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## **Gendered Implications of Tax Reform in Latin America: Argentina, Chile, Costa Rica, and Jamaica**

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In Latin American and Caribbean countries, poverty and inequality have been long-standing problems, and the momentous economic and social policy changes over the past two decades have done little to correct these trends.\* The most effective means for reducing class- and gender-based poverty and inequality would be citizenship-based entitlements to basic (i.e. allowing basic subsistence) income support, health care, and education. In advanced industrial societies, public spending is an extremely important instrument for the alleviation of class- and gender-based poverty and inequality (Moller et al. 2003; Bradley et al. 2003; Huber et al. 2001), and it could potentially play a similar role in Latin America and the Caribbean. However, responsible, that is, non-inflationary financing of such programs requires a sound system of taxation, something that is scarce in developing countries, including in Latin America and the Caribbean. Systems of taxation on their part have important implications for class and gender equity. This chapter explores changes in the systems of taxation in four Latin American and Caribbean countries – Argentina, Chile, Costa Rica, and Jamaica – from the point of view of their gendered impact.

The starting point of the argument is that effective tax collection is a necessary, though not sufficient, condition for the amelioration of gender-based poverty and inequality. Low aggregate tax collection hurts women because it prevents the establishment of programs that counteract market distribution of income, in which women are generally disadvantaged. They are disadvantaged in market income because they provide the bulk of the non-paid care work, because their paid work takes place in the informal sector to a greater extent than men's paid work, and because – if they work in the formal sector – they tend to be employed in smaller enterprises and to earn less than men.

Latin American countries as a whole have been undertaxing their populations, with an average tax burden of 14% of GDP in the first half of the 1990s, compared to 17% of GDP in a group of East and Southeast Asian countries (IADB 1996: 128). Direct taxes amount to about 25% of tax revenue only, and of this amount some 60-80% typically come from corporate tax payments, while only 10-15% come from private individuals (ECLAC 1998: 72). Interestingly, the situation in the English-speaking Caribbean has been very different, with an average tax burden in the first half of the 1990s of 27-28% of GDP, essentially double the rate of Latin America, and direct taxation on individuals and corporations accounting for some 40% of tax revenue (ECLAC 1998: 66-72). This contrast suggests that the fundamental reasons for the poor tax collection performance in Latin America are poor policy choices, rather than low levels of economic development and technological capacity.

The first task of this chapter is to outline changes in the systems of taxation in these four cases since the 1970s and to diagnose new and persistent problems in these systems. Then, the chapter will look at studies of incidence of taxes, all of which look at incidence across income or occupational categories, or classes, and none of which even consider gender. The way to arrive at some estimates about the gendered impact of tax reform, then, is to look at women's representation in the different income categories and in different positions in the labor market, and to make some assumptions about household

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budget-making. A look at the politics of tax reform over the past two decades will suggest some reasons for the neglect of gender issues in the design of these reforms. Finally, some policy lessons will emerge from this analysis.

### *Changes in Tax Structures since the 1970s*

The dominant pattern of tax reforms over the past three decades in Latin America and the Caribbean, which – with some exceptions – holds true for our four cases, has consisted of reductions of marginal tax rates on corporate and individual incomes and attempts to broaden the tax base, but these have not succeeded in significantly increasing income tax collection. At the same time, revenue from imports and exports and other international transactions declined significantly in many cases due to the lowering of tariff rates and other forms of deregulation. To make up for this decline and to facilitate tax collection, most countries have shifted more weight to value added taxes (VAT). There has been more variation in the treatment of social security contributions, corresponding to the different approaches with regards to social policy reforms.

Advocates of this pattern of tax reform, prominent among them representatives of the World Bank, have argued that reduction of marginal tax rates reduces the incentive for tax evasion (not declaring income or transactions) and tax avoidance (maneuvering within the tax code to reduce tax liability) and that broadening of the tax base reduces non-neutral tax treatment that encourages resource shifts to relatively low tax activities and thus distorts resource allocation. Moreover, reducing the complexity of the tax structure makes tax collection less costly and more effective (Thirsk 1997: 8-11). The VAT in particular is supposed to be easy to collect and – if broadly based – not to have distorting effects on resource allocation.

In all these countries, though, tax evasion and avoidance have remained fundamental problems. Both individuals and corporations continue regularly to engage in both. Despite administrative reforms to upgrade the status, equipment, and quality of personnel of the tax administration agencies, these agencies have fewer human resources and smaller budgets but higher collection costs than their counterparts in the more developed countries (ECLAC 1998:83).

