The Political Viability of Progressive Tax Reform in Mexico

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An outlier within an outlier region…

- 1910-2010: a century of failed tax reforms
- 2000-2010: a decade of failed VAT reforms
- Many causes…
  - Political: capture by organized interests vs. (poor) medium voter,
  - Ideological: “benefits principle”
  - Economic: endogenous exclusion under conditions of high inequality
  - Rational: Coverage, quality of spending
  - Oil “curse”: unstable and unsustainable finances, failed reforms, highly regressive tax burden…

An outlier within an outlier region…

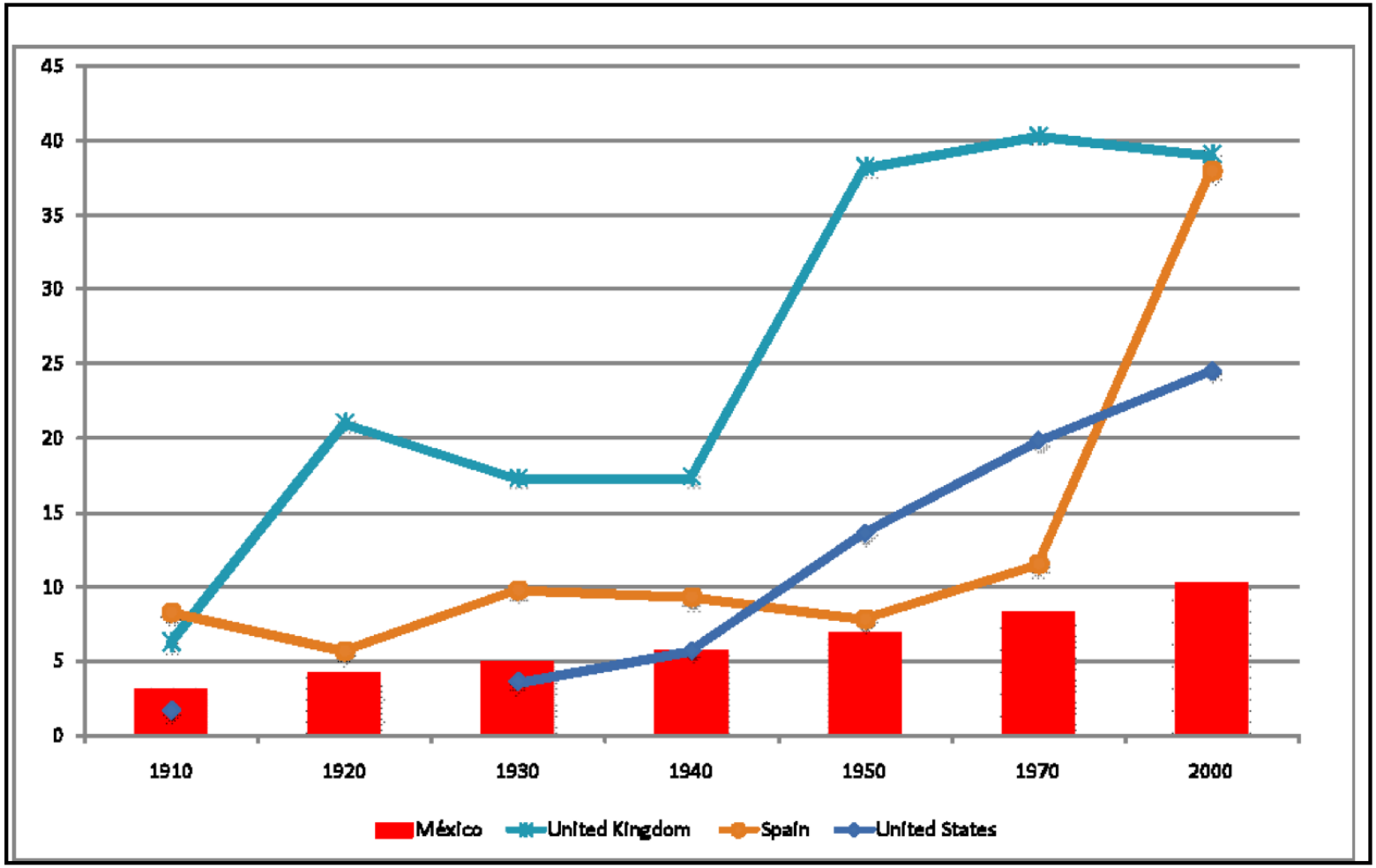
- Defining "progressive tax reforms"…
  - Progressive tax system, vs.
  - Redistributive impact of fiscal (tax-benefit) system…

  $\Rightarrow$ under conditions of high inequality, revenue potentially much more important for redistributive impact than progressivity…

  $\Rightarrow$…assuming spending capacity to benefit (all) the poor.

