The Emerging Tax Landscape in GCC & wider MENA region

Presentation at Thomson Reuters Seminar

"Preparing for VAT"

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Agenda

- ✓ **Overview of MENA Tax Landscape**
- ✓ **Designing Modern Tax Systems**
- ✓ **Taxes in the GCC: What Next?**

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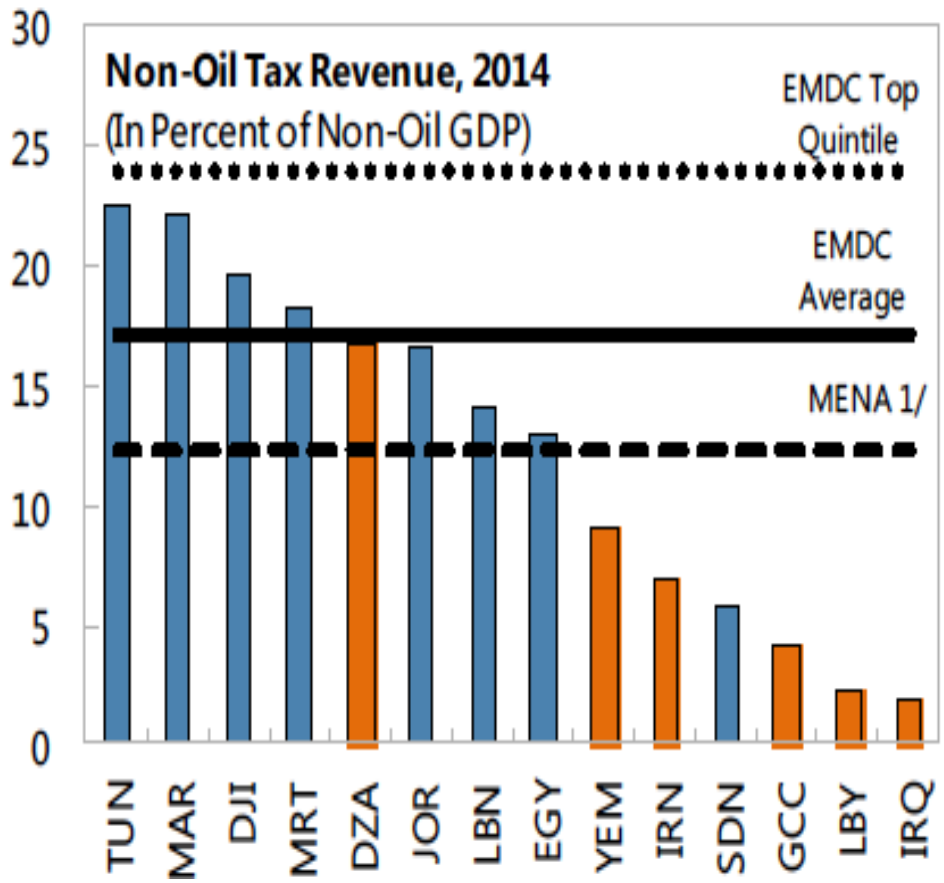
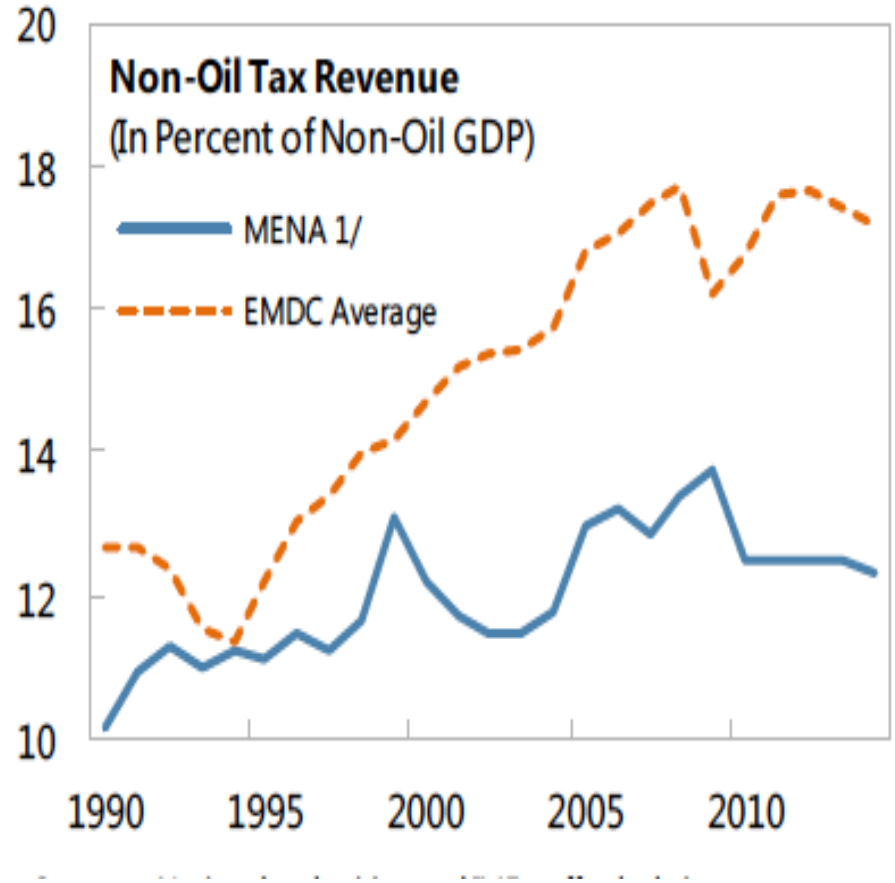
MENA taxation is low compared to other emerging & developing economies

