

International Tax Dialogue Conference on

TAXATION AND INEQUALITY

**Deputy Managing Director Min Zhu's Opening Remarks**

**10:00 December 7, 2011**

Honorable Minister, colleagues, ladies and gentlemen. It is my great pleasure to join the Minister in welcoming you to the fourth global conference of the International Tax Dialogue (ITD). I do so on behalf not only of the IMF, but of all our partner organizations in the ITD: the European Commission, Inter-American Development Bank, OECD, World Bank group and CIAT (pronounced *see-at*).<sup>1</sup> The aim of the ITD, as you know, is well-summarized by its name: to foster an inclusive international dialogue on tax matters of common interest. I am delighted to see, by the large, diverse and distinguished audience here today, every sign of success.

The topics of the ITD conferences, as you can imagine, have to be chosen quite some time in advance of the conference itself. And not the least of the successes of the ITD has been an uncanny ability to choose topics that have proved extraordinarily timely. Many of you will recall that the highly successful 2009 conference—very graciously hosted by our colleagues here from China—focused on the taxation of the financial sector. At the time the topic was chosen, it seemed perhaps rather dry and technical; by the time of the conference, of course, it had become a topic of public discussion all over the world.

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<sup>1</sup> For information: CIAT (*Centro interamericano de Administraciones Tributarias*) is the organization of tax administrations of the Americas.

And now our theme is ‘Taxation and Inequality’. This is another prescient choice. The issues are not in themselves new, of course. I am not sure what the earliest example is of unfair tax systems generating social unrest—the Peasants' revolt in England of 1381 is probably a rather recent example. At the IMF we have certainly been focused on the issues of inequality and poverty for many years, across the range of our activities. In our surveillance and program work, we have long highlighted, to give just one example,, that the benefits of the huge fuel subsidies in many countries go overwhelmingly to the richest, and that there are better ways to help the poor. In our policy development work, we published landmark books on taxation and inequality a decade ago, and have continued to be active in this area: one of our recent papers, for instance, finds that greater equality tends to be associated with more sustained growth. And in our technical assistance work we provide very practical advice to countries on the distributional effects of their tax and spending policies, and on how their equity objectives can best be met.

Today, of course, the topic has a renewed immediacy. We see concerns as to the link between taxation—indeed the fiscal system more generally—and social justice almost everywhere we look. We see them in the Occupy movement; in the Arab spring; in the debates on the expiration or not of the Bush tax cuts in the U.S., on how to distribute the pain of fiscal consolidation in Europe; on how to distribute the benefits of growth in fast growing emerging market countries; and in the needs of many lower income countries to overcome resistance from elites so as to establish tax systems with the legitimacy and revenue productivity needed for their sustainable development.

Personal value judgments will always play a large role in this area, of course. But the heated nature of and high public interest in these issues makes it even more critical to address them in an informed, professional way—and this is what we look forward to from this conference.

There are many very tough issues to grapple with. Is there, for instance, any link between the dramatic fall in top marginal tax rates on labor income—by an average of 25 percent in OECD countries over the last thirty years—and the equally dramatic increase in the Gini measure of inequality in many of these countries over this period—by about one-third?

I will leave these and other hard questions to your discussions. But let me share three thoughts on the challenges you will be addressing, ones which very much feature in our work at the Fund.

First, fiscal consolidation will be painful in many countries, but it does not have to be unfair. So high has the concentration of income in the U.S. become, for instance, that one estimate is that raising the average tax rate on the top 0.1 percent of earners in the US from 22 to 43 percent would raise about 3 percent of GDP, which is about 10 percent of total tax revenue. Of course, this potential tax base might shrink substantially if one did actually try to tax it. But the numbers are striking. As another example, eliminating the extensive reduced rates in the VAT of the U.K. could raise about £23 billion. It would also hurt the poor. But work at the IMF shows that social benefits could be reconfigured so as to protect the poorest and still

leave a sizeable revenue gain, of around £11 billion: which is something like an 11 percent increase in VAT revenue.

That leads to the second point. This is that we need to look at tax and spending sides together. Indeed about two-thirds of the redistribution that takes place in advanced economies is through government spending, not taxation. Many social benefits, such as increasingly common earned income tax credits, are indeed essentially just negative taxes. Recognizing the power of such instruments raises, not least, practical challenges: At what point does a country's administrative capacity reach a point at which such instruments become practicable? Nor is the need for an integrated view of tax and spending limited to direct measures of income support: in lower income countries, the benefit to the poorest from the public provision of basic education and health services needs to be weighed against any regressivity from the instrument, such as the VAT, used to finance them.

Third, there are many dimensions of inequality that fiscal policy can affect. There is inequality across countries, and between regions within them. There is inequality between the sexes, and by ethnicity. And there is in some cases massive intergenerational inequality that is actually created by the tax and spending systems. In Japan, for instance, those aged 60 or older are lifetime net beneficiaries from the tax-benefit system in the order of 40 million yen; future generations, however, are set to be losers in about the same amount. These and other inequities are not just troubling in themselves, but can challenge fiscal sustainability and social inclusion. They are a reminder of how key issues of taxation and inequality are to all our future prospects.

So you have no shortage of challenges to address, and I look forward to hearing the outcome.

And I look forward to hearing of the next ITD topic for 2013, as it will give us all a good clue as to where the world is heading.

Let me then close by welcoming you again on behalf of the ITD, and extending all our thanks to the Government of India for their initiative and hospitality in hosting this event.