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SUPPORT PROGRAMME FOR TAX
TRANSITION IN WEST AFRICA

TECHNICAL ASSISTANCE TO THE SUPPORT
PROGRAMME FOR TAX TRANSITION
IN WEST AFRICA

Methodological guide for evaluating tax expenses in West Africa

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Methodological guide for evaluating tax expenses in West Africa

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ABBREVIATIONS

BIC (French)	Industrial and Commercial Profits
BNC (French)	Non-commercial Profits
BTS	Benchmark Tax System
CET	Common External Tariff
CIT	Corporate Income Tax
ECOWAS	Economic Community of West African States
Excl taxes	Excluding Taxes
FTA	Free Trade Area
GDP	Gross Domestic Product
GTC	General tax code
IC	Investment code
IMF	International Monetary Fund
Inc. tax.	Including Taxes
NGO	Non-Governmental Organizations
PIT	Personal Income Tax
TE	Tax expenditures

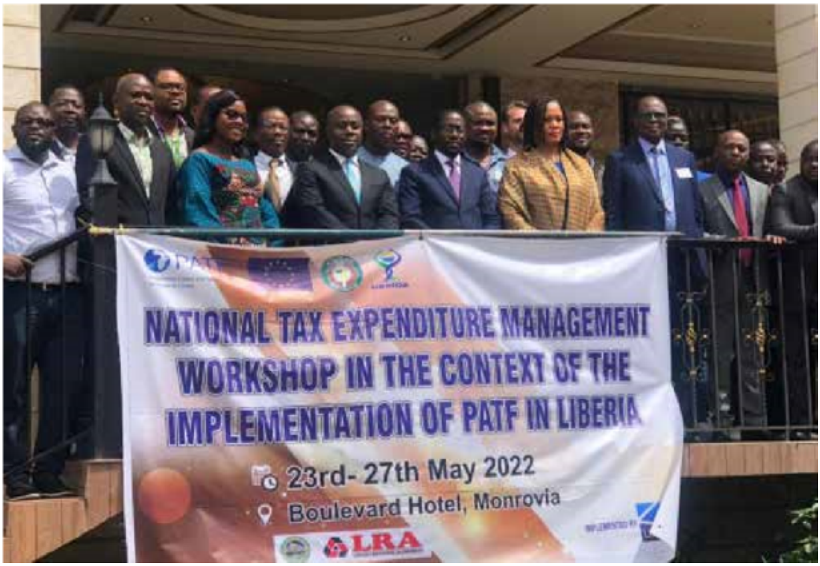
PREFACE

The mission team included Messrs. Jean-François Brun, Gérard Chambas, and Jules Tapsoba. The team conducted interviews with the authorities of ECOWAS (Mr. Salifou Tiemtoré) and UEMOA (Mr. Habasso Traoré), members of the PATF technical assistance, focal points of sixteen West African countries, and resource persons identified by the focal points.

The mission expresses its special thanks to all the participants in the regional workshop held in Cotonou from 15 to 19 November 2021. Particular thanks to the group tasked with commenting on the methodological guide for regional evaluation of tax expenditure, through its President Mr. Elimane Pouye, its Secretary Mr. Yao Kan Séraphin, the representatives of the regional institutions, and the representatives of the sixteen West African countries.

The mission's work was greatly facilitated by Mr. Daniel Saha, Mrs. Awa Kone, and Mrs. Linda lAkuesewo. The mission acknowledges the warm welcome and the high level of collaboration it received from the European Union, the ECOWAS and UEMOA authorities, the authorities of the sixteen West African countries, the Linpico Sa/Adam Smith Group, and all those with whom the team worked.

PATF, a joint Programme of the UEMOA and ECOWAS Commissions



1.

INTRODUCTION

Within the ECOWAS region, subject to compliance with harmonized evaluation rules, common to the various member countries, it would be necessary to carry out a regional evaluation of tax expenditure, which would be a summary of tax expenditure evaluations conducted within each country based on a common framework. Such a regional evaluation of tax expenditure would foster a coordinated control of tax exemptions and therefore a harmonization of tax exemption policies. Thus, a regional evaluation of tax expenditure would contribute to the success of fiscal transitions, currently undertaken in West African countries, but still threatened by extensive granting of tax exemptions.

These regional evaluations (a regional summary of the evaluations undertaken in each country based on common regional standards) aim to complement the national evaluations of tax expenditure currently carried out in several West African countries according to each country's specific objectives and which should soon be available for each of the ECOWAS countries[1]. Conducting regional evaluations of tax expenditure at a national level would certainly encourage each country to complete the national evaluation of tax expenditure by including, alongside evaluations of revenue losses, the effects of tax exemptions on economic incentives, equity, and service to taxpayers: the availability of national evaluations including all the effects related to an inclusive fiscal transition will provide much of the information needed to produce regional reports on tax expenditure.

The purpose of this methodological guide is to identify the methods by which each West African country could carry out a regional evaluation of tax expenditure that complements the national evaluation of tax expenditure; it then outlines the methods by which a harmonized summary of the regional evaluations of tax expenditure specific to each country could be produced within the regional integration area.

To define a method for the regional evaluation of tax expenditure, the following questions are addressed successively:

1) Que papel pode desempenhar uma avaliação regional das despesas fiscais efectuada em cada país para harmonizar as políticas de isenção fiscal?

2) Qual é a relação entre o controlo das isenções fiscais e uma transição fiscal inclusiva?

3) Que papel devem desempenhar as avaliações nacionais das despesas fiscais?

4) Que papel pode desempenhar a avaliação regional das despesas fiscais?

1 The final report on the development of a methodological guide for the regional evaluation of tax expenditure in West Africa presents an overview of tax expenditure evaluation in West Africa (ECOWAS and Mauritania). Thereafter, to avoid redundancy, the terms ECOWAS and West Africa are used to refer collectively to ECOWAS and Mauritania.

2.

REGIONAL EVALUATION OF TAX EXPENDITURES, A TOOL FOR THE HARMONIZATION OF TAX EXEMPTION POLICIES

The regional evaluations will be based on and will closely complement national evaluations; therefore, before defining the content of regional evaluations, it is necessary to analyze the main characteristics of national evaluations.

2.1 NATIONAL EVALUATIONS OF TAX EXPENDITURES, A PARTIALLY APPLIED INSTRUMENT IN WEST AFRICA

2.1.1 Priority to tax mobilization objectives

Challenges of mobilizing tax revenues. Since the 1980s, with the implementation of stabilization and structural adjustment policies, West African countries are particularly faced with the challenge of mobilizing the necessary levels of fiscal resources to finance public goods. Public goods are essential to economic and social development.

The challenge of mobilizing tax revenues has become all the more difficult to meet in recent decades, particularly as a result of the rise in per capita income, the need for public goods in West African countries has increased, while access to alternative sources of financing to own tax revenues (aid flows, external and internal loans) has become more difficult. Furthermore, while the relative contribution of tariff revenues to tax revenues was initially quite high, the implementation of trade liberalization policies since the 1980s has led to significant drops in tariff revenues.

Seeking alternative tax revenues to tariff revenues. Because of the initially high contribution of tariff revenues to tax revenues, West African countries faced the risk of declines in overall tax revenues. To prevent the declines in tax revenues from undermining the financing of public goods, affected countries have sought to mobilize additional internal tax revenues. In a restrictive environment focusing on tax revenues, a successful «tax transition» involved offsetting the decline in tariff revenues with alternative tax revenues that would stabilize or even increase overall tax revenues.

Tax exemptions and derogation regimes, major obstacles to raising tax revenue.Since the 1960s, all West African countries have granted extensive tax exemptions and introduced tax systems that depart from the common law tax rule: the objectives were to stimulate economic activity and, frequently, to promote greater equity. Tax exemptions have resulted in heavy losses of tax revenue but paradoxically, until around 2010, neither public finance managers nor national authorities in West African countries were able to produce conclusive evaluations of revenue losses caused by the exemptions, let alone their economic and social impact.

2.1.2 Until 2010, lack of evaluation of tax expenditure; limited fiscal transition

Lack of national evaluation of tax expenditure resulting from tax exemptions: a paradoxical situation. Until around 2010, when West African countries undertook significant efforts to track all public finance flows (revenue, expenditure, and financing of the budget balance) as exhaustively and analytically as possible, and to improve the mobilization of their tax revenues, there were no systematic evaluations of the impacts of tax exemptions (loss of revenue, economic incentive effect, impact on equity)[2]; the only available evaluations are a few one-off evaluations of revenue losses caused by a limited number of exemptions, which vary in scope and are carried out through heterogeneous methods. The lack of systematic evaluations of tax expenditure (see Box 1) is a notable shortcoming in that, for a long time, West African countries have lacked the tool they need to control the various costs incurred by granting tax exemptions, including particularly high losses of tax revenue.

2 The first evaluation of tax expenditure on the African continent was carried out in Morocco in 2005. Evaluations of tax expenditure then rapidly spread to various countries: South Africa, Senegal, Benin, countries of the East African Community, …

*Box 1 : **Definition of tax expenditure***

A tax expenditure represents a revenue foregone resulting from a reduction in tax obligations relative to a benchmark tax system. It is an alternative to direct budgetary expenditure, in particular a subsidy. A tax expenditure is the result of a tax derogation measure designed to reduce the tax burden borne by a taxpayer, a group of taxpayers, or a sector of activity. This measure results in a loss of revenue.

Derogation measures include allowances, tax credits, deductions, total or partial exemptions, tax reductions, and reduced rates. Derogation measures may be transitional or permanent. They may be included in general tax legislation or in various legal texts, such as those relating to free trade and economic areas, investment codes, sector-specific codes (mining, oil, etc.), specific decrees, and also agreements signed between the State and companies, legal entities or individuals, between the State and NGOs, etc. They appear, in various forms, in public contracts/projects, many of which are externally financed.

In most cases, derogations are granted to achieve an economic incentive or equity objective. But the expected benefit of a derogation measure is not generally evaluated accurately ex-ante. The budgetary cost of a derogation measure (revenue forgone) should therefore be compared with its actual economic benefit (amount of investment, number of jobs created, etc.) or its actual social benefit (proportion of revenue forgone taken up by the target population, etc.). Without an ex-post analysis, it is difficult to justify the merits of a derogation measure.

Limited fiscal transition based on tax revenue mobilization. From the 1980s, with the implementation of structural adjustment and stabilization policies, the mobilization of additional tax revenues, at least the stabilization of the existing revenue levels, has been a priority objective of public finance policies in West African countries.

The focus on the tax revenue objective is then so strong that it overshadows the other objectives of an «inclusive fiscal transition[3]»), i.e., the objectives of economic incentive, equity, or efficient services to the taxpayer.

3 See below for a detailed definition of the concept of inclusive fiscal transition

The primacy given to the mobilization of additional revenue has led countries to adopt a restrictive concept of fiscal transition, equating it solely with the mobilization of an optimal level of tax revenue. This primacy of the revenue objective has led countries to carry out partial national evaluations of tax expenditure that take into account only the tax revenue losses caused by tax exemptions (see §1.1.3 below).

Limits of a restrictive fiscal transition focused exclusively on the revenue objective. The restrictive concept of fiscal transition centered around the objective of stabilizing tax revenues still occupies a key place in many West African countries. It has major limitations in terms of the relevance of tax policies.

1) Stabilizing tax revenue around a ratio of revenue to GDP (as in the case of ECOWAS countries with the floor criterion for tax revenue at 20% of GDP) does not guarantee that each country will mobilize an optimal level of tax revenue.

2) Regarding the incentive objective, it is unlikely that the tax system implemented, while it may achieve a level of revenue objective, will create an economic incentive corresponding to the objectives targeted by the countries within the regional integration area.

3) Equity objective: the tax policy choices made to achieve a revenue objective are unlikely to be consistent with national equity and poverty reduction objectives.

4) Services to taxpayers: despite the strong relationship between the quality of services to taxpayers, tax compliance, and the mobilization of tax revenues (see above), the modernization of the services provided to taxpayers has, until in recent years, appeared to be a relatively low-priority objective[4] in relation to the revenue objective.

4 For example, many countries have preferred to collect VAT revenues in the short term without refunding the VAT credits that guarantee the economic neutrality of this tax (see Brun, Chambas, 2021).

2.1.3 From 2010, partial national evaluations of tax expenditure

From 2010, national evaluations of tax expenditure are carried out in a growing number of West African countries. A growing number of West African countries periodically, and often on an annual basis, produce evaluations of the tax revenue losses caused by exemptions. These evaluations, which cover an increasing number of tax exemption measures, are generally in line with international good practices. The available tax expenditure evaluations are increasingly becoming a document with a status similar to that of budget documents relating to public spending. A crucial step has therefore been taken since 2010.

Limitations of national evaluations of tax expenditure. By focusing solely on revenue losses[5], national evaluations of tax expenditure do not provide complete information on the consequences of tax exemptions: current evaluations of tax expenditure do not provide information on the consequences of exemptions in terms of economic incentives, equity, or services to taxpayers, even though these consequences relate to crucial objectives used by the authorities in the various countries to justify granting exemptions.

Despite their partial nature, national evaluations of tax expenditure in each West African country have alerted the national authorities of the importance of controlling revenue losses. Through the losses of revenue caused by the various categories of exemptions, evaluations carried out by the West African countries provide some of the information needed to define a policy for controlling exemptions. Though incomplete, the available evaluations mark an important step in showing the need for a comprehensive evaluation of tax expenditure.