Well-established Non-Hydrocarbon-Based Tax Systems





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Source: Fair Taxation in the Middle East and Northern Africa, IMF Staff Discussion Note, 2015

MENA Tax Revenue shows wide variance across countries

Tax Revenue by Category, Latest Available
(In Percent of Non-Oil GDP)

	Total	Goods and Services	VAT	Excise	Personal Income	Corporate Income	Trade	Property
Algeria	16.7	6.1	2.1	0.4	4.2	2.2	3.0	0.0
Bahrain	0.8	-	-	-	-	N/A	0.8	0.4
Djibouti	19.6	7.3	N/A	N/A	3.2	5.9	2.0	N/A
Egypt	13.0	4.6	2.6	1.7	1.6	4.5	0.9	0.9
Iran	6.9	1.8	1.3	0.3	0.3	2.3	1.0	0.3
Iraq	1.9	1.0	N/A	N/A	0.3	0.2	0.3	N/A
Jordan	16.5	11.1	11.1	N/A	0.6	2.4	1.3	0.5
Kuwait	2.2	-	-	-	-	0.8	2.0	0.1
Lebanon	14.0	5.1	4.0	1.7	0.8	2.5	2.7	1.7
Libya	2.2	-	-	-	-	N/A	0.2	-
Mauritania	18.2	9.0	2.4	1.1	5.0	2.6	2.4	N/A
Morocco	22.2	11.0	8.2	2.7	3.8	4.5	0.9	1.5
Oman	6.4	-	-	-	-	3.2	1.7	-
Qatar	12.9	-	-	-	-	12.1	0.8	-
Saudi Arabia 1/	2.4	-	-	-	-	0.9	1.5	-
Sudan	5.6	3.2	2.1	0.4	0.1	0.5	1.7	0.0
Tunisia	22.5	6.2	6.2	2.0	4.6	2.6	1.0	0.5
United Arab Emirates	4.8	-	-	-	-	1.4	1.1	N/A
Yemen	9.1	3.2	N/A	N/A	2.8	1.4	1.5	0.0

Source: National authorities; IMF staff calculations.
Note: Due to discrepancies between the latest data point across categories or incomplete information, components may not add up to the total.
1/ Does not include revenue from zakat, which could amount to up to 2.6 percent of non-oil GDP.

