



Demonstration of the Fiscal Justice Movement in the Dominican Republic, during the campaign 'No to the fiscal measures', in 2012.
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FISCAL JUSTICE TO REDUCE INEQUALITY IN LATIN AMERICA AND THE CARIBBEAN

Tax collection in Latin America and the Caribbean is low in relation to its potential and does not reflect the huge social needs in the region. Public finances reflect an inequitable social and economic model, which perpetuates power concentration and discrimination, and are undermined by high rates of tax evasion and avoidance. Courageous reforms are urgently needed in order to achieve fiscal policies to help reduce entrenched inequalities in the region.

SUMMARY

Despite economic growth and the reduction of both poverty and inequality that Latin America and the Caribbean (LAC) has experienced during the last decade, it still remains the most unequal region in the world.

LAC political and economic elites have shaped fiscal systems which, in general, have either very limited effectiveness in correcting inequalities, or actually serve to deepen them. For inequality and exclusion to be overcome, this fiscal injustice must urgently be confronted. It is characterized by:

- Insufficient tax collection and unsustainability: in general, less money is collected than should be, and there is a strong dependence on unstable public revenue sources, which are unpredictable and socially and environmentally unsustainable;
- Regressive taxation and imbalance in the contributions of the different activities and economic agents: which manifest in a higher effective tax burden on wages and consumption than on income and wealth;
- Inefficiency to promote decent and sustainable economic progress and upward social mobility of the majority of the population;
- Fiscal policy often reflects traditional views about women's role in society, thereby broadening existing gender gaps;
- High propensity for tax evasion and avoidance;
- Weak institutions and representativeness: which manifest in persistent corruption, poor accountability at all levels, a lack of transparency in the planning and implementation of fiscal policies, and also a low tax culture.

A fair and equitable fiscal system is one that consistently combines tax and public spending policies with tax and budget management in order to meet the following general principles:

1. **Full compliance with the redistributive function of the state through public budgets.** That is, sufficient and stable public spending to support quality and well-oriented basic social services, as well as strong mechanisms of social protection and reinforcement of the resilience of population groups vulnerable to internal and external shocks.
2. **The attribution of increased prominence to the role of tax systems as the instruments of redistribution of wealth in a country,** and a reduction in the negative impact that regressive and unbalanced tax systems have on the relatively poorest people in terms of the contributions made by the different economic agents to the public coffers. Tax systems should be balanced toward more progressive models, in which wealth and property and not only consumption and wages are taxed more.

3. **Expansion of the taxable base and the scope of national tax systems.** Rationalization of existing tax benefits is required, while reducing to a minimum those that have no clear positive social benefits. It is essential that tax collection is in line with the need to sustainably finance measures to reduce poverty and inequality.
4. **Reduction of the high levels of tax evasion and tax avoidance** by ensuring that fiscal policy is supported by a tax administration system that can monitor tax obligations and facilitate compliance. Related to this, it is essential to ensure effective fiscal cooperation and coordination at the regional and subregional levels, and further strengthen the enforcement capabilities of these institutions.
5. **Along with other public policies, the fiscal system must promote dignified progress for a wider base of the population,** making economic opportunities a reality for areas such as small- and medium-sized enterprises (SMEs) in agriculture or manufacturing, thereby contributing to the configuration of non-exclusive and more cohesive social models. We must put an end to the use of instruments such as tax benefits, subsidies, incentives, among others, for the unrestricted promotion of the excluding extractive model.
6. **Clear benefits must be generated to promote the progressive formalization of companies and working poor people who are invisible to the state.** While it is essential that the majority of citizens and economic sectors are taxed, it is also necessary that this is done in a manner consistent with their ability to pay, the socioeconomic situation in which they find themselves and the way they secure their income or earnings.
7. In coordination with other public policies, **promoting economic diversification and development of environmentally responsible activities that generate quality jobs.**
8. Contributing to national efforts to **dismantle discriminatory views that restrict – for reasons of race or gender – significant sectors of the population from attaining real opportunities for improvement.** In particular, further work must be carried out to study the explicit and implicit impacts of fiscal systems that reinforce traditional roles of women in society, and which deepen the gender gap.
9. **Contributing to the decentralization of political power in the societies of the region.** In this regard, it is crucial that a fair fiscal system, throughout the design, implementation, and monitoring and feedback of the designed policies, draws on an effective citizen participation that represents the interests of historically disadvantaged groups, on the basis of a framework of government transparency and responsible accountability at all levels.
10. In connection with the foregoing, we must **ensure transparency in fiscal reforms** and effective mechanisms to facilitate broad public debate on these reforms.

1 INTRODUCTION

FISCAL POLICY: A STATE'S PRIMARY TOOL TO FIGHT AGAINST INEQUALITY

Fiscal policy, which encompasses both revenue management and the amount and allocation of public expenditure, defines the social vision that a state aspires toward, and is a key tool in the economic and productive development model on which progress is to be based.

Both the revenue structure (how public policies are funded and who contributes to this funding) and the distribution of public spending (whom these public policies favour and for what purpose) are important indicators of the level of commitment to equity and solidarity of a given society. Fiscal policy plays a significant part in promoting inclusive economic growth and mitigating the adverse effects that a certain growth model imposes on the most vulnerable people.

The design of tax legislation can be seen as an expression of the political will. When a government decides, for example, to raise the tax rate of indirect taxes (levied on consumption) or to reduce tax exemptions for medicines and basic commodities, it is making a policy choice to apply the tax collection effort evenly across people and sectors, rather than according to economic capacity, which can in turn lead to greater inequality. By contrast, the introduction of a tax on large personal fortunes, on luxury goods or on the capital gains which are usually concentrated in the high-income sector of the population, demonstrates an intention of the government to redistribute the burden of tax effort and wealth – an expression of social solidarity.

Fiscal policy can provide support to inclusive and sustainable development by directing taxes and public spending in such a way as to help promote the dignified progress of disadvantaged and excluded groups, such as the rural population and poor workers in informal sectors of the economy, as well as to promote environmentally responsible and sustainable production models.

In short, fiscal policy is the expression of a significant aspect of state ideology. It is one of the most powerful tools to fight inequality; even more so when combined with supportive public policies. Fiscal policy is a more effective and accurate expression of a genuine commitment to social transformation than speeches or political rhetoric.

LATIN AMERICA AND THE CARIBBEAN: A REGION WHICH UNDERUSES FISCAL POLICY AS A DEVELOPMENT TOOL

In Latin America and the Caribbean (LAC) much remains to be done to ensure that public finances become instrumental in building more equitable, and, therefore, more unified and cohesive societies. Admittedly, the specific circumstances of each country in the region is different, but this does not diminish the fact that the fiscal policies, and particularly the tax systems in the region as a whole, reinforce inequality. Generally speaking, in LAC, public finances are still fragile, and suffer from a failure to realize the tax collection potential, reflecting an inequitable social and economic model that perpetuates the concentration of power and discrimination of marginal groups, and which therefore is partly responsible for the inequality gaps which persist to this day.

Despite economic growth and the reduction of poverty and inequality in the region during the last decade, LAC remains the most unequal region in the world. Only countries in sub-Saharan Africa and some others in South-East Asia have levels of income as unequal as those of Latin American countries.¹

Many countries in the region have introduced tax reforms which, in some cases, have resulted in a substantial increase in social public spending (some countries capitalized on the economic boom resulting from the rise in the prices of raw materials). The average Gini² Index in the region fell from 53.4 in 2002 to 49.9 in 2010,³ but there remain some starkly unacceptable poverty indicators. At the end of 2012, the population in LAC was about 575 million inhabitants, 167 million of which were poor (28.8 per cent, only one million less than in 2011), with 66 million living in extreme poverty, the same figure as the previous year.⁴ At the heart of the problem is the depth of the historical inequality in the region, which slows and reduces the sustained impact of current efforts, still insufficient, that are made to meet the social objectives.⁵

Inequality, both in terms of outcomes (income and wealth) and opportunities, is an unfortunate reality in LAC; a structural feature of the region. In fact, these inequalities are self-perpetuating, accounting for the persistence of deep poverty, which is experienced generation after generation.⁶

According to the Economic Commission for Latin America and the Caribbean (ECLAC), in 2011, the income of the richest 20 per cent of the population in LAC was 17 times greater than that of the poorest 20 per cent, and this inequality was found to be up to 25 times higher in the most unequal countries.⁷ In 2012, on average, the poorest quintile received only 5 per cent of the country's total income, ranging from less than 4 per cent (in Bolivia, Honduras, Paraguay and the Dominican

Republic) to 10 per cent (in Uruguay).⁸ In other words, for every \$100 of income earned, \$5 reached the poorest and about \$50 the richest. Moreover, the real opportunities for economic improvements are still determined by skin colour, gender, whether one is born in the countryside or in the town, or whether one is born rich or not.

Inequities are an obstacle to the progress of the poorest. True social mobility is possible only in a society in which everyone, regardless of the economic position in which they are born, has the opportunity to progress.⁹ In this regard, LAC can be considered rather immobile, especially at the extremes of the income distribution. In Mexico, 48 in every 100 Mexicans born into households in the lowest quintile of the income distribution remain in that quintile.¹⁰ In the Dominican Republic, less than 2 per cent of the population climbed to a higher income group during the decade from 2000 to 2010.¹¹

It is clear that the fiscal systems in the whole of LAC have done little to reduce the different kinds of inequality. According to information published by the Organisation for Economic Cooperation and Development (OECD) in 2009, while taxes and transfers reduce income inequality by 19 Gini points in Europe, it is reduced by only 2 Gini points in Latin America.¹² This suggests that the fiscal system in Europe fulfils, to some extent, its redistributive purpose, while in the whole of Latin America it is largely ineffective.¹³

In LAC it is necessary to refine and strengthen public spending policies to make them 'more equalizing',¹⁴ that is, to improve the chances of achieving a real transformation of the lives of the poorest people, but it is also necessary to strengthen the role that tax policy plays in combating poverty and inequality. There is substantial evidence that the tax system does not actively support (or indeed hinders) the limited improvements that have been achieved in the region through public social spending. In this regard, it is worth noting a recent study which concludes that, in Brazil and Bolivia, poverty reduction achieved as a result of direct public transfers is counterbalanced by the negative impact of indirect taxes.¹⁵ Consistent with this, another study indicates that, in the case of Bolivia, the Gini index falls by 2 per cent when direct transfers are applied; nevertheless, when the effect of indirect taxes is applied, this index falls by only 0.5 per cent.¹⁶

In summary, a regressive and inequitable tax structure intensifies the unfair concentration of income and wealth already existing in the region, and increases pressure on public spending (already inadequate) to reverse this unequal distribution. The failure to realize the tax potential in LAC countries represents an underestimation of the structural inequalities experienced, and an overestimation of the role of public spending in fiscal policy as the only means to reverse the concentration of income, wealth and opportunities.

2 DIMENSIONS OF FISCAL INJUSTICE IN LATIN AMERICA AND THE CARIBBEAN

LAC political and economic elites have shaped fiscal systems which, in general, have either very limited effectiveness in correcting inequalities, or actually serve to deepen them. To overcome inequality and exclusion, we must confront the different determinants of this fiscal injustice and develop a new way of thinking about public finances. Notwithstanding the underlying practical challenges of implementing such change, the key component necessary, often missing, is the political courage to face these difficulties resolutely.