<b>Tax Categories</b>	
<b>Direct Taxes</b>	
	Income, individual
	Income, corporate
	Property, wealth and inheritance
<b>Indirect Taxes on Consumption</b>	
	Value Added (VAT)
	Sales
	Excise on selective products; “sin” taxes, e.g. alcohol, tobacco
<b>Trade Taxes</b>	
	Import duties
	Export duties
<b>Social Security Taxes</b>	
	Employees/ self-employed in formal sector
	Employer payroll in formal sector
<b>Other Taxes</b>	

*Data and Sources:* Table 1 shows the overall level and the composition of taxes in 1980-81, before the onset of the general Latin American debt crisis, and in 1999-2000, after a decade or more of economic reforms. A note of caution is in order here. These data come from the IMF International Financial Statistics (1991, 1997, 2003) and Government Finance Statistics (1988, 1991, 1995, 2003). I decided to use them because these sources provide time series and data for all four countries (as well as many others), and they can be assumed to be most comparable. However, other authors cite other data that vary quite considerably from those presented here. For instance, Tanzi (2000) cites ECLAC, based on official data, as the source for time series data that show total tax revenue of the central government as a percentage of GDP much lower for Argentina, Chile, and Costa Rica in 1980 and 1981 than the data in Table 1. His data for Argentina show total tax revenue of 9.1% of GDP for 1980 and 12% for 1981, compared to 13.5% for 1980-81 in our data; Chile with 17.4% and 19.2% compared to 25.7%; and Costa Rica with 11.2% and 12% compared to 16.8%. For 1999, the last year in his series, he shows a higher figure for Argentina, with 17.6% compared to our 12.7% in 1999-2000, but lower figures for Chile, with 16.9% compared to 17.4%, and Costa Rica, with 12.5% compared to 18.2%. Thus, his data for Chile and Costa Rica in the earlier period and for Argentina and Costa Rica in the later period show significant discrepancies to our data.

Table 1 about here

In contrast, Carciofi and Centrángolo (1994), citing Tanzi (1987), present data for 1980/82 for Argentina that are much higher than ours, with total tax revenue accounting for 19.9% of GDP.<sup>1</sup> Presumably, they include tax revenue of provincial governments, as they have some countries in their table marked as “central government data” but not Argentina. Their data for Chile and Costa Rica are much closer to ours, with 24.8% for Chile in 1981/83 and 17.5% for Costa Rica in 1978/80. Sabaini et al. (2002) present figures for Argentina for 1997 that show central government tax revenue as 19.7% of GDP, provincial tax revenue as 3.7% of GDP and municipal revenue as 1.2%, so – assuming that this ratio is more or less constant over the past two decades – one would have to add about 25% to the total central government revenue figures to arrive at the total tax burden. For 1997, then, according to their figures total tax revenue for all levels of government in Argentina was 24.6% of GDP. If we add the 25% correction for provincial and municipal taxes to our figure of total central government revenue of 12.5% of GDP for 1995-96, the closest time period to theirs, we arrive at 15.6% of GDP. This is still a remarkable difference, even if one assumes some variation in tax receipts from year to year in accordance with economic fluctuations. These discrepancies most probably stem from a combination of different figures for tax revenue and for GDP. GDP figures are often revised repeatedly as new information becomes available, and in the case of Argentina in the second half of the 1990s, GDP figures were significantly revised.

There is a further problem having to do with comparability of tax revenue data from different sources. Different authors and institutions may classify certain taxes differently. For instance, in our Table 1, Argentina shows no individual or corporate income or property taxes at all for 1980-81, but 4.4% of GDP or 32.1% of total tax revenue coming from “other” taxes. Carciofi and Centrángolo (1994) show individual and corporate income taxes together as negligible for the same period, contributing only 0.3% of total tax revenue, but other income taxes and property taxes together accounting for 20.8% of total tax revenue, and “other” taxes for 8.6% only. Thus, they seem to have classified some of the taxes that the IMF classified as “other” under “other income” taxes. We shall encounter a similar discrepancy in the classification of foreign trade taxes below.

Having acknowledged these data problems, we can make three points to affirm the usefulness of the comparisons across countries and across time to be made here. First, our data all come from the same source and thus are more comparable than data pieced together from different sources. Second, IMF figures are important because they are used in setting targets for governments in the formulation of fiscal policy. Third, if we look at the pattern of change in composition of tax revenue over time, and if we are attentive to and correct for different classification decisions, the various sources and authors paint a similar picture: They show a decrease in reliance on foreign trade taxes and an increase in reliance on indirect taxes, with the share of direct taxes remaining roughly constant. The important exception is Jamaica.

*The Incidence of Different Categories of Taxes:* In general, the following assumptions are made regarding the incidence of different kinds of taxes. Direct taxes on income, profits, and property tend to be universally progressive and indirect taxes generally

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<sup>1</sup> They do not present time series, so the years are not entirely comparable.

regressive, though the degree to which they are regressive varies with the exemption of basic goods and services. If such exemptions are targeted narrowly on a basket of basic goods and services consumed by low income earners, indirect taxes such as sales taxes or VAT become less regressive (Hossain 2003).