5 Based on the responses to the mission's questionnaire, the only clearly identified component of the cost of tax exemptions is revenue losses. This is due to the high priority given to the objective of mobilizing revenue. Tax expenditure is evaluated using the method of «revenue loss», which estimates the revenue not collected (or foregone) as a result of tax exemptions (revenue losses). This evaluation method does not take into account the secondary effects (assumption of unchanged behavior). This choice is the one recommended by Decision No. 08/2015/CM/UEMOA dated 02 July 2015.

2.2 REGIONAL EVALUATION OF TAX EXPENDITURE, A TOOL FOR HARMONISING TAX EXEMPTION POLICIES

2.2.1 Objective of regional harmonization of tax systems

Regional dimension overlooked by national evaluations of tax expenditure. The main objective of both ECOWAS and UEMOA is to promote regional economic integration; in terms of taxation, this involves avoiding tax distortions between countries. To this end, regional authorities have put in place a regional legislative framework aimed at harmonizing and coordinating Member States' tax legislation. One important objective of harmonizing tax policies is to prevent tax competition arising from granting tax exemptions, which could lead to tax avoidance, distortions in economic incentives or lack of equity. As a result, the lack of a regional evaluation of tax expenditure providing the information needed to define tax exemption policies appears to be a major shortcoming.

Stimulate regional integration; promote regional attractiveness. Through the convergence of tax mobilization levels, the economic and social effects of taxation, and the control of tax enforcement costs, a harmonized fiscal transition within ECOWAS member countries would promote regional integration. Such a convergent fiscal transition in each member country within the ECOWAS zone would help to establish an attractive regional environment conducive to economic and social development.

2.2.2 Regional evaluations of tax expenditure as a tool for harmonizing tax exemption policies

Furthering regional harmonization of tax policies. The aim of regional evaluations of tax expenditure is to further the harmonization of national tax policies, which is already well underway for the main tax categories, by extending harmonization to policies for granting tax exemptions. Such harmonization of tax exemptions requires a homogenous evaluation of tax expenditure for each of the various ECOWAS Member States. Furthermore, in order to avoid similar shortcomings as those observed at the national level, regional evaluations must be inclusive, i.e., include an analysis of the economic and social effects of exemptions.

To facilitate the definition of a common regional framework for all tax exemption policies applicable to all member countries, the most operational solution is certainly to draw up a single document at the regional level, summarizing the regional evaluations of tax expenditure carried out by the organizations in charge of evaluation in each country and using the same methodology in all West African countries.

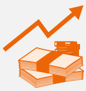
3.

INCLUSIVE FISCAL TRANSITION AND TAX EXEMPTIONS

Promoting an inclusive fiscal transition[6], i.e., adapting taxation to all the characteristics of a profoundly changing environment, is a key objective for West African countries. *The various limitations associated with a restrictive definition of fiscal transition outlined above suggest the need to identify a concept of inclusive fiscal transition encompassing all the objectives to be achieved so as to adapt taxation to changes in the budgetary, economic, and social context of West African countries while ensuring regional harmonization of these countries' tax exemption policies.*

3.1 INCLUSIVE FISCAL TRANSITION; OBJECTIVES

For each West African country, inclusive fiscal transition policies simultaneously target closely complementary objectives[7].



1) An optimal level of tax revenue[8] should help to address both the growing need for public goods and the drastic changes that have affected external capital flows, particularly aid flows.

TEC

2) By providing an economic incentive, tax transition policy also aims to adapt taxation to the changing business environment in West African countries, marked by the extension of regional free trade areas, international trade liberalization, and new trade agreements. Fiscal transition policy must also respond to the changes underway in the production systems of West African countries, in particular, the modernization of various economic activities, including agriculture; in a large number of countries, it must also adapt to the needs arising from the development of major mining activities.

6 As opposed to inclusive fiscal transition, restricted fiscal transition only takes into account the tax revenue objective.

7 The four main objectives of the inclusive tax transition are closely complementary. Thus, the population of a given country will be reluctant to accept a high tax burden if the tax levied runs counter to equity objectives. Similarly, producers will be reluctant to accept an increased tax burden if the tax distortions caused by the increased tax burden create handicaps for their production activities. Given the close complementarity of its main objectives, the success of tax transition, therefore, requires that they be achieved simultaneously.

8 Optimization must be sought between the various opportunities for financing public goods provided by each country's fiscal space.

3) Promoting equity and poverty reduction is a third major objective of inclusive tax transition policies.

4) Finally, fiscal transition policies must promote both improvement of service to taxpayers and control of tax collection costs.

Tools for an inclusive tax transition. Each component of tax revenues (direct taxation, which includes personal income tax and corporate income tax; domestic indirect taxation, which includes VAT and excise duties; and tariff-based taxation applied exclusively to imports) makes a specific contribution to each of the four aforementioned objectives of the fiscal transition.

3.1.1 Optimal level of public revenues

Raising additional tax revenues: a priority objective. In West African countries, given the overall shortage of resources to finance public goods and the difficulty of improving the efficiency of public expenditure[9], priority has been given (see above) to mobilizing public revenues and increasing them, given that they are often insufficient: the aim is to be able to finance public goods from public revenues (tax and non-tax revenues).

Stimulate a regional dynamic to mobilize tax revenues. Among UEMOA countries, the ratio of tax revenue to GDP is a key convergence criterion (currently 20% of GDP). The adoption of this criterion, UEMOA's action, and peer review pressure have created a remarkable regional dynamic (Brun, Diakité, Diarra, and Tanymoune, 2017), which has resulted in substantial progress in tax revenue mobilization over the past two decades. Stimulating a similar dynamic for all West African countries would promote more effective tax revenue mobilization.

9 To increase the supply of public goods, improving the efficiency of public expenditure is a complementary alternative to increasing the tax burden: it enables an additional supply of public goods without the need to mobilize additional tax revenue.

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3.1.2 Economically incentivizing taxation

Common external tariff: objectives of economic incentive and regional trade liberalization

Economic protection for a regional integration zone. The adoption of a Common External Tariff (CET), first by the UEMOA countries (1998) and then by all ECOWAS countries (2017), established a system of trade protection for national production of tradable goods against imports from countries outside the regional integration zone.

Liberalization of intra-regional trade. Alongside the policy of regional protection against production outside the ECOWAS zone, the liberalization of intra-regional trade has led to regional competition based on free trade between the various West African countries that are members of the regional integration zone.

Internal taxation: objectives of economic neutrality and tax revenue

Specialization of the tools as a prerequisite for effective incentives. As the objective of economic protection is achieved through tariff-based taxation, the preservation of a clear economic incentive signal from the tariff requires the economic neutrality of the other tax components (absence of effects on production costs). Achieving the objectives of tax revenue and neutrality at the same time means giving a central role to domestic indirect taxation, particularly VAT given its significant revenue potential and economic neutrality (Brun, Chambas, 2022).

VAT as a source of substantial tax revenues. If applied according to good practices, in particular with a smooth refund of credits, VAT is based on final consumption. Its revenue potential is therefore particularly high (Brun, Diakité, 2016). The size of its tax base and the efficiency of its administration, which is well suited to West African countries, means that substantial tax revenues can be mobilized.

Economic neutrality of VAT as an additional objective to that of mobilizing additional tax revenue. VAT is economically neutral: its main effect is to increase the prices of final consumption without affecting the production costs of taxable production activities. VAT, taken independently of the supply of public goods that it finances, causes a decrease in disposable income for all final consumers and, as a result, has a negative effect[10] on these agents. This negative effect is exacerbated if, as a result of irregularities, VAT deviates from economic neutrality and therefore puts a strain on the costs of taxable production: this situation arises in particular as a result of difficulties in reimbursing VAT credits. That is why tax transition reforms aim to ensure the economic neutrality of VAT by placing particular emphasis on the smooth refund of VAT credits (see below).

3.1.3 Tax levies promote equity and poverty reduction

Direct taxation of individuals, a relatively weak effect on equity in West African countries.

Direct taxation of individuals, as a preferred instrument of equity in OECD countries. Among OECD countries, direct taxation applies to all income received by households and, in some countries, to their wealth (tax on capital). Without ruling out the likelihood of shortcomings in the application of direct taxation, OECD countries' tax administrations are in a good position to ensure the effective application of direct tax legislation on all income and wealth, due in particular to their good knowledge of income and wealth. Thus, in OECD countries, direct taxation is the specific tax instrument particularly dedicated to promoting equity.

Direct taxation in West African countries: little effect on equity. In West African countries, personal income tax (PIT) cannot currently be a major instrument of equity, given that it is applied in a very imperfect manner. As a result, it is mainly based on wage income, while other major categories of income (income from sole proprietorships, property income, non-wage income, etc.) are largely untaxed. As for the tax on capital (property tax in particular), it is only marginally applied. Because it is applied only to certain types of income (wages, etc.), West African countries do not have a specific, effective tax instrument to promote equity through direct taxation.

10 Only the supply of public goods enabled by the tax levy is the source of a positive effect. Insofar as the positive effect of the supply of public goods is greater in absolute value than the negative effect of the tax levy, the national community, by choosing to finance a public good through taxation, benefits from a net increase in collective well-being.

Indirect tax exemptions and equity in West African countries

The limited capacity of direct taxation to promote social justice does not mean that it has no effect on equity: indirect taxation has a significant impact on equity.

- ***Without exemptions, VAT results in a tax levied in proportion to consumption that is likely to have a greater equity effect than income tax.*** Through proportional taxation of final consumption, VAT appears to be a more effective instrument of equity than income tax as applied in West African countries (see above): all consumers, including the well-off categories largely spared by PIT (see above), pay a levy in proportion to their consumption. In addition, self-consumption of food products, mainly by the poorer categories (small farmers), is not subject to VAT: this produces a progressive VAT effect likely to compensate, at least in part, for the regressive effect attributable to the lack of taxation of the saved portion of income.

- ***Equity effects of VAT exemptions.*** Granting domestic indirect tax exemptions, a common practice in West African countries, has significant effects on equity; contrary to most frequently stated objectives, a large proportion of these effects is regressive (see Boxes 2 and 4).

3.1.4 Controlling tax application costs for the State and taxpayers

Electronic procedures: an important step in modernizing tax administrationl. Improving the efficiency of the entities responsible for mobilizing tax revenues (traditional tax administrations or semi-autonomous revenue authorities[11]) relies on the continued efforts in administrative organization undertaken years ago and also on increasingly systematic digitization of tax data[12].

Electronic procedures, becoming widely used in West Africa The introduction of electronic procedures will drastically reduce tax administration costs for governments: combined with widespread digitization of tax data, it can help to reduce the human resources allocated to the management and processing of tax information, while providing new opportunities (creation of a more conducive environment to efficient management of tax administrations, automatic cross-checking of information from various sources, introduction of risk analyses, modernization of controls, redeployment of available human and material resources to control or management tasks, etc.).

Electronic procedures: improving services for taxpayers. As shown by the World Bank's «Doing Business» reports, businesses in West African countries take a particularly long time to meet their tax obligations. The widespread use of electronic procedures has the potential to radically improve the quality of services provided to taxpayers, particularly businesses liable for VAT, and to reduce costs for both taxpayers and administrations.

Improving the services for taxpayers is a driver of tax compliance. Electronic procedures are a key factor in improving the business climate and also in improving tax compliance: it becomes less costly for taxpayers to comply with their tax obligations. Electronic procedures also broaden the scope for controls and therefore for detecting possible fraud, which is another driver in improving tax compliance.

11 In the following, the term «tax administration» refers to the entity responsible for the internal mobilization of tax revenues, and the term «customs administration» refers to the entity responsible for the mobilization of tax revenues at borders. Revenue authorities perform both functions within the same entity but are covered by the term «tax administration».

12 In this respect, customs administrations were already well advanced in the process of digitizing information and introducing electronic procedures.

3.2 GRANTING TAX EXEMPTIONS, A MAJOR COMPONENT OF TAX POLICIES

3.2.1 Tax exemptions; a response to the negative effects of taxation.

Negative effects of taxation. While the production of public goods[13], has positive effects, tax levies taken independently of their use have negative effects: these stem from the reduction in households' disposable income following the application of taxes on consumption and income. They also come from the decline in companies' net income as a result of the application of taxes on profits and various taxes on companies' costs.

Exemptions versus comprehensive tax reform. Insofar as taxation (or some of its components) appears to be a barrier to the development of economic activities of vital importance to development and also a factor in lowering disposable income, government authorities could opt for comprehensive reform measures aimed at mitigating or reducing this negative effect of taxation. However, the difficulty of implementing a comprehensive tax reform has led West African countries to frequently opt for tax exemptions, either through changes to general legislation, or more specifically through tax benefits granted as part of investment codes, sector-specific codes, or special agreements with economic operators..

The lack of comprehensive evaluation of tax expenditure confirms the partial analyses justifying the granting of exemptions. Thus, an exemption from VAT on widely consumed products or services is often assumed, particularly by decision-makers, to promote equity, whereas only a quantified assessment of the effects of such an exemption on both consumers and producers would help identify any net positive effects. Given the large share of the most privileged groups in consumption and the often-adverse effect of VAT exemptions on domestic producers, the overall effect of VAT exemptions is often regressive (see Box 2 on the effects of VAT exemptions on rice and cereal crops in the case of a Sahelian country, member of the ECOWAS zone; see Brun, Chambas, 2010). Similarly, an exemption from corporate income tax is supposed to stimulate the creation of new businesses and additional investment, whereas an analysis of similar cases or an evaluation extending to factors other than taxation that affect the creation of economic activities (see above) would often highlight the secondary, or even marginal, influence of corporate income tax exemptions on the creation of activities.