Box 1. Overall dimensions of tax injustice in LAC

- **Insufficient tax collection and unsustainability:** in general, less money is collected than could potentially be, and there is a heavy dependence on unstable public revenue sources, which are unpredictable and socially and environmentally unsustainable.
- **Regressive taxation and imbalance in the contributions of the different activities and economic agents:** which manifest in a higher effective¹⁷ tax burden¹⁸ on wages and consumption than on income and wealth.
- **Insufficient promotion of decent and sustainable economic progress and upward social mobility for the majority of the population:** social policies are still insufficient to fight structural inequalities arising from exclusion and discrimination. In addition, the fiscal policy in LAC is suited to growth models based on the exportation of hydrocarbons and raw materials, at the expense of other economic sectors, and fails to formalize the economy in ways to improve the working and living conditions of many poor workers.
- **Fiscal policy often reflects traditional views about women's role in society, thereby deepening existing gender gaps.**
- **High propensity for tax evasion and avoidance:** this is underpinned by inefficiency and inadequacy of internal control mechanisms of the tax administration system, and is reinforced by the gaps in international regulation, harmful international treaties, opacity in the financial system and the lack of comprehensive fiscal cooperation and coordination mechanisms on a regional or subregional basis.
- **Weak institutions and representativeness:** which manifest in persistent corruption, poor accountability at all levels, a lack of transparency in the planning and implementation of fiscal policies, and a low-tax culture.

Source: Compiled by author.

INSUFFICIENT TAX COLLECTION AND UNSUSTAINABILITY

Despite recent increases in the tax burden in LAC,^{19,20} on the whole, the total tax collection of these countries is significantly lower than it could be, which is particularly problematic given the structure and the productive and industrial potential of these countries, as well as the significant social needs and gaps in fulfilling them.

Considering the level of per capita income, Mexico had, in the period 2007–2009, an estimated tax revenue gap of 11.5 per cent of gross domestic product (GDP) and Guatemala's was of 7 per cent of GDP.²¹ According to the International Monetary Fund (IMF), the tax collection potential of Paraguay in 2009 was equivalent to 21.8 per cent of GDP. Nevertheless, the tax collection that year was only 13.5 per cent of GDP (15 per cent if contributions to social security are included).²² Overall, public budgets of the countries in the region depend on a significant amount of *tax and non-tax revenues*²³ derived from the exploitation of natural resources. Estimates indicate that Trinidad and Tobago is the Latin American country with the highest degree of tax dependence on natural resources, with a relative share of 45.8 per cent of total revenues during the three years from 2009 to 2011. It is followed by Venezuela with 40 per cent of dependence, Ecuador (34.5 per cent), Mexico (32.5 per cent), Bolivia (29.9 per cent), Chile (17.3 per cent), Colombia (16.2 per cent), Argentina (13.5 per cent) and Peru (9.3 per cent).²⁴ It is worth noting that, in the case of Bolivia, total oil revenues from taxes, shares in YPF²⁵ and royalties held by the state grew by 619 per cent from 2001 to 2005 and from 2006 to 2012.²⁶

Although not in every case, this dependence usually discourages efforts, both at national and especially at subnational level, to significantly increase public revenues from taxes (tax laziness).²⁷ Mexico, for example, has the lowest tax burden in the LAC region (around 10 per cent of GDP, and falling in recent years), but a third of public revenues comes from Petróleos Mexicanos State Agency (PEMEX).²⁸ Some analysts say that the transfer of tax resources from the federal government to local public finances in Mexico meant that local governments were disincentivized from making efforts to collect taxes in their respective jurisdictions to increase revenue of their own. In this way, they avoid the political and electoral costs of imposing new taxes or increasing the existing tax rates. In 2010, out of every 100 pesos²⁹ they received from Mexican federal entities, almost 79 pesos came from the central government.³⁰ Similar effects are evident in the case of Paraguay. The revenues from Itaipú and Yacyretá hydroelectric (representing on average almost 63 per cent of non-tax revenues between 1998 and 2007) appear to be encouraging a lazy attitude toward more efficient for increasing tax collection at the municipal level³¹ via an improved tax on land, which could be crucial to meet the substantial needs of the population in rural areas and could, moreover, help to decentralize land tenure.^{32,33}

This so-called ‘tax laziness’ affects sustainable financing of social programmes, not only because the public income of some countries in LAC is highly dependent on fluctuating international prices³⁴ (and therefore is unpredictable and difficult to manage), but also because of the foreseeable depletion of non-renewable resources. This weakens environmental and social sustainability, since it perpetuates the economic reliance on the indiscriminate extraction of certain natural resources.³⁵

In Bolivia, a recent comprehensive pension reform (Law 065 of December 2010) brought into effect a non-contributory pension scheme,³⁶ which incorporates the so-called ‘Renta Universal de Vejez’ (universal old-age pension previously known as ‘Renta Dignidad’³⁷). This undoubtedly represents a step towards universal rights, and benefits a large part of the Bolivian population, mostly women, who undertake informal employment or are engaged in a familiar or household unpaid work.³⁸ However, one of the weaknesses of the scheme³⁹ derives from its reliance on funding through the Direct Tax on Hydrocarbons (IDH),⁴⁰ which involves some vulnerability to fluctuations in international prices⁴¹ and the possible depletion of hydrocarbon reserves.⁴²

Furthermore, the lack of fiscal resources, resulting in part from the low tax burden, has high social costs when it becomes necessary to resort to foreign lending to comply with spending commitments or budget deficits. Experience in this area suggests that lenders often impose conditions on access to international funding, which generally reduce the scope that Latin-Caribbean countries have to define their own social protection and development policies.⁴³

REGRESSIVE TAXATION AND IMBALANCE IN THE CONTRIBUTIONS OF THE DIFFERENT ACTIVITIES AND ECONOMIC AGENTS

In addition to insufficient revenue collection, there are two further issues that bring about serious consequences: the bias towards indirect taxes, and the imbalance in the tax effort that the different economic agents (individuals, companies and sectors) assume. Both of these problems further exacerbate existing inequalities.

Box 2. A tax policy which deepens inequalities

A characteristic of the socio-economic model of the Dominican Republic is that, despite high levels of economic growth, it fails to significantly reduce poverty and inequality. According to ECLAC, in 2012, the poorest population quintile received only 4 per cent of the country’s income, while the richest population quintile received 50.8 per cent, virtually the same share of total income of both quintiles as in 2002.⁴⁴

The tax structure, the poor quality of public policies and the lack of funding for priority areas for development all contribute to this undesirable inequality.

In 2012, 64 per cent of the Dominican Republic's total tax collection was from taxes on consumption and foreign trade (that is to say, indirect taxes), and only 36 per cent was from taxes on income and wealth.⁴⁵ The recent tax reform (2013) has merely made this situation worse.

With the 2013 reform, taxes on goods and services will account for 58.2 per cent of the expected revenue increase; an outcome associated with the scheduled increase of the Tax on Transfer of Industrialized Goods and Services (ITBIS) rate for consumption goods, previously exempt.⁴⁶ Direct taxes will only account for 27 per cent of the revenue collection increase, which, together with exemptions and allowances (tax expenditures⁴⁷) that benefit specific activities, deepen the inequities of the Dominican tax system.

Tax expenditure for 2014 will be equivalent to 6.6 per cent of GDP. Approximately 3.6 per cent of GDP will correspond to ITBIS exemptions. Nevertheless, when exemptions benefiting households are excluded from the analysis and tax expenditures are assigned to specific activities, this figure accounts for 3.4 per cent of GDP. Out of this total amount, 25 per cent will benefit the free trade zones, and 21 per cent the energy sector.⁴⁸

Moreover, the large number of regulations creates severe budgetary rigidities but are rarely enforced, thereby resulting in problems of legality, as well as the low quality of spending. This in turn delegitimizes and undermines the credibility of public institutions and thus of the Dominican government's attempts to obtain more resources for financing development and reducing inequalities.⁴⁹

Source: Rosa María Cañete Alonso (Director of Oxfam in the Dominican Republic) using ECLAC (2013), Ministry of Finance of the Dominican Republic and Fiscal Justice Movement (MJF) (2013).

The bias in consumption taxation

More than half of tax collection in Latin America and the Caribbean comes from taxing consumption.⁵⁰ In fact, the VAT (value added tax) is the only tax whose average nominal rates have increased in this region in the last decade.⁵¹ After strong growth over the last 20 years, the general consumption taxes (mainly the VAT and, in 2010, the general taxes on sales) accounted for 34.7 per cent of tax revenues in a sample of 15 countries of LAC (compared to 20.5 per cent in the OECD countries). At the same time, the share of specific consumption taxes (such as excise taxes and taxes on international trade) was 16.5 per cent of total tax revenue, while in the OECD it was around 10.8 per cent.⁵² Meanwhile, taxes on income and utilities accounted on average for 25.5 per cent of tax collection in the same group of countries of LAC, compared to 33.2 per cent in the OECD.⁵³

As a general principle, systems based on indirect taxation on consumption are more regressive and inequitable, since the taxes are levied regardless of the amount of revenue, income level or capacity to pay of taxpayers, and the relatively poorest population devotes a greater share of their income to consumption than those relatively richer.⁵⁴ The extent to which an indirect tax such as VAT is regressive depends on several factors, such as whether or not the goods and services consumed by the poorest segments of the population are exempt; what

criterion is used to measure welfare (whether consumption⁵⁵ or income are used to measure the tax incidence); and also the consumption patterns of the poorest population (for example, whether households consume what they grow). In this sense, estimates from a study carried out in 2011 show that when the income is used as a base, the VAT is regressive, as in such countries as Ecuador, Guatemala or Paraguay. When the base is consumption, the current VAT is progressive, as in Ecuador and Guatemala, but remains regressive, as in Paraguay, while the VAT without exemptions is also regressive, as is seen in Guatemala.⁵⁶

Tax benefits that reinforce the power of dominant elites

The slight contribution of direct taxation is accounted for by the exemptions and tax incentives⁵⁷ to promote domestic, and above all, foreign investment, and by the almost complete lack of taxation of unearned incomes or capital incomes⁵⁸ and of real-estate investments.⁵⁹ It is common knowledge that economic and political elites have influenced the design of unfair fiscal systems which are currently in force in LAC. These fiscal systems greatly favour these elite groups, in some cases resembling patronage,⁶⁰ and as a result, these privileges are extremely difficult to rescind once established.

Box 3. Tax benefits for the extractive sector

In Peru, the income tax is the main tax burden on mining companies, set at 30 per cent. However, these companies are granted generous tax incentives, and can benefit from lavish tax rules on depreciation and reinvestment of profits. This significantly reduces the effective contribution that these companies make to the treasury. In addition, Peru did not charge royalties on minerals until June 2004, when the Royalty Act was passed. Despite this law, most of the larger mining companies argue that the tax stability clause exempts them from their obligation to pay.^{61,62,63}

Ollanta Humala, two months after taking possession of the presidency of Peru in 2011, approved a new tax system focused on the mining industry,⁶⁴ which theoretically should allow an additional collection of 3 billion soles annually (about \$1.2bn). However, after a series of tax deductions, only 1 billion soles were collected out of the expected 3 billion.⁶⁵

A similar problem is found in Honduras. In 2007, the mining sector of this country reported gross receipts which accounted for \$198m; however, it only contributed to the treasury a total of \$283,000 in royalties, licences and rights, just 0.14 per cent of the sector gross income.⁶⁶

Source: Elaborated by the authors using Christian Aid (2012), Presidencia de la República de Perú (2011), Monge (2011), Salazar 2010, Christian Aid (2009) and Atienza & Itriago (2008).

In practice, this results in a paradox. LAC governments often promote investments which generate private profits based on the existing degree of tax sacrifice (through tax exemptions and facilities).⁶⁷ This sacrifice is eventually assumed by those vulnerable sectors of the population which have a higher need of specific public goods and services which are funded with insufficient public resources. Furthermore, tailor-made tax

benefits result in a plethora of tax codes, making the management of tax collection more complex for the tax administrations and thus putting further strain on resources.⁶⁸

In most cases, it is far from certain that this tax sacrifice will have significant positive effects in other areas, such as the transfer of technology or the generation of a sufficient mass of decent employment,⁶⁹ which is one of the key aspects of development.⁷⁰ Therefore, tax expenditure resulting from this tax sacrifice serves merely to privilege a few at the expense of many.