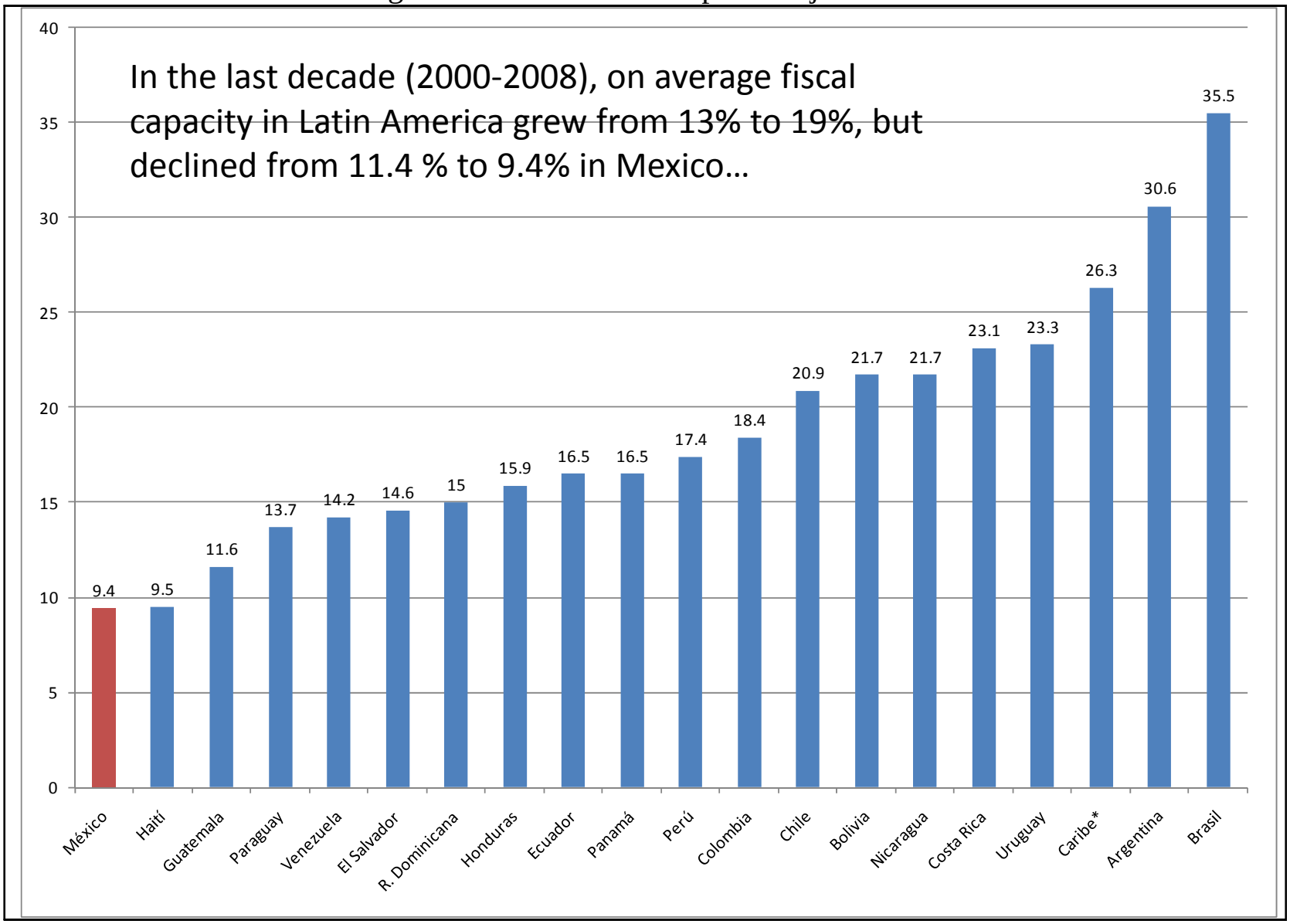
In a century when fiscal capacity expanded dramatically in much of the world, non-oil tax revenue in Mexico increased by just 7 percentage points of GDP, from 3% in 1910 to 10%

Tax revenue in Mexico and other countries



Source: Hernandez (2009)

Ingresos Tributarios como porcentaje del PIB



Fuente: CEPAL (2010),
**Promedio para países del Caribe, excluye contribuciones a la seguridad social.*