Social security taxes are ambiguous; the share paid by employees is generally tied to earnings and thus proportional, but since there are often caps on contributions, these taxes become regressive at the upper end. This is so because where income is taxed for social security up to a certain limit only, earners whose income surpasses that limit clearly pay a lower share of their total income as social security taxes. Even though these limits are generally quite high, they still advantage the highest income earners. The share of social security taxes paid by the employer may be passed on to the final price of the product and thus at least partly shared by the consumer. However, in the new open economic environment, possibilities for passing on these costs to the consumer are more limited, so we can assume that a larger share is carried by the employer and – even more likely – the employee (in the form of lower wages to absorb some of the employer's share). Again, we would expect that lower paid employees would absorb a larger share in proportion to their income than the highest paid employees.

The financing of social security systems has a further regressive feature. Typically, governments supplement social security taxes paid by employees and employers with contributions out of general revenue. The self-employed who join social security systems on a compulsory or a voluntary basis have to pay both the employee and the employer contribution, which makes it very expensive. In practice, the only segments of self-employed who join social security systems are professionals in the formal sector. Since social security coverage is limited to employees and self-employed people in the formal sector but people in the informal sector contribute to general tax revenue through indirect taxes, this system of financing redistributes money from informal to formal sector workers. Since formal sector workers on average have higher incomes than informal sector workers, this is a regressive mechanism of financing.

*The Situation in the Early 1980s:* When situating the discussion in the framework of the debt crisis and subsequent economic reforms, it is important to note that Jamaica and Argentina had very severe debt and economic problems going back to the late 1970s. In Chile, the economic downturn began in 1982 and in Costa Rica in 1981. In 1980-81, Chile and Jamaica were clearly at the upper end of Latin American countries in total tax collection as a percentage of GDP, with central government tax revenue accounting for 25.7% of GDP and 28.8% respectively, whereas Costa Rica with 16.8% of GDP and Argentina with 13.5% of GDP were closer to the mean. It is further important to note that Chile had already undergone radical economic reforms and a tax reform by this point. Indeed, Chile already relied on indirect taxes for close to half of total tax revenue, with 47%. Direct taxes, that is, income and capital gains taxes on individuals and corporations and property taxes, amounted to between 16% of total tax revenue in Costa Rica and 38% in Jamaica.<sup>2</sup> The figure for Jamaica is inflated because some earmarked

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<sup>2</sup> In Table 1, property taxes are included in the category of direct taxes, along with individual and corporate income taxes. They are low everywhere, between 4% of total tax revenue of the central government in

taxes for social policy are added to the income tax, which in other countries would be classified as social security taxes.

Chile and Argentina had already lowered taxes on foreign trade by the early 1980s, whereas they continued to play a very important role in Costa Rica, more important than income taxes. For Jamaica, we are dealing with a classification problem. Bahl (1989), for instance, shows 25.5% of total government revenue in the early 1980s coming from export duties. In addition, he shows 20% coming from import duties, so the total contribution of foreign trade taxes to government revenue in his data is 45.5%, like in Costa Rica clearly higher than income taxes. In the IMF data, stamp duties on imported goods must be classified under taxes on goods and services and thus greatly inflate that figure. If we count them as taxes on foreign trade, then Jamaica is in an intermediate position with regard to the relative share of foreign trade and domestic indirect taxes, compared to Chile and Argentina on the one hand and Costa Rica on the other. The former two countries have a low share of total taxes coming from foreign trade and a high share from domestic taxes on good and services, and the latter has a comparatively higher share coming from foreign trade and a lower one from domestic taxes on goods and services.

*Tax reform in Argentina:* In Argentina, one really cannot speak of a particular episode of tax reform, but rather has to consider a protracted process of changes in the tax system, responding to fluctuations and shocks in the macroeconomic environment.<sup>3</sup> In the 1980s, changes in the tax system responded primarily to the need for higher tax revenue. The crushing debt burden, runaway inflation, and recession required efforts to increase tax revenue. In 1985 the government imposed a forced savings scheme and attempted to strengthen the income tax that had fallen to less than 1 percent of GDP in 1984. In 1987 deteriorating terms of trade forced a lowering of export taxes, but at the end of the decade it became possible to re-impose higher export taxes to capture gains of exporters from the devaluation. The successful stabilization program of the early 1990s then opened the way for a more coherent tax reform program focused on increasing overall tax receipts and relying heavily on the VAT.

From the mid-1990s on, several minor tax changes were implemented in response to recessions and growing budget deficits, but they had generally little impact (Gaggero and Gómez Sabaini 2002: 38). The VAT rate rose from 16% in 1980 to 18% in 1991 and

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