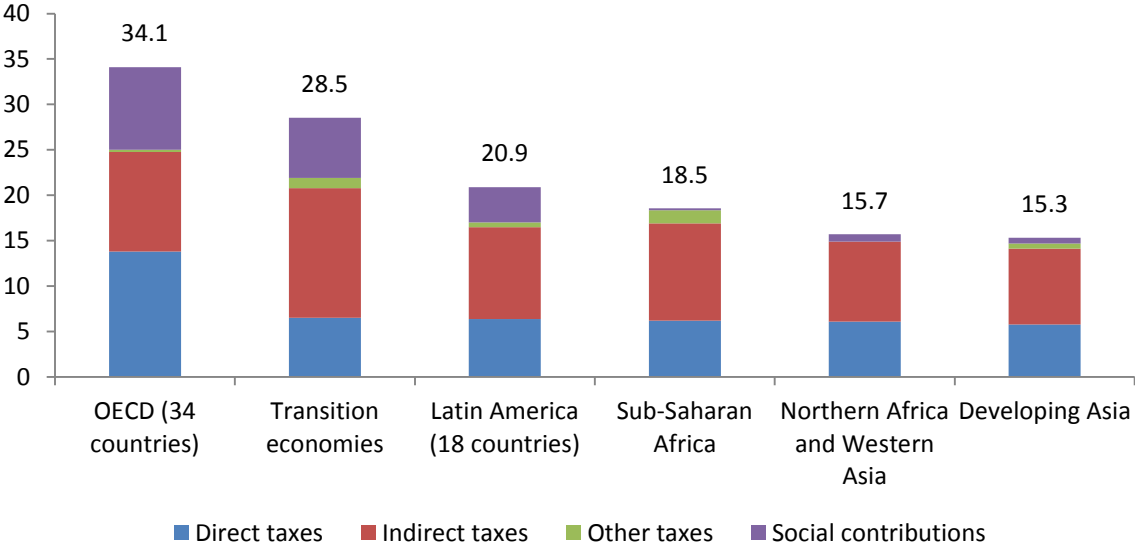
However, a number of countries in the region registered little or no increase during this period. Below average increases were registered in Mexico (3.9 percentage points of GDP), Dominican Republic (2.9 percentage points of GDP), Brazil (2.5 percentage points of GDP), Peru (2.4 percentage points of GDP) and Chile (1.9 percentage points of GDP). In the case of Brazil it is

<sup>2</sup> In Argentina the increase in tax revenues during the period was strongly affected by the nationalization of the private pension funds in 2008. Subsequent contributions to these funds are classified as social security contributions and deemed as tax revenues.

important to highlight that the country already exhibited a high tax burden in 2000 (29.6% of GDP), limiting the scope for an additional increase. In Guatemala tax revenues registered little change in 2015 relative to their 2000 levels, and in Panama there was a slight decrease of 0.2 percentage points of GDP, from 16.4% of GDP in 2000 to 16.2% of GDP in 2015.

In purely comparative terms, tax revenues in Latin America are relatively high relative to other developing regions. As figure 7 highlights, the region has an average tax take in that exceeds that of other developing regions, such as Sub-Saharan Africa (18.5% of GDP), Northern Africa and Western Asia (15.7% of GDP) and Developing Asia (15.3% of GDP). Nevertheless, these comparisons must be treated with care as the averages are affected by characteristics unique to each region. For example, in Northern Africa and West Asia the tax take skews lower reflecting a policy of low taxation in some countries due to abundant revenues from natural resources. Likewise, in Developing Asia lower tax revenues in Southern Asia (13.2% of GDP) offset higher levels in Eastern Asia (20.3% of GDP) and South-Eastern Asia (14.9% of GDP).

Figure 7  
**SELECTED REGIONS: TAX REVENUES, AROUND 2014<sup>a</sup>**  
*(Percentages of GDP)*

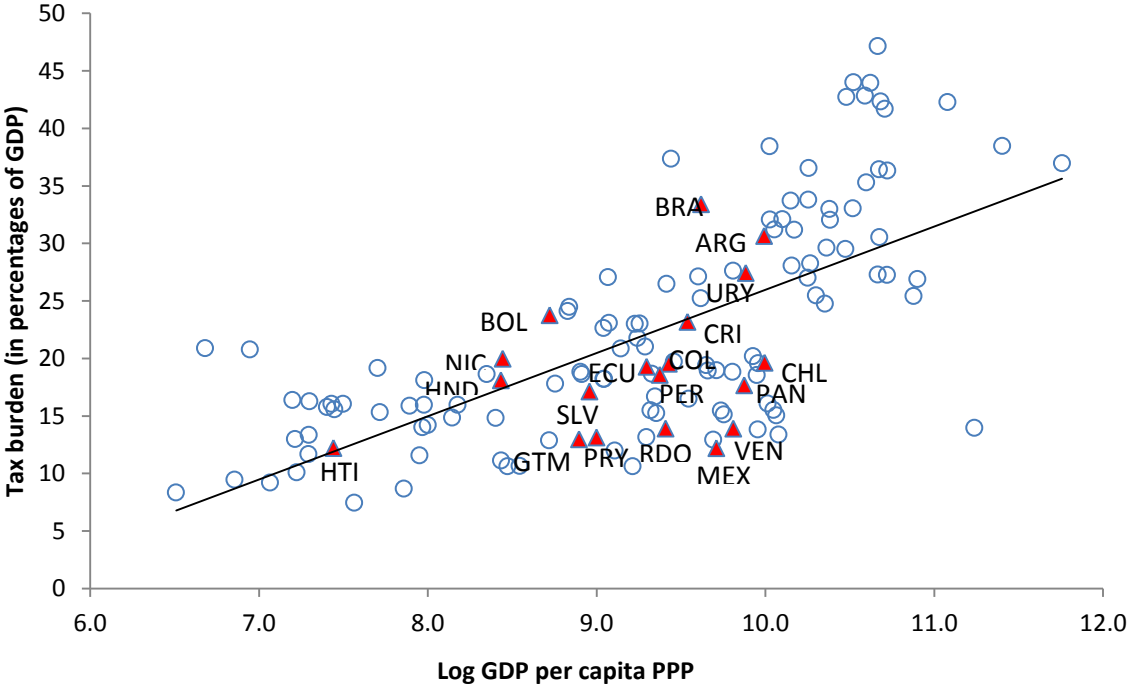


Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information from World Revenue Longitudinal Dataset (WoRLD) (IMF), OECD/ECLAC/CIAT/IDB (2017) and OECD.Stat.

<sup>a</sup> Simple averages.

However, relative to the region’s level of development – as proxied by GDP per capita in PPP terms – tax revenues in Latin America generally underperform. This is especially noteworthy in the cases of Chile, Dominican Republic, Guatemala, Mexico, Panama, Paraguay, and Venezuela where tax revenues are 5 percentage points of GDP or more from the potential level implied by the regression line in figure 8. Of the 19 countries of Latin America under consideration, 12 exhibit tax takes that could be considered below potential. At the opposite end of the spectrum, tax revenues in Argentina, Bolivia and Brazil are higher than implied by their level of development.

