CHAPTER

2 Definition and Types of Amnesties

Definition and Reasons for Amnesties

Definition[3]

A tax amnesty can be defined as *a limited-time offer by the government to a specified group of taxpayers to pay a defined amount, in exchange for forgiveness of a tax liability (including interest and penalties), relating to a previous tax period (s), as well as freedom from legal prosecution.* Amnesties generally fall in two categories: financial and legal. For the former, a tax amnesty implies a reduction (in real terms) of taxpayers' declared or undeclared tax liabilities as established by law.[4] This reduction can be achieved through a variety of measures: for example, through a reduction or cancellation of (1) interest and penalties owed on the underreported or undeclared taxes or (2) tax liabilities (or some combination of these).[5] The latter includes a waiving of civil and criminal penalties.

Tax amnesties can be designed to cover all taxpayers, broad categories of taxpayers (e.g., small taxpayers), or tax types (e.g., corporate income tax, personal income tax). Tax amnesties can also be offered with respect to social security contributions.

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[3]This paper deals with *tax* amnesties, which are understood to include amnesty programs for domestic taxes and social security contributions.

[4]Typically, a taxpayer's declared (or assessed) but unpaid liabilities would be referred to as "tax arrears" and the taxpayer as a "delinquent taxpayer," whereas undeclared or underdeclared liabilities would be referred to as "evaded taxes" and the taxpayer as a "tax evader."

[5]In some cases, only the penalty and interest components of the liability—which often account for the bulk of the overall tax debt—are forgiven, partially or fully. In other cases, the basic tax liability itself is reduced. Alternatively, the tax authority establishes a repayment schedule under which interest and penalties stop accruing altogether, or interest is assessed using below-market interest rates. Such a rescheduling is still an amnesty, because the net present value of the debt is reduced.

Tax amnesties differ from payment installment arrangements. Whereas tax amnesties provide for a reduction of all or part of taxpayers' total tax liabilities (i.e., a reduction in the net present value of the amount of tax, penalties, and interest owed), payment installment agreements maintain, in principle, the net present value of the amount of tax owed. They constitute a contract between the tax administration and the taxpayer whereby the latter agrees to pay, over a longer time period, the total amount of taxes owed, plus interest and penalties, based on ability to pay.

Rationale

Historically, the rationales provided by governments for introducing a tax amnesty program can be classified into three categories: (1) to raise revenue quickly; (2) to increase future tax compliance (e.g., by encouraging taxpayers to declare and pay previously undeclared tax, file tax returns, or register to pay taxes—and stay current on their tax obligations); and (3) to induce the repatriation of flight capital (for reasons that go beyond immediate revenue and tax compliance motives, such as balance of payments, domestic investment, or financial system considerations).

Tax amnesties are sometimes offered in periods of economic crisis, when there is a fear that taxpayers may be unable to meet their various tax liabilities, when there are major currency devaluations, or when there is a change of government. In these cases, as well as many others, the tax burden is often viewed as excessive and poorly correlated with ability to pay. As a result, a new government may introduce an amnesty program to address past or sudden problems of major noncompliance, decrease the stock of outstanding tax arrears, and give taxpayers a chance to resolve their past tax violations and get current on their tax liabilities. Governments also introduce tax amnesties in response to pressures from various interest groups for forgiveness of existing tax debts, declared and undeclared.

In addition to the above, IMF missions have found that in many countries, especially developing and transition countries, tax amnesties are introduced as a result of fundamental weaknesses in the legal framework, management, and operations of the tax administration. Box 1 describes in greater detail some of the legal, procedural, and management problems that can give rise to the introduction of tax amnesty programs in an effort to raise tax revenue in the short term and address different types of noncompliance.

Tax amnesty programs can be introduced all along the tax administration process in an attempt to remedy some of these shortcomings. Examples include amnesties for failure to comply with registration (e.g., to improve the accuracy and completeness of the taxpayer register and incorporate taxpayers engaged in informal economic activities); amnesties for failure to comply with filing and payment obligations (e.g., to raise revenue and increase the

Box 1. Weaknesses in Revenue Administration That Can Give Rise to Tax Amnesties

In many developing and transition countries, despite reforms undertaken to date, the legal framework for tax administration is deficient; it does not provide the administration with the necessary powers to enforce tax collection and it lacks key provisions to encourage taxpayers to comply with their obligations voluntarily. Examples of this deficiency include the following:

- Lack of a fair interest and penalty regime (interest rates and penalties are too high or too low, and are not structured to reflect the severity of different types of infractions);
- Limited ability of the tax administration to obtain taxpayer-related information (e.g., access to third-party or bank information);
- Nonexistence of a well-designed, fair installment payment system (e.g., one that facilitates payment for taxpayers who can show they are financially unable to meet their tax obligations in full, but are willing to pay over a longer period);
- Absence of tax administration powers to enforce collections (e.g., seize bank accounts, physical assets, accounts receivable) and reliance by the tax administration on the courts to carry out this critical function;
- Lack of tax administration powers to "write off" what the tax administration considers to be uncollectible tax debts; and
- Abuse of the appeals system to postpone payment of tax arrears. Taxpayer appeals of the tax administration's decisions or rulings are often costless to the taxpayer and have the effect of immediately suspending or canceling the tax administration's collection enforcement actions. Thus, taxpayers can easily interrupt collection enforcement actions via recourse to the appeals system.

