REGIONAL TAX COMPETITION AND COORDINATION: THE CARIBBEAN’S EXPERIENCE

Presentation to

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Quote

"In developing countries tax policy is often the art of the possible rather than the pursuit of the optimal". *Vito Tanzi*

The Caribbean's Recent Experience with Tax Competition

- In recent years Caribbean countries have experienced increased levels of competition for increasingly scarce foreign investment.
- The competition is in several forms including 'a race to the bottom' approach to offering tax incentives.
- Much of the competition for foreign investment has been in the tourism industry, which paradoxically the Caribbean 'should' have a competitive advantage in.
- However, in response to tax competition from other countries, some Govts in the region felt obligated to increase the already generous tax incentives offered to attract the limited investment.

Recent country examples

- **Barbados** government in 2013 granted a 100% 25-year tax holiday to Sandals that includes a waiver on all import duties, taxes, impost and levies on capital goods such as building materials, as well as food, alcohol and beverages.
- The concessions to be reduced by 50% over another 15 years at the end of the initial 25 years.
- Similar concessions to be extended to the entire hotel industry
- **Antigua and Barbuda** also passed legislation granting increased tax incentives to the tourism industry and other businesses investing EC$100 million or more in the country for the period 2016 to 2018.
- These include total or partial exemption from property tax, stamp duty and withholding tax.
- **Jamaica** introduced a new fiscal incentives regime in 2014 covering corporate income tax relief, customs duty and stamp duty.

Recent country examples

- In 2014 **St Lucia** Govt introduced the Tourism Stimulus and Investment Act which essentially enhanced the already very generous package of incentives to hotels and other stakeholders in the tourism industry.
- This included 100% waivers on property tax, stamp duty, import duty on furniture and fixtures for a period to be determined by cabinet.
- Currently Govt is considering further enhancing the package of incentives to the tourism industry.

Regional Coordination & Harmonization Mechanisms

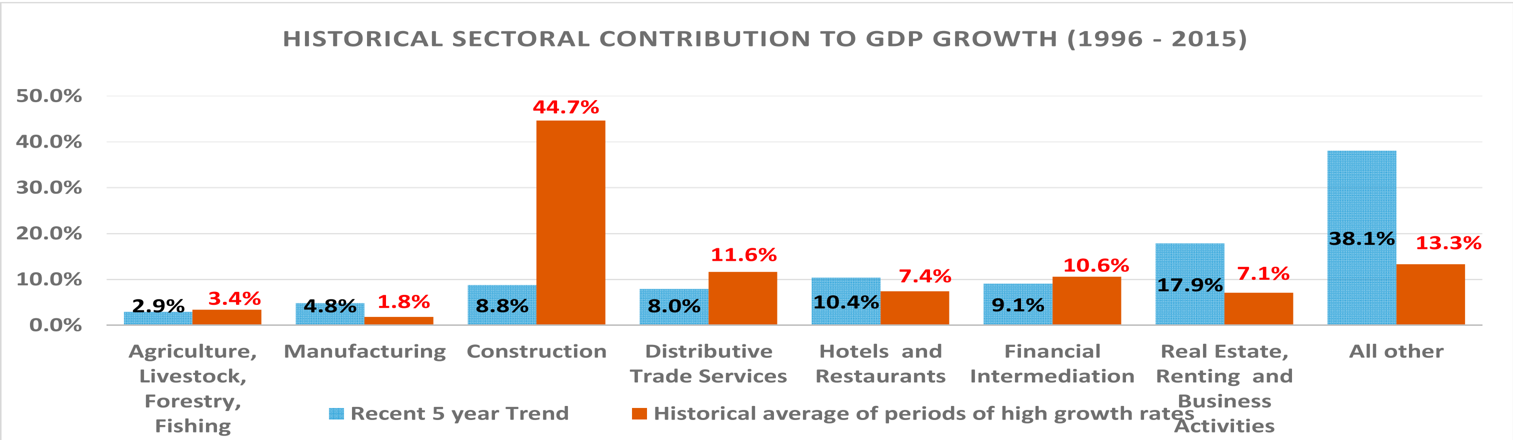
- Article 69 of the CARICOM treaty requires Member States to harmonize their investment incentives in keeping with the broader provision in the treaty for the coordination and harmonization of monetary and fiscal policies.
- The Monetary Council of the ECCB has mandated Member States to coordinate and harmonize their fiscal policy.
- However, progress on this area has been very slow.

Why do countries compete

- The pervasive use of tax incentives to promote investment in small developing countries can be seen in part, as compensation to their inherent deficiencies in skill sets, infrastructure and general lack of competitiveness.
- In addition many countries in the Caribbean have recently experienced a significant fall in inflows of FDI.
- In St Lucia the level of FDI fell by more than half over the last decade declining from an average of 15.8% of GDP during the period 2005 to 2009 to an average of 7.2% during the period 2010 to 2014.

Why do countries compete

- FDI financed activity has been a major driver of growth for many OECS countries.
- In St Lucia FDI financed construction activity has been the driver of the few episodes of high growth rates over the last 2 decades.



How much does tax incentives cost?

- There is not much comprehensive data on the cost of tax incentives in the Caribbean as most countries don’t produce tax expenditure reports.
- Chai and Goyal (2005) estimated tax revenue foregone in the ECCU at 10% to 16% but such information for all countries in the wider Caribbean is difficult to obtain.
- Jamaica’s tax expenditures in 2015 was estimated at 14.8% of GDP
- In St Lucia the MOF is just about to complete the first tax expenditure report.
- The report indicates tax expenditures in St Lucia is estimated at average of 11.2% of GDP over the period 2010 to 2013

St Lucia Tax Expenditure Summary Table

Tax Expenditure Category	2010	2011	2012	2013
Personal Income Tax	227.80	237.09	226.42	227.58
Corporate Income Tax	18.26	17.38	14.50	14.08
Customs and Excise	133.22	149.54	142.32	78.59
VAT				67.44
Total Tax Expenditures ($m XCD)	379.28	404.01	383.24	387.69
Market GDP ($m XCD)	3,353.11	3,457.68	3,506.80	3,558.74
Tax Expenditures % of GDP	11.3%	11.7%	10.9%	10.9%

Source: St Lucia Ministry of Finance

Takeaways

1. Governments in the region should improve the investment climate in the countries:
   i. Ease of doing business
   ii. Infrastructure
   iii. Labour productivity
2. Greater cooperation and coordination among countries in harmonizing their tax policies. Other countries' tax policies should be taken into consideration when Govts are crafting their own tax policies.
3. Greater transparency and accountability in providing tax incentives by regular publication of tax expenditure reports.