Figure 8  
**SELECTED COUNTRIES: TAX REVENUES AND GDP PER CAPITA IN PPP TERMS, AROUND 2014 <sup>a</sup>**  
*(Percentages of GDP)*



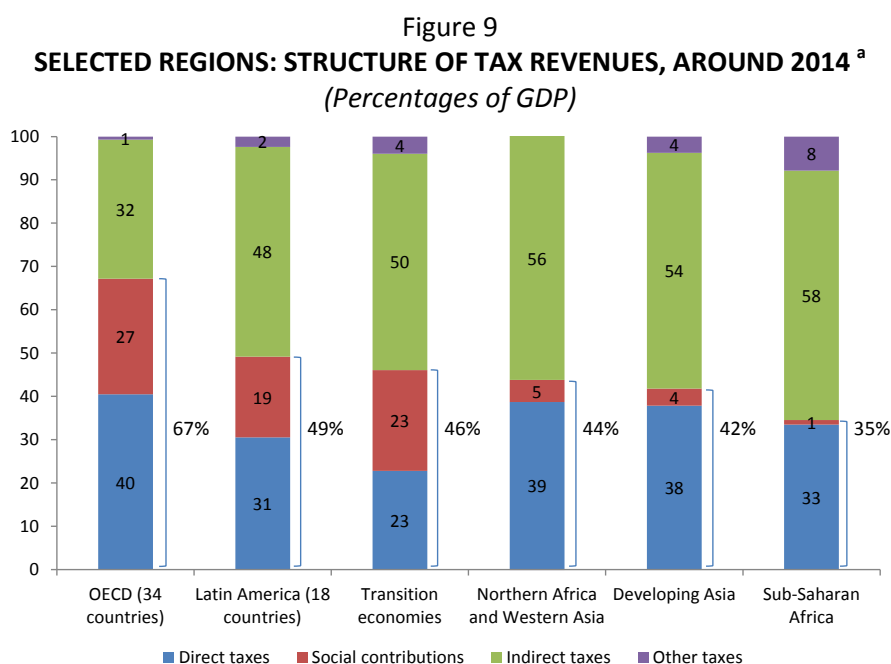
Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official information; Organization for Economic Cooperation and Development (OECD) y World Bank, World Development Indicators.

<sup>a</sup> Corresponds to the latest data available for the period 2011-2013. The coverage refers to central government for the Latin American countries, except for Argentina, Brazil, Chile, Colombia, Costa Rica, Mexico and the Plurinational State of Bolivia, where it refers to general government.

## 2. Key domestic resource mobilization challenges in light of the SDGs

### A. Weak direct taxation, inequality and sustainable inclusive growth

Among developing and transition regions direct taxes and social security contributions account for roughly one-third to one-half of overall tax revenues (figure 9). The composition of direct taxes, however, is significantly varied across regions. For example, social contributions in transition economies and in Latin America account for 23% and 19% of overall tax revenues, respectively. In contrast, these revenues – which are directly related to the provision of key public services such as pensions and other public benefits defined in the Sustainable Development Goals – make up less than 5% of overall revenues in other developing regions. Indirect taxes dominant the tax structure in most developing regions, accounting for more than half of overall tax revenues, reaching nearly 60% in Northern Africa and Western Asia and Sub-Saharan Africa.

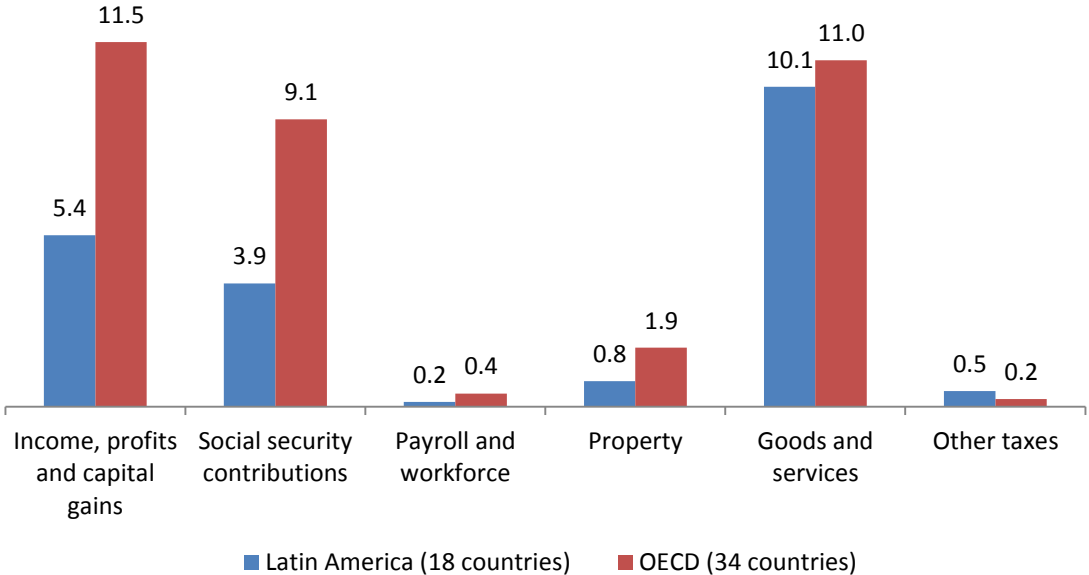


Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information from World Revenue Longitudinal Dataset (WoRLD) (IMF), OECD/ECLAC/CIAT/IDB (2017) and OECD.Stat.

<sup>a</sup> Simple averages. Values may not sum due to rounding.

In the Latin American context, there has been some improvement in the distribution of tax revenues by instrument over the past decades. Revenues from income taxes and social security contributions rose from 39% of total tax revenues in 1990 to 49% in 2015. This rebalancing notwithstanding, when analyzed purely in terms of levels – as measured as a share of GDP – income taxes and social contributions lag considerably from OECD levels: 5.4% of GDP in Latin America compared to 11.5% in the OECD for income taxes; 3.9% of GDP to 9.1% of GDP for social contributions (figure 10). Taxes on goods and services for both groups of countries, however, are roughly equal at 10-11% of GDP, highlighting the potential limitations to higher indirect taxation in Latin America and the need to advance on improving direct taxation.

Figure 10  
**LATIN AMERICA AND OECD: STRUCTURE OF TAX REVENUES, AROUND 2015 <sup>a</sup>**  
*(Percentages of GDP)*



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information from OECD/ECLAC/CIAT/IDB (2017) and OECD.Stat.

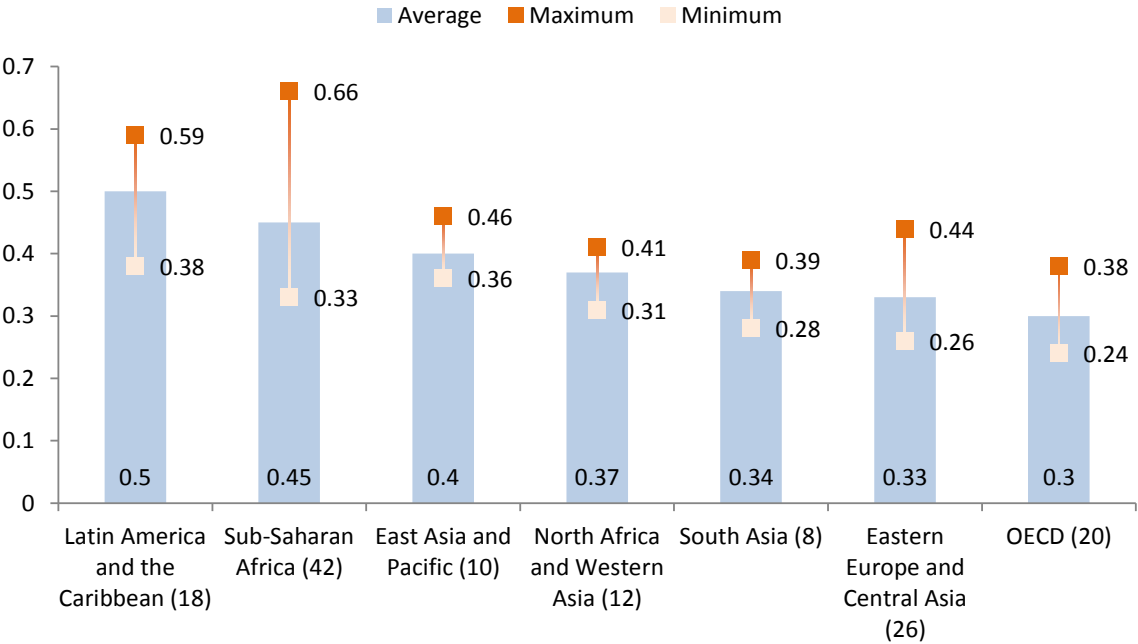
<sup>a</sup> Simple averages. Data for the OECD refer to 2014 due to data availability.

