**REFLECTIONS ON TAX REFORM IN GUYANA, 2012\***

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***Sunday Stabroek News Columns***

***January 15 – March 25, 2012***

 \*Articles written in response to President Ramotar’s Tax Reform Committee.

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**Sunday, January 15, 2012**

***The Politics and Economics of Tax Reform - Part 1***

**Introduction**Beginning last December 4, 2011 my Sunday columns have been re-visiting the global economic and financial crisis that erupted four years ago, in light of two basic considerations. First, its unexpectedly long duration and the continued absence of confident signs of recovery. And second, the emergence of both a new geographic epicentre to the crisis (the European Union, replacing the United States) and a new set of economic contradictions stalling growth (persistent joblessness, faltering private consumption and investment in rich countries, and the rise of strong political and market hostility towards continued stimulus spending). As readers know, everywhere stimulus spending had spearheaded government efforts aimed at recovery during 2008-2010.

Starting this week I shall switch focus and begin to address a number of local topics. These have become urgent because of 1) what was revealed in my coverage of the global crisis and 2) the opportunity created by the November 28 General and Regional Elections for serious engagement of a number of intransigent problems confronting the Guyana economy. My switching topics at this point however, does not imply that the global crisis has become in any way less of an urgent issue.

**Tax Reform**The first local topic I shall engage is the recent PPP/C’s administration establishment of “another” tax reform initiative. I say “another” advisedly, as both the Government and its IMF benefactors have been touting, up to very recently that there are already serious and successful fiscal reform efforts underway! Thus the IMF in its recent (June 2011) Country Report on Guyana noted the effects of the fiscal reforms led by the Guyana Revenue Authority (GRA). It refers approvingly to specific on-going measures, including: improvements to the integrated tax information system; the operations of the tax inspectorate; the functionality of the GRA; as well as training of tax personnel.

Meanwhile, the latest Guyana Poverty Reduction Strategy Paper (PRSP), 2011-2015, states that a Tax Reform Action Plan (TRAP) has been in place since 2003. The aims of this plan include 1) broadening the tax base 2) reducing marginal tax rates 3) enhancing equity and transparency and, 4) strengthening the tax administration system. Measures such as the Vat and Excise Tax legislation are part of the reforms under the TRAP, as well as the introduction of the TIN (tax identification number); organizational reform of the Guyana Revenue Authority (GRA), including IT reform; and the adoption of the total revenue integrated processing system (TRIPS).

Finally, the PRSP boasts “the reform actions of the GRA have met with tremendous success. Tax revenues have grown by an annual average of 13 percent since 2003” (Page 27).

**Committee or National Commission**Despite these publicized efforts and the boast, I believe the tax system remains in dire need of deep reforms. Indeed, I shall argue that these reforms are so deep-seated as to require a far different approach for their resolution than is possible through a Tax Reform Committee made up of persons who are seen as having good working relations with the PPP/C administration over the years, no matter how skilled, proficient and experienced they are.

Today the tax system is fractured and, far too costly, burdensome, and inefficient. It is dysfunctional in relation to promoting economic efficiency, growth, development and welfare because the deep-seated problems are as much political in nature as they are technical (economic). The sure way to overcome this is through the establishment of a broad-based National Commission on Tax Reform along the lines (and for the reasons) to be outlined in this and later columns.

The premise of my proposition is that, at the core of any well-functioning tax system, is the notion of an acceptable “political-social contract” between the major stakeholders. In Guyana, these stakeholders comprise, but are not limited to: 1) individual tax payers 2) corporate tax payers 3) the tax administration authorities 4) the governmental authorities (responsible for taxation laws) 5) relevant corporatist bodies like professional associations, workers and farmers organisations, consumer groups and 6) the general public, especially the intended beneficiaries from the expenditure of tax revenues received.

Readers should note, participants in the illegal underground economy (largely fuelled by tax evasion activities), constitute a very substantial fraction of stakeholders in the tax system. However, I shall deliberately ignore them, since it is my conviction that economic activities founded on illegality cannot be an acceptable foundation for the development of any country in today’s globalized environment.

**Stakeholders**I shall now turn to a brief review of the situation of some of the major stakeholders in order to highlight why a wide ranging National Commission on Tax Reform is needed to help foster the “political-social contract” necessary for generating a reformed and acceptable taxation system.

Among individual tax-payers, both tax avoidance and tax evasion are practised as the flagrant norm. From reports, individual tax payers perceive no acceptable connection between the services they receive from the governmental authorities and their payment of taxes. Anecdotal descriptions suggest many view the payment of taxes as a “compunction” and far from a “willing” exchange for benefits they expect to receive. There is therefore, no notion of a binding “political-social contract” between tax-payer and the tax imposing authorities. In this circumstance, the state is not regarded as a “moral leader”, which raises the question as to: why is this the case?

In large measure the behaviour of the law-making authorities is responsible. The Government is seen as continually abusing the fairness of the system because the laws, regulations and policy guidelines implemented seem to favour their cronies and political constituencies and to dis-favour or punish those political constituencies not in support, and regime critics. Meanwhile, the population at large reluctantly accepts the status quo as one in which the tax system is failing to execute a “political-social contract” acceptable to key stakeholders. The principles of openness, transparency, fairness and justice do not stand out.

Next week I shall continue this discussion of stakeholders situations and then go on to pay some attention to the more economic features of the tax system and the primary goals of its reform.

**Sunday, January 22, 2012**

***Tax Reform 2: Blindsided by foolishness and foolhardiness***

**Introduction**There is considerable irony to the fact that, as I pointed out last week, less than six months after the Poverty Reduction Strategy Paper (PRSP 2011-15) had highlighted the on-going Tax Reform Action Plan (TRAP) in force since 2003 as a “tremendous success”, the incoming minority PPP/C administration, in one of its very first deliberate post-elections economic policy actions in December 2011, has established a Tax Reform Committee! This action puts the claim of “tremendous success” into proper perspective, and perhaps confirms the view held by most thoughtful Guyanese that today’s tax system is indeed, as I claimed last week, “in urgent need of deep-seated reforms”. This ironic situation may well be a classic example of an incoming political administration of the same political ilk as the out-going administration, being blindsided by the foolish and foolhardy actions and statements of its predecessor.

In my previous column (January 15, 2012), I had challenged the wisdom of establishing a Tax Reform Committee to pursue this objective. My main concern is that this approach frames the task of tax reform in a far too “technicist” way. Experience shows that successful tax reform in circumstances like those in Guyana requires both a political and technical (economic) approach to this task. Close study also reveals that worldwide, well-functioning tax systems are founded implicitly or explicitly on the notion of a political-social contract among its key stakeholders. To achieve this in Guyana, I had respectfully recommended, as a minimum, the establishment of a National Commission on Tax Reform. This body should be empowered with all the deliberative, consultative, and legal authority normally found in such august bodies.

In support of this proposition, I started to describe last week what I believe is the mindset of the key stakeholders to Guyana’s tax system. So far I have briefly outlined the situation of three of these: individual tax payers; the law making authorities; and, the public at large. This week I shall conclude the descriptions of the remaining stakeholders.