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Excise taxes in MENA: modest contribution with significant potential

- Main excise taxes applied: tobacco, alcoholic & non-alcoholic drinks, petroleum products, cars, mobile telephony
- Excise revenues in % of GDP declined significantly in MENA since 2000, except Egypt & Lebanon
- In some countries, like the Maghreb, excises are still levied on a large no. of goods (in some cases >50)
- Excises remain untapped, potentially significant, revenue sources

Excise Tax Revenues: 2000-01 vs. 2011-12

	2000-01	2011-12
	(Percent of GDP) 1/	
Resource countries 2/		
Algeria	2.15	0.39
Iran	1.77	0.32
Non-resource countries 3/		
Maghreb		
Mauritania	2.62	0.88
Morocco	3.79	2.77
Tunisia	3.16	2.30
Mashreq		
Egypt	1.36	1.67
Jordan	0.83	0.42
Lebanon	3.51	2.96
Syria	0.26	0.20

1/ The two-year average is weighted by GDP.
2/ In the resource group, Libya & GCC do not apply excises; no data for Yemen
3/ The 2011-12 figure for Syria is for 2009-10. Jordan's figures include a real estate registration fee which could not be carved out.

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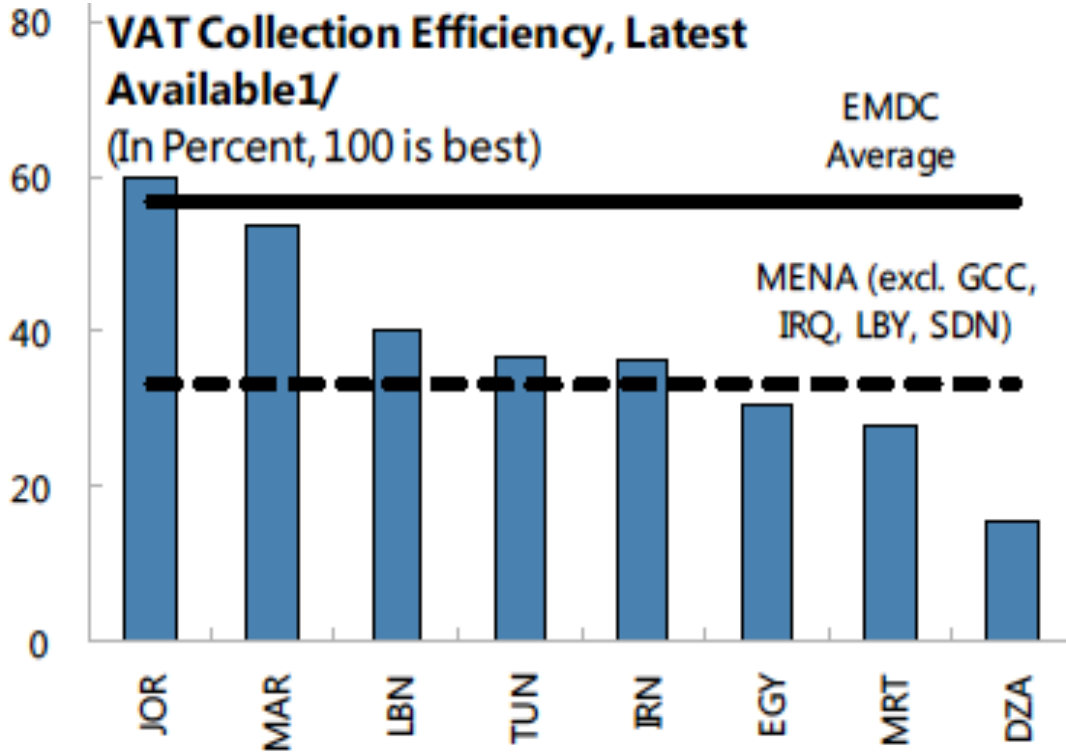
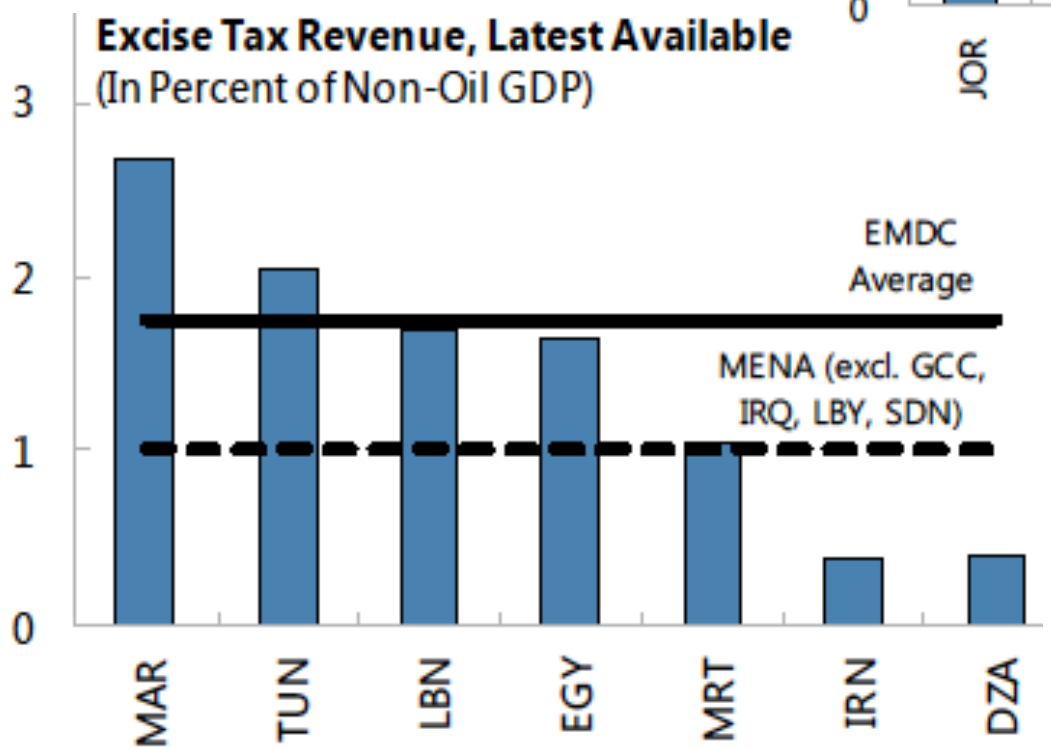
Tax exemptions, special rates and thresholds, etc. worsen limited progressivity of VAT & hamper efficiency, administration