13 Taxation plays a major role in financing public goods. An overall positive effect results from the greater social usefulness attached to the production of public goods compared with the negative effect caused by the tax levy.

Box 2: ***VAT exemptions on rice and cereal: social and economic effects, the case of Mali***

VAT exemptions on rice and cereal detrimental to equity

The most privileged consumers benefit the most from tax revenue losses, while the poorest benefit the least. In 2019, according to the Institute of Statistics, the top two deciles benefit from 50.9% of the revenue loss caused by exemptions on rice and 48.6% of the revenue loss caused by exemptions on cereal crops. The poorest group benefits from only 10.3% of the revenue loss on rice and 14.3% of the revenue loss on cereal crops.

Self-consumption reduces the share of revenue losses captured by the poorest households. Self-consumption expenditure on rice and cereal crops is higher for poor households than for better-off households. Exemptions have no effect on self-consumption because it is not subject to VAT. As a result, poor households are the least likely to benefit from the effects of the exemptions on rice and cereal crops because a larger proportion of their consumption of rice and cereal crops already falls outside the scope of VAT.

VAT exemptions on rice and cereal distort local production.

VAT exemptions on rice and cereal crops turn VAT into a tax on their inputs (water, electricity, fertilizers, etc.) for local taxable producers, who can no longer offset the VAT paid against their inputs. For non-taxable producers, VAT is, by its very nature, a tax on their inputs.

VAT exemptions lead to the de-protection of local rice and cereal production. Exempting rice and cereal crops from VAT results in lower prices for the end consumer. The producer subject to VAT receives a lower price, whereas as a result of the exemption, his costs are increased by the VAT levied on his inputs. The non-taxable producer, whose inputs were subject to VAT, also receives a lower price. As a result, the value added generated by the local producer (both taxable and non-taxable) is reduced following the grant of the exemption: VAT exemptions, therefore, result in negative effective protection for relevant local production. VAT exemptions reduce the income of rice and cereal producers. Exemptions, therefore, conflict with equity.

Source: Authors' calculations based on available data submitted to the authors in 2021 by the national authorities of a Sahelian country that is a member of ECOWAS.

Shortcomings in services to taxpayers*[14]*, drivers of the demand for exemptions. The limited progress made in modernizing tax administration, in particular the inadequate availability of electronic procedures for taxpayers, contributes to the tax uncertainty felt by operators and results in a heavy administrative burden. These two disadvantages encourage many operators to seek the protection provided by agreements on establishment or extensive exemptions.

Lack of fluidity in VAT credit refunds, a factor in the demand for VAT exemptions. A number of legal restrictions on the refund of VAT credits and malfunctions in the procedures for refunding VAT credits, which are still common in many countries, have the effect of increasing costs for businesses. This irregularity gives strong legitimacy to claims for VAT exemptions on intermediate consumption: through their claims for VAT exemptions, operators are seeking to avoid the additional costs associated with the non-refund of VAT credits. Operators also often seize the opportunity to obtain the broadest possible extension of the scope of exemptions[15].

3.2.2 Tax exemptions: weaker foundations

Many factors continue to favor the extensive granting of tax exemptions; however, in recent years, the foundations for these exemptions have become increasingly fragile.

lax exemptions and derogations: discretionary, heterogeneous, and unclear. Over the years, tax exemptions have piled up (investment codes, sector-specific codes, agreements, general tax exemptions, etc.). This has resulted in a complex system that is unclear both to economic operators and to tax authorities. The principle of discretionary grant of tax exemptions is widely applied..

Multiple sources of exemptions. ECOWAS member countries have introduced numerous exemptions, with the stated objectives of economic incentive and equity. These exemptions, which cover both direct and indirect taxes, are often initially intended to compensate for irregularities in the tax systems of West African countries and malfunctions in tax administration. Granting exemptions is then the second-best palliative solution.

14 According to Price Waterhouse Coopers' Paying Taxes report in 2018, businesses spent an average of 270 hours in Burkina Faso, 276 hours in Mali, and 270 hours in Niger to complete tax formalities (313 hours on average in sub-Saharan Africa).

15 For example, VAT exemptions granted under an Agreement on Establishment to activities relating to the construction or maintenance of infrastructure for mining may be extended to other activities.

Weaker foundations for exemptions. With the reforms undertaken for many years to improve tax legislation and tax administration, the basis for exemptions has been weakened. Thus, a common law VAT applied in line with the right principles does not affect production costs, whereas, in the past, the absence of VAT credit refunds could justify the granting of exemptions. Similarly, tax administration has been extensively adjusted to the specific context of West

African countries and has undergone numerous modernization measures. Recently, a strong commitment to the digitization of tax information and the introduction of electronic procedures have further weakened the relevance of tax exemptions.

Box 3:* *West Africa: A favorable environment for granting tax exemptions

Beneficial effect of tax exemptions, the subject of a broad consensus with fragile foundations. Consumers, businesses, trade unions, members of civil society, and political parties frequently call for tax breaks. Protests against the high cost of living (consumer goods, transport, energy) have had a major influence on demands for tax breaks, which are thought to play a key role in price formation; the focus is often on VAT. Such a consensus, based on largely non-analytical assumptions, leads to the extensive granting of exemptions. Wide-ranging investment codes, systematic exemptions included in tax legislation, and numerous agreements on establishment are driven by an overestimation of the negative effects of taxation and by an underestimation of the beneficial effects of exemptions.

Overestimation of the negative effects of taxation. Many factors other than taxation are essential for the development of economic activities. These include political stability, security, the rule of law, a low level of corruption, the availability of natural agricultural or mining resources, the skills and availability of labor, road access, maritime access, public services (electricity, transport, telecommunications), efficient management of public infrastructure, the quality of public governance, justice, access to finance, the relevance of labor market legislation, etc. However, government authorities in African countries generally regard taxation as a major obstacle to economic development: the extensive granting of exemptions, therefore, appears to be a prerequisite for the creation, development, or sustainability of any modern economic activity.

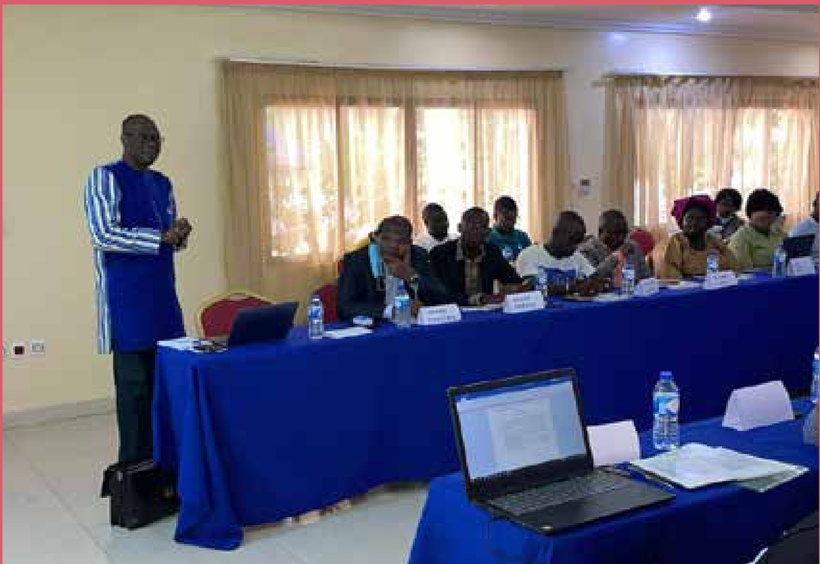
The lack of a quantified evaluation of the effects of exemptions results in an underestimation of their costs. Such underestimation is even greater insofar as the loss of revenue is deferred: decision-makers are more aware of the immediate benefits of granting the exemption (satisfying the demand of economic operators or consumers) than of its negative consequences (loss of revenue).

Underestimation of the cost resulting from tax revenue losses. The low priority given to the loss of tax revenue caused by tax exemptions is partly due to the lack of awareness of the contribution of public goods to development. This is further reinforced by the inadequacy of the supply of public goods in relation to the needs of the population.

The weakness of the consensus on the need for all citizens to contribute to the financing of public goods is partly due to a weak relationship of tax accountability. Because the tax collection method focuses, for efficiency reasons, on a small number of collectors (VAT taxpayers) or on tax withholding procedures (employer deductions for payroll taxes), taxpayers in West Africa are unable to establish a close accountability relationship between taxation and the provision of public goods.

The availability of alternative funding through contributions from development partners or through the collection of external public revenue (revenue from mining) makes it even less obvious that an own tax contribution is needed to finance public goods. As a result, it does not appear necessary to mobilize tax revenues from the population.

The successive shocks that have affected West African countries also spur the calls for tax exemptions. Tax exemption measures, whose effect on tax revenues is deferred over time, are often granted in response to shocks. They accumulate over time without any coherent assessment of their cumulative costs. The consistency of the tax system is adversely affected by the pile-up of exemptions.



Training session for the tax expenditure team in Guinea Bissau

4.

NATIONAL EVALUATIONS OF TAX EXPENDITURE; PARTIAL RATIONALIZATION OF TAX EXEMPTIONS

4.1 NATIONAL EVALUATIONS OF TAX EXPENDITURE: PRESENT STATE

4.1.1 National evaluations of tax expenditure: positive developments

National evaluations of tax expenditure, a growing number. In West Africa, a growing number of countries are publishing evaluations of tax expenditure, while others have just undertaken or plan to undertake such an evaluation in the near future[16].

Transparency and aiming for budgetary optimization. The issue of evaluating tax expenditure has now been clearly identified. Currently, for the various West African countries, the lack of information on tax expenditure, «quasi-budgetary expenditure», is no longer acceptable: such information is necessary for reducing the loss of revenue caused by tax exemptions, but also for rationalizing the granting of tax exemptions.

A Improving the quality of tax expenditure evaluations. The experience gained by the countries involved in evaluating tax expenditure at an early stage contributes to a better quality of evaluation, both for the countries directly involved and for other West African countries. As evaluations are carried out, the number of measures identified and evaluated increases. Many countries have created dedicated entities to evaluate tax expenditure and significant human and material resources are increasingly allocated exclusively to the task of evaluating tax expenditure.

16 Table 3 of the Final Report presents tax expenditure evaluations for the various West African countries.

4.1.2 National evaluations of tax expenditure: shortcomings

- ***Lack of evaluations of the economic and social effects of exemptions.*** None of the national evaluations of tax expenditure published by any ECOWAS country systematically includes the economic and social effects of exemptions, even though, given the available data, these effects could be assessed in each country to fully inform the decision-making of the national authorities.

- ***Narrowing the scope of evaluations.*** Narrowing the scope of evaluations of tax expenditure to revenue losses alone does not provide the national authorities with all the information necessary for rational decision-making on which exemptions to grant or, on the contrary, to discontinue. Limiting evaluation to revenue losses fails to take into account all the objectives of the exemptions (in particular to encourage economic activity, promote fairness and improve service to taxpayers).

- ***Changes in the scope of evaluations.*** For a given country, it is often difficult to evaluate the progress of tax expenditure due to changes in the scope of the evaluation: the scope of evaluations is often broadened for the purpose of improving the quality of the evaluation (see above).

- ***Lack of a procedure manual; heterogeneous methods of evaluation.*** A procedure manual codifying the practical methods used to evaluate each exemption measure, to be used by the operational departments in charge of evaluating tax expenditure is another prerequisite for a consistent evaluation of tax expenditure over time. Such a document would ensure the homogeneity of the evaluation carried out in each country and help save the resources allocated to evaluation because it provides information on the procedures applied in previous years.

- ***Lack of relevant indicators measuring the evolution of tax expenditure.*** It is difficult to obtain meaningful indicators of the evolution of tax expenditure for a single country given the changes in the scope of evaluation and heterogeneity in evaluation methods (see above). At the regional level (ECOWAS), it is even more difficult to compare tax expenditure amounts because of the different evaluation methods used by the various countries. It is therefore necessary to harmonize tax expenditure evaluations within the region.

Evaluation biases resulting from the choice of the benchmark tax system

Definition of the benchmark tax system: limitations on the scope of tax expenditure evaluation. West African countries, particularly UEMOA member countries[17], evaluate tax expenditure using the common law tax legislation as the benchmark tax system. This approach does not evaluate the tax expenditure generated by exemptions included in common law legislation.

However, in some countries, and generally for a few measures considered particularly important by the authorities, a different normative benchmark from the common law tax provisions is used: the objective is then to evaluate tax expenditure caused by some specific common law exemptions[18].

A Losses caused by common VAT exemptions included in common law: shortcomings resulting from the choice of the benchmark tax system. The decision by most ECOWAS countries to include VAT exemptions for foodstuffs and basic goods in the benchmark tax system is consistent with UEMOA Decision 08/2015/CM. However, this decision does not provide the national authorities with an assessment of the revenue losses caused by these exemptions under common law, which cover a large proportion of the VAT base and are therefore the source of both substantial revenue losses and significant economic and social effects.

Biases in the assessment of revenue losses caused by specific exemptions

Accounting biases in assessing VAT tax expenditure. A large proportion of VAT losses at customs does not correspond to a definitive loss of revenue, since most of the VAT collected at customs is offset in the accounts by VAT-registered businesses and therefore deducted from the net VAT to be collected at the domestic level. Only final losses should therefore be taken into account so as to avoid overestimating VAT losses.

