Fiscal Reform in Costa Rica:

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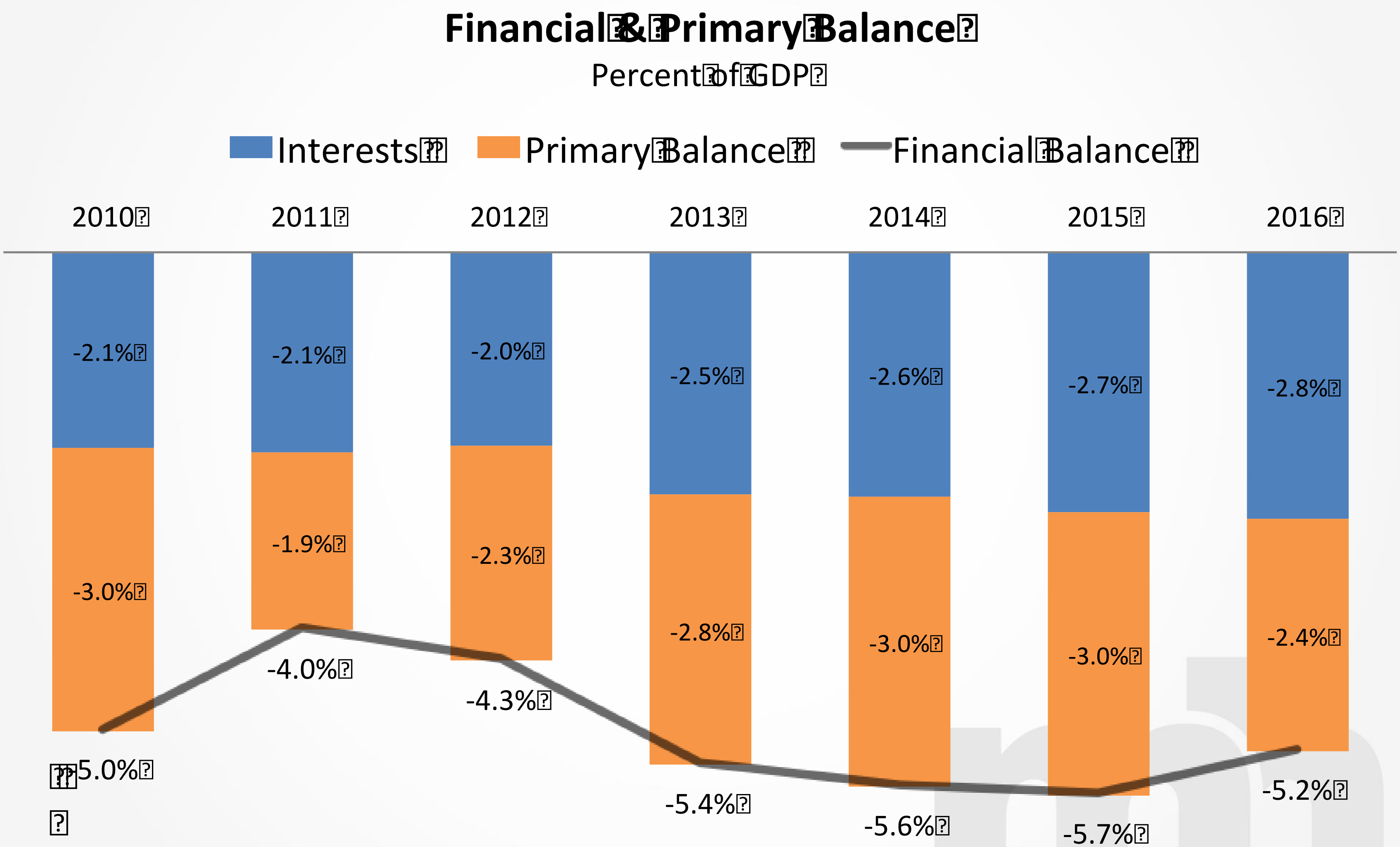
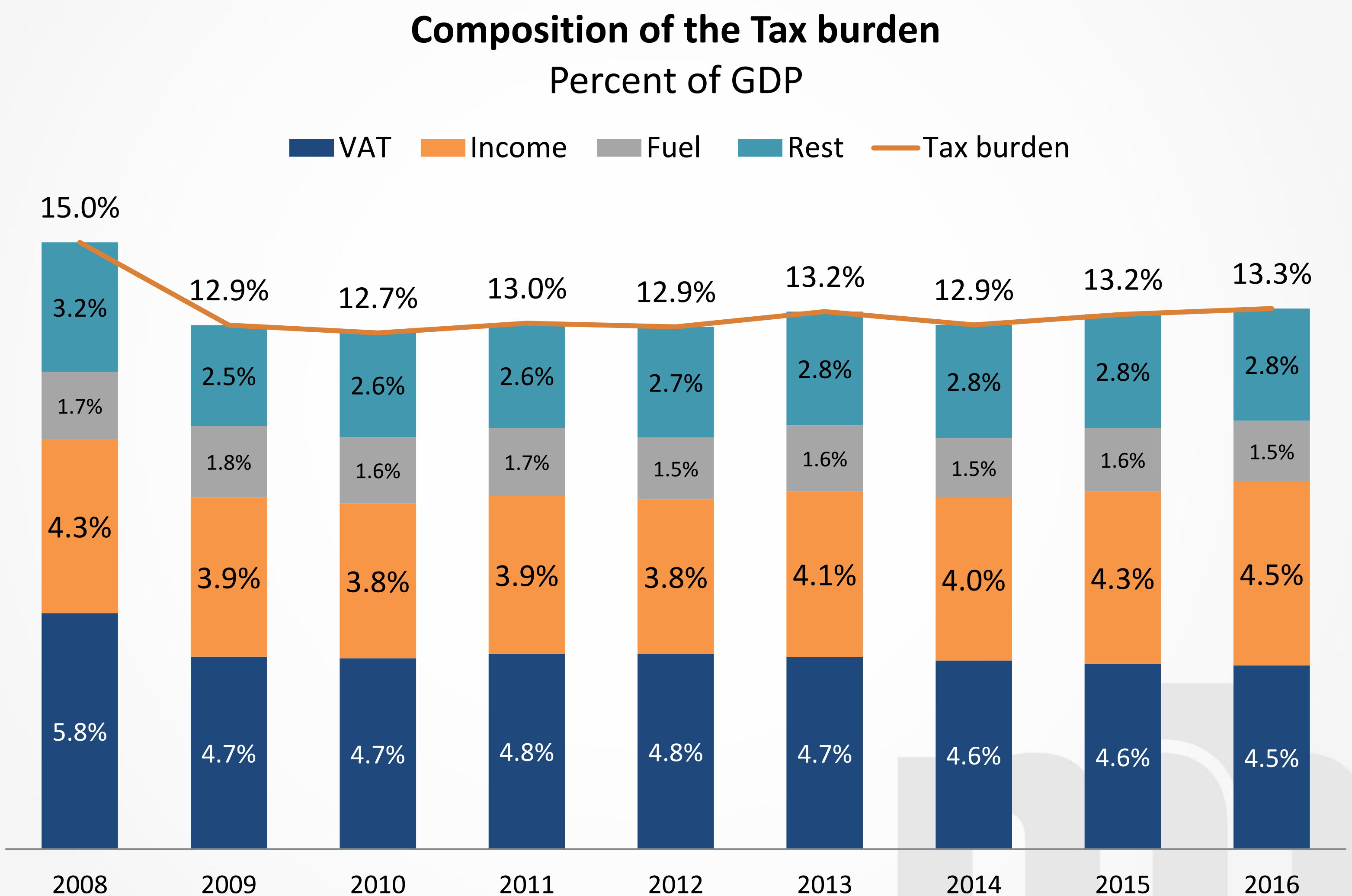
Recent Performance

