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Tax policy during the COVID-19 pandemic

Background

The report provides an overview of the tax measures introduced during the COVID-19 crisis across almost 70 jurisdictions, including all OECD and G20 countries and 21 additional members of the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting. It examines how tax policy responses have varied across countries and evolved over the last year. It also offers some guidance as to how tax policy responses could be adapted to address the short-term challenges countries face.

Key findings

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

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

Many of the tax measures introduced in the initial stages of the crisis have been prolonged, with some being more targeted to channel support to the households and businesses most affected by the crisis, especially where governments have moved away from broad-based lockdowns towards more selective virus-containment measures.

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

Another significant trend observed over the last year is that an increasing number of countries have introduced or announced new tax increases. Unlike in the emergency phase of the crisis, a number of countries reported tax increases in the second half of 2020 and early 2021. While a few of these tax increases involved one-off or temporary measures, most are intended to be permanent. Among these longer term tax increases, some represent a continuation of pre-crisis trends, such as increases in fuel excise duties and carbon taxes, which were the most common tax increases reported by countries. On the other hand, some tax increases mark a departure from pre-crisis trends. In particular, a number of countries introduced tax increases on high-income earners, including increases in top personal income tax rates reported in seven countries.

Despite some common trends, there have been notable differences across regions and countries regarding the scope and form of tax packages, reflecting different factors. A first set of factors were the varying prevalence of the virus, the timing of virus outbreaks and differences in containment approaches. For instance, many of the countries in the Asia-Pacific region that were at the epicentre of the pandemic in late February and early March 2020 have managed to contain the virus earlier, and have subsequently introduced more stimulus-oriented tax measures than other countries that are still grappling with large numbers of infections. The scope of tax packages has also reflected countries' fiscal space and their ability to rely on central bank support, with many developing and emerging economies having had less room to provide fiscal support to households and businesses than other countries. The scope and types of tax support have also depended on the architecture of countries' tax systems, the size of their informal sector and governments' administrative capacities. The likelihood of introducing tax increases has also varied across countries, with tax increases announced so far being concentrated in OECD countries.

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Guidance for policymakers

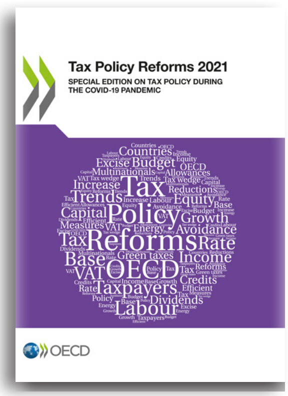
Countries should avoid the premature withdrawal of relief, but increasingly target it to severely affected businesses and households. Maintaining support for highly impacted households is essential to mitigate the unequal impact of the crisis and reduce risks of increased poverty. Similarly, relief should remain available for businesses in severely constrained sectors. Where support is extended, this should be done in ways that avoid storing up problems for the future, for instance by favouring "soft-landing" approaches, such as converting tax deferrals into interest-free tax instalments. For those sectors where support is being withdrawn, this should be done carefully to avoid sudden spikes in tax burdens or "cliff-edge" effects, for instance by progressively phasing out support.

As economies reopen, recovery-oriented stimulus, including through well-designed tax measures, could play a significant role if consumption and investment remain persistently low when containment measures are lifted. To be effective, recovery-oriented tax measures should be:

- **Carefully timed**, as introducing stimulus measures while strict restrictions are still in place could be less effective and could even potentially undermine efforts to contain the spread of the virus if they encourage greater social interactions.
- **Temporary,** to encourage businesses and households to bring their spending and investments forward and limit the impact on public budgets. This may require having clear end-dates or tying the duration of measures to the attainment of certain outcomes (e.g. recovery in certain sectors, a specified level of employment).
- **Targeted at the areas where equity needs and fiscal multipliers are likely to be highest.** For instance, in addition to being more progressive, income support targeted at less affluent households would likely have higher multiplier effects than untargeted measures to support consumption. Some stimulus measures could also be capped to limit fiscal costs.
- **Supportive of labour market recovery and business recapitalisation**. Temporary and targeted tax measures could be envisaged to encourage employers to retain their workers and hire new employees and to help companies rebuild their equity reserves.
- **Aligned with longer-term environmental, health and social objectives**. In particular, targeted support for promising clean technologies could help accelerate the transition to a carbon-neutral economy, especially if it is combined with greater carbon pricing efforts. Stimulus should also be aligned with health and social objectives and avoid regressive impacts.
- **Tailored to countries' specific needs and means.** Stimulus packages will need to be carefully calibrated to take into account country-specific circumstances. For example, factors that will be important include the size of country's decline in output, the evolution of the virus and the nature and duration of the containment measures imposed, as well as their fiscal space.

Future work

Once policymakers have successfully navigated the pandemic, the post-crisis environment will provide an opportunity for countries to fundamentally reassess their tax and spending policies along with their overall fiscal framework. The OECD will be undertaking significant work in the future to help countries reassess their public finance policies to support inclusive and sustainable economic growth.



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