Figure 2.1. **Tax revenue from different sources across selected countries**

2008

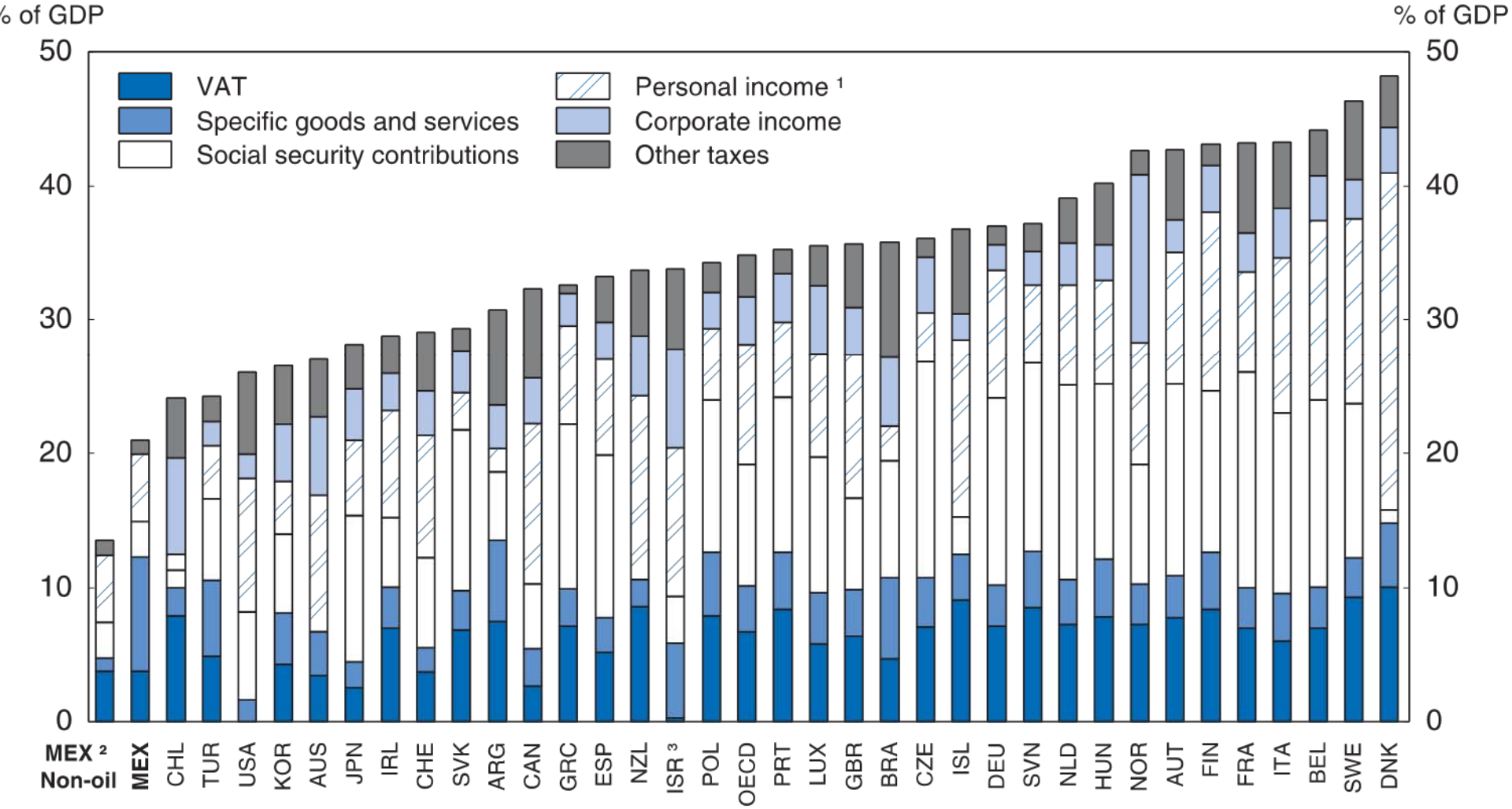
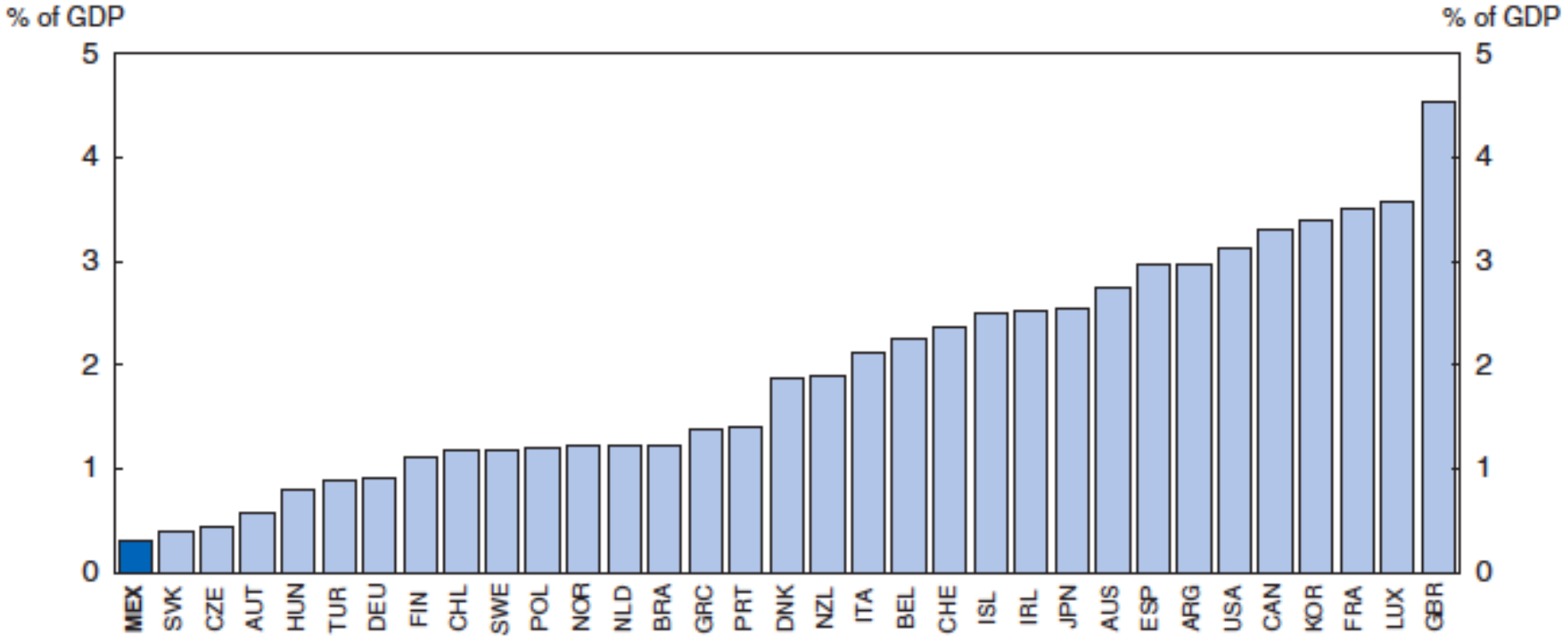


Figure 2.14. **Taxes on property**

2007



Source: OECD, *Tax Revenue Database* and *Latin American Revenue Statistics*.

