Executive summary

Scope of the report

The report has been prepared for G20 Finance Ministers and Central Bank Governors (FMCBG). The report updates the OECD report on *Tax and Fiscal Policy in Response to the Coronavirus Crisis*, which was presented to the G20 FMCBG in April 2020.

This report provides an overview of the tax measures introduced during the COVID-19 crisis across almost 70 jurisdictions since the outbreak of the pandemic. The report covers all OECD and G20 countries, and 21 additional jurisdictions that replied to a questionnaire that was circulated in January 2021 by the OECD to all members of the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting. It examines how tax policy responses have varied across countries and evolved over the last year.

The report also offers some guidance as to how tax policy responses could be adapted to address the short-term challenges countries face. In particular, it identifies some guiding principles on how countries could improve the targeting of emergency relief and implement recovery-oriented tax measures as they emerge from the grip of the pandemic and loosen mobility and other restrictions. It also gives a brief overview of the work that the OECD will be undertaking in the future to help countries reassess their tax and spending policies in the post-crisis environment.

Key economic and tax policy trends

The outbreak of COVID-19 has resulted in a global health crisis and sharp decline in economic activity that are without precedent in recent history. In just a few months, the COVID-19 pandemic turned from a health crisis into a global economic crisis whose full extent is still unfolding one year later. The COVID-19 pandemic caused a much larger contraction in global GDP than the global financial crisis in 2008, reaching nearly 10% in the first half of 2020 and an estimated 3.4% overall in 2020. A recovery has begun, but is far from complete.

The successful development and gradual deployment of effective vaccines has significantly improved prospects for a durable recovery, but uncertainty remains high. The latest OECD *Economic Outlook* projects global GDP growth of 5.6% in 2021 and 4% in 2022. Nevertheless, substantial uncertainty remains. A significant rebound in economic activity depends on the effective roll-out of vaccines across the globe and the continuation of supportive fiscal and monetary policies to boost demand. With the virus and its variants continuing to spread, targeted restrictions on mobility and activity may need to be extended or reintroduced as new outbreaks occur, which could limit the pace of recovery.

There are also increasing signs of divergence across countries, sectors and households. Extended containment measures and mobility restrictions will hold back growth in some countries and service sectors in the near term. Additional factors could lead to diverging outcomes across countries and regions, including differences in the pace of vaccinations and in the degree of policy support. Households have also been unevenly impacted by the crisis, with those on low-incomes, women and younger generations suffering higher economic costs. Without enhanced policy measures, both fiscal and structural, there are strong risks that the recovery could be unequal in both pace and scale across households, firms and countries.

Government responses to the crisis have been unprecedented since the onset of the pandemic. The scale of government support to households and businesses has varied, but it has reached unparalleled levels in many countries. Fiscal packages have often consisted of a wide variety of measures including loan guarantees, job retention schemes, direct transfers, expanded access to benefits and tax measures. Strong and timely fiscal support has played a vital role in supporting incomes, preserving jobs and keeping businesses afloat.

As part of these broad fiscal packages, tax measures have played a significant role in providing crisis relief to businesses and households. In the first half of 2020, in response to broad-based lockdowns in many countries, the focus of tax measures was almost exclusively on providing emergency relief. Last year's report on *Tax and Fiscal Policy in Response to the Coronavirus Crisis* highlighted that many tax measures were aimed at alleviating businesses' cash flow difficulties to help avoid escalating problems such as the laying-off of workers, the temporary inability to pay suppliers or creditors and, in the worst cases, business closure or bankruptcy. Countries also introduced tax measures to support households, although other tools including direct transfers and expanded access to social benefits often played an even more prominent role in providing direct relief to households.

Many of the tax measures introduced in the initial stages of the crisis have been prolonged, with some being modified to channel support to the households and businesses most affected by the crisis as it has evolved. Some countries have expanded eligibility for relief to beneficiaries initially not covered by the measures or increased the generosity of initial relief measures. As the pandemic has progressed, some countries have increased targeting to ensure that support is better directed towards those that are most severely affected, especially where governments have moved away from broad-based lockdowns towards more selective and targeted containment measures.

Tax packages have also evolved, with an increasing focus on recovery-oriented stimulus measures[3] to supplement the crisis relief provisions introduced in the early stages of the response to the pandemic. As lockdowns and other containment measures began to ease after the first wave of the pandemic, countries started introducing recovery-oriented tax measures, including in particular corporate tax incentives for investment as well as reduced VAT rates targeted at hard-hit sectors. In most countries, these stimulus measures have co-existed with prolonged relief measures.