In some LAC countries, it is estimated that tax expenditure reaches 8 per cent of GDP.⁷¹ Countries such as Nicaragua and Guatemala lead the ranking of higher levels of tax expenditure in the region. In 2008 in Nicaragua, tax exemptions amounted to \$415.6m – 40 per cent more than the Ministry of Health's total budget that year, in one of the poorest countries in the region.⁷² In 2010, it was estimated that the tax expenditure in Nicaragua amounted to \$500m, that is to say, 42 per cent of all taxes collected that year.⁷³ Without these resources this country cannot carry out the required investments in human capital and basic infrastructures, which are the building blocks and prerequisites of development.⁷⁴

Put plainly, tax privileges granted to the wealthiest segments of the population (either due to the deliberate implementation of policies which maintain a relatively low level of taxation in certain highly profitable sectors and activities, or due to tax benefits)⁷⁵ without proper compensation to the poorest segments of the population represent a huge challenge for efforts to redress the misdistribution of income and wealth. In countries like Argentina, Bolivia, Brazil, Mexico, Peru and Uruguay the redistributive impact of direct taxation is low, despite the fact that it is progressive.⁷⁶

The bias in taxes on salaries

Over time, the low taxation of unearned income and the proliferation of tax benefits which only favour capital owners combine to affect labour income (salaries) – where the middle class contributions are concentrated – thereby constituting a bias against salaried workers in the tax systems of the region. Most of the small amount levied on personal income taxes comes from the salaries of the middle class.⁷⁷ Moreover, the effective rates that companies pay (after exemptions and other tax benefits) is, in many cases, lower than that of employees.

According to estimates,⁷⁸ the sum of the nominal rates levied on earned income and contributions to social security is higher than the nominal rates of the taxes on capital. In addition, the effective rates of the taxes on labour are higher than those of the taxes on capital in almost all of the (few) countries in which the available information enables these calculation to be made. In Brazil, Colombia, Guatemala and Venezuela, employees' incomes have effective tax rates that amount to about twice the effective tax upon earnings of the business sector.⁷⁹ In Nicaragua, the nominal rate levied on companies is 30 per cent. Nevertheless, the

effective tax rate is extremely low (only 2 per cent), due, among other things, to multiple subjective exemptions provided to entire sectors of economy, where the largest and most profitable companies in the country predominate.⁸⁰

Box 4. A tax policy which worsens income distribution between employees and employers

‘...In Colombia, those who defend the recent tax reform are silent about the worsening of the income functional distribution (it refers to how the national income is distributed between labour and *capital*) that it causes ...’

Stefano Farné, Director of the Observatorio del Mercado Laboral, U. Externado.⁸¹

According to some analysts, because of the tax reform which took effect in 2013, Colombian companies will not be able to pay 6 trillion Colombian pesos (around \$2.94bn⁸², 13.5 per cent of parafiscal contributions⁸³) intended to finance the Instituto Colombiano de Bienestar (ICBF), the National Learning Service (SENA) and the health of their employees. This money will be, in whole or in part, paid by middle class salaried workers through their high taxation on income.^{84,85}

Moreover, these appear not to be the only tax benefits the companies enjoy, as according to Medium-Term Fiscal Framework (MTFF)⁸⁶ reports, in 2012, taxpayer companies were granted with income exemptions, tax rebates and deductions which accounted for 3.4 trillion Colombian pesos (around \$1.67bn).⁸⁷ Therefore, ‘from now on, middle class workers will be responsible for the health of the employees of the country companies; but in case they lose their jobs, they will not be entitled to be assisted by a EPS (Health Promoting Company, Spanish acronym),⁸⁸ unless they pay out of the pocket of the social security’.^{89,90}

In Nicaragua, the proposal of tax reform of the Reforma de la Alianza Tributaria⁹¹ advocates for the inclusion of the whole income (salary and non-salary incomes) of the resident taxpayer in a common income tax basis, and to deduct the minimum exempt as well as the other allowed tax exemptions to obtain the taxable income. Then, a tax cumulative and progressive scale should be applied on this taxable income, which would bring together all incomes (regardless of their nature) in such a way that the tax rate applies not only on salaries but also on all personal incomes. However, the applicable law recently enacted continues to give preferential treatment to capital income.^{92,93}

Source: Elaborated by the authors using Farné (2012), Sarmiento Anzola (2013), Vanguardia.com (2013), Red de Justicia Fiscal de América Latina y el Caribe (2012), Medal (2012), Navas (2012) and Acevedo (2012).

INEFFECTIVENESS PROMOTING SOCIAL MOBILITY

Improving equality of opportunity means providing quality basic social services and social protection, but it also requires that a certain level and stability for revenue sources is maintained, and that the general conditions (health and safety at work, for example) in which this income is earned are of a sufficient standard. In other words, there is a need for public investment to unlock the potential of the poorest and excluded

sectors, as well as policies to promote economic opportunities for these sectors. In this way, we can remove the current intergenerational barriers which stand in the way of a lasting transition from poverty and upward social mobility free from dependence on the state.

To promote social mobility, better conditions must be provided to the poorest sectors, and reversing the prevalence (and mitigate the negative impacts) of excluding economic and production models that open the socio-economic gaps. These models maintain historical dependence of progress-excluded groups towards governments. It is necessary to ensure that both taxes and government spending contribute to a reduction in the asymmetry of productivity in the region, which perpetuates inequalities.

The first decade of the millennium represents a turning point in the recent history of social policymaking in LAC countries. Particularly important are the introduction of non-contributory programmes of social protection with comprehensive coverage⁹⁴ such as conditional cash transfer programmes (CCTs) and, more recently, non-contributory pension programmes.

Whilst people disagree on the exact degree of impact of these instruments, the relationship between the introduction of these programmes and subsequent lower levels of extreme poverty is indisputable. Less spectacular has been the contribution of social policy as a whole in the battle against the most entrenched inequalities. Vicenç Navarro offers a partial explanation, arguing that ‘the priority given to public transfer programs for poverty reduction was adopted, in several countries, at the expense of maintaining (and even increase) the scarcity of the public services of the welfare state, such as health and education’.⁹⁵

On the other hand, taxation in many countries of Latin America is designed to fit growth models based on the export of oil and raw materials, which slow down and/or displace other – already impoverished – economic sectors, such as small-scale agriculture. Moreover, in most cases, the fiscal system has proved ineffective in helping to formalize in a coherent and flexible manner the employment of informal poor workers. These shortcomings are particularly significant given that small agriculture and small informal companies comprise the bulk of the working poor people in the region.

Social policies are still insufficient to tackle structural inequalities

By 2010, 18 countries in LAC had some CCT, with a coverage amounting to 19 per cent of the total population of the region.⁹⁶

In Brazil, many analyses indicate that, without any demerit to its achievements, the social policy of the country should be strengthened quantitatively and qualitatively in order to eradicate patterns of exclusion and discrimination and bring about substantial change. The social policy in the region should more robustly contribute to the construction of

'alternative futures', different from the ones envisioned by many people living in poverty in LAC.

Box 5. Pending social policy

Brazil has made remarkable progress in reducing poverty and income inequality. Between 2003 and 2009 poverty fell from 26.4 per cent to 14.7 per cent, extreme poverty fell from 10.1 per cent to 5.2 per cent and the Gini index decreased from 0.582 to 0.540.⁹⁷

Some estimates show that about 17 per cent of the direct reduction in income inequality that occurred in Brazil between 2001 and 2011 is due to CCTs (specifically, the programmes 'Bolsa Familia'⁹⁸ and the 'Beneficio de Prestación Continua [Continuous Provision Benefit]'),^{99,100} 19 per cent to the contributory and non-contributory pensions; and 58 per cent to the increase in labour income.^{101,102}

Sectoral education and health policies in Brazil also appear to be bringing remarkable results. Between 1995 and 2010, life expectancy increased from 68.5 to 73.4 years and the mortality in children under five fell from 41.4 to 18.6 per thousand births. At the same time, public spending on health grew progressively from 2.86 per cent of GDP in 1995 to 4.07 per cent of GDP in 2011.¹⁰³

However, although racial, gender and geographic inequalities have been reduced, there is still a long way to go. These inequalities threaten the achievements in social indicators.

In 2009, 31.6 per cent of the households in the urban areas of Brazil had no access to adequate sanitation services. In 1995, this figure was 38.8 per cent. The modest progress between the years 1995 and 2009 hides another problem: in 2009, 56.7 per cent of the households with incomes below the poverty line did not have access to adequate sanitation services. Moreover, poor blacks and mulattos were worse off: 58.7 per cent of these households did not have good sanitation services, while a lower percentage – 51.7 per cent – of poor white households suffered from the same lack of quality services.¹⁰⁴ These figures indicate that areas with high numbers of blacks and mulattos have the worst public services, a fact that is also evident in the education sector.

As in the rest of the region, the process of universalizing access to public education in Brazil was initially focused more on *access* than on *quality*, with insufficient funds and management to provide adequate infrastructure and good working conditions for teachers and other professionals.

The result is a strong negative effect on the skills acquired by students: in 1995, at the end of primary school, 37.5 per cent of students had a good knowledge of the Portuguese language and only 16.8 per cent had a good knowledge of mathematics; by 2003 these figures had fallen to 20.1 per cent and 14.7 per cent, respectively.¹⁰⁵

Clearly, Latin America and the Caribbean '... has failed to transform the education system into a driver of equal opportunities, in part because a determining factor in educational outcomes is related to the socio-economic and cultural level of the homes...'.¹⁰⁶ In fact, the most recent information on the academic performance of the countries in the region that offer the Program for International Student Assessment (PISA)¹⁰⁷ of 2009, developed by the OECD, indicates that a high percentage of the student population show significant deficiencies in the basic skills of education.¹⁰⁸ But most striking is that most of the students who are located in the lowest

socio-economic and cultural strata of the countries of the region show a level of achievement below Level 2, that is, they have not developed the basic skills necessary for reading comprehension.¹⁰⁹ One of the most dramatic results is found in Peru, where 90 per cent of the students in the first quartile do not acquire the basic reading skills to function as citizens in the modern world.¹¹⁰

Source: Elaborated by the author using Telles (2013) and Trucco (2012).

Progressive fiscal policies, even though they do not break the structural conditions that favour exclusion, may favour the poor in the short term, but become inefficient in the medium and long term. And in this sense, 'regardless of whether the provision of basic social services and social protection are seen as a right to which all citizens should aspire, it is necessary to aim for greater coverage of services which do not discriminate any group of society and which, indeed, reach the neediest'.¹¹¹

Fiscal policy promotes economic models which deepen gaps

In recent years, Latin America has experienced what some call 'The Consensus of Commodities',¹¹² in which government bodies help to develop an 'extractive' model, focused on the large-scale export of primary goods. This leads to the promotion of sectors such as agro-exports (corn, soybeans, wheat), biofuels, mining (copper, gold, silver, tin, bauxite, zinc, etc.) and hydrocarbons (oil and gas), particularly in Bolivia, Ecuador, Paraguay, Peru and Venezuela.

Meanwhile, small-scale agriculture and other small businesses receive insufficient support from the state, particularly in the areas of industrialization and production diversification, which have the potential to generate more quality jobs.¹¹³ In 2011, agriculture and the mining of raw materials accounted for 76 per cent of the exports of the Union of South American Nations (Unasur), while high-tech manufacturing accounted for only 7 per cent.¹¹⁴

The effect of the governmental policies to support an extractive model has been to obstruct the proper development of other sectors such as small-scale agriculture. This reality contradicts the goals of reducing structural inequalities and the promotion of ecologically responsible economic models.