Poorly designed excises provide limited revenues and do not currently target equity

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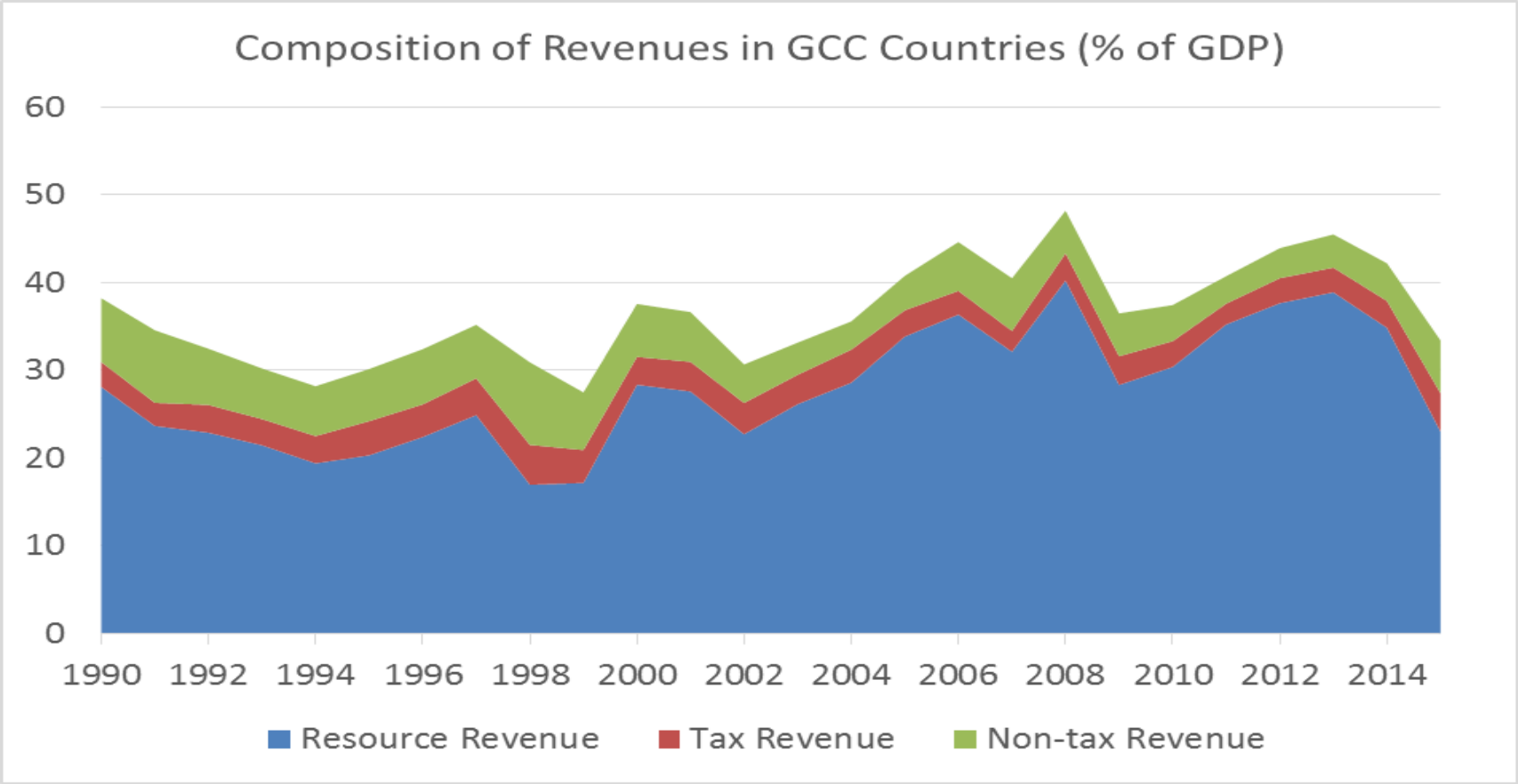
Tax revenues are negligible in GCC: lower even than non-tax revenues