Biases in the assessment of revenue losses by tax authorities. While the customs administrations of ECOWAS member countries identify a large proportion of tax revenue losses and are able, by means of computer codes, to provide information on the nature of the exemption applied, it is not the case for some tax administrations which are not yet able, in their day-to-day management and given the internal information available, to assess VAT revenue losses by origin.

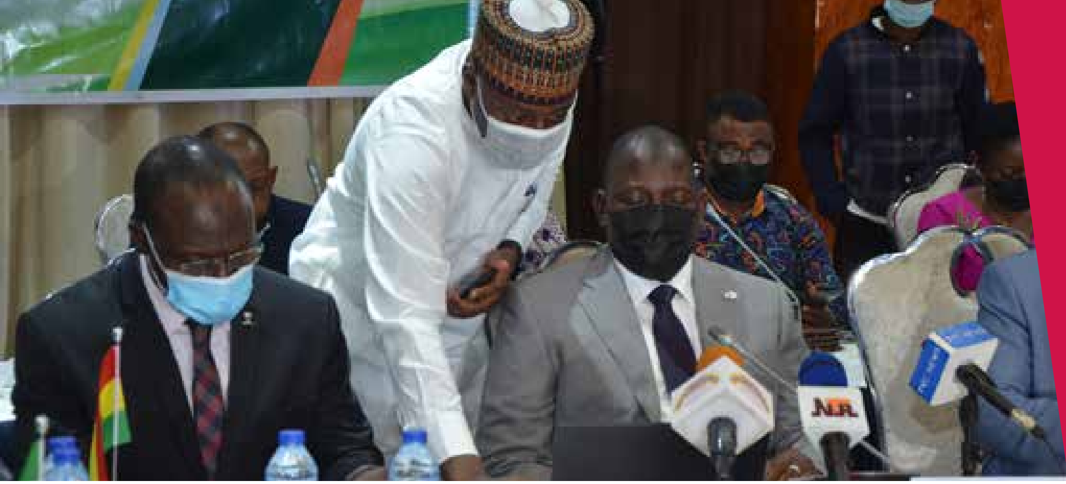
17 Decision 08/2015 on the evaluation of tax expenditure.
18 The authorities then have the necessary data to consider ending the relevant exemptions.

Reduced impact of tax expenditure evaluations

- ***Technical documents that remain difficult to access.*** Given their partial nature (evaluation of tax revenue losses only), their lack of clarity, and the lack of commitment from the Parliament, civil society, and public opinion, tax expenditure evaluations in West African countries remain mainly technical documents intended primarily for the departments of the ministry of finance.

As they relate to tax expenditure that requires no disbursement by the State, evaluations of tax expenditure do not provoke significant reactions, neither in Ministries other than the Ministry of Finance, nor in other centers of power, and as a result, evaluations of tax expenditure are still largely disregarded by decision-makers. Because of resistance from the beneficiaries of the exemptions, trade-offs leading to the removal of exemptions are rarely given priority over measures to increase tax revenue, seek alternative financing, or even reduce public expenditure.

- ***Little readability of tax expenditure evaluations for civil society.*** Civil society generally takes little or no ownership of the results because it is not properly informed about the results already achieved and the results that could be achieved through thorough evaluations of tax expenditure. This reduces the impact of tax expenditure evaluations on budgetary decisions or tax policy guidelines, particularly on the use of tax exemptions.



4.2 EXEMPTIONS, A MAJOR OBSTACLE TO FISCAL TRANSITION

In addition to tax revenue losses, tax exemptions can also lead to economic distortions or even be socially regressive; their complexity can also hamper the modernization of tax administration. Tax exemptions are therefore a major obstacle to an inclusive fiscal transition in the various countries of West Africa. However, national evaluations of tax expenditure, especially if they included an analysis of the economic and social effects, would contribute to the implementation of an inclusive fiscal transition within each country.

4.2.1 Tax revenue losses and fiscal transition

Significant tax revenue losses. National tax expenditure evaluations indicate that, given the amount of tax revenue losses, tax exemptions are a key factor weakening tax revenues and therefore a barrier to fiscal transition.

4.2.2 Economic distortions, regressive effects, and fiscal transition

Tax exemptions, the often-contradictory effects of fiscal transition.
The rationale for granting tax exemptions commonly put forward by the authorities in the various West African countries includes stimulating economic activity, improving equity, and reducing poverty. However, extensive tax exemption policies often run counter to these objectives and constitute barriers to fiscal transition in West African countries, as shown in Box 4.

Box 4: VAT exemptions, economic distortions, and undesirable social effects

VAT legislation in West African countries includes several exemptions with a social objective. A large proportion of VAT exemptions cover basic consumption. They cause heavy losses of revenue, serious economic distortions that hamper national economic activities, and, very often, undesirable social effects that conflict with the equity objectives initially sought (see Box 2).

Exemptions on food consumption mean lower prices for consumers but lower incomes for farmers and livestock breeders. These lower prices are due to the import of VAT-exempt products. (Brun, Chambas, 2010 "Regressive Nature of VAT Exemptions for Commodities in Africa" African Economic Outlook "The State of Public Resources Mobilization" OECD).

«Social» VAT exemptions on food products often cause regressive effects.

1) *Lower supply of public goods. Exemptions weaken VAT revenues and therefore the funding of public goods of which the poorest people are most likely to be deprived.*
2) *Lower prices for producers. VAT exemptions on tradable goods, such as food products, have an adverse effect on producers by lowering their output prices. In an open economy, the price level of tradable goods, including food products such as cereals, depends on the level of CIF import prices, including taxes. With VAT exemption, domestic prices of food products are lower than with tax liability. This effect of depression on domestic prices affects both the exempt products and their substitutes[19]; it leads to a decrease in the producer price and therefore in the income of farmers, who are often poor.*

The disadvantage of negative effective protection of local producers. As a result of the exemption, even if they choose to be subject to VAT (producers using modern techniques such as poultry farming, large-scale rice growing, and intensive urban market gardening), the local producers for the part of their production exempted from VAT are definitively subject to VAT on their intermediate consumption subject to VAT. The disadvantage of residual VAT places producers at a relative disadvantage (negative effective protection) against imports not subject to VAT. VAT exemptions, therefore, are counterproductive to both poverty reduction and the modernization of the agricultural sector.

19 Thus, an exemption on rice is likely to lower the producer price for all cereals, and even for other substitutes for rice.

VAT exemptions for health or education also lead to regressive effects because of the large share of favored categories in the consumption of tax-exempt public goods. Similarly, medicines are often exempt from VAT, but most of the benefit to the consumer is captured by the wealthiest consumers, resulting in a regressive distribution of the benefit of exemptions. The advantage given to poorer groups is excessively costly due to the lack of targeting.

4.2.3 Exemptions, obstacles to efficient tax administration

Costs of managing and controlling exemptions. For tax administrations, the management and control of exemptions require significant material and human resources. Consequently, they are no longer available to carry out their tax administration tasks. This leads to revenue losses and distortions in taxpayers' treatment, representing obstacles to fiscal transition, while the effectiveness of the controls needed to limit the application of exemptions to the scope initially planned is often lacking.

The widespread introduction of multiple and complex exemptions is a factor in the deterioration of services to taxpayers. Because of the complexities involved, tax exemptions are counterproductive to the objective of simplifying tax procedures; and also, to the objective of transparency.

The positive impact of the introduction of electronic procedures and the use of digital information processing tools will be all the greater if the complexity introduced by the derogations is first reduced.

Costs of tax exemption procedures for taxpayers. The uncertainties associated with the discretionary nature of the procedures for granting exemptions create dissuasive costs and uncertainties for economic operators.

In every West African country, tax exemptions hinder an inclusive fiscal transition. Thus, through the tax revenue losses they entail, tax exemptions are an obstacle to mobilizing a level of public revenue in line with the needs for public goods. Because of the distortions they cause, exemptions, particularly VAT exemptions, are incompatible with the economic neutrality of the tax levy and therefore blur the economic incentive signal provided by the customs tariff. Contrary to commonly claimed objectives, most exemptions cause socially regressive effects. Lastly, the extensive granting of exemptions introduces additional complexity to the application of tax, both for the tax authorities and for businesses.

National evaluation of tax expenditure: main operational guidelines. The main guidelines for national evaluations of tax expenditure are to evaluate tax expenditure in each country in the light of national objectives, to ensure that national evaluations of tax expenditure are transparent and properly disseminated, to review the conditions under which exemptions are granted, and to use subsidies as an alternative to tax exemptions.

4.2.4 Comprehensive national evaluation of tax expenditure and rationalization of exemptions consistent with national objectives

Promote a comprehensive national evaluation of tax expenditure. A comprehensive evaluation of tax expenditure (including the economic and social effects of tax exemptions) taking into account, for each country, all its specific national objectives would pave the way for the rationalization of exemptions in line with each country's objectives. It would also facilitate a regional evaluation based on the information already collected and the analyses thus available..

Determining the net benefit of planned or implemented exemptions for the national community requires a two-step process: firstly, the national evaluation of tax expenditure needs to be extended to exemptions included in common law (in particular VAT exemptions), and secondly, to evaluate the economic and social effects of tax expenditure as well as their implications for the services provided to taxpayers.

1) **Assessing the economic impact of tax exemptions.** There are two possible approaches to assessing the extent to which the initial objectives have been achieved and the net benefit (see below, assessment of the net benefit) of the exemption measures. To assess the extent to which the initial objectives, on which the exemptions were granted, have been achieved, the actual benefits of the exemptions are compared with the forecast benefits that determined the granting of the exemptions.

2) **Assessing the social impact of tax exemptions.** As above, the evaluation must assess the extent to which the initial objectives have been achieved: This involves comparing the anticipated social effects, particularly on the grounds of legislative or regulatory provisions or in the agreements on establishments (changes in income, employment, and living conditions of the groups targeted by the exemptions, etc.) with the actual effects observed after the implementation of the exemption measures.

A second evaluation entails assessing the net effects of the exemptions by comparing the costs of the exemption measures (tax revenue losses, economic distortions, anti-equity effects, etc.) with their actual social benefits (actual amount of investment, additional production, distributed income, exports, taxes paid and collected, possible contributions to the direct financing of public goods such as road infrastructure, dispensaries, training centers, etc.) Special attention must be paid to the effects of tax expenditure on key social groups, particularly the most underprivileged (see Table 13 in the final report).

Rationalize tax exemptions for each country. To identify the exemptions that should be continued or granted, their net benefit to the community must be assessed: the costs of the exemptions (loss of revenue, economic distortions, anti-equity effects, negative effects on the efficiency of tax administration) are weighed against their economic and social benefits (investment generated, increased production, jobs created, distributed income, tax paid or collected for the State and local authorities).

In order to assess the appropriateness of maintaining the exemptions, it is necessary to monitor the commitments entered into by the economic operators benefiting from these exemptions. Exemptions granted because of malfunctions in the common law tax system (e.g., failure to refund VAT credits) could be discontinued as long as normal operation of the common law tax system is re-established: regarding VAT exemptions, the first priority would be to create the conditions for smooth refunding of VAT credits.

Given the extent of resistance to any reduction in tax exemptions and benefits, tax expenditure evaluations do not usually lead directly to the end of exemptions, but often help prevent the introduction of new exemptions. Tax expenditure evaluations, therefore, lead to the stabilization of tax expenditure, which is a first step toward rationalizing exemptions.

4.2.5 Transparency and dissemination of national tax expenditure evaluations

Transparency and completeness of national tax expenditure evaluations

Comprehensive information and the search for an optimum. Searching for an optimal budget, and therefore retaining only those exemptions associated with this optimum, requires an assessment of all tax expenditures resulting from tax exemptions. However, it is consistent with good practice to exclude from the scope of tax expenditure evaluation those exemption measures that would be excessively costly to evaluate in terms of time or resources, and those for which the results would be particularly inaccurate.

Transparency and completeness of information versus arbitration. The objectives of transparency and completeness call for the greatest possible extension of the scope of national tax expenditure evaluations. This involves, in particular, evaluating the tax expenditure generated by VAT exemptions included in common law. The economic and social effects of tax expenditure should also be evaluated. As for any decision to abolish some exemptions, this would be a matter for the political authorities to decide, on the basis of the evaluation of tax expenditure, having all the information needed to inform their decision.

Dissemination and popularization of national evaluations of tax expenditure

Disseminating tax expenditure evaluations. Because of the similarities between budget expenditure and tax expenditure, tax expenditure evaluations tend to be appended to traditional budget documents. The best practice is to append tax expenditure evaluations to the Finance Acts: government authorities and members of Parliament then possess the information they need to make rational decisions.

Popularizing tax expenditure evaluations. In order to become a widely shared decision-making tool, it is important for national tax expenditure evaluations to be understood and therefore appropriated by a wider audience than just technicians, experts, members of Government, or Parliament.

In order to be understood by all decision-makers, professional organizations, trade unions, and also civil society, tax expenditure evaluations must be appropriately communicated to the media, professional organizations, NGOs, and public opinion as a whole, … In this respect, the official tax expenditure evaluation document should be easily readable: Morocco, the aforementioned pioneer country, has succeeded in publishing a document every year since 2006, appended to the successive Finance Acts, that complies with international best practices and is extremely readable, encouraging fruitful debate.