As alluded to in the introduction of this report, domestic resource mobilization must be seen as endogenous to the process of sustainable development and not only as a means of financing. The weak levels of direct taxation exhibited in developing regions have socio-economic impacts well

beyond the barrier it constitutes to generating public revenues. Of these a key issue relates to the ability of the tax system, and fiscal policies more generally, to contribute to the shaping of the distribution of income and wealth in developing economies in line with the targets embodied in the Sustainable Development Goals.

As figure 11 illustrates, income inequality remains a critical issue for developing regions. Available data suggests that Latin America and the Caribbean continues to be the most unequal region, with an average Gini coefficient of 0.50, followed closely by Sub-Saharan Africa (0.45). These two regions also exhibit significant spread in terms of the maximum and minimum values across countries, with a Gini of 0.66 being registered in South Africa.

Figure 11  
**SELECTED REGIONS: INCOME INEQUALITY, AROUND 2013<sup>a</sup>**  
*(Gini coefficient)*



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of data from CEPALSTAT, OECD.Stat, and World Development Indicators (World Bank).

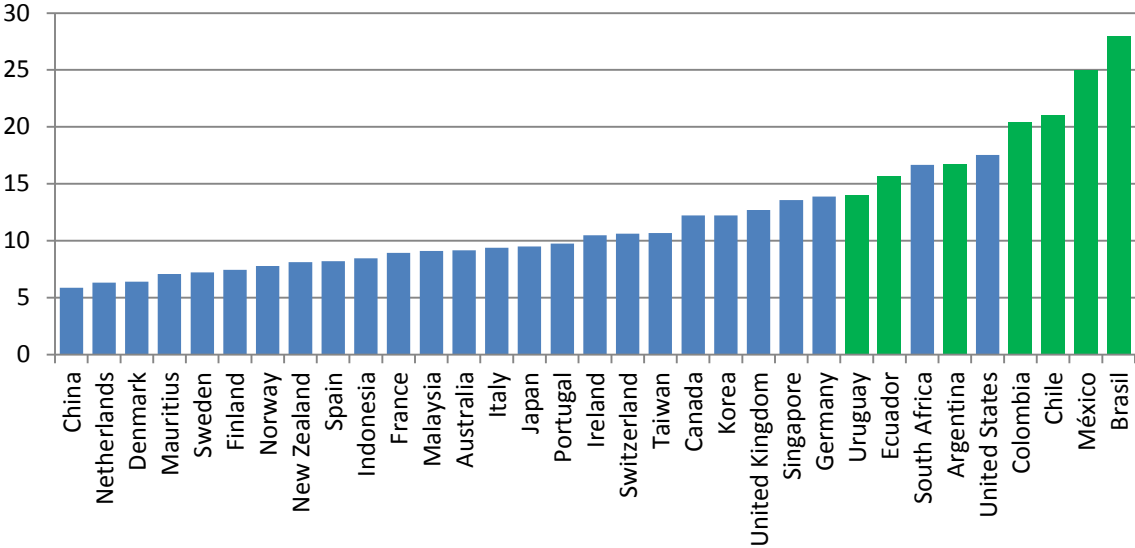
<sup>a</sup> Simple averages. Values refer to the latest available data during the period 2002-2012 due to data availability.

Other indicators suggest that inequality may be much more pronounced than that captured by the Gini coefficient calculated on the basis of household surveys. Recent research has largely focused on quantifying the concentration of income of the upper decile and increasingly of the upper



centile of the income distribution based on microdata from tax registers. While comprehensive data is not yet available, existing studies point to extremely elevated concentrations of income in some developing regions, especially in Latin America. In Colombia, Chile, Mexico and Brazil the top 1% of the income distribution captures more than 20% of national income (figure 12). These levels exceed those in most developed countries and are only closely matched by those in the United States and South Africa.

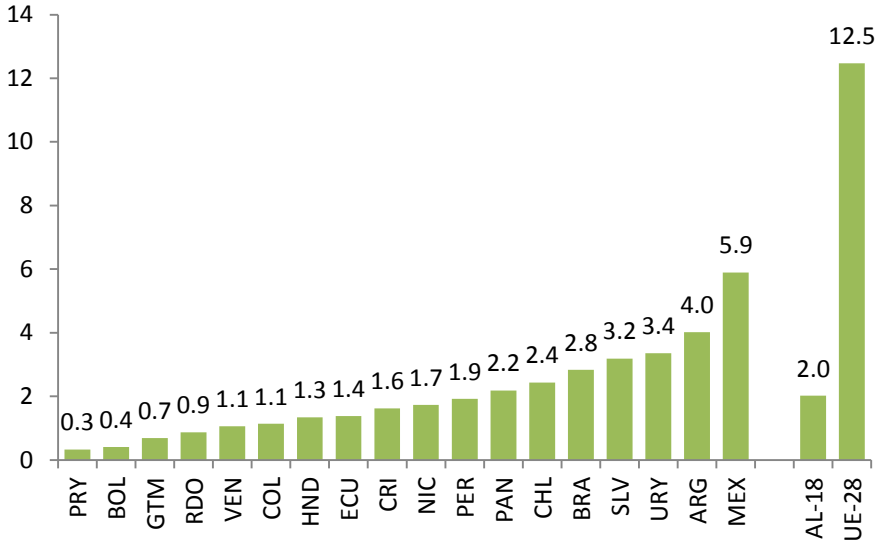
Figure 12  
**SELECTED COUNTRIES: CONCENTRATION OF INCOME OF THE TOP 1%<sup>a</sup>**  
*(Percentages)*



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of data from the World Top Incomes Database. For Chile the data are from Fairfield and Jorratt (2014), for Ecuador from Rossignolo, Oliva, and Villacreses (2016), for Mexico from Campos Vázquez, Chavez, and Esquivel (2016) and for Brazil from Morgan (2017).

Weak direct taxation, especially in the form of personal income taxes, severely limits the redistributive power of the tax system. In Latin America, the personal income tax reduced gross income inequality by just 2.0%, compared to a 12.5% reduction for the countries of the European Union (figure 13). Among the countries in the region Mexico is estimated to achieve the greatest reduction of income inequality through its tax system (5.9%), followed by Argentina (4.0%), Uruguay (3.4%), El Salvador (3.2%) and Brazil (2.8%). In contrast, in Paraguay, Bolivia, Guatemala and the Dominican Republic, the reduction in inequality is estimated to be less than 1%.