- Share of tax revenue/ GDP averaged ~1.6% (3% of non-oil GDP) in 2012-14 with wide variation across: Oman has highest non-oil tax-to-GDP ratio at 2.7% ; Kuwait lowest at about 0.8% of GDP

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Current tax regime in GCC inadequate; lack of effectiveness of fiscal policy

Main non-oil revenue taxes: customs duty, fees & charges

- Inadequate tools for counter-cyclical fiscal policy
- Do not constitute a complete panoply of modern tax tools
- Yield little revenue (low rates, narrow bases, ineffective administration, low compliance)
- Limited ability to influence behaviour of private sector
- Distortionary impediments to trade
- Significant loss in revenues due to WTO and bilateral FTAs

Move to…

Develop new tax regimes: Indirect taxes

- **Broad based taxation**:
  - VAT/GST
  - Property taxation
- **Selective taxation:** Excise taxes on:
- Fuel
- Tobacco
- Sugary drinks
- Alcohol
- Luxury vehicles

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Designing a New GCC Tax System

- Need **diversified, balanced sources of taxation** adapted to more diversified and growing digital economies
- Tax system needs to be designed to **abide with international principles and guidelines:**
  - **Ottawa Taxation Framework Conditions:** Neutrality; Efficiency; Certainty & Simplicity; Effectiveness and Fairness; Flexibility
  - **OECD International VAT/GST Guidelines 2015:** Destination and Neutrality Principles
- Ensure **Fiscal Transparency**
- **Leapfrog to Digital Public Finance & Taxation**

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Ottawa Taxation Framework Conditions

1. **Neutrality**: Taxation should seek to be neutral and equitable between forms of electronic commerce and between conventional and electronic forms of commerce. Business decisions should be motivated by economic rather than tax considerations. Taxpayers in similar situations carrying out similar transactions should be subject to similar levels of taxation.

2. **Efficiency**: Compliance costs for businesses and administrative costs for the tax authorities should be minimised as far as possible.

3. **Certainty and simplicity**: The tax rules should be clear and simple to understand so that taxpayers can anticipate the tax consequences in advance of a transaction, including knowing when, where, and how the tax is to be accounted.

4. **Effectiveness and fairness**: Taxation should produce the right amount of tax at the right time. The potential for tax evasion and avoidance should be minimised while keeping counteracting measures proportionate to risks involved.

5. **Flexibility**: The systems for taxation should be flexible and dynamic to ensure that they keep pace with technological and commercial developments.

