Financing

Financing for Development

# ECOSOC Special Meeting on International Cooperation in Tax Matters

ECOSOC Chamber, Monday 29 April 2019, 4:30 – 5:50 pm

## Session 3: Taxation and inequality

### *Purpose of the session*

This session on taxation and inequality will examine the potential of fiscal systems to increase or reduce inequalities. It will look at options available to countries at different levels of development to improve equality by taxing wealth and income and targeting public transfers and expenditure policies. Panelists will debate the broader socioeconomic implications of equitable fiscal policies and analyze the political and practical considerations that countries generally face when attempting to reduce inequality through such policies. The discussion will be conducted in the context of potential strategies in support of achieving the Sustainable Development Goals (SDGs), and the commitment to leaving no-one behind.

### *Background*

The impact of fiscal policies can go far beyond increasing domestic resource mobilization. They can be designed to foster different behaviors as taxes are raised and support resource reallocation within society as revenues are spent – helping to tackle inequality, while advancing sustainable and inclusive economic growth. This way, **fiscal policies offer important opportunities to promote strategies in support of the 2030 Agenda for Sustainable Development**. The 2030 Agenda emphasizes the importance of reducing income inequality within and amongst countries through sustaining the income growth of the most deprived, thus contributing to the eradication of extreme poverty.

> *"As we embark on this great collective journey, we pledge that no one will be left behind. Recognizing that the dignity of the human person is fundamental, we wish to see the goals and targets met for all nations and peoples and for all segments of society. And we will endeavour to reach the furthest behind first."*
>
> *2030 Agenda for Sustainable Development*

### *Why is action needed to address inequality at the national level?*

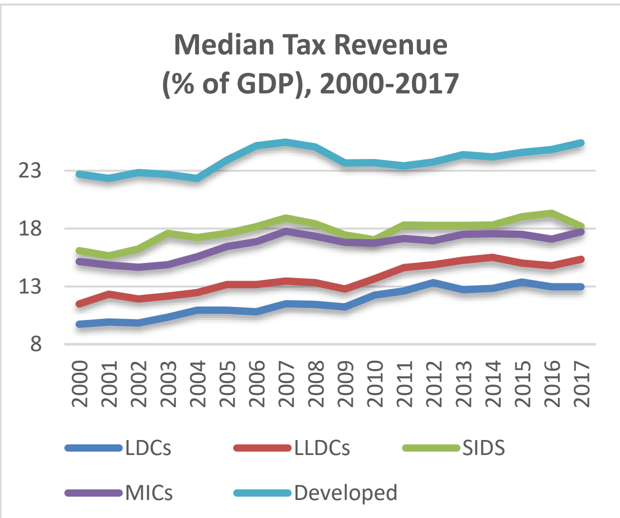
Global inequality has decreased in the past three decades, pushed by strong economic growth in some emerging countries. The situation differs **at the national level, as income inequality has risen significantly**, particularly in developed economies.[1] In developing countries, trends have been mixed, with some regions showing progress in reducing inequality in the past two decades, owing to a range of policies, including labor market improvements.[2] The reasons behind the rise of inequality vary across regions. They are connected to, among other factors, advances in technology that have ultimately benefitted higher-skilled workers to the detriment of low- and medium-skilled workers. High levels of inequality pose a major obstacle to achieving the SDGs. Effective response to such challenges will depend, to a large extent, on how countries design and implement their fiscal policies. Emphasizing the need to further **increase revenues and align expenditures with national development strategies** can play a pivotal role in combating inequality, through an adequate distribution of resources.

[1] IMF (2017), Fiscal Monitor October 2017, Washington, D.C.

[2] Ibid.

## *What is the role of fiscal policies in reducing inequality?*

Since 2000, tax revenues have increased throughout the world.[3] Yet, this has come with limited impact on equity and the wellbeing of populations, particularly those most vulnerable and in need. Despite the increased size of tax instruments, few countries have insisted on increasing their redistributive potential.




In developed countries, increases in tax revenues and recovery since the 2008/2009 global financial crisis were not taken up as opportunities to tackle the systematic issues that limit country-level achievements of SDGs 1 and 10.[4] In developing countries, even when tax revenues increased both in nominal terms and as a share of GDP, those increases were often driven by indirect taxation. Indirect taxation is levied on consumed goods rather than on income; this results in regressive taxes affecting poor households more than wealthier ones, thus limiting the redistributive potential of fiscal policies.

Governments in developed and developing countries have multiple ways of combining policy options to tackle inequalities. As **fiscal policies deeply influence inequality both when taxes are levied and revenues are spent**, they should be seen as a key option. There is no one-size-fits-all solution. Yet, fiscal policies tend to have a high potential for positive spillovers: by broadening the tax base, streamlining the tax administration, and increasing its ability to fight tax evasion, they may foster countries' capacity to spend more and more efficiently.[5]

As highlighted in the 2019 Financing for Sustainable Development Report, progressivity of fiscal systems is key. Transitioning to tax systems that rely on direct progressive taxation, or introducing taxes on capital (ownership, gains and income), would have a clear impact on the composition of the tax base, thereby shifting the distribution of wealth. However, policymakers should not only consider whether individual taxes are progressive or regressive: they should also take into account the implications of the overall fiscal policies for lower-income households.

Spending revenues towards more redistributive policies would support a decrease in inequality. Indeed, expenditures could directly target the least privileged, through cash transfer programs, or contribute to larger programs investing in infrastructure, education, healthcare, technology and innovation, or support progress in the field of political inclusion, equal opportunities and the fight against discrimination, progressively bettering the relationship between the State and people. Fiscal policy design can also create incentives for private social spending.

Multifaceted and holistic policy options, backed by the needed financing, would **benefit the entire population, providing new opportunities for all and paving the way for inclusive, strong and sustainable development**.

3 UN (2019), World Economic Situation and Prospects 2019, New York. Figure Source: IMF, World Revenue Longitudinal Set.

4 Gupta, S. (2018). Income Inequality and Fiscal Policy: Agenda for Reform in Developing Countries. Working Paper commissioned by the Group of 24 and Friedrich-Ebert-Stiftung New York. August.

5 See for example Tientip Subhanij, Shuvojit Banerjee, and Zheng Jian, eds. (2018). Tax policy for sustainable development in Asia and the Pacific. United Nations Publication ST/ESCAP/2806. Bangkok: United Nations Economic and Social Commission for Asia and the Pacific (ESCAP).

| *Suggested questions for discussion* |
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| ▪ *What is the role of taxation in reducing inequality, within countries at different levels of development? How can fiscal policies aggravate inequality?*<br><br>▪ *What are options available to countries to tax wealth and improve equality, both on the taxation and on the expenditure side?*<br><br>▪ *What are the overall economic effects of such policies? How to determine what is "desirable" income distribution?* |