Figure 13  
**LATIN AMERICA AND EUROPEAN UNION: PERCENTAGE REDUCTION IN GINI COEFFICIENT DUE TO THE PERSONAL INCOME TAX**  
*(Percentages)*

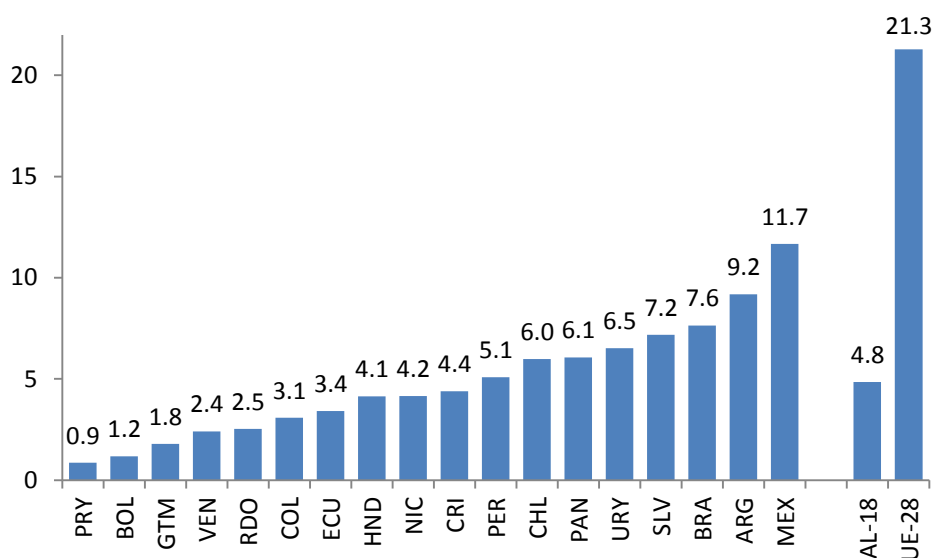


Source: Economic Commission for Latin America and the Caribbean (ECLAC), based on calculations by ECLAC and data from EuroMOD G2.0+ for EU-28.

The low redistributive power of the personal income tax in Latin America is reflected in the exceptionally low average effective tax rates that taxpayers in the highest income decile face. On average, the richest contributors in Latin America paid just 4.8% of their gross income in personal income tax, in contrast to an average of 21.3% in the European Union (figure 14). In a particularly egregious case, Alvaredo and Londoño Vélez (2013) find that the average tax rate declines with income within the top percentile using 2010 data, a finding that holds even when taking into account withholding taxes on dividends. This reflects the fact that in the region the top 1% enjoy significant tax advantages from relatively low marginal rates and generous tax exemptions, especially as related to capital income, which reduces their tax obligations (Rossignolo 2015).

Figure 14

**LATIN AMERICA (18 COUNTRIES) AND EUROPEAN UNION (28 COUNTRIES): AVERAGE EFFECTIVE TAX RATE OF THE 10<sup>TH</sup> DECILE, AROUND 2014**



Source: Economic Commission for Latin America and the Caribbean (ECLAC), based on calculations by ECLAC and data from EuroMOD G2.0+ for EU-28.

**B. Tax evasion, tax avoidance and illicit financial flows**

A key barrier to greater domestic resource mobilization in Latin America and the Caribbean, as well as other developing regions, is a high and persistent level of tax evasion and avoidance that undercuts public revenues. ECLAC estimates that tax non-compliance is equivalent to 2.4% of GDP in the case of VAT and 4.3% of GDP in the case of income tax, giving a combined total of US\$ 340 billion in 2015 (CEPAL 2016b).

Of the major tax instruments in the region, estimates of the evasion of the value-added tax are better developed, more widely available and above all more timely. These estimates often produced and published by national tax authorities point to an average evasion rate of roughly 28 percent in the region. Of the countries considered, Uruguay registered the lowest estimated evasion rate at 13.4% followed by Bolivia at 17.9% (table 1). At the other end of the spectrum, evasion of this tax reached an estimated 38.6% in Dominican Republic and 39.7% in Panama.

While high, these results are not substantially different from those for some European Union members, such as Italy, Greece and Poland (CEPAL 2016a).

Table 1  
**LATIN AMERICA: VALUE ADDED TAX (VAT) AND INCOME TAX EVASION RATES, LATEST YEARS  
 AVAILABLE**  
*(Percentages)*

	VAT		Income tax			
	Year	Evasion rate	Year	Total	Corporate	Personal
Argentina	2007	19.8	2005	49.7	49.7	49.7
Bolivia (Plurinational State of)	2013	17.9	...	...	...	...
Brazil	2015	27.5	2014	28.1	26.6	34.1
Chile	2015	20.3	2009	31.0	31.0	27.0
Colombia	2015	20.1	2012	34.4	34.4	...
Costa Rica	2013	33.1	2013	66.2	70.0	57.3
Dominican Republic	2014	38.6	2009	65.2	68.9	51.8
Ecuador	2004	31.8	2005	63.8	65.3	58.1
El Salvador	2010	33.1	2005	45.3	51.0	36.3
Guatemala	2015	34.2	2006	63.7	62.8	69.9
Mexico	2012	24.3	2012	28.9	31.4	26.3
Nicaragua	2013	31.8	...	...	...	...
Panama	2012	39.7	...	...	...	...
Paraguay	2014	30.9	...	...	...	...
Peru	2014	28.3	2006	48.5	51.6	32.6
Uruguay	2012	13.4	2013	...	39.6	...
Venezuela (Bolivarian Republic of)	...	...	2000-2005	45.6	...	...

**Source:** Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information from the Inter-American Centre of Tax Administrations (CIAT) and national tax administrations; J.C. Gómez Sabaini, J.P. Jiménez and A. Podestá, "Tributación, evasión y equidad en América Latina y el Caribe", *Evasión y equidad en América Latina*, Project Documents, No. 309 (LC/W.309), Santiago, ECLAC, 2010; and Union of Attorneys of the National Treasury (SINPROFAZ), "Sonegação no Brasil: uma estimativa do desvio da arrecadação do exercício de 2015", Brasília, June 2016 [online] <http://www.quantocostaobrasil.com.br/artigos/sonegacao-no-brasil-uma-estimativa-do-desvio-da-arrecadacao-do-exercicio-de-2015>.

Evasion of the income tax is estimated to be much more severe. Existing studies suggest that Latin American countries collect on average only 50% of the income tax receipts that their systems should theoretically generate. However, as table 1 highlights, at the country level there is significant heterogeneity in results with estimated evasion in excess of 60% in Guatemala, Ecuador, Dominican Republic and Costa Rica, compared to estimates of less than 30% in Mexico and Brazil.

On the whole, evasion rates are estimated to be higher for corporate than for personal income tax, with averages of 48.9% and 44.3%, respectively. This is explained by the common practice of employers withholding at source the tax payable by their employees, who account for the bulk of revenue, since other income sources (dividends, interest, income from public securities and capital gains) are often untaxed (or were when the measurement was carried out) or taxed at a lower rate. Recent studies in Costa Rica and in Mexico give evidence to this phenomenon, finding that evasion by salaried workers – in the order of 11.9% and 15.5%, respectively – is significantly lower than that of the self-employed (with estimated evasion of 90.9% and 83.4%, respectively) who often operate in the largely informal economies that characterize the region (Ministro de Hacienda de Costa Rica 2014; Fuentes Castro et al. 2013).

An area of growing concern for policymakers in the region is the international aspect of tax evasion and avoidance. The use of aggressive tax planning strategies by multinational corporations and high net-worth individuals has had a deleterious impact on the tax bases of countries in the developed and the developing world, as well as raising important questions about equity, fairness and economic efficiency. While much of the initial international debate of this issue focussed on base erosion and profit shifting in developed economies, there is increasing awareness of the seriousness of the issue for developing regions, where tax codes and administrations often are not equipped to deal with issues that their developed-country partners struggle with.