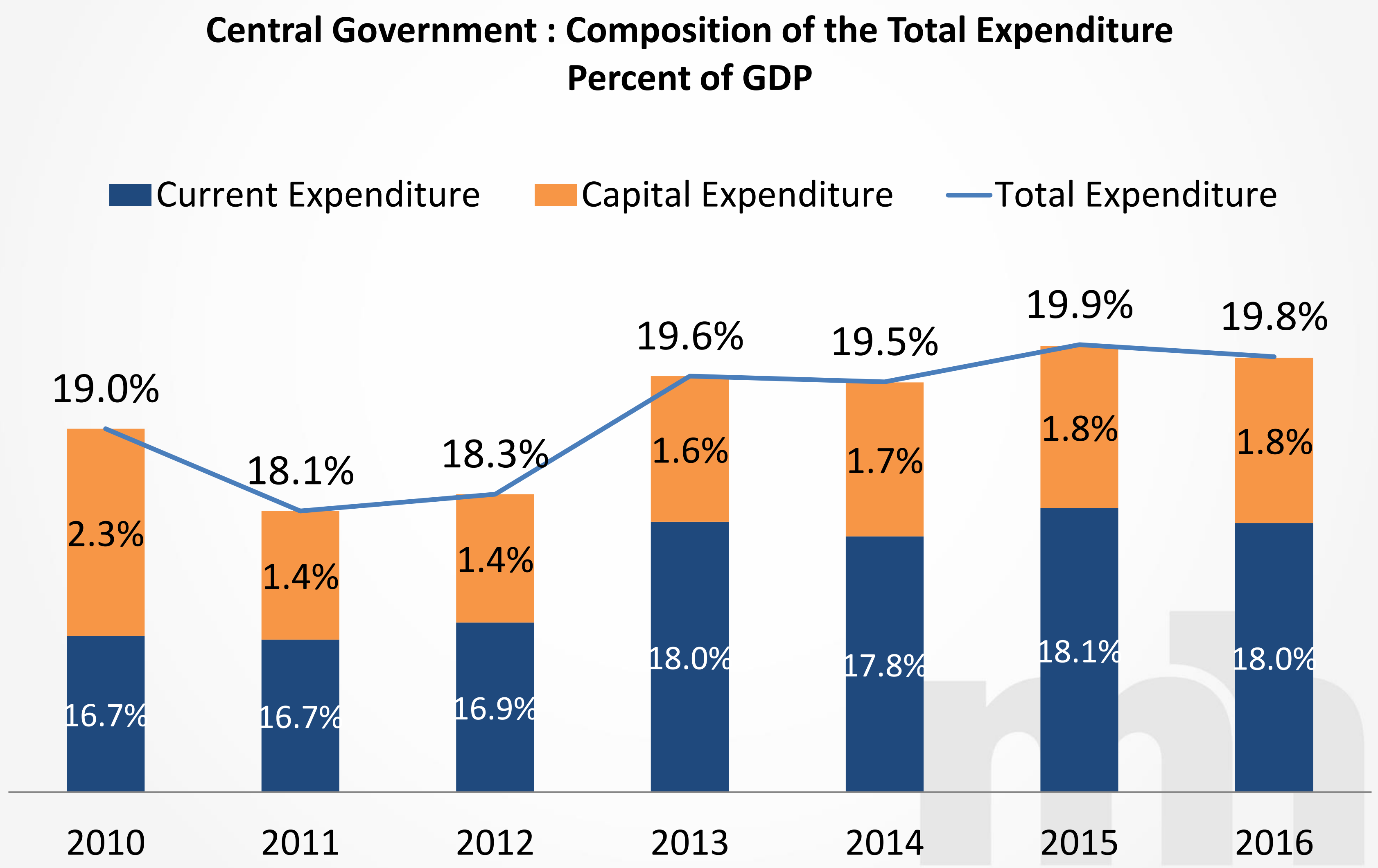
Fiscal deficits over 4% of GDP since 2010