StatLink http://dx.doi.org/10.1787/888932383831

1980	VAT introduced	10%	0% basic food basket and some agricultural godos 6% US border	1980: +0.29% GDP disapeared by 1982
1983	Response to crisis	15%	Exemptions reduced	2.2% => 3.2% (1984-1989)
1991		10%	Applied in US border	2.7% (1992-1994)
1995	Response to crisis	15%	Exemptions: Food, books, medicines	2.8% (1995) - 3.3% (2000)
2001-2010	Response to crisis & declining oil reserves; + 2% generalized linked to transfers to poor	16%	Failed attempts to generalize VAT	3.45%

Recaudación por Impuestos Generales al Consumo
(% del PIB)
2007

PAISES OCDE		PAISES América Latina	
EUA	2.2	Panamá	1.0
Japón	2.6		
		México	*3.5*
*México**	*3.5*		
		Argentina	4.0
Suiza	3.9	Brasil	4.9
Australia	4.0	Paraguay	5.4
Corea	4.5	Ecuador	5.4
Canadá	4.7	Guatemala	5.4
Turquía	5.5	Costa Rica	5.4
Luxemburgo	5.7	Perú	5.6
Alemania	6.3	Colombia	5.7
Italia	6.3	Venezuela	6.6
España	6.4	El Salvador	7.0
República Checa	6.6	Nicaragua	7.3
Reino Unido	6.7	Chile	7.4
Holanda	7.3	Bolivia	8.8
Bélgica	7.4	Uruguay	9.1
Francia	7.5		
Grecia	7.5	**Promedio**	5.8
República Eslovaca	7.6	**Coef. Var.**	0.35
Austria	7.7		
Irlanda	7.9		
Noruega	8.0		
Polonia	8.1		
Finlandia	8.6		
Portugal	8.9		
Nueva Zelanda	9.0		
Suecia	9.2		
Hungría	9.8		
Dinamarca	10.2		
Islandia	11.3		
Promedio	6.83		
Coef. Var.	0.33		

Fuente: OCDE Revenue Statistics 1965-2007 y CEPAL;
México: elaboración propia datos SHCP, promedio 2003-09

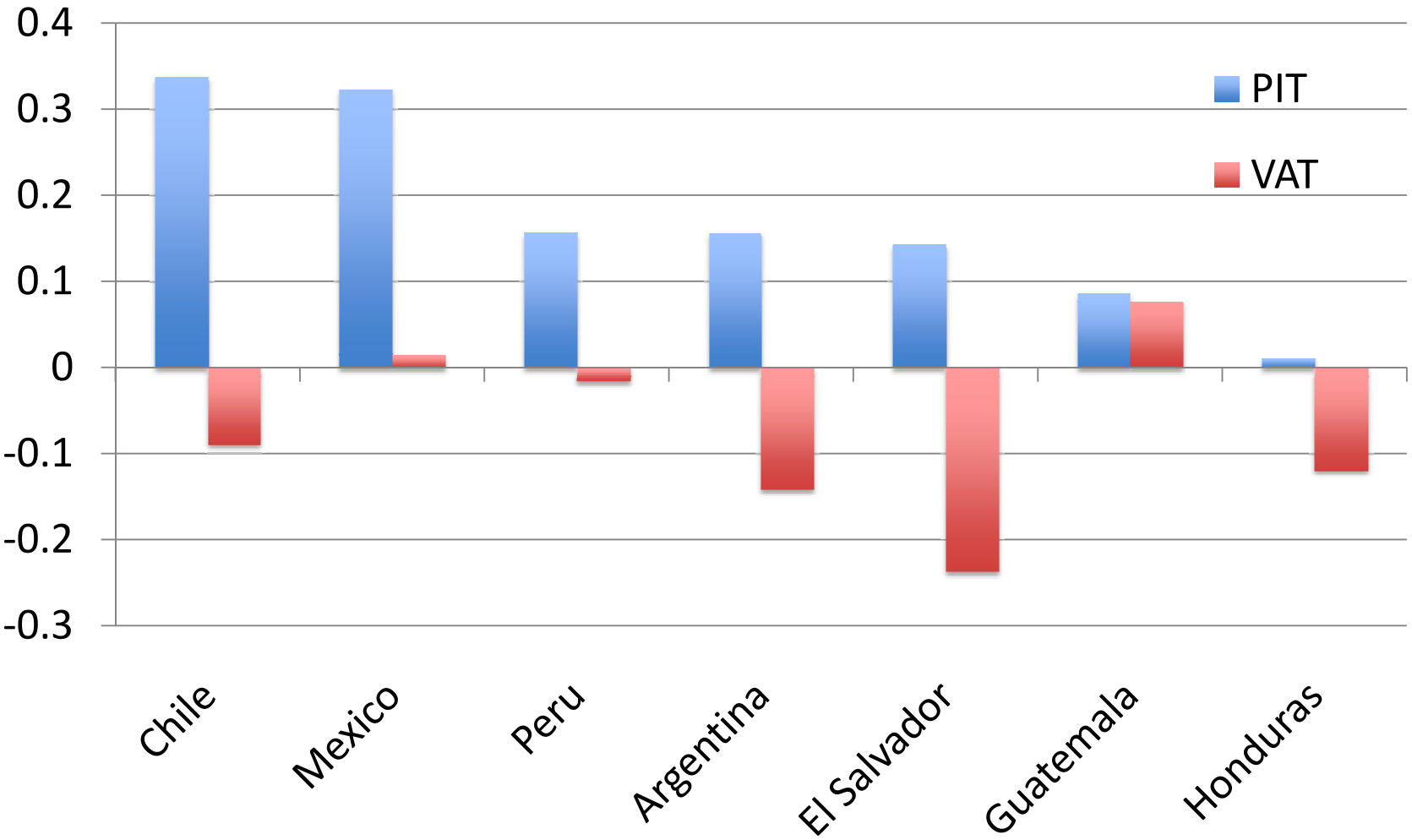
Productividad del IVA
(Recaudación % de PIB por punto porcentual de tasa de IVA)
2007