At the global level revenues losses associated with base erosion and profit shifting of multinational corporations is estimated in the hundreds of billions of dollars per year (table 2). OECD (2015) estimates put these losses in the range of US\$100-240 billion per year, equivalent to 4-10% of global corporate income tax receipts. Based on a different methodology, UNCTAD (2015) estimates revenue losses at US\$200 billion, or 8% of corporate income tax receipts. Finally, ECLAC estimates that illicit financial flows arising from the manipulation of international trade prices in the region results in the evasion of US\$31 billion, or roughly 10-15% of the region's corporate

income tax receipts (CEPAL 2016b; Podestá, Hanni, and Martner 2017). While these estimates are necessarily imprecise and fail to fully identify the phenomenon in all its aspects, they are highly suggestive of a significant loss of public revenues.

Table 2  
Base erosion and profit shifting estimates

Estimate	Methodology	Scale	Range (US\$ billions)	Year
OECD aggregate tax rate differential 2015	Estimated as the shifting of profits due to differences in tax rates between affiliates of multinational and comparable national enterprises	Global	100-240 (4-10% of CIT)	2014
UNCTAD offshore investment matrix 2015 <sup>a</sup>	Estimated on the basis of profits shifted through FDI flows through offshore financial centers	Global	200 (8% of CIT)	2012
ECLAC international trade price manipulation	Estimated on the basis of illicit financial flows deriving from the manipulation of international trade prices	LAC	31 (10-15% of CIT)	2013

<sup>a</sup> Does not consider profit shifting through trade price manipulation.

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of OECD (2015) and UNCTAD (2015).

International tax evasion and avoidance by high net-worth individuals has increasingly come into the public spotlight in recent years. The work of investigative journalists has uncovered provided key information that has exposed a number of the actors and mechanisms used to evade the payment of taxes through the use of offshore finance centers. The scale of this issue is further amplified by estimates that suggest that upwards of US\$ 7.6 trillion in financial wealth is held offshore, of which 80% is estimated to have not been declared to national tax authorities (Zucman 2015). While at the global level this is equivalent to 8% of financial wealth, the share of national wealth held abroad for some developing regions is much higher: 30% for Africa and 22% for Latin America (table 3).

Table 3  
**Estimated national financial wealth held offshore**

Region / country	Offshore financial wealth	Percent of national financial wealth held offshore
Europe	2,600	10%
United States	1,200	4%
Asia	1,300	4%
Latin America	700	22%
Africa	500	30%
Canada	300	9%
Russian Federation	200	52%
Persian Gulf	800	57%
<b>World</b>	<b>7,600</b>	<b>8%</b>

Source: Zucman (2015).

Recent results of tax amnesties in Latin America point to significant undeclared offshore holdings and give credence to these findings. While the characteristics of these programs differed between countries – see CEPAL (2017) for details – they generally allowed taxpayers to declare their assets in return for an income tax payment at a reduced rate on the declared amount. As highlighted in table 4, the programs in Argentina, Brazil and Chile resulted in the declaration of a significant amount of previously undeclared assets. In particular, in Argentina fully US\$116.8 billion in assets were declared, an amount equivalent to 21% of the country’s GDP. In all three countries these programs resulted in a significant inflow of revenues through the payment of taxes and fines, ranging from 0.6% of GDP in Chile to 1.8% of GDP in Argentina. A number of other countries in the region are putting similar tax regularization programs into place, including Mexico and Peru which launched programs during 2017 and are currently in process.

Table 4  
**Results of recent tax amnesties in Latin America**

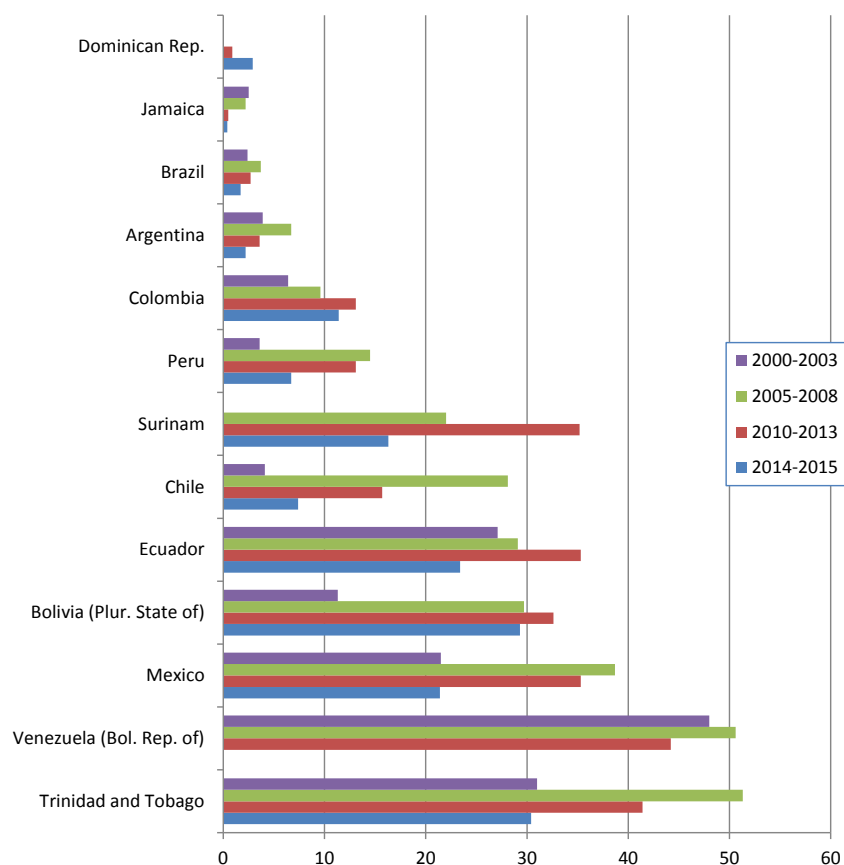
Country	Number of declarations	Value of undeclared assets registered	Value of taxes / fines paid
Argentina (2016-2017)	254,700 (96% natural persons, 4% corporations)	US\$ 116.8 billion (21% of GDP) (80% of declared assets were held abroad)	US\$ 10.2 billion (1.8% of GDP)
Brazil (2016)	25,114 (99.6% natural persons, 0.4% corporations)	US\$ 53.4 billion (3% of GDP)	US\$ 16.0 billion (0.8% of GDP)
Chile (2015)	7,832	US\$ 19.0 billion (8% of GDP)	US\$ 1.5 billion (0.6% of GDP)

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official documentation.

### C. High dependence on natural resources related revenues

Public revenues deriving from the exploitation of non-renewable natural resources play an important role in financing government expenditures in a number of countries in Latin America and the Caribbean. During the 2005-2008 period these revenues represented on average more than 25% of total public revenues in Bolivia (29.7%), Chile (28.1%), Ecuador (29.1%), Mexico (38.7%), Surinam (22.0%), and more than 50% in the cases of Trinidad and Tobago (51.3%) and Venezuela (50.6%) (figure 15).

Figure 15  
**LATIN AMERICA AND THE CARIBBEAN: SHARE OF FISCAL REVENUES FROM NON-RENEWABLE NATURAL RESOURCES IN TOTAL REVENUES, 2000-2016<sup>a</sup>**  
*(Percentages)*



Source: Economic Commission for Latin America and the Caribbean (ECLAC).