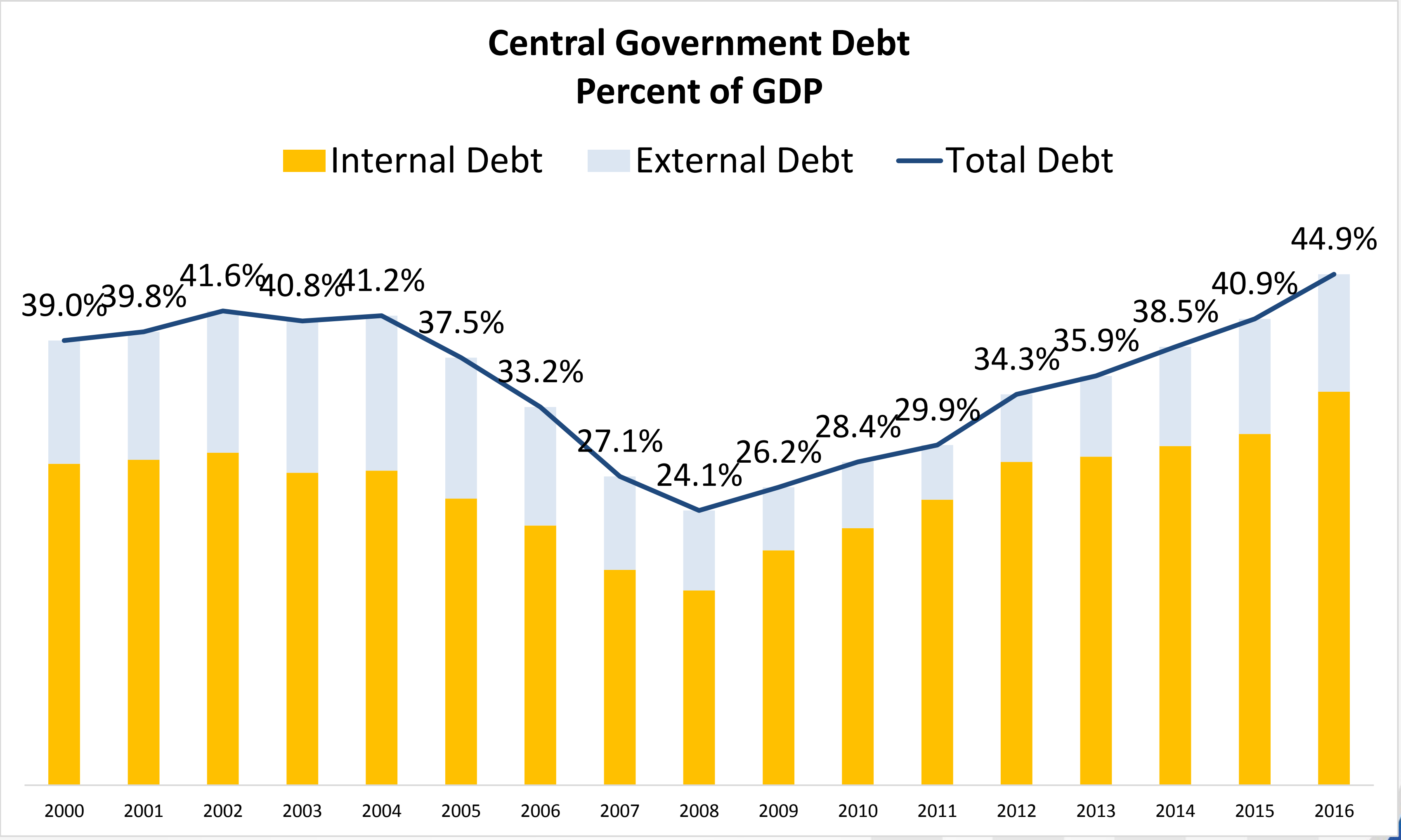
Reason 1. A constant tax burden



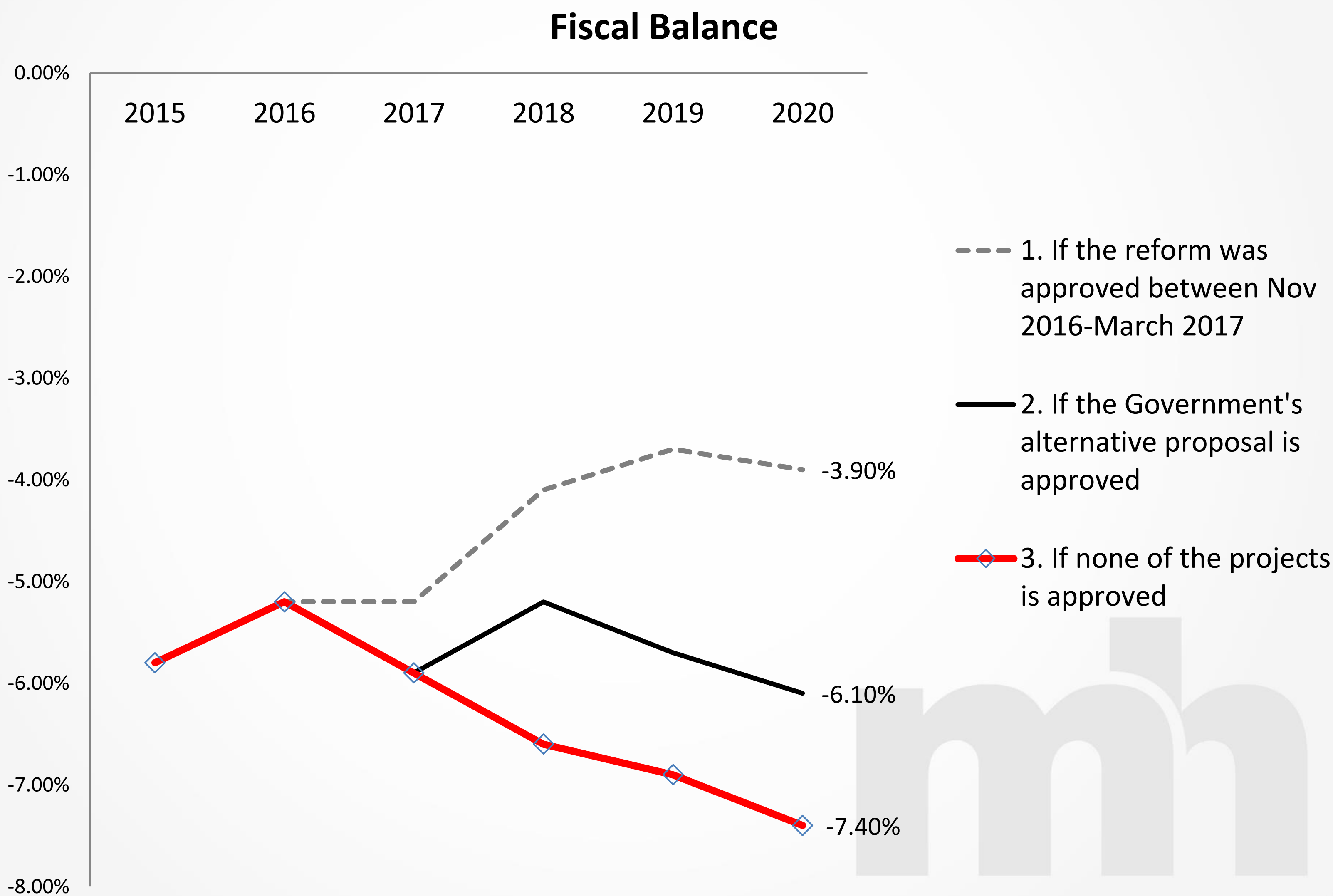
Reason 2. Expenditures continue growing



As a result, debt almost doubled since 2008



Financial deficit could exceed 7% in three years without reform
With reforms (approved in 2016), it would be less than 4%



The Fiscal Reform: proposal

General considerations

- Fiscal strategy characterized by:
  - Legal and administrative measures
  - Balance between new taxes and expenditure control
  - Legal reform aimed at strengthening MoF capacity to collect taxes more efficiently
- No drastic spending cuts
  - Protection to social expenditures and public investment
- Strong modernization of the IT platforms

The Fiscal Reform Agenda

Taxes

- VAT
- Income Tax
- Anti-smuggling *
- Anti-Fraud *
- Tax Legal Entities *
- Tax Exoneration

Expenses

- Pension Reform * (Budget Regime)
- Single account *
- Fiscal Rule

*Approved

Main contents of the initial tax proposal

- **Sales tax:**
  - Move from sales to VAT
  - Increase VAT from 13% to 15%
  - Refund VAT to families in the first four income deciles
  - Expected tax collection: 1.3% GDP

- **Income tax**
  - Expand Tax Base to include all types of capital gains and profitable activity
  - One single and uniform tax rate for those activities: 15%
  - New tax rate for salaries over 2 million colones (US$3,500)
  - Expected tax collection: 0.6% GDP

Economic and political environment of the Reform

- High political fragmentation in Congress: over 12 specific fractions, even inside some political parties
  - Fast track
  - Divergent ideological approaches
- “Broad agenda”: conditionality to discuss reform
- Time is gold
- The sequence of the discussion: taxes first, then expenditures?