The new extractive model, according to Svampa, 'bursts into the territories and, as it passes, it deconstructs regional economies, destroying biodiversity and dangerously deepening the process of land grabbing, displacing rural, agricultural or indigenous communities, and violating the processes of public decision'.¹¹⁵ In addition to this, an extractive approach is generally based on activities intensive in capital but not in labour. In Peru, transnational mega-mining employs only 2 per cent of the economically active population (EAP), compared to 23 per cent for agriculture, 16 per cent for trade and almost 10 per cent for manufacturing.¹¹⁶

The least productive sectors, especially those with a high expansion

potential (such as small-scale agriculture or manufacturing SMEs) require special support to enhance productivity, so that the gap in the productivity and labour conditions between them and the more dynamic sectors can be reduced.¹¹⁷ Likewise, it is crucial to take measures to decentralize control of productive resources. However, as shown in the case of Paraguay (Box 6), the instruments of fiscal policy (tax benefits, subsidies, incentives, etc.) have been directed toward the promotion of the extractive model.

Box 6. Fiscal injustice traps Paraguay in poverty

'A weak tax system and a high level of deregulation make possible and profitable for multinationals to exploit farmland in the developing world using models that undermine and marginalize small local farmers. Furthermore, uncollected taxes from these companies go to fatten funding gaps that prevent the governments of the developing world to establish, fund and implement those multi-year and multi-sector food security strategies that have proven useful in the eradication of hunger.'

Olivier De Schutter, UN Special Rapporteur on the Right to Food.¹¹⁸

Paraguay is one of the world's leading suppliers of food (particularly soy), but it is also one of the poorest and most unequal countries in Latin America. Although smallholder farmers represent 8 out of 10 farms, their country's total area represents only 4.3 per cent of agricultural land.¹¹⁹ Increased production and export of soy – controlled by foreign investors and large producers – has marginalized other food security crops that depend on family farming. Fiscal policy has played a prominent role in the configuration of this unfair reality.

Privileges minimize the tax contribution of the soybean industry through the Tax on Agricultural Income¹²⁰ (less than 1 per cent of total revenues until 2013 and almost 3 per cent at present).¹²¹ Despite the high concentration of land, landowners pay basically nothing for its tenure (between 0.23 and 0.5 cents of dollar per hectare per year to pay property tax). This promotes the use and concentration of land as a means of saving and for speculation. In other words, this policy may be obstructing the rural population from accessing a key productive resource.

Moreover, while small-scale agriculture has received funding representing barely 5 per cent of public expenditure,¹²² between 1995 and 2000 over 70 per cent of public spending on agriculture was directed to subsidies that mostly benefited large agro-exporting producers.¹²³ Some analysts suggest that in the period between 2003 and 2008 the subsidy received by the soy sector in the country was over \$100m.¹²⁴ In other words, scarce public spending is directed to one of the most dynamic and profitable national economic sectors.¹²⁵

Moreover, the lack of sufficient environmental regulation on soy production has resulted in a continued threat to livelihoods and the ecosystem where the rural population lives.

Source: Elaborated by the authors using Itriago (2012a), Itriago (2012b), Itriago (2012c), Guereña (2011) and Villagra (2009).

Fiscal policy does not generate adequate incentives to formalize working poor people

*'In the region there is a clear correlation between non-formalization and inequality.'*¹²⁶

Elizabeth Tinoco, Regional Director for Latin America and the Caribbean, International Labour Organization

Despite recent improvements in the unemployment rates and quality of employment,¹²⁷ fiscal policy in the region still struggles to successfully formalize the work of poor people, thereby ensuring a progressive contribution to public finances through taxes. This ineffectiveness is unfortunate, partly due to the resulting depletion of tax revenues, but primarily because the precarious labour markets tend to increase origin inequalities, whether class, gender, age or ethnicity.¹²⁸ The persistence of informal working practices in the region often go hand in hand with the lack of rights enjoyed by poor workers.¹²⁹

Inequalities are exacerbated by informal working practices, because such practices tend to be carried out in low quality and low productivity employment, characterized by poor wages and poor labour rights, which are undertaken by the most vulnerable segments of the population. Recent data continue to reflect labour gaps at the expense of women, especially in countries of the region such as Nicaragua, Bolivia, Peru and Colombia. In these countries, 59.4 per cent, 54.3 per cent, 51 per cent and 50.9 per cent of working women, respectively, have lower quality jobs.¹³⁰ The percentages for men are 33.4 per cent, 29.8 per cent, 31.4 per cent and 40.3 per cent, respectively.¹³¹

In Mexico, only 30 per cent of small businesses (businesses with ten or fewer employees) are registered.¹³² The situation is even more dramatic in countries like El Salvador, where only 1 per cent of all microbusinesses and 3 per cent of non-micro-entrepreneurs are registered.¹³³ In LAC, 47 per cent of people with a job in the non-agricultural sector are working under conditions of non-formalization: 'about 100 million people in an informal situation that hardly allows subsistence and without any protection'.¹³⁴

Although it is necessary to analyze the factors that generate and maintain informal labour markets and informal goods and services markets,¹³⁵ there are indications that, for a significant percentage of the poor people working informally in the region, the specific costs for formalization far outweigh its potential benefits.^{136,137} The low productivity of the informal activities in LAC results in low and unstable income, increasing the vulnerability of those involved in them. This situation is exacerbated by the general lack of basic services and/or social protection systems that might generate real productivity increases, along with the lack of state support or the skills to deal with contingencies (resilience) such as diseases or natural disasters. Therefore, when the informal poor worker or the poor entrepreneur has to adopt regulations and pay taxes resulting from formalization, such reforms offer them extremely diffuse benefits.¹³⁸

Poor people working in informal activities need fiscal policies which lead unequivocally to formalization. In order to achieve this, it is necessary, at minimum, to significantly increase the level and quality of public spending and investment to improve the allocation of human and physical capital of small informal companies, to extend coverage protection systems (without requiring formalization as a requisite for social protection), and to devise tax and other regulations that are adaptable to the labour dynamics of the poorest workers in the region.

FISCAL POLICY OFTEN REPRODUCES TRADITIONAL VIEWS OF THE ROLE OF WOMEN IN SOCIETY

Fiscal systems reproduce a predetermined idea of society in which women are not sufficiently taken into account as economic agents. Part of the contribution that women make to the economy, both in the productive sphere and in the reproductive sphere through the work of care and life support, is ignored.¹³⁹ This happens predominantly, though not exclusively, in rural areas.^{140,141} In turn, this omission prevents the careful analysis of the explicit¹⁴² and implicit impacts¹⁴³ that fiscal systems may have on women and men.

Due to the different positions of men and women in society, fiscal systems can increase or reduce pre-existing gender inequalities.¹⁴⁴ Tax policy may end up being more regressive, costly and inefficient for women than for men, given their different consumption patterns, their economic activities, or their role of 'caregivers' that society has credited them with by default.

In Mexico, the incidence of indirect taxation (based on the income and not the household consumption) is higher in households in which women generate more income than in households where men earn more.^{145,146} Similarly, there may be negative biases in other existing taxes of fiscal laws, in the way that tax reductions or exemptions are assigned, and in the way that tax returns are made, among others.¹⁴⁷ One clear example of discrimination is evident in the exemption for personal income tax, wherein only men can deduct for 'family responsibilities' (dependents) and women cannot. This happens as a result of traditional gender roles and gender-based division of labour: in most cases the spouses with the lowest income (and with unregistered incomes) are women, so they will rarely benefit from this policy.¹⁴⁸

Box 7. Some of the omissions in the Bolivian tax legislation affecting women

In the Bolivian tax legislation there is no exemption or tax benefit associated with personal circumstances (such as family responsibilities, number of children, being the only head of household, or the degree of disability of a person). This particularly affects women, who often bear the negative aspects of reproduction and caregiving, sometimes exclusively (as in the case of households headed by single women). In this legislation,

there are no tax benefits subject to the achievement of certain objectives which could benefit women, such as the creation of stable employment, hiring young people, developing goods and services that promote private sector responsibility for care provision (day-care or canteens in workplaces, among others).¹⁴⁹

Source: Coello Cremades and Fernández Cervantes (2013).

The gaps can also be deepened because governments do not provide adequate funding to goods and services designed to meet the specific needs of women (particularly those related to reproduction and care of children and dependents), or because the underlying ideology of many policies and social programmes, despite favourable reporting in the media, reinforces the role of women as caregivers and as economically subordinate. Such policies do not change the place of women in society, but are merely palliative, and do not tackle the socio-economic dynamics that limit the independence of women. This argument forms the basis of criticisms of the Human Development Grant Program (PBDH, Spanish acronym)¹⁵⁰ in Ecuador and the Solidarity Program in the Dominican Republic,¹⁵¹ and it has contributed to initiatives such as the Presupuestos sensibles al Género o con Enfoque de Género (Gender Responsive Budgeting or Budgeting from a Gender Perspective).¹⁵²

According to a PBDH assessment conducted for the ECLAC:

*(...) the Program by itself and the suggested conditionalities show contradictory effects on the rights and the social burden on women (...) the 'Programa del Bono de Desarrollo Humano' does not incorporate a gender perspective that recognizes the cultural subordination that affects women in relation to income, welfare and decision making within the household, as well as the conditions of social exclusion that place these women in situations of increased vulnerability towards men...*¹⁵³

Amparo Armas Dávila, Consultant for ECLAC

PROPENSITY FOR TAX EVASION AND AVOIDANCE

In LAC, tax evasion and avoidance are high, and are particularly evident in taxes on personal and corporate income. A recent study of estimates of income tax evasion in LAC countries shows considerable levels of corporate tax evasion (46 per cent in Mexico and 65 per cent in Ecuador) and tax evasion on personal income (33 per cent in Peru and 70 per cent in Guatemala),¹⁵⁴ higher than in the case of VAT.¹⁵⁵

Despite the considerable efforts toward a greater professionalization of tax administration in the region, a poor tax culture (which in many cases is the result of the low credibility of governments in managing tax), inadequate and ineffective internal control systems, and impunity for tax offences combine to reduce the effectiveness of the authorities responsible for tax collection. On average, only three out of every 100 taxpayers are subject to some control of their tax returns and only three sentences for tax offences are processed per year in every Latin

American country.¹⁵⁶ White collar criminals who carry out economic crimes are therefore prevalent in the region.¹⁵⁷

While recognizing these internal weaknesses, it is worth noting that there are serious flaws in the architecture of the international fiscal system, which favours some large corporations by failing to prevent systemic weaknesses that can be exploited by companies to considerably reduce their tax contribution. Moreover, the design and implementation of international treaties (such as agreements to avoid double taxation¹⁵⁸), in practice, are harmful to many Latin American countries. Together with the global financial opacity, these factors make it virtually impossible to significantly reduce the capital flows that escape LAC countries and end up in tax havens.

Four Latin American countries are in the list of the 20 nations that have the most money in tax havens
*BBC World.*¹⁵⁹

Brazilians hid in places like the Caribbean, Antigua and Barbuda, Bahamas or Dominica some \$519.5bn, equivalent to 160 per cent of the external debt of the South American giant. The bill includes funds that left that country between 1970 and 2010 and the profits they generated outside of tax control. Mexico follows, with \$417.5bn, 224 per cent of their foreign liabilities. Then there is Venezuela, with \$405.8bn, no less than 728 per cent of the external debt. And then, Argentina, with \$399.1bn, or 308 per cent.