It is therefore necessary to publish comments and documents designed to inform the general public. Reports on the evaluation of tax expenditure should be freely downloadable by all citizens via the website of the Ministry of Finance.

4.2.6 Alternatives to tax exemptions

Substituting subsidies for exemptions to achieve incentive or equity objectives. For equity objectives (aid to consumers, support to vulnerable producers), it is generally more effective to use targeted subsidies rather than exemptions. Compared with exemptions, subsidies are often less costly in budgetary terms, more effective in terms of economic effects, and easier to target. The specific issue with subsidies is the strong constraint on the cash disbursement of additional budget expenditure.

Deepening ongoing tax reforms. As highlighted above, many tax exemptions are granted to compensate for either irregularities in tax legislation or malfunctions in tax administration. Such is the case with VAT exemptions granted to overcome the lack of fluidity in VAT credit refunds. It would be preferable to promote a seamless refunding of VAT credits to avoid weakening tax administration and inflicting various costs on VAT taxpayers.

Continuar a melhorar o clima empresarial. As highlighted above (see box 3), several factors other than taxation are major determinants of the development of economic activity. To assess the appropriateness of a tax exemption, it is essential to examine alternative measures that would be more effective in improving the business climate[20]. Again, the aim is often to seek first-tier solutions rather than granting exemptions. Alternatives to tax exemptions include workforce qualification and training, opening up the roads, opening up the sea, and providing efficient public services (electricity, transport, telecommunications).

20 For example, it may be more advisable to provide a sustainable cold chain at an acceptable cost for the preservation of fishery products than to grant tax exemptions on fishermen's equipment. Similarly, good maintenance of the road network and the eradication of highwaymen ("coupeurs de route") is a first-rate solution as opposed to a tax exemption on transport equipment.

The Abidjan workshop harmonized the data collection practice and presentation of annual reports evaluating tax expenditures in West Africa

5.

REGIONAL EVALUATIONS OF TAX EXPENDITURE

5.1 OBJECTIVES OF REGIONAL EVALUATIONS OF TAX EXPENDITURE

5.1.1 Comparing tax expenditure across West African countries

Challenges in cross-country comparisons. Owing to the heterogeneous methods used by West African countries to evaluate tax expenditure at the national level, it is impossible to make overall comparisons of tax expenditure levels between countries: the scope of tax expenditure evaluation, the benchmark tax systems used, and the operational procedures for evaluating tax expenditure differ across countries. Only partial comparisons, of limited significance, are possible.

The problem of comparing tax expenditure between West African countries, and hence the lack of any reliable regional indicators for relevant comparisons, is a major obstacle to establishing a regional dynamic for optimizing and harmonizing national tax exemption policies, such a dynamic being based on benchmarking and peer monitoring.

Conditions for homogenous comparisons of tax expenditure levels. *Achieving homogeneous comparisons requires all West African countries to contribute to a regional evaluation of tax expenditure based on national evaluation reports using a common regional analytical framework*. This entails adopting a common typology of the various taxes whose exemptions will be covered by the regional evaluation of tax expenditure, choosing a benchmark tax system for an identified category of tax, and selecting evaluation procedures that comply with common principles.

A regional procedure manual, similar to the procedure manuals to be developed for national evaluations, would help to identify the principles to be applied by each country for the operational evaluation of tax expenditure. However, it is important to provide sufficient room for adjustment : *Each country must be able to take into account its specific constraints, such as the availability of statistical data and the possibility of applying a particular method of evaluating tax expenditure.* As with national evaluations, simplicity and transparency in the evaluation methods used should prevail for regional evaluations.

5.1.2 Understanding changes in tax expenditure

Current issues in understanding changes in tax expenditure. To steer tax exemption policy at the regional level, it would be useful to know the evolution of the amount of tax expenditure both nationally (regional evaluation reports on tax expenditure specific to each country) and regionally (regional evaluation report, summary of regional reports relating to each country).

The currently available national evaluations of tax expenditure do not enable an analysis of the evolution of tax expenditure in a given country due to changes in the scope or evaluation methods. With the experience gained and sometimes increased resources dedicated to evaluating tax expenditure, countries carrying out successive evaluations tend to broaden the scope of the evaluations over the financial years. In addition, it is not unusual to notice changes in the methods of tax expenditure evaluation: to improve the quality of evaluations, the assumptions or evaluation methods for some tax expenditures are sometimes adjusted, and new data sources are used. Under these conditions, it is difficult to get consistent evaluations of tax expenditure over time and therefore to be able to assess changes in tax expenditure using reliable indicators.

Evaluation of tax expenditure using a constant scope and homogeneous procedures. To overcome the bias caused by a change in the scope of the analysis, a homogeneous evaluation aimed at making comparisons over time implies carrying out constant scope evaluations for each ECOWAS country. This like-for-like evaluation of tax expenditure, complying with regional evaluation rules, is a specific task that is not exclusive of national evaluations carried out within a broader scope. In addition to evaluating on a constant scope basis, it is necessary to apply the same evaluation methods which, in practical terms, means complying with the instructions of a set of procedures (see above) that will maintain the memory of the evaluation methods applied in previous years.

5.1.3 Reducing the risk of tax competition by coordinating tax exemption policies at the regional level

Regional coordination of tax exemption policies. The regional coordination of tax exemptions and their rationalization on the basis of *a homogenous regional evaluation of tax expenditure that enables meaningful comparisons between Member States,* for a given period, would reduce the risk of tax competition resulting in overbidding in granting exemptions The aim is to enable meaningful comparisons of tax expenditure levels between the various West African countries and their economic and social effects. As emphasized above, the regional coordination approach in no way precludes the pursuit, as in the past, of a national evaluation of tax expenditure that takes account of each country's specific objectives.

Regional coordination and tax competition. National choices by West African countries regarding the granting of tax exemptions are an essential component of their tax policies. Regional coordination of the tax exemption policies pursued by each ECOWAS member state would help to mitigate the risks of intensive granting of tax exemptions and growing losses in tax revenue. On an operational level, *the regional evaluation of tax expenditure, as a summary at the ECOWAS level, should be the preferred tool for promoting the harmonization of tax exemption policies.*

5.2 INNOVATIONS IN TAX EXPENDITURE EVALUATION

5.2.1 Institutional organization for a regional evaluation of tax expenditure

National entities responsible for the regional assessment. *The entities already in charge of national evaluations of tax expenditure would be responsible, in addition to their regular duties, for carrying out regional evaluations of tax expenditure. Each West African country would therefore produce a regional evaluation of tax expenditure in addition to its national evaluation. Regional evaluations per country would be centralized by a dedicated ECOWAS entity,* which would then be responsible for producing the Regional Tax Expenditure Evaluation Report, a summary of the regional reports produced by each country.

Each national organization would therefore have a dual mission:

1) As in the past, to produce a national evaluation of tax expenditure based on each country's specific criteria.

2) To develop a regional evaluation of tax expenditure in line with the regional standards[21], for submission to the dedicated ECOWAS entity.

Regional entities responsible for evaluation at the ECOWAS level. A special entity would be needed for the regional evaluation of tax expenditure. This entity would be supplied with the regional reports produced by the relevant entities in each Member State, and centralised at the regional level. Each year, this entity would produce the regional report on tax expenditure evaluation, which would enable the regional authorities to assess the extent to which the regional framework governing exemptions is being complied with. This entity could also provide technical support to the regional authorities in making the necessary adjustments to the regional framework for exemptions.

5.2.2 Inclusion of economic and social impact assessments in national and regional evaluations of tax expenditure

Inclusive evaluations of tax expenditure: a priority step at both national and regional level. To define a tax exemption policy at both national and regional levels that is representative of the choices made by the government authorities, it is necessary to take into account all the objectives assigned to tax exemption policies. Both national and regional evaluations of tax expenditure must therefore include not just an assessment of tax revenue losses, but also an assessment of the effects of exemptions on economic incentives, equity, and, lastly, service to the taxpayer.

Operational methods for evaluating the economic and social effects. Assessing the economic and social effects of derogation measures involves (i) identifying the objectives (economic and social) targeted by each derogation measure and (ii) clearly stating them in the inventory of these measures

This analysis also entails (iii) collecting the information and data needed to compare the objectives achieved with those targeted. For example, for a VAT exemption targeting the poor, it is necessary to (iv) calculate the proportion of uncollected (or foregone) revenue that actually benefits this population group. For an investment tax incentive, the amount of investment achieved should

21 Thus, it would be advisable to create an entity at the ECOWAS level with the mission of producing a summary of the evaluations.

be compared with the expected amount, and, where applicable, the number of jobs actually created should be compared with the expected number of new jobs. In all cases, the ex-post analysis provides the information needed to assess whether or not to keep a derogation measure based on its benefits and budgetary cost.

Regional and national evaluations being complementary. A Carrying out a regional evaluation of the above-mentioned effects will be greatly facilitated by a comprehensive national evaluation in each country: the country-specific regional evaluation will benefit from the information collected and the tax expenditure evaluation procedures applied to carry out the national evaluations (see below). To move from a national evaluation to a regional evaluation, it would be necessary to comply with the Regional Tax Expenditure Evaluation Framework, the definition of which must derive from ***a negotiated agreement between all the countries.***

Data sources for the regional evaluation of tax expenditure. Much of the data required for a regional evaluation is already collected as part of the national evaluation of ***tax expenditure***; however, a new use of the data would be necessary.

1) Member States use tax data compiled from customs and tax declarations to estimate revenue losses. Where such data is not available, they may use macroeconomic and/or sector-specific data to recreate the tax bases removed from taxation..

2) Integrating economic and social impact analysis into national and regional evaluations of tax expenditure requires access to data managed by bodies other than those responsible for collecting taxes: for example, the Directorate of Budget, the National Institute of Statistics, development agencies, the Agency for Economic Development, water companies, electricity companies, etc.

5.2.3 Structure of regional tax expenditure evaluation reports

In each country, the national entity usually responsible for the national evaluation of tax expenditure would have the additional task of producing a regional report on the evaluation of tax expenditure. This report should include the following elements.[22]

1) ***Assessment of the revenue losses covered by the regional evaluation;*** the assessment would be based on an inventory of the derogation measures, together with their initial objective, the quantified amounts of the revenue losses per type of tax, per beneficiary, per sector of activity, per objective (presenting the results as ratios in relation to GDP and in relation to tax revenue).

2) ***Analysis of the economic and social effects of the derogation measures,*** based on an inventory of the analyzed derogation measures, a reminder of the methods used to evaluate the economic and social effects of the derogation measures, a presentation of the results at the national level, and finally, an analysis of the results at the national level.

The regional report on the evaluation of tax expenditure a summary based on the various regional reports produced by each country, must include the following components.

1) Summary of the regional tax expenditure evaluations produced for each West African country. This summary should include summary tables covering all countries, along with an analysis of these tables.

2) Inventory of derogation measures, for each country and per tax category, together with their initial objective, subject to evaluation in the regional report.

3) Evaluation of tax expenditure including the definition of the regional benchmark system for each tax and a reminder of the method used to evaluate tax expenditure.

4) Evaluation of the amounts in current monetary units, revenue losses by type of tax, by beneficiary, by sector of activity, by objective. Presentation of results in terms of ratios to GDP and tax revenue.

5) Analysis of the results at the regional level with comparisons across countries.

22 Only VAT is covered at this stage.

6) Analysis of the economic and social effects of the derogation measures, including a reminder of the methods used to assess the economic and social effects of the derogation measures, a presentation of the results at the regional level, and finally an analysis of the results at the regional level with comparisons across countries.

5.2.4 Dissemination: objective of transparency/civil society

Establish a regional framework for tax exemption policies. As with national evaluations, the effectiveness of regional tax expenditure evaluations in promoting a policy of controlling exemptions depends closely on the status of the evaluation documents produced (summary reports and country reports). These documents are designed to be used by regional bodies to define a set of regional laws (Directives, Regulations, or other Community laws) to provide a regional framework for tax exemption practices in all West African countries.

Compliance with the regional framework for tax exemption policies. Compliance with the aforementioned regional framework should be ensured by regional monitoring, including peer monitoring. This is a prerequisite if comparisons of tax exemption policies implemented by the various West African countries are to contribute to the rationalization of tax exemption policies.

Dissemination and popularization. To ensure that the appropriateness of carrying out regional evaluations of tax expenditure and establishing a regional framework for tax exemption policies is widely recognized and appropriated in ECOWAS member countries, it is important to undertake appropriate information campaigns aimed at political decision-makers, economic operators, civil society, donors, NGOs, and the general public to publicize the results of regional evaluations of public expenditure and the grounds for a regional framework for tax exemption policies.

Contribution to budget transparency. The reports on the regional evaluation of tax expenditure (country reports and summary report) should be widely disseminated. Regional reports should be published on the ECOWAS website. Though more difficult than at the national level, it is desirable to organize specific regional dissemination campaigns aimed at trade unions, employers' organizations, the media, consumer organizations, and civil society in general, focusing on the regional dimension to avoid confusion with national evaluations.

5.3 OPERATIONAL PROCEDURES FOR IMPLEMENTING REGIONAL EVALUATIONS OF TAX EXPENDITURE

5.3.1 Gradual broadening of the scope of regional evaluations of tax expenditure

Rationale for a gradual approach based on domestic indirect taxation. Clearly, in view of the foreseeable difficulties, it would seem appropriate to recommend a gradual approach, suggesting to prioritize the tax categories that are most conducive to a regional evaluation of tax expenditure and that are most important in terms of revenue, economic incentives, equity, and services to taxpayers. These criteria should lead to prioritizing domestic indirect taxation.