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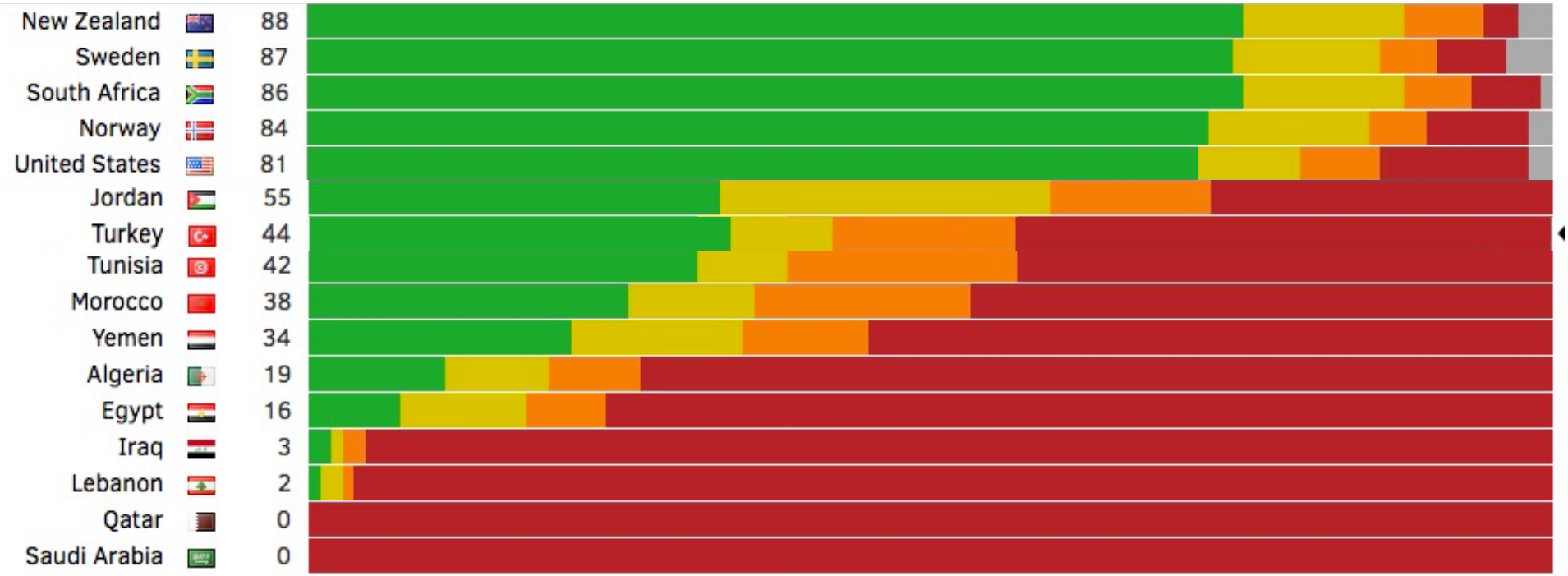
MENA countries rank poorly on Fiscal Transparency

- **Open Budget Survey** evaluates whether governments provide public information on Expenditures, Revenue, Debt, Performance, Pre-Budget Statement, Executive's Budget Proposal, Enacted Budget, Citizens Budget, Periodic Reports, Audit Report
- Also assesses capacity and independence of formal oversight institutions & whether the public has opportunities to participate in budget process

The Open Budget Index 2015 Score: Top 5 vs MENA & Turkey



International Initiatives aimed at improving Fiscal Transparency

IMF:
- Codes of Good Practices (Manual) on Fiscal Transparency
- Fiscal transparency Report on the Observance of Standards and Codes (Fiscal ROSCs – 111 in 94 countries)

Statistical front:
- GFSM 2001,
- IMF's Statistics Department 2008 *Guide on Consolidation of Non-financial Public Sector Statistics,*
- FAD *technical note on the Financial Oversight of Public Corporations*

WB:
- Fiscal Risk Management DPLs

IPSAS:
- International Public Sector Accounting standards,- International Federation of Accountants

Fiscal Transparency

OECD:
- Best Practices for Budget Transparency

IMF, World Bank, other international Partners:
- Public Expenditure and Financial Accountability (PEFA) Report (285 reports covering 135 countries.)