Países OCDE		PAISES América Latina	
México	***0.23***	Argentina	0.21
		Panamá	0.21
Chec Rep	0.30		
Italy	0.32	***México***	***0.23***
Turkey	0.32		
República Eslovaca	0.33	Brasil	*0.25*
Noruega	0.33	Perú	0.30
Bélgica	0.35	Colombia	0.36
Suecia	0.37	Chile	0.39
Polonia	0.37	Uruguay	0.40
Irlanda	0.38	Costa Rica	0.42
Luxemburgo	0.38	Ecuador	0.45
Finlandia	0.38	Guatemala	0.45
Reino Unido	0.38	Venezuela	0.47
Grecia	0.38	Nicaragua	0.49
Austria	0.39	Paraguay	0.54
Holanda	0.39	El Salvador	0.54
Hungría	0.39	Bolivia	0.68
Alemania	0.39		
Australia	0.40	**Average**	**0.40**
España	0.40	**Coef. of Var.**	**0.34**
Dinamarca	0.41		
Francia	0.42		
Corea	0.45		
Islandia	0.46		
Portugal	0.47		
Japón	0.52		
Suiza	0.52		
Canadá	0.67		
Nueva Zelanda	0.72		
Average	**0.41**		
Coef. Of Var.	**0.25**		

Elaboración propia con base en OCDE Revenue Statistics 1965-2007 y CEPAL

Source: Chávez-Presa y Hernández Trillo (2011)

Progressivity of personal income (PIT) and value added (VAT) taxes: Kakwani coefficient



Source: Mexico 2008 (Scott), rest 1989-2000 (Lora, 2007, "Trends and Outcomes of Tax Reform," in *The State of State Reform in Latin America* (Table 6.8, p. 204).

Incidence of generalized consumption tax of 2%

Decil	Recaudación				efecto de impuesto 2% gral		efecto de impuesto y gasto			
	% recaudación		Pesos por hogar (mensual)				sin focalizar		con oportunidades	
	IVA	+ 2% gral	IVA	+ 2% gral	Pesos mensual	% ingreso	Pesos mensual	% ingreso	Pesos Mensual	% ingreso
I	2.9%	3.1%	$144	$194	-$50	-1.8%	$74	2.6%	$451	15.9%
II	3.9%	4.1%	$192	$257	-$65	-1.4%	$59	1.3%	$240	5.2%
III	4.8%	5.1%	$233	$308	-$75	-1.3%	$48	0.8%	$101	1.7%
IV	5.6%	5.8%	$273	$359	-$85	-1.2%	$38	0.5%	$13	0.2%
V	6.6%	6.8%	$330	$426	-$96	-1.1%	$28	0.3%	-$24	-0.3%
VI	7.9%	8.0%	$389	$494	-$105	-1.0%	$18	0.2%	-$69	-0.7%
VII	9.5%	9.6%	$476	$597	-$122	-1.0%	$2	0.0%	-$96	-0.8%
VIII	11.4%	11.3%	$588	$731	-$143	-1.0%	-$19	-0.1%	-$133	-0.9%
IX	16.0%	15.7%	$807	$990	-$183	-1.0%	-$60	-0.3%	-$176	-1.0%
X	31.5%	30.4%	$1,510	$1,816	-$306	-0.8%	-$183	-0.5%	-$302	-0.8%
Nacional	100.0%	100.0%	$497	$620	-$123					

Se asume que **impuesto recae en su totalidad sobre los consumidores.**
Deciles de hogares ordenados por ingreso per cápita
Fuentes: ENIGH 2008, Simuladores fiscales, CEFP