Another significant trend observed over the last year is that an increasing number of countries have introduced or announced new tax increases. Unlike in the emergency phase of the crisis, a number of countries reported tax increases in the second half of 2020 and early 2021. While a few of these tax increases involved one-off or temporary measures, most are intended to be permanent. Among these longer term tax increases, some represent a continuation of pre-crisis trends, such as increases in fuel excise duties and carbon taxes, which were the most common tax increases reported by countries. On the other hand, some tax increases mark a departure from pre-crisis trends. In particular, a number of countries introduced tax increases on high-income earners, including increases in top personal income tax (PIT) rates reported in seven countries and the move from flat to progressive PIT systems in the Czech Republic and Russia. In addition, in contrast with the trend towards lower statutory corporate income tax (CIT) rates in recent decades, the United Kingdom has announced a CIT rate increase from 19% to 25% for profits above GBP 250 000 from April 2023.

Despite some common trends, there have been notable differences across regions and countries regarding the scope and types of tax packages, in part reflecting the varying prevalence of the virus and different containment approaches. Countries with severe lockdown policies have generally introduced more comprehensive tax support measures, while countries adopting less restrictive containment measures have generally introduced fewer COVID-19 related tax relief measures. The types of tax measures introduced by countries have also partly reflected the timing of virus outbreaks. For instance, in the Asia-Pacific region, many of the countries that were at the epicentre of the pandemic in late February and early March 2020 have managed to effectively contain the virus, and have subsequently introduced more stimulus-oriented tax measures than other countries that are still grappling with large numbers of infections.

The scope and scale of tax policy packages has also reflected countries' fiscal space and their ability to rely on central bank support. Some developing and emerging countries entered the crisis with more limited fiscal space, especially in Africa and Latin America. In addition, some developing and emerging countries have not been able to use monetary policy in response to the crisis in the same way as advanced economies have. Overall, many developing and emerging economies have had less room to provide fiscal support to households and businesses than other countries. The report generally finds that countries with higher tax-to-GDP ratios have introduced larger and more comprehensive tax packages.

Tax policy responses have reflected other country-specific factors. The types of measures introduced have depended on the architecture of countries' tax systems. For example, there has been less income support to households via the PIT in emerging and developing countries as most low-income earners are not subject to PIT in these economies. More generally, where tax bases are narrow, countries have had less room to provide support or stimulus via the tax system. The size of the informal sector and governments' administrative capacities have also influenced the scope and form of tax support. Finally, with only a few exceptions, so far announced tax increases have been concentrated in OECD countries, possibly reflecting the fact that they are among the countries that have introduced the most generous support packages.

Way forward

A key priority in the short run will be to improve the targeting of tax relief to ensure that support is channelled to those who need it most and to carefully withdraw it where it is no longer needed. The report highlights the importance of avoiding the premature withdrawal of relief but of increasingly targeting it to severely affected businesses and households. Maintaining support for highly impacted households is essential to mitigate the unequal impact of the crisis and reduce risks of increased poverty. Similarly, relief should remain available for businesses in severely constrained sectors. Targeting has become more feasible with increasing information on the economic and distributional impacts of the crisis. For those sectors where support is being withdrawn, this should be done carefully to avoid sudden spikes in tax burdens or "cliff-edge" effects, for instance by progressively phasing out support. Where support is extended, this should be done in ways that avoid storing up problems for the future, for instance by favouring "soft-landing" approaches, such as converting tax deferrals into interest-free tax instalments.

As economies reopen, fiscal stimulus, including through well-designed tax measures, could play a significant role if economic activity remains sluggish. Recovery-oriented stimulus policies should be considered if consumption and investment remain persistently low when containment measures are lifted and activities are allowed to resume. Larger and more prolonged stimulus measures might be needed where recovery is anaemic. However, where economies rebound strongly, the size and length of stimulus packages may need to be curtailed as stimulus measures could have pro-cyclical effects if they are maintained once economic recovery is on a solid footing. More generally, there will be a need for continued policy flexibility, as continued restrictions are making conventional stimulus policies somewhat less effective and the timing of policy implementation more difficult.

In order to be effective, stimulus policies need to be carefully timed. Introducing recovery-oriented stimulus measures while strict restrictions are still in place could be ineffective and could even undermine the primary health objective of containing the spread of the virus. In fact, there is evidence that some of the tax stimulus measures introduced after the first wave of the pandemic have had less of an impact than anticipated because they were introduced when restrictions were still in place or because they encouraged greater social interactions.