**Tax Administration Authorities**The tax administration authorities as a group of stakeholders also follow the basic patterns outlined last week. Tales abound about how friends, contacts, and the criminally inclined are “facilitated” by the tax administration. Tellingly, perceived associates and members of the ruling political elites are also “facilitated” by these authorities. While these observations by themselves would represent a system gone horribly wrong, we find that, in addition, many tax payers look on the tax administration authorities as not only rewarding those who are politically favoured, but also using the system to punish those politically out-of-favour.

Regrettably, once the tax system acquires the reputation of being misused and abused for political ends, it becomes exceedingly difficult to recover the authenticity of the system. To recover authenticity requires a social and political process founded on redress and reconciliation, as the essential way towards embedding transparency, fairness, efficiency and other desired attributes into the system. Such a process underscores my call for a National Commission on Tax Reform as opposed to a Tax Reform Committee.

**Business Tax-Payers**As a rule corporate and other business tax payers not only support but indeed thrive on the dysfunctionalities of the tax system. Like their individual tax paying counterparts, tax avoidance and tax evasion are flagrantly practised as the norm. This group however, is much better equipped than individuals to pursue their illicit activities. Businesses are generally better able to employ skilled personnel to aid them in these endeavours. Financial, legal, accounting and tax advisory enterprises routinely collude with businesses to defraud the tax revenue authorities. This is so well-known by the average Guyanese that I cannot imagine the tax administration authorities are unaware of its pervasive effects on the non-payment of taxes.

In later columns I shall discuss the economic issues centering on the measurement of what economists term the tax-gap, which this generates. For now readers should be aware that in their routine activities they would have certainly come across several instances of businesses practising tax evasion. Good examples are: 1) when they are given the option of paying VAT or not 2) when they observe under-reporting by local producers of their output of goods and services 3) when they observe the undervaluation of imports 4) when they observe the widespread availability for sale (or public display) in business establishments of “smuggled” items like cigarettes, alcohol, and beverages 5) when they observe the falsification of labelling details on products for sale and, 6) when they encounter goods and services, which are  illegally obtained, being re-sold.

Added to this, powerful businesses have a reputation of “bullying the tax authorities”. Occasionally incidents are reported in the media, as when Stabroek News (28/9/2011 – Page 14) reported conflicts between a Shivraj firm and the National Insurance (social security) tax inspectorate. Perhaps local and overseas firms operating in the minerals sector (gold, diamond, manganese, copper and petroleum) have the worst reputation for tax avoidance. The desperate efforts by government to sustain the scramble for the country’s mineral resources seem to be interpreted by these businesses as a licence for non payment of taxes. Finally, another glaring example has been recently revealed in the FBI “sting operation” to entrap operatives in the Guyana Gold Corporation, as revealed in the Canadian press (Vancouver Sun).

**Corporatist Bodies**Various corporatist bodies also constitute a key group of stakeholders in the tax system. As would be expected, these include established workers (trade unions) and farmers’ organisations, as well as consumer groups, NGOs, and professional/technical organisations. Generally, these stakeholders have a very strong interest in the promotion of tax reform, as they are acutely aware of the deep-seated defect.

Next week I shall continue this discussion and begin by directing attention to where the taxes come from.

**Sunday, January 29, 2012**

***Tax Reform 3: The Taxes We Pay***

**Introduction**The mind-set of five major groups of stakeholders to the tax reform process (individual tax payers; the law-making authorities; the public at large as beneficiaries of government spending; the tax administration authorities; corporate and other business tax payers; as well as organisations like unions, farmers’ organisations, consumer groups and professional associations interested in greater transparency, fairness and efficiency in the tax system) have been briefly described in my two previous columns.

It should be further noted here that two principal considerations may have encouraged the previous Government’s boast that on-going tax reform since 2003 has been “a tremendous success”. When this claim was made the administration had highlighted 1) administrative improvements in tax collections and 2) strong annual growth in tax revenue (in excess of 13 percent annually since 2003).

Next week I shall consider whether these two considerations justify the pronouncement of success, as this directly relates to the question: what are the goals of tax reform? Before treating with this, readers should have some knowledge of 1) total tax revenue collected 2) its relation to total output 3) the contributions made by various taxes to this total and, 4) tax revenues collected in Guyana compared with other countries. I shall attempt this in today’s column.

**Tax Revenue by Type**While the available classification of Guyana’s tax revenue by type is not ideal for economic analysis, what has been reported is adequate for our present purposes. As shown in Table 1 total tax revenue collected in 2010 was G$102 billion. Unlike more developed economies, the share of taxes on goods and services of all kinds clearly predominate, as this represents over 60 percent of the total. When these revenues are disaggregated, however, it is seen that the bulk comes from two sources: Value Added Taxes (27 percent) and Excise Taxes (21 percent) of the total.

In 2010, taxes on income constituted the second main pillar, at 39 percent of the total.  When further disaggregated the resultant shares are 21 percent for taxes on business; 15 percent on personal taxes; and, 2 percent came from taxes collected from the self-employed.

Based on the available classification, tax revenue from international trade and international transactions was equal to ten (10) percent of the total.  The main sub-categories are: imports at eight (8) percent, and travel tax (G$1 billion or one (1) percent).  If, however, Value Added Taxes on imported items, 15 percent (as against domestic supplies at 12 percent) are added to excise taxes on imported items, 19 percent (as against domestic supplies at 2 percent) we get the grand sum of 42 percent for import-based tax revenue.

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| ***Table 1: Guyana: Distribution of Tax Revenue, 2011*** | | | |
| ***Tax Revenue by Type*** | ***$ billion***\* | ***Percent***  ***of Total***\* | ***Percent of GDP***  ***(at Current Basic Prices)*** |
| 1: ***Total Income Taxes*,**of which:  -          Company Taxes  -          Personal Taxes  -          Self-Employed | **43**  23  17  3 | **38**  21  15  3 | **9.3**  5.0  3.7  0.6 |
| 2:  ***Property Taxes & Estate Duties*** | **2** | **2** | **0.4** |
| 3:***Value Added Taxes, of which:***  -          Imported items  -          Domestic supplies | **31**  18  13 | **28**  16  12 | **6.7**  3.9  2.8 |
| 4: ***Excise Taxes,***of which:  -          Imported items  -          Domestic supplies | **22**  19 | **20**  18  2 | **4.6**  4.1  0.4 |
| 5: ***Taxes on International Trade,  and Transactions, of which:***  -          Imports  -          Travel tax | **11**  10  1 | **10**  9  1 | **2.3**  2.2  0.2 |
| 6: ***“Other” Taxes, etc.*** | **3** | **3** | **0.7** |
| 7: ***Total Tax Revenue*** | ***112*** | ***100*** | ***24.3*** |
| **Note:** \*figures rounded.  **Source:** Government of Guyana, Estimates Vol. 1, 2011. | | |  |

A few observations are pertinent at this stage.  First, the data in Table 1 reveal how little the self-employed contributed to tax revenue (G$3 billion, out of a total of G$112 billion) in 2011. Second, because total tax revenue collected is G$112 billion, the absolute value of tax revenues raised by each type of tax approximates its percentage share of the total. Thirdly, taxes on property (including estate duties) also contributed marginally, at 2 percent of total tax revenue. Fourthly, total tax revenue as a ratio of rebased GDP (at current basic prices) for 2011 was about one-quarter (24.3 percent). And, finally total tax revenue in 2011 increased by 12 percent over 2012 ― about the same as Government’s average rate previously indicated for the period 2003-2010.