The scope of the evaluation could be gradually broadened according to the following phases:

1	2	3	4
Phase I : VAT exemptions including common law exemptions	Phase II: Derogation measures applied to tariffs, i.e., customs duties and statistical fees	Phase III: Derogation measures applied to corporate income tax	Phase IV: Personal income tax, registration tax, and local taxes (business tax, property tax).

Phase I, regional evaluation of tax expenditure incurred by VAT exemptions

In the first phase, the regional evaluation of tax expenditure should focus on domestic indirect tax, VAT, and excise duties, for the following reasons. Internal indirect taxes offer the greatest potential for additional revenue that could be generated by reducing exemptions. Moreover, by promoting greater economic neutrality in indirect taxation, reducing VAT exemptions would help preserve the integrity of the trade protection provided by the common external tariff. Finally, reducing VAT exemptions would avoid discretionary procedures and introduce conditions conducive to improving service to taxpayers (on these various aspects see Brun and Chambas, 2022).

Another argument for prioritizing a regional evaluation of domestic indirect tax expenditure would be the relative ease of defining a common regional benchmark tax system for West African countries.

Identifying a common benchmark system for all West African countries is a prerequisite for producing homogeneous evaluations that facilitate comparisons across countries. The choice of the benchmark VAT tax system should be based on a consensus between the various West African countries, in particular on the number and level of rates; it would also be necessary, at the regional level, to define the tax base used as a benchmark. Once these choices have been made, the benchmark VAT tax system should be as stable as possible over time in order to facilitate the analysis of changes in VAT-related tax expenditure.

Regional evaluation of tax expenditure on tariffs

Once the regional evaluation of tax expenditure on VAT exemptions has been completed, the regional evaluation of tax expenditure could be extended to include tariffs. Because of the protective effect of tariffs, the evaluation of tax expenditure generated by tariff exemptions is complementary to that of VAT, which is an economically neutral tax. Evaluating tax expenditure generated by tariff exemptions is important not only from a revenue aspect but also from the dual aspect of the coherence of the economic incentives implemented and the effects on equity.

Identification of the benchmark tariff. The Common External Tariff for all ECOWAS countries would help to identify a common benchmark tax rate system for all West African countries. When the customs duty applied is lower than the theoretical customs duty (CET), a tax expense under tariff revenue is incurred. However, Economic Partnership Agreements (EPAs) introduce a specific feature in the evaluation of tax expenditure: when a tariff rate lower than the CET is applied under an EPA agreement, a tax expenditure is generated that reflects the budgetary cost of the EPA agreement.

Regional evaluation of tax expenditure on income tax

EIncome tax is the third major tax category to be considered when evaluating tax expenditure at the regional level. This tax, whose legislation is relatively comparable from country to country, is the second largest source of tax revenue after VAT. Income tax (rates, definition of tax base, scope of exemptions) also contributes to economic incentives.

Profit tax; definition of a benchmark tax system. Defining a regional benchmark tax system for income taxes (tax rates, definition of the tax base, etc.) is more complex than for consumption taxes or tariffs (see above). In West Africa, income tax practices vary across countries and it is therefore difficult to identify the benchmark regional tax system.

To overcome this difficulty, it seems possible, according to Heady and Mansour (2019), to harmonize the tax base by considering «temporal aspects as tax expenditures (in other words, excluded from the benchmark system) and tax avoidance or tax-base erosion measures as part of the benchmark system». For example, accelerated depreciation, which increases the deduction of expenses at the beginning of the period, provides an advantage over time and should therefore be excluded from the benchmark tax system. It is equally difficult to identify best practices in terms of corporate tax rates. For each country, the common law single standard rate could be used. Another option would be to consider a single regional corporate tax rate[23].

Regional evaluation of tax expenditure on various taxes

This category includes personal income tax, local taxes (business tax, property tax, registration fees, and various local taxes). For this category of taxes, it is particularly difficult to define a regional benchmark tax system because legislation differs from one country to another. A regional evaluation of tax expenditure on these various local taxes is a long-term objective.

23 The disadvantage would be a negative tax expenditure for countries where the common law rate is lower than the regional rate.

5.3.2 Regional evaluations of tax expenditure generated by VAT exemptions

Setting a common regional VAT benchmark for all West African countries

To avoid undermining the momentum for regional evaluation of tax expenditure and pending a regional agreement, complying with VAT principles could temporarily lead to using the broadest base (private and public final consumption) to which a single rate would be applied. For each country, this rate could be a common regional VAT rate for all West African countries[24]. The VAT benchmark tax system would not, therefore, include any exemptions or reduced rates, except for the zero rates on exports, which is designed to neutralize the VAT effect. Under such an approach, VAT exemptions included in the common law would be evaluated at the regional level. One advantage of such a benchmark system would be transparency of information, enabling the evaluation of tax expenditure incurred by the application of reduced VAT rates and all legal VAT exemptions.

At the regional level, it is necessary (see above) to assess both the revenue losses and the economic and social effects of VAT exemptions, as well as their implications for the quality of service to taxpayers. These guidelines for a regional evaluation of the various effects of exemptions are similar to those that should be applied at the national level.

Objective of economic neutrality, harmonious refund of VAT credits and control of exemptions

VAT credit refunds: uneven situations. While some ECOWAS member countries have succeeded in making smooth refunds of VAT credits sustainable, most West African countries have not yet taken this step.

Controlling VAT exemptions involves promoting smooth VAT credit refunds. The aim is to establish a system enabling smooth refunds of VAT credits within a timeframe corresponding to international best practices. Failure to ensure that VAT credits are refunded smoothly means that economic operators suffer an undue increase in costs, which is detrimental to the competitiveness of the activities subject to VAT: it is then very difficult for the authorities, given the additional costs incurred by businesses, to refuse to grant VAT exemptions on intermediate consumption.

24 As with corporate income tax, the disadvantage of this choice would be a negative tax expenditure for countries where the common law rate is lower than the regional rate.

Need for a regional dynamic to promote smooth VAT credit refunds

- ***National initiatives to ensure smooth refunds of VAT credits may be challenged.*** External crises or shocks could jeopardize the sustainability of VAT credit refund schemes (e.g., Stopping the funding of the escrow account that replenishes VAT credit refunds, introducing procedures that prevent VAT credit refunds from running smoothly).

- ***Stimulating a regional dynamic to promote smooth VAT credit refunds would create favorable conditions for a reduction in VAT exemptions.*** An analysis of VAT credit refunds could be included in the regional evaluation of tax expenditure generated by VAT exemptions. Fluidity of VAT credit refunds in the various West African countries could be assessed on the basis of simple, easily computable, and verifiable indicators (see Box 5). Insofar as the fluidity of VAT credit refunds would become a regional performance indicator, the sustainability of the fluidity of VAT credit refunds could be strengthened by a regional dynamic. Thus, one of the major causes for granting numerous VAT exemptions could disappear.

Box 5: ***: Indicators for smooth refunds of net VAT credits***

Predictability and brevity of VAT credit refund periods, conditions for VAT's economic neutrality, are key factors in improving the business climate. Given the specific nature of the behavior of VAT taxpayers and the refund procedures to be implemented according to risk, the indicator of the fluidity of VAT credit refunds must be assessed for each group of taxpayers classified by risk: good administrative practice governing the refund of VAT credits involves classifying VAT taxpayers according to the risk and, for low-risk taxpayers, substituting a posteriori control for a priori control, which enables shorter refund periods without undermining the effectiveness of controls.

For each group of VAT taxpayers, the weighted average time between the submission of an application for a VAT credit refund and the actual refund can be evaluated. This indicator should be supplemented by an indicator relating to changes in the stock of pending refund applications.

Evaluation method of the average refund period. To assess the weighted average time taken for a group of VAT taxpayers in a given year, it is necessary to record the refunds of VAT credits made during that year to that group, to assess the time between payment and submission of the claim and, finally, to weight the assessed time by the amounts of refunded VAT credits. In addition to evaluating the average time, it is useful to assess the stock of pending VAT credits, which is indicative of the degree of fluidity of VAT credit refunds in the past.

6.

CONCLUSION

Complementarity between national and regional evaluations of tax expenditure. The common objective of national and regional evaluations of tax expenditure is to provide each country with the necessary information to achieve optimum public finances by rationalizing exemptions.

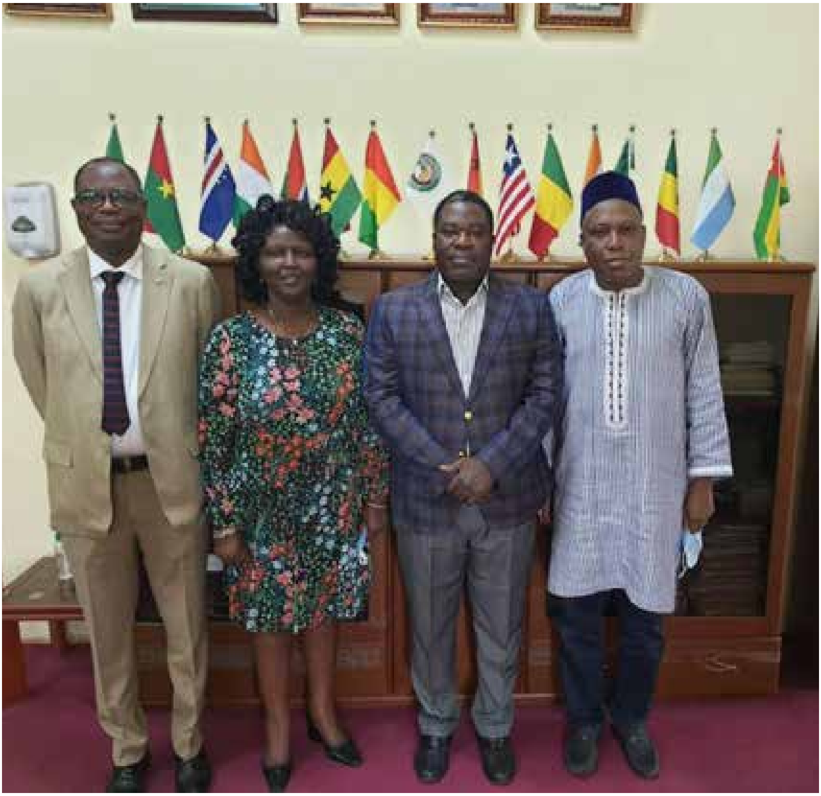
National evaluations of tax expenditure and rationalization of tax exemptions. National evaluations of tax expenditure in line with best practices create the right conditions for decision-makers in each country, based on specific national objectives, to make rational choices about tax exemptions: keeping, ending, or adopting specific exemptions, choosing between subsidies and tax exemptions, or choosing between tax incentives under common law such as smooth refunds of VAT credits and derogations measures such as exemptions included in Agreements on Establishment.

Regional evaluations, including the regional summary evaluation, are an instrument for the harmonization of tax exemption policies. The ultimate goal of this approach is to reduce tax distortions among West African countries which are members of the same regional integration area: the aim is to take a crucial step towards tax coordination among West African countries by compensating for the distortions caused by the granting of specific exemptions within each country.

Filling an essential gap in the coordination of tax policies by harmonizing exemption policies. While the main components of taxation are the subject of regional coordination measures, particularly through Directives, and despite long-standing attempts to adopt a Community Investment Code among WAEMU countries, there is no regional coordination of derogation measures, such as tax exemptions.

The coordination of exemptions resulting from a regional evaluation of tax expenditure should make it possible to reduce tax competition between West African countries. Thus, it should encourage decision-makers to allocate a more rational place to tax exemptions and other derogation tax measures. The development of an extensive culture of exemptions, inconsistent with the search for an optimal situation, could thus be avoided.

Implementing tax co-ordination to rationalize tax exemptions is all the more necessary given that tax revenues in most West African countries have been affected in recent years by major exogenous shocks: many of these shocks have led to a decrease in tax revenues at a time when the need for public goods is rising sharply. Shocks of various kinds suffered by West African countries have frequently combined their effects (2008 international financial crisis, sharp fluctuations in the prices of primary products - agricultural or mining products, political instability, insecurity, particularly in the Sahelian strip, extreme climatic phenomena, more recently the COVID-19 health crisis, etc.). These factors have contributed to instability of tax revenues in West African countries, and have had a negative impact on their level.



7.

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8.

APPENDIX TO THE METHODOLOGICAL GUIDE FOR A REGIONAL EVALUATION

A. BACKGROUND AND JUSTIFICATION OF THE ECOWAS DIRECTIVE

It is not easy to provide a detailed procedures manual applicable to all ECOWAS Member States and Mauritania.

However, the main regional guidelines have been defined so that each Member State can develop a specific procedure manual in line with the Community Directive on tax expenditure management.

This annex discusses the Regional Evaluation of Tax Expenditure: The aim is to provide ECOWAS with a regional evaluation of tax expenditure. This regional evaluation would be carried out by a dedicated ECOWAS entity. It would be a summary of the regional evaluations produced by the national entities currently in charge of national tax expenditure evaluations.

The national entities would therefore be assigned a dual role:

- To carry out, as in the past, a national evaluation of tax expenditure based on country-specific criteria;
- Produce a regional evaluation of tax expenditure in line with regional standards; these regional evaluations are intended for the dedicated ECOWAS entity[25] which will centralize them and draw up a summary report based on the regional reports submitted by each country.