Stimulus measures should be temporary and targeted at the areas where equity needs and fiscal multipliers are likely to be highest. Temporary stimulus encourages businesses and households to bring their spending and investments forward and limits the impact on public budgets. Ensuring that stimulus measures are temporary may require having clear end-dates (with possibilities for temporary extensions) or tying their duration to the achievement of certain outcomes (e.g. economic recovery in specific sectors, level of employment). In addition, stimulus policies should be targeted at areas where they are most likely to generate additional consumption and investment. For instance, untargeted tax measures to support household consumption would partly subsidise spending that is likely to occur anyway, especially among higher income households who have accumulated additional savings during the pandemic and will be eager to consume once restrictions are lifted. On the other hand, income support targeted at less affluent households would have higher multiplier effects, in addition to being more progressive. Regarding corporate taxation, expenditure-based tax incentives tend to generate greater additional investment than profit-based ones.

Governments should also prioritise measures that support labour market recovery and business recapitalisation. Given the unprecedented job losses resulting from the crisis and the risks of long-term scarring effects on labour markets, tax measures could be used to encourage businesses to retain their workers and hire new employees. For instance, temporary and targeted reductions in employer social security contributions could be considered. To mitigate the impact of the crisis on companies' capital structure and solvency, tax measures could also be used to support business recapitalisation. Measures could include temporary schemes allowing companies to exempt part of their profits by recording them under a capital reserve aimed at rebuilding their equity. Such schemes could be capped and targeted at SMEs, and accompanied by strict rules to prevent any abuse. It is important to note, however, that while tax measures can be helpful instruments, non-tax measures will likely play a more critical role in supporting employment and business recapitalisation.

Tax stimulus measures should be aligned with longer-term environmental, health and social objectives. Stimulus policies could simultaneously support recovery and the attainment of longer-term objectives. For instance, targeted support for promising clean technologies could encourage recovery and help accelerate the transition to a carbon-neutral economy, especially if it is combined with greater carbon pricing efforts. Special tax incentives could also be granted to support businesses adapting their workplaces or facilities to strengthened sanitary protocols. Finally, stimulus should be aligned with social objectives and avoid regressive impacts.

These guiding principles can be useful across countries, but well-designed stimulus packages will naturally need to be tailored to countries' specific circumstances. Stimulus packages will need to be calibrated to the size of countries' output declines and the removal of their containment measures. Stimulus should also be aligned with countries' means and take into account their fiscal space. While limited stimulus may result in a slower recovery, disproportionate stimulus packages compared to countries' available fiscal space may undermine market confidence, which could weigh on the recovery. However, the near-term fiscal space of many countries has risen thanks to declining debt servicing costs and growth is often a major contributor to fiscal sustainability.

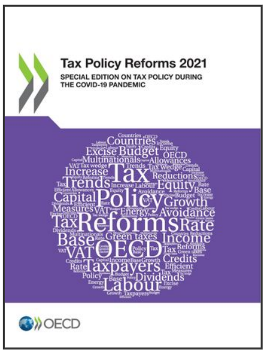
While the short-term priority is to effectively navigate the pandemic and build a robust and inclusive recovery, countries will need to start thinking about whether their public finance strategies are capable of meeting the medium and long-term challenges they face. Once the recovery is firmly in place, the post-crisis environment will provide an opportunity for countries to undertake a more fundamental reassessment of their tax and spending policies along with their overall fiscal framework. Such a reassessment will need to take into account both the challenges brought to the fore by the crisis as well as those related to ongoing structural trends, including climate change, rising inequalities, digitalisation and population ageing. The OECD will be undertaking significant work in the future to help countries reassess their public finance policies to support inclusive and sustainable economic growth in the longer term.

Notes

[1] In some cases, the responses provided by countries to the questionnaire has been complemented with additional information from other sources.

[2] The additional 21 Inclusive Framework members that responded to the OECD questionnaire are: Albania, Andorra, Barbados, Bulgaria, Croatia, Honduras, Jersey, Macau, Mauritius, Nigeria, Republic of North Macedonia, Panama, Paraguay, Peru, Seychelles, Singapore, Thailand, Trinidad and Tobago, Tunisia, Turks and Caicos, and Uruguay.

[3] Broadly speaking, stimulus can refer to all discretionary fiscal policy actions beyond automatic stabilisers, including for instance higher government spending on health, income support schemes and tax relief measures. In this paper, however, references to stimulus measures should be understood as recovery-oriented measures, whereas measures aimed at providing income and liquidity support are referred to as relief measures.



From:

Tax Policy Reforms 2021

Special Edition on Tax Policy during the COVID-19 Pandemic

Access the complete publication at:

https://doi.org/10.1787/427d2616-en

Please cite this chapter as:

OECD (2021), “Executive summary”, in *Tax Policy Reforms 2021: Special Edition on Tax Policy during the COVID-19 Pandemic*, OECD Publishing, Paris.

DOI: https://doi.org/10.1787/b0aa159d-en