

Editorial

With monetary policy starting to return to normal in many countries, support provided by fiscal policy, including to a large extent through tax policy, has become more significant. Many countries have eased their fiscal stance to stimulate the economy by lowering taxes, increasing government spending, or both. This year's report highlights that the focus of the most recent tax reforms has been on cutting taxes on businesses and individuals with a view to boosting investment, consumption and labour market participation, continuing a trend that started a couple of years ago.

Among the countries that introduced the most significant tax reforms were a number of countries where tax reform was long overdue. The United States introduced the most sweeping tax reform, which completely overhauled its tax system, including both business and personal taxes. The year 2018 also saw the entry into force of significant tax reform packages in Argentina, France and Latvia. Broad tax reform packages are consistent with the view that tax systems should be considered as a whole and that, as opposed to looking at tax policies in isolation, the focus should be on the efficiency and equity effects of the overall tax system.

Other countries have introduced tax measures in a more piecemeal fashion, but many of these measures are a step in the right direction. A number of countries have sought to encourage greater labour market participation, most notably through the expansion of earned income tax credits. Efforts have also been made to broaden tax bases and to continue the fight against international corporate tax avoidance, in line with the commitments made by countries to implement the minimum standards and recommendations agreed upon as part of the OECD/G20 Base Erosion and Profit Shifting (BEPS) project. Administrative improvements and anti-fraud measures, in particular in the area of VAT, were also among the measures commonly adopted to enhance efficiency and collect greater tax revenues.

Going forward, however, greater action and coordination will be needed to avoid certain risks:

With global economic growth now closer to longer-term norms, the need for additional short-term fiscal stimulus is significantly lower. Fiscal policy choices should avoid the risk of excessive pro-cyclicality and be focused on medium-term challenges. Despite being on a declining trend, public debt and deficit levels remain high in many countries. As economic times improve, there is an opportunity to rebuild fiscal buffers, which will ultimately give more room for policy stimulus in the event of any future downturn. The focus of tax reforms should also shift to supporting the longer-term drivers of growth and equity. In this context, it is particularly important that tax reforms be financed in a manner that ensures their long-term sustainability.

Continued cooperation will also be important to prevent harmful tax competition. So far, while the declining trend in the average OECD corporate tax rate has gained renewed momentum since the crisis, corporate tax rate reductions are still less

pronounced than before the crisis. Besides, the countries that introduced corporate tax rate cuts in 2018 included some of the countries that had the highest tax rates in 2017. If anything, these countries appear to be engaged in a “race to the average” rather than in a “race to the bottom”, with their recent corporate tax rate cuts now placing them in the middle of the pack. There will be much interest in observing how countries respond to this trend in the future.

The report also highlights the crucial need to continue addressing equity issues and environmental challenges, which remain significant despite progress in recent years.

Tax policies should continue to focus on inclusiveness to ensure that improvements in incomes and standards of living are shared widely across the population. This is especially true in a context where positive developments in terms of employment are being overshadowed by wage stagnation, especially for low-wage workers. While there have been continued cuts in personal income taxes for low and middle-income earners, these have typically been small. In general, there is still ample scope to strengthen inclusiveness through tax systems, in particular by continuing to lower-labour tax wedges on low and middle-income workers, removing tax expenditures that disproportionately benefit the wealthy, and ensuring the effective taxation of personal capital income. Efforts to partly shift the financing of welfare systems from social security contributions towards general taxation could also be pursued further. Identifying the winners and losers of tax reforms and adequately compensating those who will lose out from new tax measures, particularly where they are at the bottom of the income and wealth distribution forms part of an inclusive tax agenda.

Progress on environmental taxation is urgently needed. While some progress has been achieved regarding the taxation of energy use, recent tax increases have not been meaningful enough to encourage significant carbon abatement outside of road transport. Aligning energy prices with the costs of climate change and air pollution is a central element of a cost-effective environmental policy. More generally, an increased emphasis should be placed on environmental taxation to encourage changes in behaviour that deliver improved environmental outcomes and help raise the levels of revenue collected from green taxes, which can be used to finance cuts in more distortive taxes.



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From:
Tax Policy Reforms 2018
OECD and Selected Partner Economies

Access the complete publication at:
<https://doi.org/10.1787/9789264304468-en>

Please cite this chapter as:

OECD (2018), "Editorial", in *Tax Policy Reforms 2018: OECD and Selected Partner Economies*, OECD Publishing, Paris.

DOI: https://doi.org/10.1787/tax_pol-2018-2-en

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