**Drawing Comparisons**For readers benefit, Table 2 below shows the unweighted average distribution of tax revenue by type for the 34 Member States of the Organisation for Economic Cooperation and Development (OECD). The ratio of their total tax revenue to GDP is 34 percent, as compared to Guyana’s 26 percent. The range, however, is quite wide, from 19 percent (Mexico) to 46 percent (Sweden). Seven OECD countries have a ratio of 42 percent or over, while two have a ratio of 21 percent or lower.  Further, five OECD countries approximate Guyana’s ratio of 24 percent or less.

|  |  |
| --- | --- |
| ***Table 2: Distribution of Tax Revenue in OECD countries, 2009*** | |
| ***Tax Type*** | ***Percent of Total\**** |
| 1: ***Total Income Taxes*,**of which:  -          Personal Taxes  -          Corporate | **33**  25  8 |
| 2: ***Social Security Taxes,***of which:  -          Employer  -          Employee  -          Other | **27**  15  9  3 |
| 3:***Payroll Taxes*** | **1** |
| 4: ***Property Taxes*** | **5** |
| 5: ***Consumption Taxes,*** of which  -          General  -          Specific | **31**  20  11 |
| 6: ***“Other” Taxes*** | **3** |
| 7: ***Total*** | ***100*** |
| **Source:** OECD Website and Eurostat (2011). | |

Two cautionary observations are warranted. Firstly, the difference in the total tax revenue/GDP ratio between Guyana and the OECD reflects different economic structures. Secondly, apart from structural differences contributing to the different ratios, different incremental trends in economic growth rates and tax revenue elasticity can also result in variations in the tax revenue/GDP ratios. Thus when growth rates rise faster than tax revenue yield, the ratio would fall, and vice versa. That is, if tax responsiveness is rising at a faster rate than GDP, the ratio would rise.

Next week I shall continue from this point and seek to address the question: what ought to be the primary goals of tax reform?

**Sunday, February 5, 2012**

***Tax Reform 4: The Taxes We Do Not Pay***

**Introduction**I have tried to make it clear that my treating with tax reform in current Stabroek News (SN) columns has been deliberate. It is entirely based on the establishment last December, 2011 of a Tax Reform Committee by the incoming Ramotar administration. I share the view that the tax system is in dire need of reform but I hold firmly to the position this is best accomplished through a National Commission on Tax Reform, in which key stakeholders are represented. Only such an august and representative body could command the legal, administrative, consultative, and institutional gravitas required for full public participation in this endeavour. Already there are complaints that the public has little or no idea of what the Tax Reform Committee is doing, when it is expected to complete its task, or even if public involvement is encouraged.

Readers should recall that, less than six months ago, the outgoing Jagdeo administration had laid in the National Assembly its cornerstone economic strategy document, which boasted its on-going Tax Reform Action Plan (in force since 2003) was a “tremendous success”. Support for this assertion was illustrated in the claim that tax revenue had been growing at an average annual rate of 13 percent since then.

It should not escape alert readers this rate of growth is about five-to-six times faster than the real growth of Guyana’s GDP since 2003! I presented data in last Sunday’s column confirming an annual rate of growth of 13 percent for 2010, and further indicated the ratio of tax revenue-to-GDP in Guyana was 26 percent for the same year ― with most of the revenue being derived from taxes on goods and services.

This week I shall address some important related features of this tax revenue ― GDP ratio.

**The Tax-Gap**No doubt most readers would consider Guyana’s tax revenue-to-GDP ratio of 26 percent to be undesirably high in the sense that 1) there is too much taxation and 2) the value received from its related Government expenditure does not justify this. However, perhaps the sadder truth is that total tax revenue collected in 2010 (G$102 billion) is a substantial underestimate of the taxes which ought to have been paid and collected given the tax measures currently in force!

**The Tax-Gap in Guyana**To comprehend why this may be the case, one has to understand the concept of the tax-gap, developed by economists and occasionally estimated in other tax jurisdictions. Simply put, the tax-gap in Guyana may be defined as the difference between 1) the value of the theoretical liability of Guyanese tax payers (based on the existing tax code) and 2) what they actually pay. In practical terms this difference is made up of 1) illegal tax evasion in the regular/official economy (that is, underreporting, not filing at all, or deliberate under-payment of taxes due on legal income earned in a particular fiscal year) and2) illegal tax evasion of income earned in the underground economy. Based on my informal estimation, this difference could well be as large as the total value of taxes actually collected. This is indeed remarkable.

My estimate is based on several considerations; including 1) my own separate estimates of the size of the underground economy, which has been carried in several previous SN columns. (This could plausibly be as high as 50 percent of the officially recorded GDP) and 2) the systematic underpayment of taxes in significant sectors of the Guyanese economy.

One of these sectors has been recently highlighted by the Minister in the newly created Ministry of Natural Resources and the Environment. Echoing earlier estimates carried in a number of reports and research papers dealing with the small-scale mining sector, the Minister referred to declared gold output in 2010 (363,000 ounces) as being only about two-thirds of actual production in that year (600,000 ounces). This difference translates into lost tax payments on about G$80 billion of gold production for 2010.

Other sectors, which are equally notorious are: 1) those profitable independent farmers who for years have paid negligible income/property taxes 2) self-employed professionals who routinely evade paying taxes due on their incomes 3) skilled artisans in similar positions 4) retail outlets of all types that evade VAT and excise taxes 5) foreign companies (particularly those engaged in the scramble for minerals) that inflate expenses and under-declare income.

**Tax-Gap: Other Jurisdictions**As an individual researcher, I do not have access to tax returns for Guyana.  I cannot therefore draw samples from these in order to estimate more accurately the size of the tax-gap.  However, in other jurisdictions this has been done by the authorities. Thus, the Internal Revenue Service Office and the Congressional Budget Office in the USA, as well as the Public Accounts Committee of the UK Parliament and Her Majesty’s Revenue and Customs have reported on their estimates of the tax-gap for their respective countries.

**What do these other estimates show?**The US authorities measure only three components of the tax-gap, namely, non-filing; underpayment; and, non-payment. The last item accounts for 80 percent of their estimated tax-gap. The authorities declare they make no effort to estimate taxes lost through the operations of the underground economy. However, I have included these in my discussion of the tax-gap in Guyana. For recent years various estimates of the US tax-gap converge around US$300-500 billion, or about one-sixth to one-fifth of total tax revenue.

Meanwhile in Britain emphasis is placed on taxes lost through the illegal manipulation of the tax code by corporations and wealthy individuals. Indeed, the authorities express deep concern about the army of accountants, lawyers and financial analysts who seem to dedicate their skills towards evading tax obligations. They claim technical expertise is used to support tax evasion as a priority over professional regard to personal and business social responsibility. Estimates of the tax-gap in Britain range between 10 percent and 35 percent.