International Budget Partnership (IBP):
- Open Budget Survey (OBS) in over 100 countries

Digital Public Finance

- Structure of taxation in MENA needs to change to take account of shift in economic activity towards services, knowledge based and digital economy;
- Fiscal authorities need to adopt and use modern ICT and FinTech both for the delivery of services as well as for revenue collection and administration (e-VAT and e-Tax) and as part of e-Government;
- Efficiency of government services can be greatly enhanced by using Big Data
- FinTech can mean financial inclusion, access and participation in the formal economy to benefit from government services
- Leapfrog by establishing digital public finance soft & hard infrastructure

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E-VAT & electronic filings

E-filing and electronic payments can help to improve efficiency and reduce processing time and costs for tax administrations and VAT/GST payers alike => opportunity for GCC to leapfrog to e-VAT

According to EY's global survey (published 2014):

- VAT/GST payers currently file periodic VAT returns electronically (use e-filing) in 66 countries
- VAT/GST payers can currently pay VAT/GST balances electronically in 75 countries
- Currently, less than half of the 86 countries surveyed allow businesses to deal with VAT/GST registration matters electronically
  - 36 countries allow electronic registration
  - 38 countries allow VAT/GST payers to notify changes in their details electronically.
  - 23 countries allow VAT/GST payers to deregister electronically
- "Electronic data processing audits" or e-audits are the next step

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How are the GCC nations planning to raise non-oil revenues?

- **No clear vision of public finance and fiscal regimes announced to date**
- **Bahrain** started increasing a number of fees, including for health care services, and recently increased tobacco and alcohol taxes
- **Oman** has increased corporate taxes and fees this year
- **Saudi Arabia** has boosted non-oil receipts, primarily through higher transfers from entities outside the central government budget; Other measures include introducing airport charges, raising visa fees etc.
- **No current plans to introduce personal income taxes. Remittance taxes?**

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Tax Sequencing is important

- **Introducing VAT**: A low-rate VAT should be considered as a natural first step as it is efficient and broad-based
- **Starting to develop a CIT**: A low-rate CIT would be relatively easy to justify on the basis of the benefit principle & large economic rents
- **Setting up property taxes and excises***:* Property taxes, typically on land and real estate, would be relatively simple to introduce; these plus excise taxes would help address wealth inequality and indirectly income inequality
- Make plans for the *future introduction of personal taxation*
- ***Caveat: Build administrative capacity and taxation expertise that can be leveraged later to scale up tax systems***

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GCC VAT: the story so far

- GCC VAT framework is **expected to be finalized & formally announced by end-2016**. The provisions of the *GCC Framework Agreement* will be transposed into **domestic tax law** in the GCC prior to the effective date
- GCC **agreed to implement VAT regimes in 2018**. Most are working to implement by 1 Jan 2018 to avoid distortions arising from intra-GCC trade. All GCC States will need to have implemented VAT by end-2018
- **Main design issues**: (a) Single or Multiple Rates; (b) Zero-rated and Exemptions; (c) Coverage: registration threshold; (d) international issues: VAT usually destination based. Zero-rating of exports; (e) treatment of financial services and digital products
- Confirmed that **certain essential food items and industries such as healthcare, social services and education will be exempt** from VAT

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GCC: Estimated VAT Revenue

		Using average C-efficiency ratio (0.58) of selected sample of countries with experience relevant to the GCC			Assuming the base = 90% of private consumption		
			Revenue at VAT rate of			**Revenue at VAT rate of**	
	Year	**Share of final consumption in GDP**	**5%**	**10%**	**Share of private consumption in GDP**	**5%**	**10%**
Bahrain	2014	56.6	1.6	3.3	41.0	1.8	3.7
Kuwait	2015	48.2	1.4	2.8	30.0	1.4	2.7
Oman	2015	54.8	1.6	3.2	30.4	1.4	2.7
Qatar	2015	30.7	0.9	1.8	15.8	0.7	1.4
Saudi Arabia	2015	57.5	1.7	3.3	33.7	1.5	3.0
UAE	2015	58.3	1.7	3.4	45.1	2.0	4.1

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Policy Recommendations for Governments

- **Indirect taxation** can be the principal & reliable source of government revenue
- Use **VAT & Excises to replace large number of fees, charges and stamp duties** that raise cost of doing business
- **New tax structures should be harmonized, coordinated and synchronized across the GCC**
- Undertake a **policy impact assessment** when introducing new taxes
- **Digital Public Finance:** Adapt modern technology for tax administration & collection: introduce e-filings, e-VAT/GST, digital markers, track & trace systems etc.
- **Fiscal Transparency** needs to be built-in
- MENA countries need to wake up to **taxing digital economy**

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Thank you

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