B. COMMENTS ON THE ECOWAS DIRECTIVES

1. Definitions and concepts

a) ***A tax expenditure*** is a foregone tax revenue arising from a reduction in tax liability relative to a benchmark tax system. Tax expenditure is an alternative to direct budgetary expenditure. Tax expenditure is the result of a tax derogation measure designed to reduce the tax burden borne by a taxpayer, a group of taxpayers or a sector of activity. This measure results in a loss of revenue.

25 It would therefore be advisable to create an entity at the ECOWAS level with the task of drawing up a summary of the regional evaluations submitted by each West African country.

b) Derogation measures include:

- Abatements: a deduction applied to the taxable base subject to tax;
- Tax credits: amount deducted from the tax due;
- Deductions: amounts deducted from the reference income to obtain the tax base;
- Exemptions (total or partial): amounts excluded from the tax base;
- Tax deferral: relief in the form of a tax payment deferral;
- Rate reduction: reduced rate applied to a category of taxpayers or taxable transactions;
- Tax reduction: sum deducted from the amount of tax due.

These measures may be included in common law tax legislation or in various legal provisions, such as those relating to free zones, investment codes, sector-specific incentive codes (mining, oil, etc.), or specific decrees. They may also be included in agreements between the State and economic operators, or between the State and NGOs, etc. They also appear in public contracts/projects, many of which are externally financed.

c) Derogation measures are most often granted in order to achieve an economic incentive or equity objective. However, the expected benefit of derogation measures is generally not assessed ex-ante. Therefore, in order to evaluate the advantage provided by the derogation measures, it is necessary to compare their budgetary cost with their economic benefit (amount of investment, number of jobs created, etc.) or social benefit (proportion of the loss of revenue captured by the targeted populations, etc.). In the absence of an ex-post analysis, it is difficult to justify the merits of a derogation.

2. Frequency

The regional evaluation of tax expenditure would be carried out annually. It would be based on the national evaluations carried out by the dedicated entities set up within the Member States. The evaluation of revenue losses for year n-1 would be carried out during year n and appended to the Finance Bill for year n+1.

3. Scope of the regional evaluation

The regional evaluation will cover derogation measures in relation to the common benchmark tax system for West African countries. In order to avoid burdening tax expenditure evaluation units beyond their capacity, the scope of the evaluation should be gradually broadened in the following phases:

- ***Phase I:*** VAT and duty exemptions, including exemptions under common law;
- ***Phase II:*** derogation measures applied to customs duties and statistical fees;
- ***Phase III:*** exemptions and derogations applied to corporate income tax;
- ***Phase IV:*** exemptions and exceptional measures relating to personal income tax and local taxes (business tax, property tax, registration fees).

Eventualmente, a revisão e a análise comparativa poderiam basear-se nos últimos três anos (N-1, N-2 e N-3).

4. Benchmark tax system for regional evaluation

The regional benchmark tax system adopted should comply with the principles of economic neutrality, efficiency, equity, and simplicity, which are common to all West African countries. Its adoption should be the result of regional negotiations[26]. However, pending agreement between the various countries, the following principles could be adopted.

VAT

The key characteristics of VAT (a general tax on final consumption) lead to the use of the broadest possible base (private and public final consumption) to which a single rate would be applied. For each country, the standard common law rate (simple and operational) could be used. Another option would be to determine a single regional VAT rate[27].

The recommended VAT benchmark tax system, therefore, does not include any exemptions or reduced rates, apart from the zero rate on exports, designed to neutralize the economic effect of VAT. VAT exemptions contained in the common law of each country would therefore be assessed at the regional level.

26 A regional meeting to define the regional benchmark tax system should be planned every year.

27 The disadvantage of this option would be a negative tax expenditure for countries where the common law rate is lower than the regional rate.

Customs duties

The benchmark system would be the Common External Tariff (CET). When the customs duty applied is lower than the theoretical customs duty (CET), a tax expense is recorded under tariff revenue. Case of Economic Partnership Agreements: when a tariff rate lower than the CET is applied under an EPA agreement, a tax expenditure is generated reflecting the budgetary cost of the EPA agreement.

Corporate income tax or tax on profits[28]

A regional benchmark tax system for corporate income tax is more complex to define than for consumption taxes or import tariffs: in West Africa, practices differ, making it difficult to identify a regional benchmark tax system for this category of tax.

It would be advisable, according to Heady and Mansour (2019), to harmonize the tax base by considering «temporal aspects as tax expenditures (in other words, excluded from the benchmark system) and tax avoidance or tax-base erosion measures as part of the benchmark system». For example, accelerated depreciation, which increases the deduction of expenses at the beginning of the period, provides an advantage over time and should therefore be excluded from the benchmark tax system.

It is also difficult to identify best practices in terms of corporate income tax rates. For each country, the standard common law rate could be used. Another option would be to determine a single regional corporate income tax rate[29].

Other taxes: personal income tax and local taxes

For this category of taxes, it is particularly difficult to define a benchmark regional tax system. However, their role in terms of revenue losses can be considered small relative to the aforementioned taxes. Including them in the regional evaluation of tax expenditure is a long-term objective.

28 Most countries have introduced a corporate income tax.

29 As with VAT, the disadvantage would be a negative tax expenditure for countries where the standard rate is lower than the regional rate.

5. Methods of evaluation

a) The evaluation of tax expenditure will definitely be based on the revenue loss method, which is the only method currently used by the entities in charge of national evaluations. This method is simple and well-understood.

b) The analysis of the economic and social effects of the derogation measures will involve:

- Identifying the objectives (economic and/or social) sought by each derogation measure and mentioning them specifically in the inventory of these measures;
- Collecting the information and data needed to compare actual results with the initial objectives. For example, for a VAT exemption targeting the poor, it is necessary to calculate the proportion of revenue not collected (or foregone) that actually went to the poor. In the case of a tax incentive for investment, the amount of investment made should be compared with the amount expected, and, where applicable, the number of jobs actually created should be compared with the expected number of new jobs.
- An ex-post analysis providing the information needed to assess whether or not a derogation should be kept by comparing its benefit with its budgetary cost.

6. Data sources for regional evaluation of tax expenditure

a) To estimate revenue losses, Member States use tax data compiled from customs and tax declarations to estimate revenue losses. Where such data is not available, they may use macroeconomic and/or sector-specific data to recreate the tax bases removed from taxation.

b) Integrating economic and social impact analysis into national and regional evaluations of tax expenditure requires access to data managed by bodies other than those responsible for collecting taxes: for example, the Directorate of Budget, the National Institute of Statistics, development agencies, the Agency for Economic Development, water companies, electricity companies, etc.

7. Entities in charge of evaluating tax expenditure

At the ECOWAS level, a dedicated entity would be needed for the regional evaluation of tax expenditure. This entity would be supplied mainly with regional reports drawn up by the relevant entities in each Member State. It is recommended to organize, in the first quarter of each year, a regional workshop to define the common SFR.

At the national level, the entities responsible for the national evaluation of tax expenditure would be tasked, in addition to their regular mission, with carrying out the regional evaluation of tax expenditure. Each West African country would therefore produce a regional evaluation of tax expenditure in addition to the national evaluation. The regional evaluation would be centralized in the designated ECOWAS entity, which would then be responsible for producing the regional tax expenditure evaluation report, a summary of the regional reports produced by each country.

8. Structure of the report on the regional evaluation of tax expenditure

O The report on the regional evaluation of tax expenditure, drawn up from the various national reports in accordance with regional standards (see point 8 below), must include:

a) ***Summary of regional evaluations*** of tax expenditure produced for each West African country. This summary must include summary tables covering all countries, together with an analysis of these tables. The analysis may be carried out per tax, per beneficiary, per sector of activity, per objective.

b) ***Inventory, for each country and per tax category, of the derogation measures*** together with their initial objective, subject to evaluation in the regional report. For VAT, these are the exemptions contained in common law and also various exemptions (see above).

c) ***Evaluation of tax expenditure:***

- Definition of the regional benchmark system for each tax;
- Reminder of the method used to evaluate tax expenditure;
- Figures of revenue losses per type of tax, per beneficiary, per sector of activity, per objective. Results are presented in the form of ratios to GDP and to tax revenue;
- Analysis of results at the regional level, with comparisons across countries.

d) Analysis of the economic and social effects of the derogation measures:
- Reminder of the methods used to assess the economic and social effects of the derogation measures;
- Presentation of results at the regional level;
- Analysis of the results at the regional level with comparisons across countries.

9. Mission of national entities in drawing up the regional report on the evaluation of tax expenditure

Each national entity prepares a regional report on the evaluation of tax expenditure. This report should include the following[30]:

a) Evaluation of tax expenditure covered by the regional evaluation:
- Inventory of the derogation measures, and their initial objective;
- Figures of revenue losses per type of tax, per beneficiary, per sector of activity, per objective. Presentation of results in terms of ratios to GDP and to tax revenue;
- Reminder of the method used;
- Analysis of results at the national level.

b) Analysis of the economic and social effects of derogation measures:
- Inventory of the analyzed derogation measures;
- Reminder of the methods used for evaluating economic and social effects of derogation measures;
- Presentation of the results at the national level;
- Analysis of the results at the national level.

10. Publication and dissemination of the regional report on tax expenditure evaluation

To contribute to budget transparency, the regional report on tax expenditure evaluation should be broadly disseminated. As such, the report should be published on the ECOWAS website. It would also be advisable to organize dissemination campaigns aimed at trade unions, employers' organizations, the media, consumer organizations, and civil society in general, both at the regional level and within individual countries. The aim is to use benchmarking to promote regional convergence of tax exemption policies.

30 Initially, only VAT would be covered.

C. APPENDIX 2 –DRAFT DIRECTIVE ON THE METHODOLOGY FOR EVALUATING TAX EXPENDITURE

ECOWAS COMMISSION
COMMISSION DE LA CEDEAO
COMISSÃO DA CEDEAO

ORDINARY SESSION

OF THE COUNCIL OF MINISTERS 2022

DRAFT DIRECTIVE C/DIR 05/12/2022
ON THE HARMONIZATION OF TAX EXPENDITURE EVALUATION METHODS WITHIN ECOWAS MEMBER STATES

THE ECOWAS COUNCIL OF MINISTERS,

MINDFUL of Articles 10, 11, and 12 of the ECOWAS Treaty as amended, establishing the Council of Ministers and defining its composition and functions;

MINDFUL of Article 3 of the said Treaty stipulating the areas in which the Community shall deploy its actions, to achieve its goals and objectives;

TMINDFUL of Article 5 of the said Treaty reiterating the commitment of Member States to abide by the decisions and regulations of the Community;

MINDFUL of Directive C/DIR.1/05/09 on the harmonization of value-added tax laws of ECOWAS Member States;

MINDFUL of Directive C/DIR.2/06/09 on the harmonization of excise duties laws of ECOWAS Member States;

MINDFUL of Directive C/DIR.1/12/13 adopting the ECOWAS fiscal transition program;

CONSIDERING that the implementation of the ECOWAS Common External Tariff, coupled with the conclusion of international trade agreements and trade liberalization policies, will lead to a considerable decrease in import duties that cannot be offset by the Community compensation measures alone;

CONSIDERING that the harmonization of Member States' tax regulations is a necessity to realize the attainment of a common market and that it will also contribute to establishing coherence in the domestic systems of taxation, ensuring equal treatment for trade operators within the Community and enhancing the proceeds from the various taxes;

CONSIDERING that the commitments entered into by Member States as part of their poverty reduction strategies aimed at achieving the Millennium Development Goals require greater mobilization of financial resources;

AWARE of the need to strengthen the ECOWAS common market and to support the economic growth of the Community's Member States while mobilizing the necessary resources to finance development;

DESIRING to provide Member States with tax management tools in order to improve their performance in mobilizing tax resources and thereby strengthen the measures of the fiscal transition program undertaken by the Member States;

CONVINCED that it is in the interest of the Community to put in place a coherent program of fiscal and customs reforms for the transition from door-to-door taxation to internal taxation in order to offset any losses of door-to-door revenue generated by the opening of the Community market and the conclusion of international trade agreements;

CONVINCED that domestic taxation should enable the mobilization of revenue while promoting business competitiveness;

DESIROUS to provide the Community with a harmonized methodology for evaluating tax expenditure, common to all Member States; Having obtained the opinion of the Committee of Statutory Experts dated XXX October 2022

PRESCRIBES AS FOLLOWS:

ARTICLE 1: OBJECTIVE

The objective of this Directive is to define the procedures for evaluating tax expenditures within ECOWAS.

ARTICLE 2: DEFINITIONS

For the purposes of this Directive:

"Tax administration", the entity, institution, or body in each Member State responsible for the administrative management of tax.

"Commission", the Commission of ECOWAS established under Article 17 of Supplement Protocol A1SP1/06/06 dated 14 June 2006;

"Community", the Economic Community of West African States whose establishment is reaffirmed by Article 2 of the Treaty;

"Council", the Council of Ministers set up by Article 10 of the Treaty of the Economic Community of West African States;

«Member State or Member States», Member State or Member States of the Economic Community of West African States;

«President of the Commission», the President of the Commission of the Economic Community of West African States provided for in Article 19 of the Additional Protocol A/SP1/06/06;

«Treaty», the Revised Treaty of the Economic Community of West African States signed on 24 July 1993 and all subsequent amendments thereto;

«Tax expenditure», is a tax revenue foregone resulting from the implementation of legislative, regulatory, or contractual provisions that derogate from a Benchmark Tax System (BTS). These measures result in a definitive loss of tax revenue.