<sup>a</sup> Includes tax and non-tax revenues from hydrocarbons and mining. Data refers to revenues of the central government except in the case of Argentina (non-financial public sector), Bolivia (general government), Brazil (general government), Colombia (non-financial public sector), Ecuador (non-financial public sector), Mexico (federal public sector), and Peru (general government).



As these revenues have fallen on average, relative to GDP, to pre-boom levels, so has their participation in total revenues in a number of countries. For example, revenues from non-renewable natural resources in Mexico and in Trinidad and Tobago in the 2014-2015 period have returned to the levels registered in the 2000-2003. However, in a number of countries the participation of these revenues remains higher than in the pre-boom period, reflecting an increase in production, this is the case in countries specialized in mining (Chile and Peru) as well as emerging producers of hydrocarbons (Bolivia and Colombia).

The continuing dependence on revenues from non-renewable natural resources poses a significant challenge for policymakers in the region. The high correlation between international commodities prices and revenues based on commodities, combined with their high share in overall revenues, creates the potential for significant volatility. Bova, Medas, and Poghosyan (2016) find that the average amplitude of changes in real commodity prices during periods of booms and busts are of the order of 40% to 80%, depending on products. In some cases the amplitude can reach in excess 200%. As a result, these authors estimate that fiscal revenues for oil producers can swell by 8-13% of GDP during upswings, with declines of upwards of 15% of GDP during downswings.

Additionally, this volatility reinforces the typically pro-cyclical nature of fiscal policies in developing countries. van der Ploeg and Poelhekke (2009) argue that rising government spending in response to windfall natural resources related revenues increases overall macroeconomic volatility to the detriment of growth. Fiscal rules that could serve to dampen these swings are not widespread in the developing world, but in some countries they have reduced the pro-cyclicality of fiscal policies during the last decade. Céspedes, Parrado, and Velasco (2014) find that in Chile the adoption of a fiscal rule has allowed for the accumulation of savings during good times to soften the blow of downswings, allowing the country to adopt a modestly counter-cyclical fiscal stance.

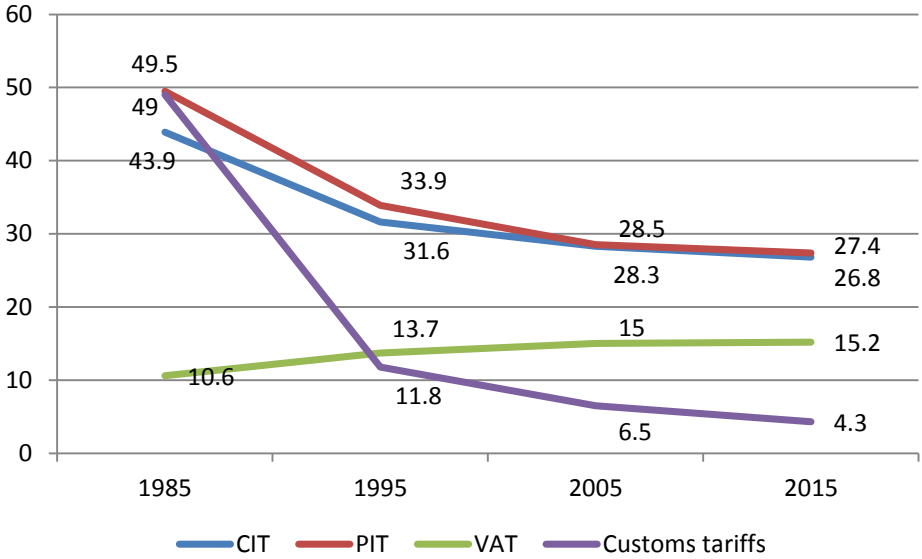
High dependence on non-renewable natural resources has also been linked to lower levels of domestic resource mobilization through taxes. Ossowski and González-Castillo (2012) find that natural resource related revenues in Latin America and the Caribbean have a statistically negative impact on other public revenues, though to differing degrees depending on tax instruments. More generally, Crivelli and Gupta (2014) find that in a sample of 35 resource-rich economies across the

globe, each additional percentage point increase in revenues from natural resources there is a 0.3 percentage point decline in other revenues.

### D. Harmful tax competition

In response to deepening globalization policymakers in the region have repeatedly taken measures – such as lower tax rates, or offer incentives – in the hope (often vain) of attracting investment to their countries. For many developing regions, as is the case in Latin America and the Caribbean, this has resulted in a race to the bottom, with countries vying to offer the most “attractive” fiscal framework for potential investors, or at the very least providing a comparable package to that of their neighbors. The most visible manifestation of this has been the secular decline in income tax rates, which nearly halved between the mid-1980s and 2015 (figure 16).

Figure 16  
**LATIN AMERICA: GENERAL RATES FOR THE MAIN TAXES <sup>a</sup>**  
*(Percentages)*



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of D. Morán and M. Pecho, “La tributación en América Latina en los últimos cincuenta años”, Inter-American Center of Tax Administrations (CIAT), 2017.

<sup>a</sup> Simple averages.

Tax incentives, of which the public may not be fully aware, have been used extensively in the region as a means of attracting – or even maintaining – foreign direct investment (FDI). The region’s long experience with tax incentives calls into question their effectiveness. In part, this is due to the fact that investment decisions are largely determined by the quality of the institutional framework, and firms in fact appear to afford little importance to tax advantages (CEPAL 2015). Indeed, many investments would very likely have materialized anyway, given a given country’s endowment of other investment determinants such as access to key resources or market size.

The doubtful effectiveness of tax incentives in Latin America also reflects the fact that the majority of fiscal incentives on offer take the form of tax holidays, which often have a limited relation to the actual performance of the particular investment. Agostini and Jorratt (2013) in a survey of 10 countries in the region found that of the 337 incentives identified, fully 256 were exemptions or tax holidays (76%) (table 5). These authors found that instruments with a stronger link to investment outcomes – such as accelerated depreciation, investment credits or investment allowances – were little used in the region.

Table 5  
**LATIN AMERICA (10 COUNTRIES): NUMBER OF FISCAL INCENTIVES FOR INVESTMENT BY TAX INSTRUMENT AND TYPE OF INCENTIVE**

Type of incentive	Tariffs	CIT	VAT	Other	Total
Credit		12			12
Deduction		24			24
Deferral		16	7		23
Stability	3	6	2	3	14
<b>Exemption (Tax holiday)</b>	<b>62</b>	<b>102</b>	<b>63</b>	<b>29</b>	<b>256</b>
Reduced rate		7	1		8
Total	65	167	73	32	337

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of Agostini and Jorratt (2013).

Note: Covers Argentina, Chile, Colombia, Dominican Republic, Ecuador, El Salvador, Guatemala, Honduras, Nicaragua and Peru.

Fiscal incentives also come at a significant cost, which must be balanced against any potential gains. Tax expenditures aimed at attracting investment are estimated to have resulted in significant annual foregone revenues in Argentina (1.1% of GDP), Colombia (0.8% of GDP), Chile

(2.2% of GDP), Ecuador (1.6% of GDP) and Guatemala (0.9% of GDP) (Agostini and Jorratt 2013). Additionally, the heavy use of tax holidays creates incentives to game the system, leading them to become entrenched and resulting in a permanent loss of revenues.

### **3. Recent policy responses and potential options for mobilizing domestic resources in challenging economic times**

For policymakers in Latin America and the Caribbean boosting domestic resource mobilization is an imperative and is very much a prominent topic of regional debate. Elevated and persistent fiscal deficits and rising public debt necessarily require a review of tax policies, as simple expenditure cuts alone are unlikely to be enough on their own, especially given the existing needs that exist in the region for social services and public investment in infrastructure.