Next week I shall wrap up this discussion of the tax-gap.

**Sunday, February 12, 2012**

***Tax Reform 5: The “Nuts and Bolts” of its Design***

**Introduction**Last week I claimed the value of taxes not paid in 2010 but which ought to have been paid under the tax code was roughly equivalent to that actually paid (G$102 billion). Taxes paid therefore were only about one-half that theoretically due. This week I consider some important “nuts and bolts” considerations essential to designing successful tax reform. These support my contention that only a National Commission on Tax Reform can fully address it in all its varied social, political, and cultural dimensions.

**Tax Expenditures**First, the estimate of the Guyana tax-gap, which I provided last week is conservative. It includes three components: 1)the indicators US authorities use (under-reporting; under-payment; and, non-filing) 2) tax-evasion in the underground economy and, 3) serious tax-evasion in such sectors as gold mining; retailing; independent small farming; skilled artisans; and the self-employed. However, it specifically excluded tax giveaways (tax expenditures).

Readers should be aware that, from an economic standpoint, if the tax code offers an enterprise a tax holiday its economic effect is similar to one where the enterprise pays the tax and then the government returns it. In other words a tax expenditure has both revenue and expenditure effects. My solution to this conundrum is for each individual researcher to decide on whether to include tax expenditures when measuring the tax-gap, as long as he or she specifies the components covered.

**Tax Level and Structure**Second, readers need to appreciate the difference between the tax level and tax structure. The tax level is captured in the tax revenue-to-GDP ratio, which as I indicated is 26 percent for Guyana. This simple average was also compared to that for the group of OECD countries (where it ranged from about 19 percent to 48 percent). Recent worldwide estimates though, show a range from under 10 percent (mostly in small, poor, open economies) to about 50 percent (mainly in high income European countries). Data further show that, while the average tax/GDP ratio rises as income levels rise; this is a weak relation.

Economists broadly portray a country’s tax level as a function of its economic structure and preference function or political/social choices. The former depends on such considerations as size; degree of income poverty; level of dependence on natural resources; and degree of openness. Guyana is a small open economy with high levels of both income poverty and reliance on natural resource-based economic activities.

On the other hand, the tax structure refers to the share of various taxes in total tax revenue collection. Based on data I have already provided, the most noteworthy feature for Guyana is the difference in its tax structure when compared to developed economies, particularly:1) taxes on goods and services versus income and property 2) taxes on personal incomes versus business income and, 3) the role of imported items in providing tax revenues through VAT and excise taxes.  
Available data suggest a country’s tax structure is a function of its economic structure; historical evolution; conditions in the countries with which it principally deals; and, preference function.

**Tax Buoyancy and Elasticity**Third, last week I indicated Guyana’s rate of growth of tax revenue as compared to the rate of GDP growth reveals considerable tax buoyancy and a high income elasticity of tax revenue. However, readers should note while these two concepts are related, they do not have the same meaning. Tax elasticity is measured only in the absence of tax policy changes. Therefore, tax policy changes in Guyana (Tax Reform Action Plan (TRAP), VAT, etc.) must be isolated to arrive at this measure. When tax policy changes are not isolated, it is more accurate to speak of tax buoyancy. My reference last week therefore, to the high responsiveness or elasticity of tax-revenue in Guyana (because it grew by several multiples (5-6) of GDP growth since 2003), is better represented by the notion of tax revenue buoyancy rather than elasticity. Further, the overall elasticity of Guyana’s tax system can be interpreted as the average of the elasticity of individual taxes weighted by their individual shares of tax revenue collected.

**Volatility**A related measure to tax elasticity and tax buoyancy is tax volatility. Tax revenue does not flow at a regular steady rate into the Treasury. There are seasonal variations to these flows. I do not want to unnecessarily complicate the discussion for the general reader, but this is the major reason why governments, like Guyana’s, issue short-term Treasury bills ― to smooth out cash flow variations.

However, variation or volatility in tax revenue flows is not only seasonal, but can also be cyclical and secular. It is cyclical, when these reflect short-to-medium term cycles in the level of economic activity. This is captured in the experiences of expansion (boom) and decline (recession) as in the current global economic crisis. Although a weak relation, when economic activity rises, generally tax revenues rise and when it declines vice versa.

Secular declines in tax revenue however, reflect long-run declines in the sources of income from which revenue derives. This can be located in the decline of the whole economy (as in the case of a depression) or in particular sectors from which the tax revenue mainly derives.

Because of the above tax reform should be aimed at reducing both tax revenue volatility and long-term secular decline. To avoid these, taxes must be diversified across the economy and made less reliant on volatile sources of income and employment generation.

Next week I shall conclude this aspect of my discussion by addressing three remaining “nuts and bolts” considerations, namely: “tax stability”; taxation and “economic efficiency”; and the “economic costs” of taxation, before proceeding to introduce what would be my targeted goals for tax reform in Guyana.

**Sunday, February 19, 2012**

***Tax Reform 6: Building Blocks for Redesigning Guyana’s Tax Regime***

**Introduction**Last week’s column briefly examined four of the “nuts and bolts” considerations, which inform tax reform, namely: tax expenditures; tax level and structure; tax buoyancy and elasticity; and, tax volatility. Today, I treat with the remaining five: tax stability; taxation and economic efficiency; tax burden (incidence); the costs of taxation; and, taxation and fairness (equity). Together, these nine items constitute the minimum basic analytical constructs that underlie all tax systems. They are therefore, essential building blocks required for successful re-design of Guyana’s tax regime.  
  
Two additional comments are warranted about the “nuts and bolts” matters previously considered. One, where the value of tax revenue is measured in relation to a base (say GDP) it is absolutely essential that the values used are real, and not nominal; that is, these are adjusted for price increases. If nominal values are used mathematical bias will result. Two, the requirement to isolate the effects of tax policy changes before calculating tax elasticity (as against tax buoyancy) is stringent. This procedure requires a counterfactual analysis (as economists term it). That is, an analysis which hypothesizes an outcome that did not occur (assuming what happened, did not take place)! Of course this manipulation is far easier to do for individual taxes, as opposed to the total tax system.

**Tax Stability**Revenue from taxes varies from year to year. Governments therefore, prefer taxes that do not yield significant annual revenue changes, for the obvious reason that this makes forecasting and planning annual budgets easier. For this reason also governments are wary of taxes that affect revenue stability. I do not wish to unnecessarily complicate this column, but in recommending tax policy changes economists would be careful to indicate the level of projected tax stability by calculating coefficients of variation (CV) for various tax revenue flows.