*Alejandro Rebossio, correspondent of the newspaper El País in Buenos Aires quoting Tax Justice Network (TJN).*¹⁶⁰

Tax havens are a clear incentive for tax evasion and avoidance and the real black hole in public finances. Besides the low taxation (or no taxation) that they apply, the essential problem in these jurisdictions lies in how easy it is to establish front companies ('shell companies' and 'trusts'¹⁶¹), as well as the lack of tax cooperation with tax administrations of third countries (manifested in a lack of effective protocols of exchange of tax information and the opacity generated by bank secrecy). The existence of such jurisdictions facilitates practices such as the manipulation of transfer mispricing through the undersizing of sales and the oversizing of costs artificially derived to tax havens between companies of the same group in order to reduce their tax basis. It is estimated that undersizing of sales to evade tax obligations in countries like Panama amounts to about 40 per cent of total sales.¹⁶²

Moreover, as a result of the lack of financial information provided by companies concerning the operations that they develop in third countries, it is not possible to track 'aggressive tax planning' schemes, which are extremely harmful to the public coffers. These schemes are often used to artificially relocate profits to jurisdictions with low or no taxation in which, as noted above, the opacity and lack of tax cooperation predominates.

The mechanisms of aggressive tax planning have become so widespread that the OECD, under mandate of the G20, has launched an ambitious reform project known as BEPS (Base Erosion and Profit Shifting¹⁶³), intended to correct the distortions which are the breeding

ground for these harmful practices in the international tax system. However, there is a high risk that this project will only respond to the interests of some of the more advanced economies.¹⁶⁴

The existence of tax havens, the opacity of the global financial system and particularly the abuse of multinational companies, do not only impair the revenue capacity of the countries in the region but they also reduce the scope for progress on progressive policies. The issue is that capital, in its more mobile version, takes advantage of opacity and loopholes in the international financial system in order to become diluted and thereby deplete public coffers. This fact further complicates the attempts to raise public revenue from the wealthier segments of the region.

Despite the loss of resources incurred by tax evasion and tax avoidance, LAC has not developed mechanisms of tax cooperation between tax administrations (including tax havens) either within the region or with the rest of the world, which translates into a serious limitation on efforts to combat tax evasion and avoidance.

Recently, the Pacific Alliance¹⁶⁵ has begun to explore an automatic information exchange mechanism between tax administrations, and Mexico has chosen to join the EU pilot countries in this area. However, these constitute only minor efforts, given the level of economic and trade exchanges that occur within the area.

WEAK INSTITUTIONS AND REPRESENTATION

In order to prevent inequality in LAC there is a need for fiscal policies capable of balancing economic (and therefore political) power between the different social groups. Therefore, in addition to equitable tax policies, it is necessary to ensure that the interests of all sectors are truly represented in public spending priorities, especially those of the most vulnerable groups. It is crucial to achieve a public spending programme that serves the common good, ensures basic rights for all, and brings about greater transformative capacity. Furthermore, it is essential that wastage of public revenues is reduced, and action is taken to prevent the subordination of public spending to political priorities which result in patronage and corruption. However, these scourges and other inefficiencies in most of the countries of LAC continue to threaten the availability of public finances allocated to the objectives of reducing poverty and inequality.

According to the Corruption Perceptions Index (2013) published annually by the organization Transparency International, countries like Haiti, Venezuela, Paraguay, Honduras, Nicaragua, Guatemala and the Dominican Republic are among those with the highest perceived levels of corruption.^{166,167}

Box 8. And where is the money?

The Fiscal Justice Movement (MJF)¹⁶⁸ in the Dominican Republic objects to the tax reform presented by the government of Danilo Medina. In this reform, the creation of a new tax package ('el paquetazo') is proposed to address the million-dollar debt left by the previous administration of the same party: in 2012 President Leonel Fernandez left the country a deficit of nearly €3.5bn, more than 8 per cent of the GDP, for expenditures not approved by the Budget Law for the election year.¹⁶⁹

This reform is being driven without the approval of the Economic and Social Council.¹⁷⁰ Legitimately, the MJF requests that the government provides an explanation for the cause of the debt before raising any tax, and that they assume the relevant responsibilities for the mismanagement of public spending.¹⁷¹

Along the same lines, the MJF notes that in the report of the first quarter of 2013 on budget execution, specifically, the announcement of the investment of RD\$9bn (€164m¹⁷²) for the stimulation of the economy, the government made deliberate omissions and manipulations of budget data that confuse and misinform the public.¹⁷³

According to the MJF, the delays in budget execution had negative effects on national economic dynamics, further exacerbating the strong impact of the tax package approved in late 2012. 'So, rather than an increased efficiency, it is a double economic blow on the population: first, more taxes, and second, delays in the execution of public spending, with the aggravating circumstance that the greatest delays were experienced in social services, which reached only 18.9 per cent of the total scheduled for the year.'¹⁷⁴

The MJF also denounces the decline in both the sequence and the quality of the reports published by the Directorate General of Budgets (DIGEPRES, Spanish acronym), to which it attributed a poor professionalism: 'The report focuses the fiscal debate on abstract numbers without taking into account the development objectives, even violating the Organic Law on Budget in the literal A of Article 61 which provides analysis of variances between planned objectives and targets with respect to the action taken and determine their causes'.¹⁷⁵

In addition, the organization said that since November 2012 citizens cannot access the information on spending, financing, inversion projects and income status that authorities used to publish on the website 'City Portal', and described as inconsistent the fact that the results of budget implementation in the first quarter of 2013 are made public before the final report of the 2012 budget.¹⁷⁶

Source: Elaborated by the author using Bolívar Díaz (2012), Inspiration (2012) and Fiscal Justice Movement (MJF) (2013).

In LAC the level of transparency on fiscal matters; the responsibility for planning, tax collection and execution of public expenditure (reflected in a comprehensive and effective rendering of accounts); as well as the mechanisms for citizen participation in fiscal policies, still leave much to be desired. Shortcomings in practice serve as an obstacle to the fulfilment of the rights of those who are least able to influence government policy decisions.

In turn, these deficiencies further undermine citizen confidence in the institutions responsible for devising and implementing fiscal policies, including tax administrations and planning bodies, as well as public expenditure at both national and subnational level, which cultivates a low-tax culture. Moreover, they prevent the analysis and implementation of corrective actions to address historical problems in LAC countries, such as the poor execution of public spending or unaccounted for inconsistencies between the amounts budgeted and that actually spent in the allocated areas. These problems undermine the necessary process of institutional strengthening of these key aspects of development.

Box 9. The greatest deficit: effective citizen participation in public policies

In 2011 in Mexico, the General Budget Transparency Index (IGTP, Spanish acronym)¹⁷⁷ score was 45 points (on a scale of 1 to 100), its lowest value since 2003. This indicates that, despite progress in the regulatory framework for public spending and accountability, experts continue to believe that transparency in the budget process is far from optimal. Over the past nine years, the average IGTP score was 50 points. The highest rated variables were: Action on Access to Information, Trust in the Information, Capacities of External Control Organism and Legislative Powers & Engagement. The lowest rated variables were: Citizen Participation in the Budget, Changes in the Budget, and Internal Control Assessment.¹⁷⁸

Source: Elaborated by the authors using the Latin American Index of Budget Transparency – 2011.

Citizen participation in tax matters (and in public policies in general) has the advantage of promoting a better tax culture, gives legitimacy to a social contract oriented toward equity, and strengthens democracy. In Ecuador, the participation of civil society (among other groups) in the process of drafting the current Constitution, created a favourable climate for the progressive tax reforms, which have subsequently been implemented and have been reflected in the spectacular growth of public spending oriented toward basic social services.¹⁷⁹

While not a guarantee, the resources generated from taxes help to foster a social contract on which a more reciprocal relationship between state and citizenry can be achieved.¹⁸⁰ Increased tax revenues require a greater degree of transparency and accountability on the part of the state, which will in turn result in higher quality institutions.¹⁸¹ Such an outcome is far less common with non-tax revenues, such as income from the exploitation of natural resources. Institutions that are forged around the exploitation of extractive resources tend to be weak¹⁸² and weak institutions run the risk of political patronage, corruption, populism and fiscal laziness.¹⁸³

3 RECOMMENDATIONS: A FAIR FISCAL SYSTEM FOR LATIN AMERICA AND THE CARIBBEAN

Comprehensive tax reforms in LAC must urgently be addressed. The fact that public spending has been increasing but extreme inequality persists as a hallmark of the region, is indicative of the need for a more transformative approach to public policy, and especially fiscal policy.

The fragility of the growth and social progress experienced in the region in the last decade should instil a conviction among policymakers to promote new measures to achieve fair and equitable fiscal systems which guarantee fundamental rights and truly serve a model of cohesive societies.

A fair and equitable fiscal system is one that consistently implements tax and public spending policies, and effectively oversees tax and budget management in order to meet the following general principles:

1. **Full compliance with the redistributive function of the state through public budgets.** That is, sufficient and stable public spending to support quality and well-oriented basic social services, as well as strong mechanisms of social protection and reinforcement of the resilience of population groups vulnerable to internal and external shocks.

Regardless of whether the provision of basic social services and social protection are considered as a right to which all citizens should aspire, **we must aim for a greater coverage of quality services that do not discriminate any group in society**, and which indeed mean real opportunities for the advancement of the people who receive them.

Efforts to design public policies with real transformative capacity should be intensified, such as, for example, those seeking to improve the performance of pupils at the lower socio-economic level; to provide greater human capital to population groups that have been systematically excluded; or to improve coverage of early child care.

2. **The role of tax systems as the instruments of redistribution of wealth in a country should be increased.** This involves the reduction of the negative impact that regressive and unbalanced tax systems have on the relatively poorest people in terms of the contributions made by the different economic agents to the public coffers. Tax systems should be balanced toward more progressive

models, in which wealth and property and not only consumption and wages are taxed more.

3. **The taxable basis and scope of national tax systems should be expanded.** Rationalization of existing tax benefits is required, as well as the reduction to a minimum of those that have no clear positive social impacts. It is essential that the final tax collection relates to the industrial and productive potential of the country, in line with the needs of stable funding of programmes to reduce poverty and inequality.
4. **High levels of tax evasion and tax avoidance should be reduced** by ensuring that fiscal policy is accompanied by a tax administration that can monitor tax obligations and facilitate compliance. Related to this, it is essential to ensure effective fiscal cooperation and coordination at the regional and subregional levels, and further strengthen the enforcement capabilities of these institutions. Furthermore, the tax administration should be part of an institutional system that ensures effective punishment of non-compliance with tax obligations. This is crucial to discourage the tax evasion and tax avoidance which results from impunity.
5. **Along with other public policies, the fiscal system must promote dignified progress for a wider base of the population,** making economic opportunities a reality for sectors such as small agriculture or manufacturing SMEs, thereby contributing to the development of non-exclusive and more cohesive social models. We must put an end to the use of instruments such as tax benefits, subsidies, incentives, among others, for the unrestricted promotion of the extractive model. In particular, we should utilize the full potential of tax policy to help reverse the inequitable access to, or the extreme concentration of, resources and productive assets such as land.
6. **Clear benefits must be generated to promote the progressive formalization of companies and working poor people who are invisible to the state.** While it is essential that the majority of citizens and economic sectors are taxed, it is also necessary that this is done in a manner consistent with their ability to pay, the socio-economic situation in which they find themselves and the way that they earn their income or earnings. Moreover, formalization should not be a prerequisite for realization of rights such as health, education and social protection of the many poor people employed in informal and precarious jobs in the region.
7. In coordination with other public policies, **economic diversification should be promoted, and environmentally responsible activities that generate quality jobs should be developed.**
8. In conjunction with national efforts, **discriminatory views that prevent – for reasons of race or gender – significant sectors of the population from realizing real opportunities for improvement must be dismantled.** In particular, further study of the explicit and implicit impacts of fiscal systems which reinforce traditional roles of women in society, and which serve to obstruct efforts to reduce gender gaps, must be carried out.