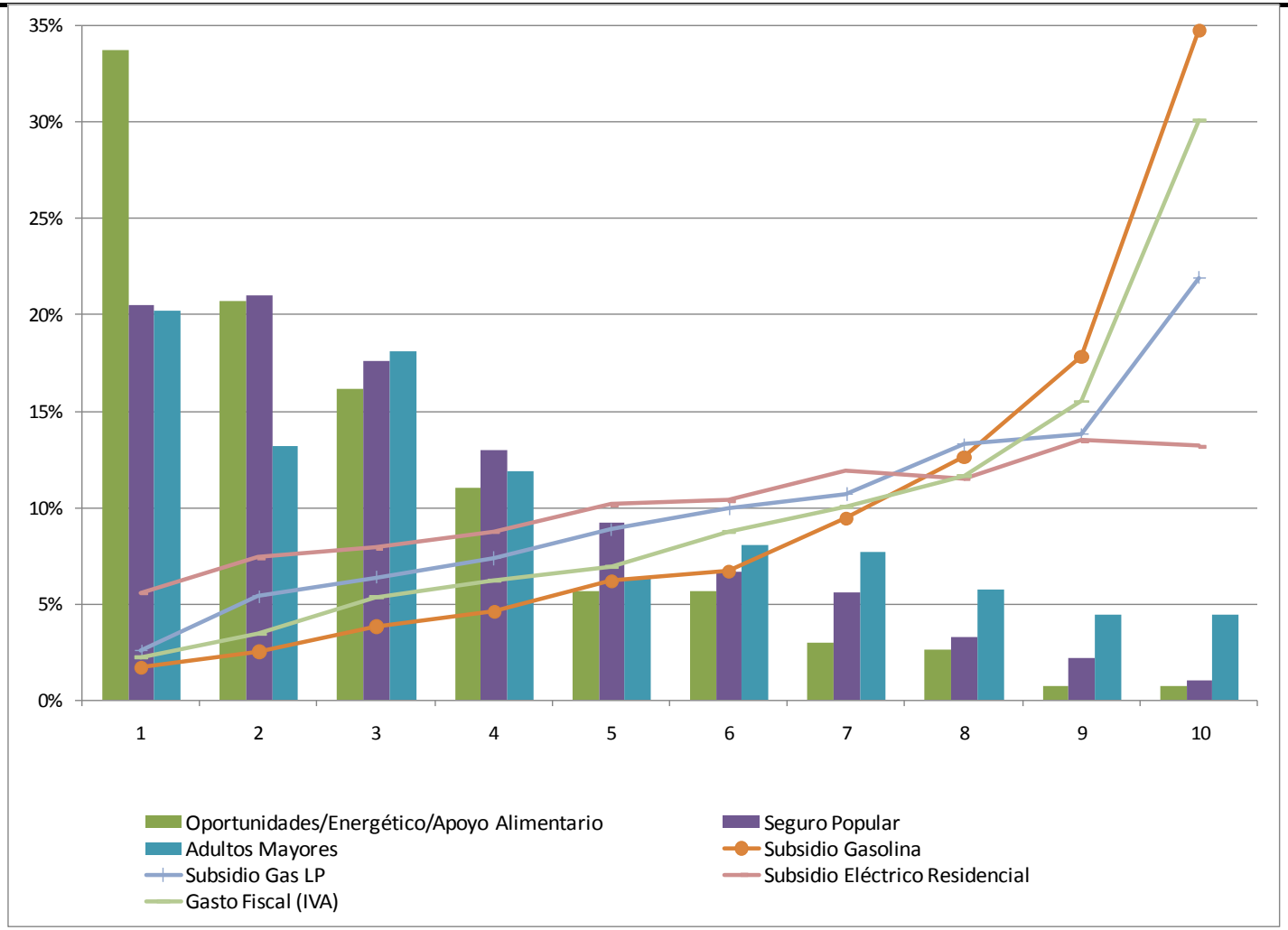
Reformed passed: 1% VAT (with exemptions)

	2% Generalizado			1% IVA		
	Impuesto	+ Gasto	% Ingreso	Impuesto	+ Gasto	% Ingreso
I	**-$50**	**$451**	**15.9%**	**-$10**	**$125**	**4.4%**
II	-$65	$240	5.2%	-$13	$69	1.5%
III	-$75	$101	1.7%	-$16	$32	0.5%
IV	-$85	$13	0.2%	-$18	$8	0.1%
V	-$96	-$24	-0.3%	-$22	-$3	0.0%
VI	-$105	-$69	-0.7%	-$26	-$16	-0.2%
VII	-$122	-$96	-0.8%	-$32	-$25	-0.2%
VIII	-$143	-$133	-0.9%	-$39	-$37	-0.3%
IX	-$183	-$176	-1.0%	-$54	-$52	-0.3%
X	-$306	-$302	-0.8%	-$101	-$99	-0.3%
Nacional	-$123			-$33		

Cuadro 6 Gasto dirigido y subsidios generalizados en 2008		
	Millones PM	**% PIB**
Generalizados (estimados)	**577,998**	**4.8%**
Subsidio Gasolinas	260,000	2.2%
Subsidio Gas LP	37,000	0.3%
Subsidio Eléctrico Residencial	70,000	0.6%
Gasto Fiscal (IVA)	210,998	1.8%
Dirigidos (aprobados)	**89,706**	**0.7%**
Apoyo Alimentario "Vivir Mejor"	4,500	0.0%
Oportunidades	38,082	0.3%
Seguro Popular	37,355	0.3%
Adultos Mayores	9,769	0.1%

Fuentes: Segundo Informe de Gobierno, 2008; CFE; Presupuesto de gastos fiscales, 2008, SHCP; Presupuesto de Egresos de la Federación 2008. Notimex: Agustín Carstens, Sept. 8 2008.