**Taxation and Economic Efficiency**As I had observed in my analysis of the 2011 Budget (March 6, 2011):“laypersons are wont to confuse economic efficiency with such notions as economic growth, poverty reduction, wealth increase, and productivity enhancement”. However, this is a technical term that specifically refers to an outcome in private markets where the marginal cost of producing an additional unit of any good or service just equals the marginal benefit or satisfaction to be derived from consuming it. This outcome is always assured where perfectly competitive market conditions prevail. This in turn requires several conditions to be present, including 1) many sellers and buyers in the market place and 2) no barriers to entry for new sellers. In such a situation production and consumption are optimized in a private economy, ensuring that the lowest opportunity costs prevail. This is economically efficient because scarce resources are not wasted. Wasted resources indicate market failure. As we shall see below taxation can waste resources through generating market failure.

**Tax Burden (Incidence)**Readers should realize that those who have the legal liability to pay taxes to the Guyana Revenue Authority (GRA) are not necessarily the same as those who feel the economic burden of the taxes. Thus retailers pay over VAT to the GRA, but purchasers carry the burden of the VAT.

Tax burden or incidence refers to the allocation of the burden of paying a tax between buyer and seller. As a rule, most of the burden is borne by the seller if 1) its supply is inelastic or unresponsive to price reductions and 2) demand for the product is highly elastic or sensitive to price changes. The reverse would apply. That is, the smaller the price elasticity of demand and the larger the price elasticity of supply, the greater the burden of the tax on the buyer. Tax burden or incidence therefore describes the effect of taxes on products traded in the marketplace between buyers and sellers. This in turn depends on the elasticities of supply and demand for the taxed items.

**Cost of Taxation**To the average Guyanese the cost of taxation is seen in financial or accounting terms; that is the amount of money paid over to the GRA. From an economic standpoint, however, taxes result in the transfer of resources from the private to public sector of the economy and are not a cost per se. Economic costs are incurred if, and only if, this transfer entails a reduction in the economy’s resources. This reduction can in fact occur in a variety of ways, as indicated below.

First, taxpayers usually utilize scarce economic resources in fulfilling their tax obligations, separate and distinct from the taxes they pay. A good example is the time and effort involved in preparing tax returns. Second, the GRA also utilizes scarce resources to run the tax administration system. Third, over and beyond the resources used by taxpayers and the tax authorities, the general public (or “third parties”) also uses resources to facilitate the administration of the tax system. Good examples are when 1) employers withhold employee taxes under PAYE for payment to the GRA 2) banks and other organisations facilitate the collection and payment of taxes and 3) the media provide public information on taxation.

Furthermore, there is resource distortion (market failure) occasioned by taxes. Taxes create wedges between prices in the market place and those that sellers and buyers receive and pay. Thus, in so far as relative prices efficiently guide economic behaviour, taxation alters this, and hence people’s economic behaviour. Economists refer to this as “deadweight” costs, because buyers and sellers are guided by relative prices in the market place and would suffer welfare losses (surplus) when the market price is raised somewhat by the tax.

Additionally, taxes do not only alter relative prices of products in the market place, they also affect income and indirectly therefore, the incentive for productive factors to engage in economic activity.

I have run out of space and next week I shall continue the discussion from this point.

**Sunday, February 26, 2012**

***Tax Reform 7: Fairness and the Tax Regime***

**Introduction**So serious are the defects in our tax regime I do not believe that Guyanese will be fobbed with anaemic or banal recommendations from the Tax Reform Committee. In the two preceding columns, I treated with eight of the nine analytical constructs, which underlie all tax regimes: (tax giveaways; tax level and structure; tax buoyancy and elasticity; tax volatility; tax stability; taxation and economic efficiency; tax burden; and, the cost of taxation). This week I will consider the ninth and most contentious ― taxation and fairness or equity. Before I address this however, let me add a comment to the “cost” and “economic efficiency” of taxation, which, were considered last week.

Two major generalisations arise from that earlier discussion. First, because from an economic standpoint, taxes transfer scarce resources from the private to the public sector, in order to minimize their distorting economic effects, economists recommend that tax rates should be kept as low as required to reach a given revenue target. And, secondly, the tax base should be made as broad as possible, given the desired goals of the tax system.

Estimates for rich developed economies (with sophisticated tax systems) show that the economic efficiency costs of maintaining well-functioning tax systems, normally range from about one-fifth to one-third of the total value of the taxes collected, although in unusual circumstances this value is considerably higher. In small poor open developing economies like Guyana (with lower administrative sophistication and weaker markets) one can project a worse outcome. Readers would recall from earlier discussion that the economic distortionary costs of taxes derive from their impact on relative prices, with empirical studies revealing that these are proportionately related to the square of the tax rate. Thus, if the tax is doubled or trebled, the distortionary costs would grow four-fold (2x2) or nine-fold (3x3).

**Triad of Considerations**Apart from being highly contentious, tax fairness (equity) is widely recognized as perhaps the most important consideration in the design and reform of tax regimes. Recall that, from an economic standpoint, taxes transfer resources from the private to the public sector. As a consequence, tax fairness emerges as one of a triad of fundamental considerations around which well-functioning tax systems revolve (the other two being, how efficiently and how cheaply are taxes raised).

Regrettably, there is, and indeed can be, no objective standard of tax fairness. Different classes, groups, communities, as well as individuals, hold their own and therefore, widely differing notions of what constitutes a fair tax system. It is for this reason, more than any, why I have strongly advocated a National Commission on Tax Reform as the way to proceed in Guyana. To my mind, this is the only workable modality for arriving at a broad social consensus or contract on what is socially, politically, culturally and economically acceptable as a fair and equitable tax system.

**What is Tax Fairness?**Some economists however, approach tax fairness through the concepts of horizontal and vertical equity. Horizontal equity purports that persons in similar economic circumstances should pay the same amount of taxes, because they have the same ability or capacity to pay taxes. In the tax code this is defined as their having the same amount of taxable income and wealth. While plausible sounding this is illusory. The devil lies in the details of translating this requirement to taxable income and wealth in the tax code; consider a few examples. What if tax-payers have different abilities to evade taxes? This can readily occur in Guyana because tax-payers have differential access to illegal untaxable income trafficked in the underground economy. Alternatively, what if taxpayers in similar economic circumstances have different tastes and expectations? Do these taxpayers enjoy the same welfare? Correspondingly, persons supposedly in similar economic circumstances may be differentiated in their access to the benefits to be derived from government expenditures funded from taxes.

Vertical equity however, purports that “appropriately” differentiated taxes should be applied to tax-payers with unequal economic circumstances (taxable income and wealth). Vertical equity focuses on pre-tax inequalities while horizontal equity focuses on pre-tax equalities. This creates a unique philosophical conundrum, in that tax fairness embodies notions of both sameness (persons in the same circumstances being treated the same) and difference (persons in different circumstances being appropriately treated differently).

Discussion on tax fairness inexorably raises concern about whether the overall tax structure, and/or groups of taxes and individual ones are progressive, proportional or regressive in their impact on the distribution of the tax burden. Progressivity exists when tax rates rise as income rises. That is, the tax structure is graduated in a manner designed to ensure higher income brackets pay a higher share of their income in taxes, than the share paid by lower income brackets. Proportionality requires that all taxpayers pay the same rate or percentage of their taxable income in taxes. Finally, regressivity requires that taxpayers with higher taxable income pay a lower tax rate than those with a lesser amount of taxable income.