9. **The fiscal system should contribute to the decentralization of political power in the societies of the region.** In this sense it is crucial that the effective participation of historically disadvantaged groups is secured throughout all phases (design, implementation, monitoring and feedback) of fiscal policymaking, on the basis of a framework of government transparency and responsible accountability at all levels. We must ensure effective citizen participation mechanisms which ensure that spending, financed through taxes and other non-tax revenues, serves to protect, finance and promote the economic and social progress of the poorest and most vulnerable people. It is essential that citizens perceive that their taxes are used to improve their circumstances, in order to generate greater social awareness, a stronger tax culture and favourable conditions for future necessary tax reforms.

The process of political participation must, along with other efforts to strengthen institutions, bring about real reductions in the levels of corruption and patronage. This constitutes a basic element of legitimacy of any tax reform in favour of greater equity.

10. In connection with the foregoing, **we must ensure transparency in fiscal reforms** and implement effective mechanisms of broad public debate on these reforms. This public accountability should include a clear analysis of the distributional impact of tax reforms and potential negative outcomes (and any necessary mitigation measures) on the poorest people.

In conclusion, in order to close the enormous socio-economic gaps in the region, the design of tax systems must be guided by the basic principles of progressivity and equity. Public resources must be oriented toward the protection of social rights (the right to education, health, food security, etc.), sustainable development, and the eradication of exclusionary and discriminatory patterns that negate many of the benefits of progress.

NOTES

¹ Gasparini and Cruces (2012), *Pobreza, Desigualdad y Políticas Públicas en América Latina. Evaluación de resultados y agenda futura*, CEDLAS (Center for Distributive, Labor and Social Studies for their Spanish acronym).

² The Gini coefficient is a measurement of inequality devised by the Italian statistician Corrado Gini. Although it is typically used to measure income inequality within a country, it can also be used to measure any form of uneven distribution. The Gini coefficient is a number between 0 and 1, where 0 corresponds to perfect equality (everyone has the same income) and 1 corresponds to perfect inequality (one person has all the income and the rest have none). The Gini index is the Gini coefficient expressed as a percentage and is equal to the Gini coefficient multiplied by 100.

³ Gasparini and Cruces (2012), *Pobreza, Desigualdad y Políticas Públicas en América Latina. Evaluación de resultados y agenda futura*, CEDLAS (Center for Distributive, Labor and Social Studies).

⁴ Data provided by Alicia Bárcenas, general secretary of the Economic Commission for Latin America and the Caribbean (ECLAC) days prior to the VII Summit between Latin America and the Caribbean (CELAC) and the EU (European Union), held in Santiago de Chile in January 2013: http://internacional.elpais.com/internacional/2013/01/29/actualidad/1359488372_433575.html

⁵ Alicia Bárcena (2012), 'Hoy ya no es suficiente crecer para igualar, sino que es fundamental igualar para crecer (Today it is not enough to grow in order to equalise, but it is necessary to equalise in order to grow)': http://www.eclac.org/prensa/noticias/discursossecretaria/6/46776/SeminarioTributacionyDesarrollo_27de_abril2012e.pdf

⁶ See for example Tuñón (2012), 'Los vicios de la pobreza estructural': <http://www.lanacion.com.ar/1532329-los-vicios-de-la-pobreza-estructural>

⁷ 'Cepal: la desigualdad es el problema más urgente para América Latina': <http://www.americaeconomia.com/economia-mercados/finanzas/cepal-la-desigualdad-es-el-problema-mas-urgente-para-america-latina>

See also Bárcenas (2011), 'Distribuir riqueza. La pobreza y la desigualdad han disminuido en América Latina en los últimos años, pero aún queda mucho por hacer', Economic Commission for Latin America (ECLAC), <https://www.imf.org/external/pubs/ft/fandd/spa/2011/03/pdf/Barcena.pdf>

⁸ ECLAC (2014), *Panorama Económico y Social de la Comunidad de Estados Latinoamericanos y Caribeños, 2013*, p. 30: <http://www.cepal.org/publicaciones/xml/7/52077/PanoramaEconomicoYSocial.pdf>

⁹ <http://www.movilidadsocial.org/content/%C2%BFque-es-movilidad-social>

¹⁰ Center of Studies Espinosa Yglesias (CEEY, Spanish acronym) (2013), 'Report on social mobility in Mexico 2013', http://www.ceey.org.mx/site/files/resumen_ejecutivo_imsn_0.pdf. See also Paes de Barros, Ferreira, Molinas Vega and Saavedra Chanduvi (2009), *Measuring Inequality of Opportunities in Latin America and the Caribbean*: http://siteresources.worldbank.org/LACEXT/Resources/258553-1222276310889/Book_HOI.pdf and the results of the ESRU's Survey on Social Mobility 2006 in Mexico: <http://www.movilidadsocial.org/content/resultados-encuesta-esru>

¹¹ Báez and López-Calva (2014), *Cuando la prosperidad no es compartida. Los vínculos Débiles entre el Crecimiento y la Equidad en la República Dominicana*, Banco Mundial: http://www-wds.worldbank.org/external/default/WDSCContentServer/WDSP/IB/2014/03/06/000442464_20140306134338/Rendered/PDF/857600v10WP0P10SH0Executive0summary.pdf

¹² OECD (2009) 'Perspectivas Económicas de América Latina 2009': <http://www.oecd.org/dev/americas/perspectivaseconomicasdeamericalatina2009.htm>

¹³ It is noteworthy that in some countries of LAC, the redistributive effect of public social spending on education and health, for example, has much greater redistributive impact than direct cash transfers.

¹⁴ Alicia Bárcena (2012), 'Hoy ya no es suficiente crecer para igualar, sino que es fundamental igualar para crecer (Today it is not enough to grow in order to equalise, but it is necessary to equalise in order to grow)': http://www.eclac.org/prensa/noticias/discursossecretaria/6/46776/SeminarioTributacionyDesarrollo_27de_abril2012e.pdf.

¹⁵ Lustig, Pessino and Scott (2013), *The impact of taxes and social spending on inequality and poverty in Argentina, Bolivia, Brazil, Mexico, Peru and Uruguay: an overview*, CEQ Working Paper No. 13, p. 10, figure 2. Spanish abstract available at: http://www.commitmentoequity.org/publications_files/Latin%20America/CEQWPNo13%20Resumen%20Ago%202013.pdf

¹⁶ Coello Cremades and Fernández Cervantes (2013) quoting Paz Arauco, Gray Molina, Jiménez Pozo and Yáñez Aguilar (2012), *Política Fiscal y Equidad de Género en Bolivia: Análisis y Propuesta para la Construcción del Pacto Fiscal hacia el Vivir Bien*, UN Women, La Paz, September 2013.

The same result is presented in Lustig, Pessino and Scott (2013), *The impact of taxes and social spending on inequality and poverty in Argentina, Bolivia, Brazil, Mexico, Peru and Uruguay: an overview*, p. 9, Table 1. CEQ Working Paper No.13.

¹⁷ In this concept the contributions to social security and non-tax revenue such as fees, fines, revenues from the sale of goods produced by public enterprises, royalties, permits or licenses to exploit natural resources, etc. are not included. In other words, government revenues obtained as compensation for a public service (rights), payment for the use or exploitation of property in the public or private domain (products), or revenues from the imposition of fines and surcharges (exploitations) are not included.

¹⁸ After tax reductions or exemptions.

¹⁹ 'The tax burden or pressure (not including social security contributions and non-tax revenue) has increased more in LAC countries than anywhere else in the world: about 2.7 points of the GDP since the early 1990s until the second half of the 2000s; see graphic 1.4 in Interamerican Development Bank - IDB (2013). 'Recaudar no basta: los impuestos como instrumento de desarrollo (Collecting is not enough: taxes as a development instrument)', <http://www.iadb.org/es/investigacion-y-datos/publicacion-dia,3185.html?id=2013>. (Note that in this document, the fiscal pressure, unlike the tax burden, is a broad concept that includes social security contributions and other non-tax revenues such as royalties or licenses for exploitation of natural resources.)

²⁰ See Rebossio (2013), 'Los países latinoamericanos donde se pagan más y menos impuestos': <http://blogs.elpais.com/eco-americano/2013/03/los-pa%C3%ADses-latinoamericanos-donde-se-pagan-m%C3%A1s-y-menos-impuestos.html>

²¹ Interamerican Development Bank - IDB (2013), 'Recaudar no basta: los impuestos como instrumento de desarrollo (Collecting is not enough: taxes as a development instrument)', <http://www.iadb.org/es/investigacion-y-datos/publicacion-dia,3185.html?id=2013>, graphic 1.2.

²² Rodríguez (2011) quoting the IMF, *Análisis del sistema tributario en el Paraguay y Potencial de recaudación. Proyecto Alianza Ciudadana para la Transparencia y el Desarrollo Paraguay*, Decidamos - Campaña por la Expresión Ciudadana - y Centro de Documentación y Estudios (CDE).

²³ They refer to social security contributions and revenue obtained from export income, as a compensation for a public service (rights), payment for the use or exploitation of public property or private land (products), or fines and surcharges (exploitations).

²⁴ See CEPAL (2013), 'Panorama fiscal de América Latina y el Caribe. Reformas tributarias y renovación del pacto fiscal', pp. 16-18, <http://www.eclac.cl/publicaciones/xml/6/49276/PanoramaFiscaldeALC.pdf>

²⁵ Yacimientos Petrolíferos Fiscales Bolivianos (Bolivian Fiscal Oilfields).

²⁶ Management Report 2012, President Evo Morales Ayma, sheet 108: <http://comunicacion.presidencia.gob.bo/docprensa/pdf/20130124-15-33-48.pdf>

²⁷ Although there remains room for improvement, in recent years, some LAC countries have increased the tax burden on extractive activities.

²⁸ CEPAL (2013), 'Panorama fiscal de América Latina y el Caribe. Reformas tributarias y renovación del pacto fiscal', Box 1.2, p. 16; Mayoral Jiménez (2010), 'El presupuesto descansa en Pemex': <http://www.cnnexpansion.com/presupuesto-2011/2010/09/12/pemex-impuestos-presupuesto-gravamen>

²⁹ One hundred Mexican pesos are equivalent to \$7.53 (at the exchange rate of 12 March, 2014).