However, after a period of intense reform – between 2010 and 2015 15 countries implemented significant changes to their tax codes (Arenas de Mesa 2016)<sup>3</sup> – there exists a certain amount of “reform fatigue” in the region. For example, in Mexico after enacting a tax reform in 2013 the government committed itself to not change the tax system between 2014 and 2018 in order to provide economic actors with certainty about the fiscal system with the aim to boost investment and growth.<sup>4</sup> Indeed, in a period of slow growth, tax stability is being seen as a means of attracting and even maintaining investment.

In the short-term countries may consider taking measures to grow revenues organically by strengthening their existing tax systems. Many countries in Latin America and the Caribbean are implementing or considering measures to reduce tax evasion and avoidance as a means to generate additional revenues. For example, electronic invoicing – which facilitates compliance and reduces administrative costs for tax administrations – will be mandatory in 11 countries of the region in 2017, with several others considering its implementation (CEPAL 2017).

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<sup>3</sup> These include Brazil (2015), Chile (2014), Colombia (2010, 2012, 2014), Dominican Republic (2012), Ecuador (2011), El Salvador (2011), Honduras (2010, 2013), Guatemala (2012), Nicaragua (2012), Mexico (2013), Panama (2010), Paraguay (2012), Peru (2012, 2014), Venezuela (2014).

<sup>4</sup> Acuerdo de Certidumbre Tributaria, available at: [http://www.shcp.gob.mx/Biblioteca\\_noticias\\_home/acuerdo\\_gabinete\\_mexico\\_prospero\\_27022014.pdf](http://www.shcp.gob.mx/Biblioteca_noticias_home/acuerdo_gabinete_mexico_prospero_27022014.pdf)

Tax administrations in the region are increasingly exploring the potential of linking information between different data sources to identify potential cases of tax evasion and avoidance. In Mexico, for example, thanks to the widespread use of electronic invoicing, the existence of institutional databases and the information received by the tax authority, audits began to be conducted with a view to identifying inconsistencies between the information provided by taxpayers and that available elsewhere. Likewise, in Costa Rica the linking of information from third-parties to administrative records has allowed the tax administration to identify tax payers in arrears, which has resulted in the recovery of significant of tax revenues.<sup>5</sup>

These efforts within the domestic sphere are being complemented by greater sharing of tax and financial information among countries. In Latin America and the Caribbean, 11 countries have signed the Convention on Mutual Administrative Assistance in Tax Matters, a multilateral agreement designed to promote international administrative cooperation on tax advice and collection, with a view to combating avoidance and evasion. The Convention extends the network of countries and jurisdictions with which information can potentially be exchanged for tax purposes and has now come into force in seven of them (Argentina, Brazil, Chile, Colombia, Costa Rica, Mexico and Uruguay).

Of the countries in the region, Argentina, Colombia and Mexico are noteworthy for having committed themselves under the Multilateral Competent Authority Agreement on Automatic Exchange of Financial Account Information to conducting their first automatic exchange of banking information for tax purposes in September 2017, while another four countries (Brazil, Chile, Costa Rica and Uruguay) will do so in September 2018. A large number of jurisdictions are signatories to the convention – 95 as of August 2017 – which will allow countries to greatly enhance their monitoring and control of the foreign assets of their nationals.

The success of recent tax amnesties in the region, as discussed above, which allowed taxpayers to declare assets held overseas may reflect to some extent the increasing knowledge of these agreements in the region and that there are soon to enter into effect. As an example, the regularization program launched by Mexico in 2017 mentioned the coming automatic exchange of financial information prominently in its communications to the public.

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<sup>5</sup> <http://www.hacienda.go.cr/noticias/14089-en-el-2016-tributacion-recupera-cerca-de-13-mil-millones-mediante-plan-de-control>

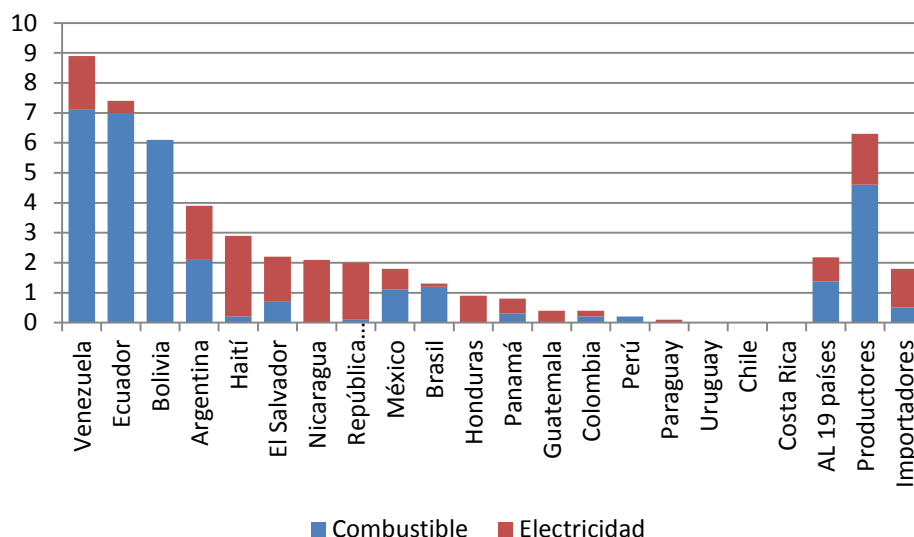
Additionally, 65 jurisdictions – as of July 2017 – have also signed the Multilateral Competent Authority Agreement on the Exchange of Country-by-Country Reports, the purpose of which is to establish the rules and procedures needed for the competent authorities in signatory jurisdictions to be able to implement the automatic exchange of country-by-country reports on the global operations of multinationals. These reports will provide tax administrations with an overview of these companies' operations, as they must indicate where firms' profits, taxes and economic activities are declared. Specifically, they will have to report their revenues, profits before tax, corporation tax paid and accrued, number of workers, stated capital, undistributed profits and tangible assets in each of the jurisdictions where they operate.

Domestic resource mobilization could also be bolstered through the reform of fiscal incentives in the region. As discussed above, these incentives entail significant foregone revenues and therefore their use should be cost-efficient, effective and transparent. As there is arguably a role for their continued existence within the framework of the Sustainable Development Goals – for example, to spur the development of markets for low-carbon products or drive investments with high social or environmental returns – countries should seek to reform their incentives frameworks to incorporate the latest in international best practices.

In the specific case of Latin America and the Caribbean, this will require a phasing out of tax holidays in favor of performance-based or investment-linked incentives such as accelerated depreciation, investment credits or investment allowances. Additionally, there is a need to establish strong institutional frameworks to ensure that incentives are granted on the basis of principled cost-benefit analysis and are fully transparent (both for citizens and for potential investors). Finally, monitoring and control mechanisms must be built into future contracts to limit potential abuses of incentive programs – including ongoing cost-benefit analysis.

Another area that merits specific consideration in developing regions, and Latin America and the Caribbean in particular, is the use of subsidies for energy products and electricity (Di Bella et al. 2015). These are widespread in the region, with an average cost during the 2011-2013 period of 1.4% of GDP per year for fuels and 0.8% of GDP per year for electricity (figure 17). While the use of these subsidies have been justified on various grounds – often responding to social or industrial policy aims – they create significant fiscal and economic costs, and in a highly unequal region are largely captured by individuals in higher deciles of the income distribution. Reform of energy subsidies is politically challenging, but it would pay significant dividends in the long-term.