**Conclusion**The preceding discussion indicates that Guyanese need to agree on what economists’ term their preference function or the ethical framework, which should guide the tax regime. It is my considered opinion that this cannot be arrived at by a group of “experts”, no matter how well-qualified they are. In this sense therefore, the triad on which a good tax system rests (administrability, efficiency and fairness) has to be forged through the potentially inclusive and participatory modality of a representative National Commission. By the same token, as we shall see in coming columns, reforming the tax system is inextricability linked to concerns about how our taxes are spent. Tax fairness should be seen as budgetary fairness, combining both taxes and spending.

Next week I shall proceed from the observation that tax fairness is illusory and cannot be arrived at without broad-based national dialogue and consultation.

**Sunday, March 4, 2012**

***Tax Reform 8: Tax or Budgetary Fairness and Equity***

**Introduction**Last week I started a discussion on the notion of tax fairness and equity, which I indicated is an essential feature for all well-functioning tax systems and thus tax reform in Guyana. More specifically, I argued that, in regard to tax regimes, fairness and equity simultaneously embody notions of sameness (or pre-tax equalities) and difference (or pre-tax inequalities). Sameness requires that taxpayers in similar economic circumstances (that is, having the same taxable income and wealth) should pay the same amount of taxes, as they are presumed to have similar capacities or abilities to do so. Difference requires that taxpayers with unequal economic circumstances (that is, different taxable income and wealth) should pay “appropriately” differentiated taxes. The above conditions hold if, and only if, we assume: 1) taxpayers’ sources of income and wealth are all equally capable of being caught in the tax net 2) no differences in the benefits from government spending received by taxpayers in similar circumstances, and 3) no differences in taxpayers “tastes”. It is only under these assumptions that pre-tax income and wealth would equal taxpayers’ welfare.

Implicit to this logic is that there is, and can be, no objective standard of what constitutes tax fairness and equity. A social view of the fairness is therefore required. And, for Guyana’s tax system this can only be arrived at through national dialogue, led by a stakeholder representative National Commission on Tax Reform. In my view, this is the only workable modality for arriving at an “ethical framework” (or a “social preference function” as tax analysts term it) for addressing tax reform and fairness in Guyana. Furthermore, the brief comments that I offered last week on “horizontal and vertical equity”, and “progressivity, proportionality and regressivity of taxes”: reinforce how theoretically suspect are contemporary neo-liberal approaches to tax reform. Hopefully, this approach will not be applied to Guyana.

This week I shall wrap-up the discussion on tax fairness and equity. Thereafter, beginning next week, I shall introduce my considered recommendations as regards the desired goals of tax reform in Guyana.

**The preferred tax-base: consumption or income**Neo-classical tax analysts often raise the issue of the relative fairness of consumption-based as against income-based taxes. Their argument describes taxpayers’ income (output) as what they in effect contribute to the size of the national cake (GDP) and consumption as what they withdraw from it. In light of this consideration, they purport that consumption-based taxes are more pro-growth (that is, fostering increases in society’s well-being) than income-based taxes. Moreover, they argue, over the long-run (life time!), consumption expenditure of households is far more stable and therefore a better indicator of sustained ability to pay taxes than income received, as the latter suffers from greater long and short-term variations.

The flaw in this proposition is readily revealed. Readers have only to ask themselves the question: is it fair to say consumption is a better measure of ability to pay? Consider a situation where one taxpayer consumes all his/her monthly income ($50,000) while another consumes the same amount ($50,000) but this represents only half of his/her income ($100,000)! The neo-liberal solution to this obvious weakness is to propose taxing savings as well (that is the difference between consumption expenditure and income). However, from every standpoint this objective would be more easily achieved through directly taxing income. There is no presumptive superiority of consumption-based over income-based taxation.

**Overall impact**The above conclusion also supports the observation made last week that, the overall distribution impacts of both taxing and government spending have to be evaluated before the determination of fairness can be arrived at. A taxpayer who benefits from tax giveaways is not in similar economic circumstances as one who has the same taxable income and wealth without the benefit of tax giveaways. Their welfare positions clearly differ by the value of tax giveaways. It can be said therefore that a broader political economy of tax fairness or equity is not captured in the current theory and/or practice of tax reform. Unacceptable levels of neo-liberal orthodoxy have penetrated tax analysis.

**Taxation and income distribution**Further, most readers are well aware that taxes maybe geared to wider non-economic objectives. Consider as examples; 1) taxes which aim to promote hinterland development over coastal development 2) taxes which promote rural areas over towns; and 3) taxes that support savers over spenders. There are also taxes (like our Value Added Tax) VAT, which are expected to capture income earned in the underground economy when it is spent in the official economy on consuming goods and services. Finally, readers should also note that empirical studies do not provide supporting evidence for income and wealth taxation effectively reducing income and wealth inequalities, which are routinely generated in private market-based economies. This is true for both developed and developing market economies.

As I indicated in earlier columns of this series, in 2010 about two-thirds of tax revenue was generated by taxes levied on the consumption of goods and services (VAT, excise taxes, trade and “other” taxes). Compared to developed economies, taxes levied in Guyana, on personal income and business income only yielded 15 percent and 21 percent respectively. Of note also, taxes on wealth (property taxes) contributed marginally (two per cent) to total revenue in 2010.

I am confident that, in the long run, government targeted spending on the poor in Guyana (pensions, health, social security, and other targeted benefits), offer the greatest scope for supporting budgetary fairness in Guyana.

**Conclusion**Next week I shall begin my discussion on the goals of tax reform in Guyana. A driving conclusion of the analysis thus far is that designing tax reform requires a deep appreciation of 1) the socio-economic structure in Guyana (including political fractures, the pervasive influence of the underground economy, and its openness) 2) the limitations of much of the received tax analysis literature (briefly reviewed in this and earlier columns) and 3) the likely future evolution of the economic structure and therefore sources of tax revenue (including the potential for rapidly increasing reliance on mineral production ― oil, manganese, gold, diamond, etc). Globally, the latter has uniformly created highly complex problems of tax capture and sustainability.

**Sunday, March 11, 2012**

***Tax Reform 9: The Traditional (Standard) Goals of Taxation***

**Introduction**Among other things, in the previous eight Sunday columns of this series on tax reform I have sought to establish three broad propositions. The first of these is that I readily welcome the recognition by the new Ramotar political administration that, contrary to boasts in official documents, which I have cited, Guyana’s tax regime is full of defects and therefore in dire need of reform. This is so even though, like the general public, I am not aware of the “terms of reference” of the Tax Reform Committee the President has established and when it should be reporting. Second, the evidence indicates that the existing defects in the tax system (some of which I drew attention to in previous columns) are sufficiently severe and urgent, as to require nothing less than a full-fledged stakeholder representative National Commission on Tax Reform (invested with the august powers ― legal, consultative, executive and administrative) that such bodies routinely embody, to address them. Third, a propos of this proposal, I have presented readers with a general assessment of the key “building blocks” (nine of them) which tax analysts consider to be essential to all well-functioning tax systems. My remaining aim at this stage is to put forward my view of the desired goals for the reform of Guyana’s tax regime.