³⁰ Reyes Tépac M. (2012), *La deuda pública de las entidades federativas explicada desde la perspectiva del federalismo fiscal mexicano*, Dirección General de Servicios de Documentación, Información y Análisis. Subdirección de Análisis Económico, p. 8, <http://www.diputados.gob.mx/sedia/sia/se/SAE-ISS-17-12.pdf>

³¹ By law, these revenues are mainly for capital expenditure investment (assets) in the municipalities, see 'Transparencia en Royalties': <http://www.transparenciaenroyalties.org.py/V3/faqs>

³² See Itriago (2012a), *Justicia tributaria para la población campesina paraguaya*, pp. 18-22, Oxfam, <http://www.oxfam.org/es/crece/policy/justicia-tributaria-para-la-poblaci%C3%B3n-campesina-paraguaya>

³³ 'El irrisorio impuesto inmobiliario actual no contribuye al desarrollo del país': <http://iberoamerica.net/paraguay/prensa-generalista/abc.com.py/20130708/noticia.html?id=l2n10P2>

³⁴ On the redistributive impact of volatility see Chapter 1 in ECLAC (2010), 'Estudio económico de América Latina y el Caribe 2009-2010': <http://www.eclac.org/cgi-bin/getProd.asp?xml=/publicaciones/xml/3/40253/P40253.xml&xsl=/de/tpl/p9f.xsl&base=/tpl-i/top-bottom.xsl>

³⁵ See Itriago (2009), *Contra la 'Maldición' de los Recursos Naturales. Como pueden y deben beneficiarse las personas pobres de la renta de las extractivas*, Oxfam, <http://www.oxfamintermon.org/es/documentos/20/01/10/contra-maldicion-de-recursos-naturales-como-pueden-deben-beneficiarse-personas-p>

³⁶ See 'La Ley de Modificación de la Ley de Pensiones incrementa la Pensión Solidaria 2013/11/08', http://www.economiafinanzas.gob.bo/index.php?option=com_content&view=content&id=3056&Itemid=306&seccion=306&categoria=446

- ³⁷ Renta Dignidad is an uninheritable lifetime payment for all Bolivians from 60 years of age living in the country; see <http://www.aps.gov.bo/Comunicacion/Publicaciones/La%20Renta%20Dignidad%20y%20Gastos%20Funerales/files/cartilla.pdf>
- ³⁸ See Coello Cremades and Fernández Cervantes (2013). *Política Fiscal y Equidad de Género en Bolivia: Análisis y Propuesta para la Construcción del Pacto Fiscal hacia el Vivir Bien*. UN Women, La Paz, September 2013. This report shows a detailed analysis of the current Bolivian tax system from a gender perspective.
- ³⁹ Ibid.
- ⁴⁰ For the year 2012, from the total IDH revenues, municipal governments received 35.3%, dignity revenue (renta dignidad) 25.6%, the central state (State General Treasury) 18.3%, departmental governments 10.1%, public university 7%, leaving the remaining for the indigenous fund (3.5%) and the fund for civic education; see Martínez Céspedes and Inch S. (2012), *A siete años del IDH ¿en qué se gastan los recursos?*, Fundación Jubileo.
- ⁴¹ See CEDLA (Center of Studies for Labour and Agricultural Development), 'Por baja del IDH, gobierno usa otro fondo para Renta Dignidad': <http://plataformaenergetica.org/content/30806>
- ⁴² For further detail on the depletion of Bolivian gas reserves, see: Velásquez G. (2013), *Situación de los Hidrocarburos en Bolivia*, Serie Debate Público No.27, Fundación Jubileo, <http://www.jubileobolivia.org.bo/publicaciones/revistas-especializadas/item/255-situacion-de-los-hidrocarburos.html>
- ⁴³ For the case of Central America see Colino Cámara, Álvarez de Cienfuegos, Parrado Díez and del Pino Matute (2007), 'Avances y Obstáculos en el Fortalecimiento del Estado en Centroamérica y República Dominicana. Un análisis de la capacidad institucional, la reforma de la Administración y la gestión pública', Instituto Nacional de Administración Pública, 2007. http://bci.inap.es/alfresco_file/5d0e305b-4670-4ae5-8827-445904d184c2
- ⁴⁴ ECLAC (2013), 'Panorama Social de América Latina 2013', Box 3, p. 23, <http://www.eclac.cl/publicaciones/xml/9/51769/PanoramaSocial2013.pdf>
- ⁴⁵ Aggregate data of the Ministry of Finance of the Dominican Republic: http://hacienda.gov.do/politica_legislacion_tributaria/ingresos%20fiscales/ingresos%20anuales/INGRESOS%20FISCALES%201990-2012.xls
- ⁴⁶ Fiscal Justice Movement (MJF) (2013), 'El presupuesto de 2014 y la situación fiscal de República Dominicana', <http://justiciafiscal.com/2013/01/el-presupuesto-de-2014-y-la-situacion-fiscal-de-republica-dominicana-2/#more-905>
- ⁴⁷ The tax expenditure of the state includes any kind of preferential treatment that benefits a specific sector, region or group of taxpayers.
- ⁴⁸ Fiscal Justice Movement (MJF) (2013), 'El presupuesto de 2014 y la situación fiscal de República Dominicana', <http://justiciafiscal.com/2013/01/el-presupuesto-de-2014-y-la-situacion-fiscal-de-republica-dominicana-2/#more-905>
- ⁴⁹ Ibid.
- ⁵⁰ This figure may be somewhat higher, as it is obtained from a publication in which total tax revenue includes other kinds of public revenue such as security contributions. See OECD, ECLAC and IATTC (Inter-American Center of Tax Administrations) (2012), 'Estadísticas Tributarias de América Latina', p. 22.
- ⁵¹ Interamerican Development Bank (IDB) (2013), 'Recaudar no basta: los impuestos como instrumento de desarrollo', <http://www.iadb.org/es/investigacion-y-datos/publicacion-dia,3185.html?id=2013>
- ⁵² OECD, ECLAC and IATTC (2012), 'Estadísticas Tributarias de América Latina'.
- ⁵³ OECD, ECLAC and IATTC (2012), 'Estadísticas Tributarias de América Latina', p. 22. Note that revenues from direct taxes may be slightly overestimated, since in this publication charges of social security are considered 'taxes'. See: <http://www.cepal.org/cgi-bin/getProd.asp?xml=/ofilac/noticias/paginas/2/45832/P45832.xml&xsl=/ofilac/tpl/p18f.xsl&base=/ofilac/tpl/top-bottom.xsl>
- ⁵⁴ Consumer demand depends on the volume of income. When incomes are very low there is some consumer demand, which is called 'autonomous consumption', since even those who have nothing need to consume something in order to survive. From there, the higher the income, the higher the consumption. The consumption function increases with the income, but so will savings, since the richer a society is, the greater the proportion of their income may be allocated to savings. It is expected that high-income households save a higher proportion of their income, while families who earn low incomes need to consume even more of what they earn. The percentage of the consumption in total income declines when income increases. We will call that percentage 'average propensity to consume'; the average propensity to consume is decreasing.
- ⁵⁵ In time, consumption is distributed less unequally than income, because of the average propensity to consume. See previous note.

⁵⁶ Jorratt (2011), *Evaluando la equidad vertical y horizontal en el impuesto al valor agregado y el impuesto a la renta: el impacto de reformas tributarias potenciales. Los casos del Ecuador, Guatemala y el Paraguay*, ECLAC, <http://www.eclac.org/cgi-bin/getProd.asp?xml=/publicaciones/xml/1/44151/P44151.xml&xsl=/de/tpl/p9f.xsl&base=/de/tpl-i/top-bottom.xslt>

Note that in the case of Ecuador, the main source of information used by the study to assess the equity of the VAT was the National Survey on Income and Expenditure of Urban Households (ENIGHU), 2003, conducted by the National Institute of Statistics and Census (INEC). In the case of Guatemala, the main source of information used to assess the equity of the VAT was the National Survey of Living Conditions (ENCOVI), conducted by the National Statistics Institute (INE) of Guatemala between March and September of 2006. And in the case of Paraguay, the source of information used to assess the equity of the VAT was the Household Budget Survey 2005-2006, implemented by the Department of Statistics, Surveys and Census (DGEEC), between July 2005 and June of 2006.

⁵⁷ See Itriago (2011), *Dueños del desarrollo. Impuestos para combatir la pobreza*, pp. 16-17, Oxfam, <http://www.oxfam.org/sites/www.oxfam.org/files/rr-owning-development-domestic-resources-tax-260911-es.pdf>

⁵⁸ Financial investments, interests on government securities, mutual fund profits, capital gains in real estate and equities, etc. The financial investments are deposits of funds made in term banking from seven days to over a year, with higher interest rates than savings accounts.

⁵⁹ '(...) we can see the existence of preferential generous received by capital incomes (...) in most of the countries of the region, which are either fully exempt or subject to very low effective rates (...)'; see Gómez S. J.C., Jiménez J.P and D. Rossignolo (2012), *Imposición a la renta personal y equidad en América Latina: Nuevos desafíos*, ECLAC, http://www.eclac.org/de/publicaciones/xml/9/46529/SERIE_MD_119.pdf

See also the IDB (2013), *Recaudar no basta: los impuestos como instrumento de desarrollo*, graphic 1.9 (El sesgo antilaboral de los impuestos: razón de las cargas tributarias del trabajo y del capital), <http://www.iadb.org/es/investigacion-y-datos/publicacion-dia,3185.html?id=2013>

⁶⁰ For questions related to the influence of elites in shaping fiscal systems, see, for example, Martín and Scartascini (2011), *Why Don't We Tax the Rich? Inequality, Legislative Malapportionment, and Personal Income Taxation around the World*, Interamerican Development Bank (IDB), http://www.iadb.org/en/research-and-data/publication-details,3169.html?pub_id=IDB-WP-282; <http://www.condistintosacentos.com/desigualdad-instituciones-politicas-y-redistribucion-resolviendo-el-enigma/>

The study includes 17 countries of Latin America and the Caribbean. See the graphic on inequality in political representation versus Personal Income Taxes as a percentage of GDP produced by the Banco Interamericano de Desarrollo: <http://www.iadb.org/es/noticias/articulos/2011-12-02/representacion-politica-desigual-e-impuestos,9710.html>

⁶¹ Christian Aid (2012), *El Escándalo de la Desigualdad en América Latina y el Caribe*, p.48, <http://www.christianaid.org.uk/images/scandal-of-inequality-latin-america-and-caribbean-spanish.pdf>

⁶² Salazar 2010, 'MINERÍA-PERÚ: Negocio millonario y exonerado de impuestos', <http://www.ipsnoticias.net/2010/01/mineria-peru-negocio-millonario-y-exonerado-de-impuestos/>

⁶³ See Atienza and Itriago (2008), *Letra pequeña, grandes abusos. Por qué los contratos petroleros en América Latina son un obstáculo para el desarrollo*, pp. 17-18, Intermón Oxfam.

⁶⁴ <http://www.presidencia.gob.pe/jefe-de-estado-promulgo-tres-leyes-tributarias-mineras>

⁶⁵ See Presidencia de la República de Perú (2011), 'Jefe de Estado promulgó tres leyes tributarias mineras', <http://www.presidencia.gob.pe/jefe-de-estado-promulgo-tres-leyes-tributarias-mineras>; and Monge (2011), 'Sobre el acuerdo con los mineros: ¿Total, cuánto es? ¿Y a quién va?', <http://www.conades.org.pe/index.php?pg=2>

⁶⁶ Christian Aid (2009), *Socavando a los pobres: reformas tributarias mineras en América Latina*, p.1.

⁶⁷ As suggested by Jiménez, Gómez Sabaini and Podestá (2010), *Evasión y equidad en América Latina*, ECLAC, http://www.eclac.org/publicaciones/xml/8/38398/Evasi%C3%B3n_y_equidad_final_16-04-10_con_portada.pdf

⁶⁸ '(...) these schemes provide all types of evasion and avoidance operations by related companies, members of the same economic group. The existence of tax-exempt companies allow utilities to be transferred to them by other companies of the same economic group through operations of transfer mispricing or thin capitalization, or the creation of rights to the refund of VAT tax credits for fictitious transactions (...)'; see, Acevedo (2012), 'El gasto tributario y la evasión: dos enfermedades crónicas y degenerativas del sistema tributario', <http://www.canal15.com.ni/videos/36487>

⁶⁹ According to the International Labour Organization (ILO), decent work sums up the aspirations of people in their working lives. It involves the opportunity to have a productive job that delivers a fair income; security in the workplace and social protection for families; better prospects for personal development and social integration; freedom for people to express their opinions, organization and participation in decisions that affect their lives; and equality of opportunity and treatment for all women and men.

⁷⁰ There is no conclusive evidence about the effectiveness of certain tax incentives in promoting high value-added investment and its impact on development. See Keen and Simone (2004) quoted in Itriago (2011), *Dueños del desarrollo. Impuestos para combatir la pobreza*, p. 36, Oxfam, <http://www.oxfam.org/sites/www.oxfam.org/files/rr-owning-development-domestic-resources-tax-260911-es.pdf>

⁷¹ Itriago (2011), *Dueños del desarrollo. Impuestos para combatir la pobreza*, pp. 35-37, Oxfam, <http://www.oxfam.org/sites/www.oxfam.org/files/rr-owning-development-domestic-resources-tax-260911-es.pdf>

⁷² Ibid.