Tax expenditure is mainly generated by the following measures:

- Exemptions
- Tax credits
- Tax reductions
- Reduced tax rates
- Tax allowances
- Tax abatements

«Tax incentives» are tax measures designed to guide, regulate, or promote economic activity, and to encourage or dissuade desirable or undesirable behavior or activities.

The «benchmark tax system» considered here is the tax system that applies to all taxpayers or all economic transactions; it indicates, for each tax, duty, or levy, the benchmark tax base and the standard rate of taxation.

ARTICLE 3: FREQUENCY OF THE EVALUATION OF TAX EXPENDITURE

Member States shall evaluate tax expenditure each year by applying the evaluation methodology common to the Member States. Each Member State shall draw up a national report which shall be sent to the Commission. The evaluation of tax expenditure for year n-1 is carried out during year n and appended to the Finance Bill for year n+1.

ARTICLE 4: SCOPE OF TAX EXPENDITURE EVALUATION

The evaluation of tax expenditure relates to measures that diverge from the reference tax system.

ARTICLE 5: METHODS FOR DETERMINING THE BENCHMARK TAX SYSTEM

The benchmark tax system for each tax, duty, or levy is adopted by the Member States on the basis of the regional guidelines for domestic tax and customs legislation. As part of the regional evaluation, the benchmark tax system must be common to all Member States.

ARTICLE 6: METHODS FOR EVALUATING TAX EXPENDITURE

1. The evaluation of budgetary costs is based on the method of «revenue losses» or «revenue foregone».
2. The budgetary cost of tax expenditure is evaluated, for each measure, in relation to the benchmark tax system and by type of tax or levy.
3. Member States shall carry out an analysis of the economic and social effects of tax expenditure in addition to the budgetary evaluation of revenue foregone.

ARTICLE 7: DATA SOURCES FOR EVALUATING TAX EXPENDITURE

Each Member State shall set up a system for collecting the data needed to evaluate tax expenditure (data from customs and tax returns; macroeconomic data, sector-specific data, and/or data from other sources).

ARTICLE 8: TAX EXPENDITURE EVALUATION GRID AND SPECIFIC MONITORING GRID FOR TAX INCENTIVES

A grid for evaluating tax expenditure and a specific grid for monitoring tax incentives for investment shall be defined and applied by the Member States in order to facilitate the harmonization of practices for data collection, processing, and analysis of tax expenditure.

ARTICLE 9: STRUCTURE OF THE TAX EXPENDITURE EVALUATION REPORT

Each tax expenditure evaluation report includes the following:

1. **Definition of concepts and review of the evaluation methodology. This involves** defining the main concepts, reviewing the regional benchmark tax system, and presenting the evaluation methodology.
2. **Analysis of the budgetary evaluation results.** It identifies the derogation measures, presents the evaluated measures, and the related tax expenditure.

Where data is available, each report on tax expenditure presents data for the previous three years. Member States may produce projections for the coming year.

3. **Tax expenditure is analyzed by:**
   - Type of tax;
   - Types of derogation;
   - Legal basis;
   - Objectives;
   - Categories of beneficiaries;
   - Sectors of activity;
   - Budget functions or programs for countries that have adopted program budgeting;
   - Ratios: tax expenditure over tax revenue, tax expenditure over Gross Domestic Product, etc.

4. **Analysis of economic and social effects, where applicable.**

ARTICLE 10: ENTITIES RESPONSIBLE FOR EVALUATING TAX EXPENDITURE

At the national level: each Member State shall set up a cross-sectoral entity, attached to the Ministry responsible for tax policy, which shall carry out the evaluation of tax expenditure at the national level in accordance with a methodology common to the various Member States.

At the ECOWAS level: the Commission draws up the summary report on the basis of the regional reports drawn up by each Member State.

ARTICLE 11: SUBMISSION, PUBLICATION, AND DISSEMINATION OF TAX EXPENDITURE EVALUATION REPORTS

1. The regional report on tax expenditure evaluation drawn up by each Member State shall be submitted to the ECOWAS Commission simultaneously with the submission of the national evaluation report to be appended to the initial finance bill or the annual budget.
2. Member States disseminate their regional tax expenditure evaluation report to all stakeholders, in particular employers' organizations, consumer organizations, civil society, and the media.
3. The ECOWAS Commission publishes the regional summary report on tax expenditure evaluation on its website.

ARTICLE 12: FINAL PROVISIONS

1. This Directive shall be published by the Commission in the Community Official Journal within thirty (30) days of the date of signature by the Chairman of the Council of Ministers. It shall equally be published by each Member State in its National Gazette thirty (30) days after notification by the Commission.
2. Member States shall adopt the necessary legislative, regulatory, and administrative measures in order to comply with this Directive no later than 31

December 2023.

3. The measures referred to in Paragraph 1 of this article, as adopted by the Member States, shall make reference to this Directive or shall be accompanied by such reference upon their official publication.
4. Member States shall inform the ECOWAS Commission of the measures or provisions they will adopt to comply with this Directive.
5. Member States shall notify the President of the Commission of the difficulties they encounter in the implementation of this Directive. The President of the Commission shall report such difficulties at the next session of the Council of Ministers which shall, in turn, take the appropriate measures to ensure the effective implementation of this Directive.
6. The Commission and the Member States are responsible for the implementation and monitoring of this Directive.

DONE AT ABUJA, this 2022

For the Council of Ministers

Chairman XXXXXXX

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S.E SUZI CARLA BARBOSA

D. APPENDIX 3 - REGIONAL TAX EXPENDITURE EVALUATION GRID

The PATF draft regional grid has been developed to harmonize tax expenditure evaluation methods in West Africa.

HYPOTHESES

- Regional BTS: ECOWAS directive on VAT
- Reference rate: Standard rate in line with the ECOWAS Directive on VAT: 18% (Abidjan Workshop, June 2022)
- Method for calculating loss of revenue: Theoretical tax - Tax actually paid;

The main harmonization criteria

- First harmonization criterion: TE/nominal GDP ratio (in %);
- Second harmonization criterion: TE/TR ratio (in %);
- Third harmonization criterion: Evaluation rate of derogation measures inventoried (in %) = Number of evaluated measures / Number of inventoried measures.

NB: Make available the tax legislation in force (VAT, profit tax, customs duties, etc.).

Order no.	Tax Code	CET Code (Products)		Benchmark or legal basis	Conformité à la Directive Communautaire	Taxes in question	Types of exemption	Basic elements of taxation	Temporal scope	Goals	Activity area	Beneficiaries
1	Label of Derogation Measure	Compliance with Community Directive		Relevant Taxes	1 - Compatible	VAT	Rate reduction	Turnover	Permanent	Incentive investment	Agriculture	Public companies
2	Types of derogation		Basic elements of Taxation	Full exemption from VAT	0 - Not compliant	VAT	Full exemption	Benefits/Profits	Temporary	Make access easier on the phone	Reproduction	Companhias privadas
3	Temporal Scope		Objectives	Partial VAT exemption		VAT	Partial exemption	Customs value	Temporary	Make access easier for computer	Pisciculture	NGOs/ Associations
4	Sectors of activities		Art. XX of any specific law			VAT	Congé fiscal (suspention des impositions)		Temporary	Promote energy	General trade	Business
5	VAT0001	CET Code	Art.XX of Tax Code	Reduction by 10 points of the VAT rate for one sector of activity	Compliant	VAT	Rate reduction	Turnover	Permanent	Promote investment	Agriculture	
6	VAT0002	Empty	Art.XX of MiningCode	Total VAT exemption	Not compliant	VAT	Total exemption	Benefits/Profits	Temporary	Facilitate access to phone services	Husbandry	

Beneficiaries	Public enterprises	Private businesses	NGOs/ Associations	Companies	Economic affairs	Economic affairs
Fonte de dados estruturais	INSD	INSD	DGI/INSD	DGI	Customs Department	DGI
Data source (Computer application) Calculation	Financial status	Financial status	Extraction of financial statements	SYDONIA	SINTAX	SINTAX
Calculation method	To offer	To offer	To offer	To offer	To offer	To offer
Amount 2019	PM	PM	PM	PM	PM	PM
Amount 2020	PM	PM	PM	PM	PM	PM
Amount 2021	PM	PM	PM	PM	PM	PM
Amount 2022	PM	PM	PM	PM	PM	PM
Amount 2023	PM	PM	PM	PM	PM	PM
Year of adoption of the measure	Year	Year	Year	Year	Year	Year
Measurement Status on CGI	Dans CGI = 1	Hors CGI = 0				
Observations/ Comments						

D. APPENDIX 3 - REGIONAL EVALUATION GRID OF TAX INCENTIVES FOR BUSINESSES

ORGANIZATIONS GRANTED TAX AND CUSTOMS EXEMPTIONS
CONSOLIDATED STATEMENT ON TAX INCENTIVES - CUSTOMS DUTIES, EXCISE DUTIES, VAT, AND OTHER TAX AND CUSTOMS EXEMPTIONS

Order number Company	Company reference code (associated with NIF and name/business name not communicated)	Legal form of the company	Company sector of activity	Objectives/main activities of the project	Number of employees		Production capacity		Type of incentive	Period of entitlement to tax incentive		Exemption from customs duties, excise taxes, VAT and fees.																					Nota: Beneficios esperados Incentivo fiscal
					Current	Strange	Location	Installed		Start	FIM	Start END Description (Raw materials/inputs, equipment, motor vehicles, consumer goods, others)	Estimated volume of imports		Unit price	Value of imports (in NGN)	Value of imports (in NGN)	Taxes and fees otherwise payable					Taxes and fees payable					Taxes and fees to be exempt					
													Quantity/Quantity	Unit of measurement					Consumption tax	TVA	Specimens	Others	Customs duties	Consumption tax	TVA	Specimens	Others	Customs duties	Consumption tax	TVA	Specimens	Others	
																		a	b	c	d	e	f	g	h	i	j	k=(a-f)	l=(b-g)	m=(c-h)	n=(d-i)	o=(e-j)	
(A)	(B)	(C)		(F)	(G)	(H)	(I)	(J)	(K)	(L)	(M)	(N)	Uni-dade de medi-da	(P)		(R)	(S)		(U)	(V)	(W)	(X)	(Y)	(Z)	(AA)	(AB)	(AC)	(AD)	(AE)	(AF)	(AG)	(AH)	(AI)
															Value of iM-ports (in NGN)			Taxes and fees to be exempt															
TOTAL																																	

Certified by:
Last name first name:
Designation:
Date

STRUCTURES THAT BENEFIT FROM TAX AND CUSTOMS EXEMPTIONS CONSOLIDATED STATEMENT ON INCENTIVE-BASED TAX INCENTIVES IN INCOME TAXES

Order number Company	Company reference code (associated with NIF and name/business name not communicated)	Legal form of the company	Company sector of activity	Objectives/main activities of the project	Number of employees		Production capacity		Type of incentive	Period of entitlement to tax incentive		Financial performance in the last three (03) years									Losses of tax and customs revenue					Notes: Potential environmental impact
												Years 1			Years 2			Years 3								
					Current	Strange	Location	Installed		Start	FIM	Products	Collections	Gross profit	Products	Collections	Gross profit	Products	Collections	Gross profit	TVA	Income tax	Customs revenue	Other taxes and fees	Total tax expenses	
(A)	(B)	(C)	(D)	(E)	(F)	(G)	(H)	(I)	(I)	(J)	(K)	(L)	(M)	(N)	(O)	(P)	(Q)	(R)	(S)	(T)	AA	AB	AC	AD	AD	AE
1	Liberia0001	4467888990A	2015	Company	Agriculture	See Contract	Number	Number	investment	Year	Year	PM	PM	PM	PM	PM	PM	PM	PM	PM	Quantity	Quantity	Quantity	Quantity	Quantity	
2	Liberia0002	4566778898B	2018	Individual business	Industry	Cf. Convention	Number	Number		Year	Year	PM	PM	PM	PM	PM	PM	PM	PM	PM	Quantity	Quantity	Quantity	Quantity	Quantity	

Certified by:
Last name first name:
Designation:
Date

E. APPENDIX 4 - STEPS IN THE PROCEDURE FOR EVALUATING TAX EXPENDITURE

1. *Set up a unit dedicated to monitoring tax expenditure*
2. *Determine the nature of the tax*
3. *Draw up an exhaustive list of derogations for customs and internal procedures for each tax, duty, or levy*
4. *Enter the legal basis*
5. *Complete the CET column*
6. *Fill in the first two columns (chronological references)*
7. *Indicate whether the derogation complies with the Community Directive*
8. *Specify the type of derogation*
9. *Indicate the basic elements of taxation (nature of data)*
10. *Indicate the temporal scope*
11. *Specify the objectives of the derogation measure*
12. *Identify relevant sector of activity*
13. *Identify beneficiaries*
14. *Indicate the budget function*
15. *Identify the data source (structure)*
16. *Identify the data source (computer application, other sources)*
17. *Set up a system for collecting the data needed to quantify revenue losses.*
18. *Collect data according to sources*
19. *Calculate the loss of tax revenue*
20. *Specify the year in which the derogation was adopted*
21. *Indicate the status of the measure in relation to the fundamental text*
22. *Analyze data according to the structure of the regional report*
23. *Draft and present the report using the required format.*

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