I should inform readers there are four traditional (standard) goals of taxation, on which tax analysts seem to agree. While I readily endorse these, I categorise them as non-specific goals. That is, they are applicable to all tax systems. In this sense therefore, they are befitting of a one-size-fits-all approach to tax reform and, from my perspective, therefore, inherently limited. To these I shall add several specific or particularistic goals, based on the requirements and characteristics of Guyana’s economy and society.

To introduce these readers should recall I had concluded last Sunday’s column by drawing attention to three pertinent aspects of Guyana, which affect tax reform, namely: 1) its particular socio-economic structures and deep-seated related features (such as, political fracturing, small size, extreme openness, and the existence of a pervasive underground/parallel economy), which directly affect the functioning of the tax system; 2) the likely future evolution of Guyana’s economic structure, and in particular the potential for rapidly increasing reliance on mineral production. This is worrisome in light of empirical studies that indicate severe difficulties for revenue capture and the sustainability of revenue flows in export mineral-dependent economies; and, 3) the weaknesses of the tax reform analysis literature (some of which I have drawn readers’ attention to) is also a matter of deep concern.

**One-size-fits-all goals**The four traditional (standard) tax goals found in the tax literature are: 1) revenue raising; 2) reduction in excessive income and wealth inequalities; 3) political considerations; and, 4) ability to use taxes in order to influence economic behaviour in private markets. These one-size-fits-all goals, as I have labelled them will be addressed below. Starting next week I shall introduce further Guyana-specific goals, (which may or may not be applied elsewhere).

One is the revenue goal. To be sure, this goal does not simply require taxes designed to maximizing revenue yield, rather, the intention is to raise revenue after adjusting the tax mix so as to ensure stability and sustainability of revenue flows over the short-medium-long term. These therefore require taxes, which are sensitive to the dynamics of economic reproduction in Guyana while keeping to the forefront at all times that revenue is being raised in order to be spent.

Second, there is the redistribution goal. This goal focuses on the tax system as an instrument for remedying the systemic inequalities in the distribution of income and wealth, which private market economies reproduce, if left on their own. I had previously observed that, worldwide, there is no strong supporting evidence that taxes can in fact significantly reduce the systemic reproduction of inequality in market-driven economies. I consequently proposed that the redistribution goal of taxation should be framed in the context of overall budgetary actions, that is, both Government’s taxing and spending tax revenue. The rationale for this is that the empirical evidence does reveal income and wealth equality enhances the rate of economic growth, as well as the reduction in social conflict. As a consequence for me the redistribution goal, while important per se, has a broader purpose, which is the promotion of economic growth and development.

The political goal as presented in traditional/standard tax analysis is often captured in the phrase: “no taxation without representation”. Clearly it is reasonable to expect that groups and individuals would not allow the routine compulsory seizure of their income (which is what taxes do) without accepting the legitimacy of the tax authorities. This goes without saying and is therefore, fundamental to successful tax reform. The corollary of this however, is that, political stability (consensus) and political will are also key ingredients for successful tax reform. It is easier politically to “give-in” to the special interests, which benefit from the existing tax system (especially when, as in Guyana, they comprise important fractions of the ruling political elite) than to confront them with tax reform. I would therefore, place heavy emphasis on the need for political will if the goal is to avoid tinkering with the tax code and push for fundamental and comprehensive tax reform.

Finally, as I have shown repeatedly, in private market economies taxes on goods and services alter economic behaviour because they add to cost and therefore shift the relative prices of goods and services in the market place. This in turn affects their demand and supply, thereby allowing a repricing goal to emerge out of taxation. This is seen when there is deliberate tax-induced alteration of relative prices aimed at producing desired economic effects. There are numerous cases of this type of taxation, for example, 1) taxes that are directed at reducing negative environmental effects (pollution taxes); and, 2) taxes designed to encourage beneficial behaviour (tax exemption for education and medical expenses).

Next week I shall take the discussion on the goals of tax reform beyond these traditional ones.

**Sunday, March 18, 2012**

***Tax Reform 10. Guyana: The Inherent Limits of Traditional Tax Reform Goals***

**Introduction**I trust that there is no ambiguity whatsoever in the minds of readers as regards my opinion of the four traditional or standard goals of taxation, which I introduced in last week’s column (raising revenue; reducing income and wealth inequalities; politically facilitating stakeholder representation in the tax regime; and altering relative prices of goods and services in order to reward-punish economic choices). Putting it as clearly as I can, in my view the traditional goals play obvious and important direct roles in all tax systems, Guyana included. My description of them as one-size-fits-all goals is not intended to be dismissive but only to emphasize that there are other, Guyana-specific goals that have to be considered if tax reform is to be fundamental and comprehensive in its scope. The corollary of this observation therefore, is that, the traditional goals, whilst remaining essential, are inherently limited in their ability to fully address tax reform in Guyana.

**Economic Efficiency**The first additional specific goal, which I introduce, is the requirement that, in the context of Guyana’s circumstances, the tax system is made as efficient as possible from an economic standpoint. In economic terms this requires at least the following three conditions: 1) ensuring resources dedicated to tax collection are utilized at their most effective level 2) minimizing resources dedicated to tax avoidance and evasion, as from an economic standpoint such resources are as real as those dedicated to tax collection, and 3) the resources indicated at 1 and 2 are those utilized by the tax authorities; tax payers themselves; and those third parties that are always involved in tax collection (for example, banks; businesses administering PAYE; social security agencies; VAT and excise tax collectors; legal and enforcement agencies; and so on).

Some tax analysts argue that this goal should be routinely added to the four traditional goals that I have already cited. They classify it as one element of a necessary managerial triad to accompany all tax reform namely: political will; administrability; and, sound implementation. The maxim they put forward is: “a tax system is only as good as it is administered!” I believe most Guyanese would accept this since our tax regime is seen as: capricious, discriminatory, politically biased, cumbersome and non-transparent. Consequently the management goals of reform are transparency, credibility, practicability, fairness, and, political neutrality. To my mind all this adds up to achieving economic efficiency, given the goals of tax reform.

To summarize therefore, a necessary complement of the traditional goals of tax reform is managerial and administrative reform of the agencies of taxation. This cannot be achieved without 1) high level (quality) skilled and professional staffing; 2) the requisite staff training being put in place;3) pay and remuneration at levels required to fairly reward and motivate staff; and, 4) oversight/monitoring/verification (OMV) arrangements so as to eliminate corrupt practices and encourage the judicious execution of duties.  
**Taxpayers ― Thieves or Clients**It may consequently be argued that, in order to transition the existing tax regime in Guyana from what it is, to a reformed system of tax governance, taxpayers have to be treated as clients of the tax authorities and not as potential thieves, tax evaders, or source of bribes. The enormity of this endeavour reinforces my judgement that tax reform in Guyana is not the task of a Tax Reform Committee (no matter how technically proficient) but a broad-based stakeholder-driven consultative National Commission.