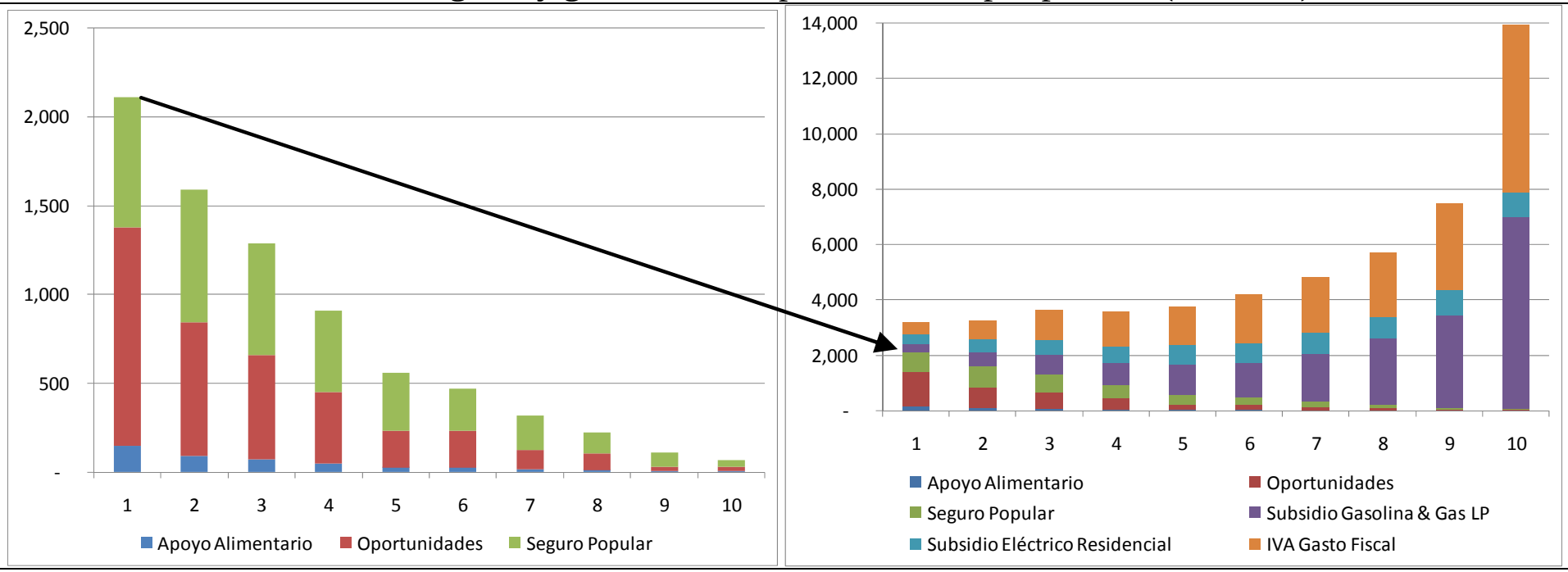
Gráfica 32
Distribución de Beneficios de Programas Dirigidos:

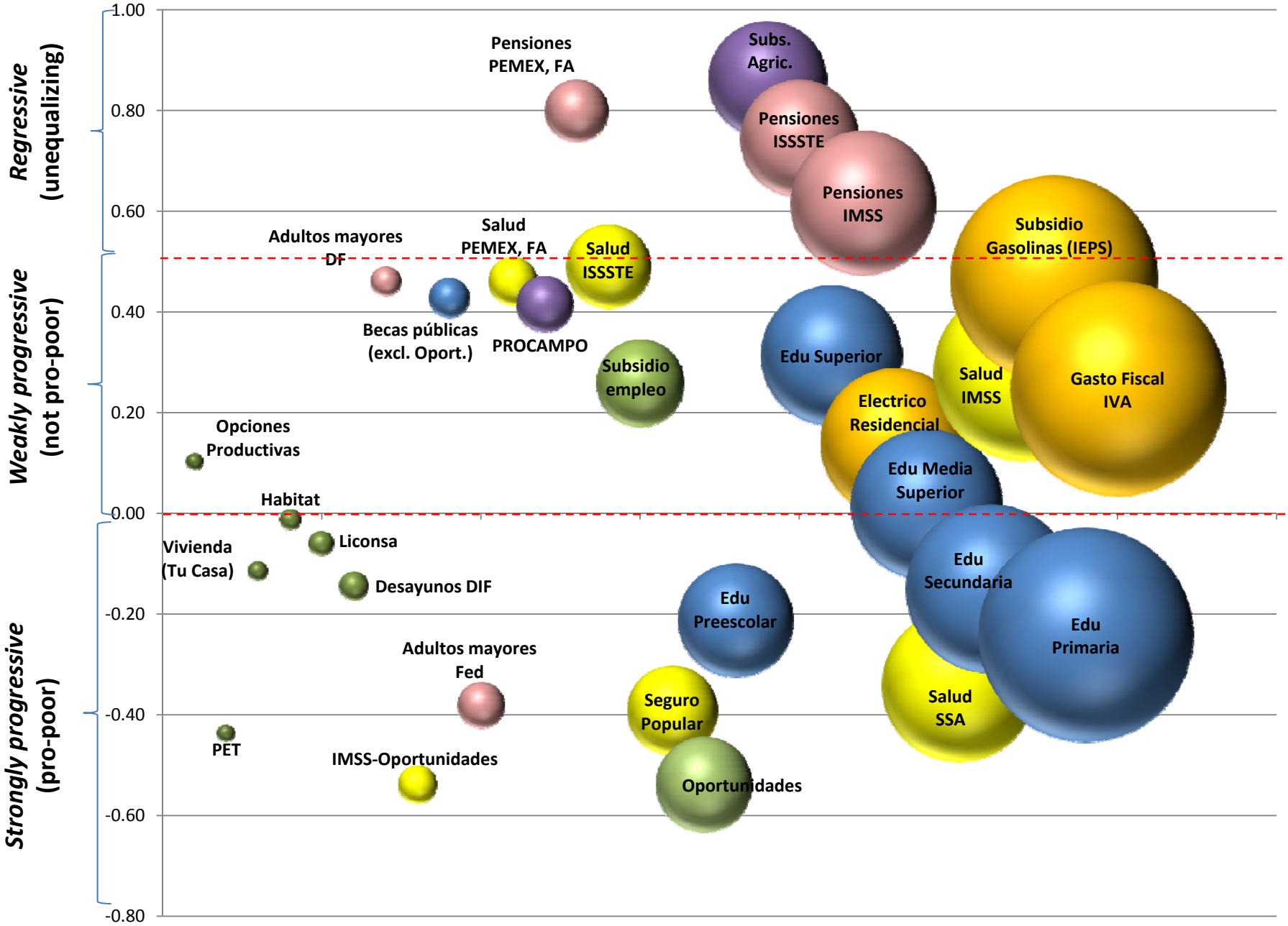


Fuente: calculos del autor a partir del " Modulo de Programas Sociales", ENIGH (2004).

Indirect generalized subsidies cancel the redistributive effect of targeted transfers…

Subsidios dirigidos y generalizados: pesos anuales por persona (GP 2008)




Regressive (unequalizing)
Weakly progressive (not pro-poor)
Strongly progressive (pro-poor)
1.00
0.80
0.60
0.40
0.20
0.00
-0.20
-0.40
-0.60
-0.80
Pensiones PEMEX, FA
Subs. Agric.
Pensiones ISSSTE
Pensiones IMSS
Subsidio Gasolinas (IEPS)
Adultos mayores DF
Salud PEMEX, FA
Salud ISSSTE
Becas públicas (excl. Oport.)
PROCAMPO
Subsidio empleo
Edu Superior
Salud IMSS
Gasto Fiscal IVA
Electrico Residencial
Edu Media Superior
Opciones Productivas
Habitat
Liconsa
Vivienda (Tu Casa)
Desayunos DIF
Edu Secundaria
Edu Preescolar
Edu Primaria
Adultos mayores Fed
Salud SSA
Seguro Popular
PET
IMSS-Oportunidades
Oportunidades

	Net transfers		Transfers	Taxes					
						non-oil taxes			
	net of oil and non-oil taxes	net of non-oil taxes		Total non-oil & oil taxes	Oil taxes	Total	Direct	Indirect	Social security contributions (Health)
Million pesos			1,639,640	1,622,384	708,649	913,735	382,109	531,626	116,161
1	52%	127%	137%	81%	75%	7.2%	0.0%	6.2%	1.0%
2	24%	60%	68%	42%	36%	7.2%	0.0%	6.1%	1.1%
3	17%	42%	51%	32%	25%	7.6%	0.0%	6.3%	1.3%
4	11%	30%	40%	26%	20%	8.0%	0.0%	6.6%	1.4%
5	7%	21%	32%	22%	16%	8.2%	0.1%	6.7%	1.4%
6	4%	15%	26%	19%	12%	8.3%	0.5%	6.3%	1.5%
7	2%	10%	22%	18%	10%	9.5%	1.3%	6.7%	1.5%
8	-1%	5%	19%	16%	8%	10.5%	2.2%	6.7%	1.6%
9	-4%	-2%	15%	15%	5%	12.3%	3.6%	7.0%	1.6%
10	-6%	-6%	8%	13%	2%	13.2%	5.7%	6.2%	1.3%
Average	0%	7%	20%	**18%**	**9%**	**11.2%**	3.3%	6.5%	1.4%

Tax – benefits reforms: universal benefits, effective taxation…

- **Generalizing VAT (eliminating generalized subsidies) and reducing/eliminating other indirect subsidies benefits the poor** even with current (non targeted) spending allocation (without compensation)**…a*) potentially (quality of services), b) "on average"***
- But the coverage of indirect taxes among the poor is wider than even the largest and best targeted transfers (Oportunidades) as well as the combination of all mayor transfers, so **many poor households (40-50%) pay indirect taxes to finance benefits for the non-poor**

Tax – benefits reforms: universal benefits, effective taxation…

- Exclusion errors are inevitable in any administratively targeted transfers (CCTs): we need effective and credible compensation mechanisms capable of **guaranteeing universal coverage among the poor…**
- **Universal social security/protection, *effectively* universal services**
- **Oil rents: basic (taxable) income**