Figure 17  
**LATIN AMERICA: ENERGY SUBSIDIES BEFORE TAXES, 2011-2013**  
*(Percentages of GDP)*



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of Di Bella et al. (2015), “Energy subsidies in Latin America and the Caribbean: Stocktaking and policy challenges”, IMF Working Paper, Nº WP/15/30, Washington, D.C., 2015.

Achieving sustainable and inclusive growth will however require more fundamental reforms that recognize the endogenous role of domestic resource mobilization in the development process. To that end a fundamental barrier to achieving the 2030 Agenda for Sustainable Development is the high level of inequality that exists in the region and other developing regions, that severely limits the actualization of the fundamental human rights embodied in the Sustainable Development Goals. ECLAC has been at the forefront of this issue in Latin America and the Caribbean, advocating forcefully for putting equality at the center of development policymaking (CEPAL 2010, 2012, 2014, 2016c).

Outside the region as well there is increasing recognition of the negative impacts of inequality on the development process and on economic growth. Ostry, Berg, and Tsangarides (2014) find that inequality is harmful for medium term economic growth, even when controlling for the potential negative impacts arising from redistribution policies; additionally growth spells are found to be longer when inequality is lower. These findings are further bolstered by recent research by the IMF (2017), which find that higher income taxes for individuals in the top 1% of the income distribution would not result in a negative impact on economic growth.

To that end, a strengthened mobilization of domestic resource through direct taxation would not only serve to significantly decrease income and wealth inequality, with the potential for pro-growth impacts, but it would also provide the revenues necessary to finance high quality public services and benefits as defined in the Sustainable Development Goals. ECLAC has called for governments to pursue a renovation of the fiscal pacts that exist in their countries, mainstreaming the Sustainable Development Goals as a means of re-engaging with their citizens and reestablishing a sense of common reciprocity, where citizens commit to paying taxes in exchange for public services and investment.

#### **4. Building international partnerships to bolster domestic resource mobilization efforts**

Mobilizing the resources required to achieve the Sustainable Development Goals, and to do so in a manner that recognizes that domestic resource mobilization is endogenous to the development process, will necessitate a significant effort on the part of the international community to support these activities. Both the Addis Ababa Action Agenda and the 2030 Sustainable Development Agenda clearly foresaw these needs, and encouraged countries to take steps to support developing countries to improve domestic capacity for tax and other revenue collection.

The recent success of the G20/OECD Base Erosion and Profit Shifting (BEPS) project, which catalyzed a significant upgrading of international best practices for dealing with aggressive tax planning in a relatively short amount of time, is suggestive of the potential for creating meaningful policy changes in the framework of an international partnership. The emerging network for the automatic exchange of financial information and detailed company information from multinationals gives further evidence to the importance of bringing countries together to foment change.

However, at the global level there is currently a lack of an institutional forum with a strong mandate to push for international fiscal cooperation. Within the United Nations system the Committee of Experts on International Cooperation in Tax Matters provides key support to developing countries in the area of taxation policy, but their remit does not extend to serving as a permanent intergovernmental body charged with forging greater international tax cooperation.



Recent efforts by the OECD – the *inclusive framework on BEPS* – may serve to bolster the adoption of the BEPS package of measures, but without universal membership and a strong multilateral mandate it too is limited in its ability to drive countries towards greater international fiscal cooperation. To that end, the creation of an intergovernmental organ within the United Nations with a strong mandate in the area of international fiscal cooperation would be a key step towards achieving the aims of supporting financing for development worldwide.

At the global level, within the framework of the Sustainable Development Goals – in particular, goal 17 – greater efforts are needed to provide critical support to developing countries in the area of domestic resource mobilization. These efforts can be assisted by measures to promote the rapid adoption transparency measures such as automatic exchange of financial and fiscal information. Additionally, the international community should review potential multilateral instruments to tackle double non-taxation and aggressive tax planning in developing countries (including a review of all tax related provisions in double taxation treaties and bilateral investment treaties).

At the regional level there is substantial scope for South-South cooperation and policy coordination to boost domestic resource mobilization. Harmful tax competition saps revenues in many developing countries, therefore efforts to potentially harmonize corporate income tax systems and or rates could place a lower bound on any potential race to the bottom. Likewise, fiscal incentives should be reviewed with an aim to adopting a regional code of conduct in their application to prevent the excessive erosion of the tax base.

South-South cooperation could also play a key role in building domestic resource mobilization capacities in the region. Efforts in this area could be bolstered by the creation of a regional working group on taxation issues to facilitate the exchange of information and best practices. Likewise, within the same framework the creation of regional tools to facilitate analysis of international transactions (a regional database of arm's length pricing information, etc) would go a long way to increasing access to the information necessary for tax administrations to properly review and audit tax filings.

Finally, these efforts to build greater international partnerships must be accompanied by the adoption of concrete policy measures at the country level. To that end, it is key to raise awareness among all relevant economic authorities of the crucial importance of greater cooperation in tax affairs, including between countries as well as between ministries in countries. Tax administrations

must continue to be strengthened, especially in the area of international taxation, in order to gain the benefits of greater international cooperation. In the same vein, tax codes must be updated and brought into line with newly established best practices (BEPS), empowering tax administrations to carry out their duties. Finally, governments should undertake a fundamental review of their use of fiscal incentives with the aim of enacting reforms to bring them into line with international best practices.

## Conclusion

Boosting public revenues is a key financing for development policy issue in Latin America and the Caribbean. The rise in the average tax burden over the past decade, most recently supported by numerous tax reforms and measures, has provided relief from plunging non-renewable natural resources revenues, but has not kept pace with public spending demands. Future measures in the region must not only contemplate an increase in the tax take, but a change in its composition, away from indirect taxes and towards a greater participation of direct taxes. Tackling this issue could complicate reform efforts, reflecting the need to forge agreements between economic actors and society at large.

Given the difficult political economy of tax reforms, it is more important than ever for countries to tackle tax evasion and avoidance. Estimates of the revenues losses due to tax non-compliance are substantial. For example, on the basis of existing studies, ECLAC has estimated that in 2015 the region lost \$340 billion in revenues due to the evasion of the income tax and the value-added tax. Importantly, these estimates largely do not take into account the potential losses arising from international tax evasion and avoidance by multinational enterprises and high net-worth individuals. A number of countries in the region are pursuing innovative ways to tackle these issues with the aim to grow revenues. These efforts should be supported, especially by the international community, in line with goal 17 of the Sustainable Development Goals.

High dependence on revenues deriving from the exploitation of non-renewable natural resources continues to present significant challenges to policymakers in the region. Evidence suggests the volatility of these revenues has a negative impact on long-term growth. Likewise, higher levels of commodities-based revenues tend to weaken public revenues from other sources. Moving

towards revenue structures that are more heavily weighted towards permanent revenues will be key for the region. This will be especially important in the future given the expected increased demands on public spending arising from the demographical and epidemiological transitions.

The 2030 Agenda for Sustainable Development offers the countries of the region an opportunity to revisit their most basic social contracts. In the fiscal sphere, the high levels of tax evasion observed in the region suggest that current fiscal pacts are relatively weak. Therefore measures to strengthen domestic resource mobilization must be considered within a more holistic reform of public policies, including both tax and spending. The aim of which would be to renew fiscal pacts between citizens and their States, recreating the essential bonds of reciprocity to ensure that the payment of taxes results in the provision of high-quality public goods and services (CEPAL 1998, 2013).

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