**Macroeconomic Goal**The tax system is important both to the promotion of long-term economic growth and development in Guyana, as well as to the promotion of short-run or near-term macroeconomic stability. The latter, means modulation of short-run variations in prices, income, output and employment. In this regard, the Government of Guyana presently relies heavily on both monetary regulation and fiscal policy (taxation and spending). However, worldwide it has come to be realized that the former (monetary policy) is far more flexible and adaptive than fiscal policy in the short-run.

Officially, the Government of Guyana has described its macroeconomic policy goal over the decades as “centered on fiscal discipline, price and exchange rate stability”. Based on this, its fiscal policy has been directed at reducing the government deficit to a sustainable level and in support of price and exchange rate stability. Exchange rate variation is considered as the principal source of price instability and inflationary pressures.

This official posture is to my mind quite reasonable. However, of recent note there have been pressures on the government deficit (public debt), exchange rate and price level. Clearly tax reform will have to address these issues in its recommendations.

Above all, the most difficult consideration is that, in open economies like Guyana, variations in tax revenues tend to be pro-cyclical, rather than the more desired anti-cyclical (which supports government spending in time of need). Thus when export revenues fall in Guyana, output falls and so do tax revenues. But at this time counter cyclical policy (government stimulus spending) is needed to sustain employment and incomes. This problem will become increasingly exaggerated as Guyana’s reliance on mineral exports intensifies in the future. This dilemma calls for innovative taxation, finance, and savings arrangements, as the worldwide experiences of other highly mineral dependent exporting economies reveal.

**Initial Conditions Matter**In conclusion, consideration of these issues clearly highlight that, while tax reform has to pay close attention to initial conditions, Guyana finds itself at a crossroads as it has to also deal with (anticipate) the future dynamics of growth and development. By definition therefore, tax reform cannot be based on the static considerations of initial conditions in Guyana.

Next week I shall wrap us this series of articles on tax reform. After the Tax Reform Committee reports, I shall assess their analysis and recommendations in future columns. However, if the 2012 Budget is presented before that, I shall assess that first, in a manner designed to accompany my previous assessment of the National Budget for 2011 (published in Stabroek News columns (February 6 – May 22, 2011)).

**Sunday, March 25, 2012**

***Tax Reform 11: Closing the debate for now***

**Introduction**For now this is my last column in the series considering tax reform, following President Ramotar’s appointment of a Tax Reform Committee ― the first significant policy initiative of his administration. Regrettably, although the Committee was established months ago, it remains a mystery to the general public. There has been no pronouncement on its Terms of Reference, intended reporting date, or mode of operation. Such non-transparency in public affairs is commonplace, but like most Guyanese I expected in the new post-election political environment the Opposition would have sought a public declaration on the aims and modus operandi of the Committee.

Beginning next week I shall deal with the Budget 2012 and return to discussing tax reform, after the Committee reports.

**Tax expenditures**To recall, last week I introduced two further goals to the traditional (standard) ones previously introduced, namely, the managerial triad and the fiscal policy (macroeconomic) goals. The former refers to administrability, sound implementation and, the political will needed to operationalize reform. The latter focuses on fiscal policy to promote growth, development, and macroeconomic balance (that is, ensuring the tax system has built-in automatic stabilizers in support of government’s spending and revenue flows).

A third goal, I now introduce is the rationalization (if not elimination) of the rampant tax giveaways presently embedded in the tax code. Giveaways (or tax expenditures) have the same economic effect, as if their beneficiaries had paid the taxes due under the tax code (if giveaways were absent), and the government afterwards returned these monies to them. In reviewing the 2011 Budget, I had roughly estimated the value of these tax expenditures (giveaways) to be as large as the tax revenue collected. One year later I stand by that estimate.

**High returns to investments**The fourth goal I recommend follows from the rampant fraud and corruption, which Guyanese contend with in the operations of the tax system. Reform recommendations should recognize that this means high returns can be gained from investments in improved compliance and enforcement of the tax code. It is so cost-effective that expending economic resources on tax administration improvement should be a top most priority.

**Captive taxpayers in a sea of tax evaders**While tax avoidance is legal, tax evasion is not. The line between the two, however, is blurred. And, an army of experts (accountants, lawyers, tax and financial consultants) are determined to keep it that way. As a result, there are certain groups of taxpayers, who are held “hostage” by the tax authorities. By “hostage” I mean these taxpayers are forced to carry a disproportionate burden of taxes, especially, individual income taxes under the P.A.Y.E. arrangements. These taxpayers work mainly as regular (non-contract) employees in the Central Government, Public Sector enterprises and organisations, as well as large long-established private firms.

A fifth goal therefore, is the broadening of the personal income base to improve collections from self-employed professionals and non-professionals (farmers, trades persons, service personnel) and persons working in businesses where non-payment of taxes has become routine.

**Local government taxation**A sixth goal is to address the basic defects in the system of local government taxation. While I admit this cannot be accomplished without the reform of local government in Guyana, I merely wish to draw attention to the structural features of local government taxation, which needs to be addressed. These are the determination of 1) a stable tax base 2) a suitable tax rate formula (one that reflects the varying capacities of the local authorities), and, 3) a legal formula for sharing of Central Government revenue (after taking into full account issues of size and scale as these impacts on tax collection and compliance, spending and oversight).

**Taxation, globalisation and regionalisation**   
A seventh goal is integrating Guyana’s tax regime into the globalised (and regionalized) tax and financial environment. This environment has certain clear distinguishing features, including: 1) large unstable financial flows (as revealed in the on-going global financial crisis and regional financial shocks, which have severely impacted Guyana’s financial system ―  the collapse of the CLICO and Stanford Financial Groups; 2) an exceptional mobility of productive factors and technology; 3) unprecedented deepening of global/regional financial systems; and 4) the rapid reduction in barriers to trade, financial, and factor flows. These features place a heavy premium on predictability, certainty, flexibility, transparency and economic relevance of provisions in the tax code.

In the case of CARICOM it further means ensuring that Guyana avoids at all costs, a competitive race to the bottom, where Member Countries strive to outbid each other in their tax giveaways. Competition for investment flows should rest heavily on the quality and management of the tax code, not arbitrary and potentially corrupt tax giveaways.

**Conclusion**The World Economic Forum in its 2011-2012 global competitiveness survey indicates that enterprises in Guyana identify “tax rates” as the third most important problematic factor impeding business activity out of a total of 15 such factors. The first two in the list are “crime and theft”, and “corruption”. This result underscores the far-reaching importance of the work entrusted to the Tax Reform Committee.

In conclusion I therefore, urge as a final goal (12 in total) that the Guyanese public treats the Report of the Tax Reform Committee with the seriousness the subject matter it deals with fully deserves. While I shall return to the topic after the Committee reports, Guyanese should not allow tax reform to be reduced to a matter for “tax experts”. They should be ever vigilant and prepared to reject neoliberal orthodoxy, as this may be presented to them as self-evident tax wisdom! The purveyors of this outlook are wont to rely heavily on recommending practice copied from elsewhere and uncritically applied to Guyana.

As I leave this topic for now readers should note that, after all is said and done, tax reform must address the overall tax system, group of taxes, as well as those individual taxes, which are the most aggravating to the public (VAT).