⁷³ Acevedo (2012), 'El gasto tributario y la evasión: dos enfermedades crónicas y degenerativas del sistema tributario', <http://www.canal5.com.ni/videos/36487>

⁷⁴ Ibid.

⁷⁵ Jiménez, Gómez Sabaini and Podestá (2010), *Evasión y equidad en América Latina*, ECLAC, http://www.eclac.org/publicaciones/xml/8/38398/Evasi%C3%B3n_y_equidad_final_16-04-10_con_portada.pdf

⁷⁶ See Lustig, Pessino and Scott (2013), *The impact of taxes and social spending on inequality and poverty in Argentina, Bolivia, Brazil, Mexico, Peru and Uruguay: an overview*, Figure 1, and Table 1, pp. 8 and 9.

⁷⁷ Jiménez, Gómez Sabaini and Podestá (2010), *Evasión y equidad en América Latina*, ECLAC, http://www.eclac.org/publicaciones/xml/8/38398/Evasi%C3%B3n_y_equidad_final_16-04-10_con_portada.pdf

⁷⁸ IDB (2013), 'Recaudar no basta: los impuestos como instrumento de desarrollo', graphic 1.9 (El sesgo antilaboral de los impuestos: razón de las cargas tributarias del trabajo y del capital), <http://www.iadb.org/es/investigacion-y-datos/publicacion-dia,3185.html?id=2013>

⁷⁹ Ibid.

⁸⁰ Acevedo (2012), 'El gasto tributario y la evasión: dos enfermedades crónicas y degenerativas del sistema tributario', <http://www.canal5.com.ni/videos/36487>

⁸¹ Farné (2012), 'Reforma tributaria y equidad distributiva', http://190.7.110.123/pdf/6_derechoSeguridadSocial/observatorio/publicaciones/articulos-prensa/Articulo31.pdf

⁸² According to the exchange rate of 12 March 2014.

⁸³ In Colombia, parafiscal contributions are a special contribution made by employers to SENA, ICBF and Family Compensation Funds, so that these entities can overtake programs of social nature, according to their task: <http://www.gerencia.com/aportes-parafiscales.html>

⁸⁴ Farné (2012), 'Reforma tributaria y equidad distributiva', http://190.7.110.123/pdf/6_derechoSeguridadSocial/observatorio/publicaciones/articulos-prensa/Articulo31.pdf

⁸⁵ Sarmiento Anzola (2013), 'Reforma tributaria, desigualdad y pobreza', <http://alainet.org/active/61028&lang=es>

⁸⁶ http://www.virtual.unal.edu.co/cursos/eLearning/dnp/1/html/contenido-3_2_2-MFMP.html

⁸⁷ Farné (2012), 'Reforma tributaria y equidad distributiva', http://190.7.110.123/pdf/6_derechoSeguridadSocial/observatorio/publicaciones/articulos-prensa/Articulo31.pdf

⁸⁸ The health-promoting entities, known for their Spanish acronym EPS, are companies of the health system in Colombia, which do not provide medical services but promote such services to users in an insurance scheme. People become members of the EPS in order to be treated in clinics and hospitals, which do provide medical services but do not charge for these patients.

⁸⁹ Farné (2012), 'Reforma tributaria y equidad distributiva', http://190.7.110.123/pdf/6_derechoSeguridadSocial/observatorio/publicaciones/articulos-prensa/Articulo31.pdf

⁹⁰ See also 'Senador Robledo insiste en críticas contra reforma tributaria', <http://www.vanguardia.com/actualidad/colombia/190404-senador-robledo-insiste-en-criticas-contra-reforma-tributaria>

⁹¹ Alliance comprising the Institute of Strategic Studies and Public Policy (IEEPP, Spanish acronym), the Civil Coordinator, the Nicaraguan Institute for Fiscal Studies and Research (INIET, Spanish acronym) and Oxfam.

⁹² Tax Justice Network of Latin America and the Caribbean (2012), 'Comparación de propuestas tributarias en Nicaragua', <http://www.justiciafiscal.org/2012/09/comparacion-de-propuestas-tributarias-en-nicaragua/>

- ⁹³ Medal (2012), 'La reforma tributaria es más de lo mismo y el desarrollo sostenible, un reto nunca asumido en nuestra historia', in *Envío Digital*, <http://www.envio.org.ni/articulo/4627>; Navas (2012), 'Reforma fiscal antisalariados', in *Prensa Móvil*, <http://m.laprensa.com.ni/activos/111425>; Acevedo (2012), 'Reforma Tributaria: ¿Tanto secreto para tan pocas nueces?', in *Correo para Ciegos*, <http://www.correoparaciegos.com/reforma-tributaria%C2%BFtanto-secreto-para-tan-pocas-nueces-n292.html>
- ⁹⁴ Gasparini and Cruces (2013), *Políticas Sociales para la Reducción de la Desigualdad y la Pobreza en América Latina y el Caribe. Diagnóstico, Propuesta y Proyecciones en Base a la Experiencia Reciente*, p. 11, Centro de Estudios Distributivos, Laborales y Sociales (CEDLAS), Work document No. 142.
- ⁹⁵ Navarro, V. (2014), 'Las limitaciones de los programas antipobreza', in *Pensamiento Crítico*, <http://blogs.publico.es/vicenc-navarro/2014/02/11/las-limitaciones-de-los-programas-antipobreza/>
- ⁹⁶ Gasparini and Cruces (2013), *Políticas Sociales para la Reducción de la Desigualdad y la Pobreza en América Latina y el Caribe. Diagnóstico, Propuesta y Proyecciones en Base a la Experiencia Reciente*, p. 12, Centro de Estudios Distributivos, Laborales y Sociales (CEDLAS), Work document No. 142.
- ⁹⁷ Telles (2013) quoting the IPEA (Instituto de Pesquisa Econômica Aplicada) and others (2011), *Brazil: Poverty and Inequality. Where to Next?*, Oxfam (2014).
- ⁹⁸ <http://www.americaeconomia.com/economia-mercados/finanzas/experiencia-brasileña-en-transferencia-de-renta-y-mejora-de-la-vida>
- ⁹⁹ Ibid.
- ¹⁰⁰ Telles (2013) quoting the IPEA (2012), *Brazil: Poverty and Inequality. Where to Next?*, Oxfam (2014).
- ¹⁰¹ According to Telles (2013), *Brazil: Poverty and Inequality. Where to Next?*, Oxfam (2014), this increase was driven primarily by systematic increases in the minimum wage and changes in the regulations for microenterprises that allowed many entrepreneurs and workers of the informal sector to move to the formal economy, in addition to the important contribution of employment generation through economic growth.
- ¹⁰² See Telles (2013), *Brazil: Poverty and Inequality. Where to Next?*, Oxfam (2014).
- ¹⁰³ Ibid.
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- ¹³⁶ For the case of Peru see Machado (2014), to be published. In this document, Machado Machado argues that there are determining factors of non-formalization that cause 'non-formalization of exclusion' (e.g. labour market fragmentation prevents workers to enter the formal market) and 'non-formalization of escape' (e.g. many workers and families make a cost-benefit analysis to see if they should formalize and many voluntarily choose not to formalize because they find few benefits and high costs).
- ¹³⁷ As will be noted in the next subsection, for women, the decision to formalize may pose greater obstacles because fiscal systems tend to reproduce patterns that keep them occupying traditional roles of subordination in all spheres.

- ¹³⁸ See Itriago (2011), *Dueños del desarrollo. Impuestos para combatir la pobreza*, Box 8, Oxfam, <http://www.oxfam.org/sites/www.oxfam.org/files/rr-owning-development-domestic-resources-tax-260911-es.pdf>
- ¹³⁹ Coello, Itriago and García Salamanca (2014), *Ajustar la lente. Fiscalidad desde un enfoque de género. Metodología de Análisis*, Oxfam, forthcoming.
- ¹⁴⁰ Note that in the countryside the assignation of roles that gives men the primary responsibility for the production and restricts women to reproduction is even more rigid than in cities. In rural areas, women are considered as secondary workers whose role is ultimately to supplement household income, to undertake unpaid family work or to work as producers for the own consumption; see ILO (2012), 'Panorama Laboral 2012. Latin America and the Caribbean', http://www.ilo.org/wcmsp5/groups/public/---americas/---ro-lima/documents/publication/wcms_195884.pdf
- ¹⁴¹ A report published by the ILO notes that in the coffee crop, both in Costa Rica and Mexico, most of the workers are migrants who come to the crops accompanied by their families and stay with them in the farms and in the surroundings throughout the work period. However, only men establish a working relationship with the producer, who requires a daily minimum fee collection as a requirement to pay the agreed amount. Breaching the target involves not receiving wages for that day. Given this, the most widespread strategy is the organization of the family to 'help' the worker and thus achieve the required amount of product. Thus, unpaid family labour undertaken by women (and children) does not count. See Valenzuela, Reinecke and Scaglione (2012), special subjects: *El empleo de las mujeres rurales en América Latina en OIT* (2012), 'Panorama Laboral 2012. Latin America and the Caribbean', http://www.ilo.org/wcmsp5/groups/public/---americas/---ro-lima/documents/publication/wcms_195884.pdf
- ¹⁴² Those embodied in regulatory provisions (laws or rules) that give men and women different categorizations and treatment. Explicit gender bias is easily identifiable because usually it appears in writing in the tax code or regulations, but may also be reflected in informal practices.
- ¹⁴³ Those provisions of law and regulation that, due to typical social conventions and economic behaviour, have different consequences for men and for women. Implicit gender bias is more difficult to identify because this requires observing the different ways in which the fiscal system affects men and women.
- ¹⁴⁴ Coello, Itriago and García Salamanca (2014), *Ajustar la lente. Fiscalidad desde un enfoque de género. Metodología de Análisis*, Oxfam, forthcoming. Other authors have studied how macroeconomic policies, specifically fiscal policies, are not gender neutral and have different outcomes and impacts on men and women that affect existing inequalities, and may help to increase them or, conversely, to reduce them. See, for example, the work of Nilufer Cagatay, María Pazos, Lucía Claría Pérez Fragoso, Francisco Cota González, Corina Rodríguez Enríquez, Caren Grown and Imraan Valodia, among others.
- ¹⁴⁵ Grown and Valodia (2010), *Taxation and Gender Equity: An eight-country study of the gendered impact of direct and indirect taxes*, p. 5, <http://www10.iadb.org/intal/intalcdi/PE/2011/08031.pdf>
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- ¹⁴⁷ See Coello, Itriago and García Salamanca (2014), *Ajustar la lente. Fiscalidad desde un enfoque de género. Metodología de Análisis*, Oxfam, forthcoming.
- ¹⁴⁸ Ibid.
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- ¹⁶⁰ Rebosio (2012), 'Los ricos latinoamericanos guardan en paraísos fiscales tanto como el PIB brasileño', Blog de Economía, *El País*, 24 July, <http://blogs.elpais.com/eco-americano/2012/07/los-ricos-latinoamericanos-guardan-en-para%C3%ADsos-fiscales-tanto-como-el-pib-brasile%C3%B1o.html>
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- ¹⁶² McKinsey and Company (2009) quoted in IDB (2010), *Taxes and Productivity: A game of hide and seek*, Washington D.C: Inter-American Development Bank.
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- ¹⁷⁵ Ibid.

¹⁷⁶ Ibid.

¹⁷⁷ <http://www.iltpweb.org/>

¹⁷⁸ Índice Latinoamericano de Transparencia Presupuestaria (Latin American Index of Budget Transparency). Sixth Edition – 2011. Results for Mexico, <http://www.iltpweb.org/>

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