These weaknesses in the legal framework can affect every link in the chain of basic tax administration procedures: taxpayer registration, collection, audit, and enforcement. Specific problems that are observed in many developing and transition countries include the following:

- Taxpayers have high noncompliance rates with respect to their filing and payment obligations (e.g., basic compliance controls are weak and the sanctions and penalty regimes are ineffective);
- The taxpayer register is inaccurate and outdated, and large numbers of potential taxpayers in the informal economy are not registered (related to lack of access to third-party information);
- The installment payment system(s) is poorly designed (e.g., taxpayers are not encouraged to settle their tax arrears by paying installments of overdue tax on their capacity to pay. Many installment payment schemes are difficult to administer; repayment periods are excessively long; interest and penalty structures are inappropriate; and taxpayers are not required to remain current with their new tax obligations); and

Box 1 ***(concluded)***

- There is a large and increasing stock of overdue tax arrears. Often this occurs because the tax administration lacks collection enforcement powers and powers to write off uncollectible tax debts. But this also reflects shortcomings in administrative procedures (e.g., the information on tax arrears is inaccurate; the tax administration does not classify arrears based on their priority or ease of collection and does not take prompt action to recover arrears as they arise; administrative actions are not concentrated on the newer, larger tax debts, but instead on older, smaller tax arrears that are more difficult to collect; and there are too few collection enforcement officers and they lack appropriate skills).

Finally, weak management of the tax administration—including a management team that is unaware of the above-mentioned problems, lacks management information to monitor basic procedures, and does not take action to remedy these shortcomings—can be a major contributing factor to the weak tax administration performance that in many countries has led to the adoption of tax amnesties.

Source: IMF staff.

number of active taxpayers); and amnesties that limit the tax administration's audit powers in exchange for taxpayers reporting previously undeclared income and declaring more accurately and honestly in the future (e.g., to increase revenue).

However, the disconnect between the advertised rationale for and the roots of tax amnesties often leads to the design of amnesty programs that do not address the sources of the problem. As shown in Chapter 4, which discusses in greater detail some of the different types of tax amnesties that various countries have introduced, in many developing and transition countries, amnesties rarely address specific weaknesses in the tax administration's legal framework, procedures, and management—the very issues that contributed to low compliance levels or weak revenue performance in the first place.

Types of Tax Amnesties

A Taxonomy of the Most Common Types of Tax Amnesties

Although the specific provisions of the most common types of tax amnesties have differed widely, they share a common feature: a temporary grace period during which delinquent taxpayers can pay outstanding tax debts or correct other tax law infractions with reduced financial and legal penalties. Amnesties are most often designed to include all taxpayers or large groups of taxpayers, although the amnesty's specific conditions may differ. For example, the

Table 1. Possible Design Features of Tax Amnesties

Who Is Targeted	What Taxes Are Covered	What Is Forgiven	Accompanied by	Other
Unregistered taxpayers	Personal taxes	Interest	Increased enforcement	Duration - One-time - Permanent
Nonfilers	Business taxes	Tax penalties	Increased audit	
Delinquent taxpayers: - Unpaid tax liabilities	Property taxes	Criminal prosecution: - Civil penalties - Imprisonment	Tax reform: - General - Designed, in part, to address non-compliance	Basis: - Legislative - Administrative decree
Evaders: - Nonreported tax liabilities - Underreported tax liabilities	Other	Tax liabilities: - Small amounts - Any amount		

Source: Pellechio (1993).

program may be designed to encourage taxpayers who have failed to file tax returns to file. The focus may be on taxpayers who have filed tax returns but underreported income, or taxpayers who have reported accurately but failed to pay. Table 1 indicates some of the factors that have typically been taken into account in designing the most commonly observed types of tax amnesties.

Other Types of Amnesties

Many countries have introduced amnesties that do not provide for an outright waiver of penalties and sanctions for undeclared or underreported taxes, but that do provide other incentives for taxpayers who have not complied with the tax laws to start doing so. Examples include audit amnesties and legal amnesties.

Audit amnesty programs have varied features. One type provides for a limit on the tax administration’s capacity to audit taxpayers for a certain period as long as they increase the amount of tax paid in present or future periods, or both. The incentive to participate is that taxpayers who “voluntarily” declare previously undeclared taxes will not be audited. Colombia offered such a program in 1998: taxpayers who declared a 30 percent increase in their taxable income for the 1996, 1997, and 1998 tax years would not be subject to an audit by the national tax and customs directorate (DIAN) of their income tax returns for those years. This benefit could be extended to taxpayers who did not file income tax returns in 1996 and 1997.

Another type of audit amnesty is a guarantee against audits of returns filed in future years, but not for past returns. This approach is usually employed on a temporary basis when the tax administration does not have the capacity for adequate audit and enforcement. Portugal offered such a program in 1986: it guaranteed that a corporate taxpayer whose tax liability increased by at least 30 percent would not be audited for the next five years through the standard selection process; taxpayers could nonetheless be audited for serious cause such as suspected fraud. This type of amnesty poses significant problems, not least of which is a strong incentive for companies with greater than the specified increase in tax revenue to limit their tax payment to the minimum required.

Finally, another audit amnesty is a guarantee to the taxpayer that his or her tax returns for earlier tax periods will not be audited as long as his or her most recent tax return is correct. Countries that have introduced this type of audit amnesty include Colombia, the Dominican Republic, and Mexico. The incentive for the taxpayer to participate is that it forbids audits for earlier tax periods. However, the incentive might be weaker than it might seem because, for the audits to be forbidden, the taxpayer will always have to file correctly in the future. Otherwise, the possibility of auditing (all) previous returns will apply once again. On the other hand, strong participation externalities exist for this type of amnesty: the more taxpayers participate in the amnesty, the higher the probability of an audit for those who do not participate in the amnesty (for a given audit capacity of the tax administration). Because the results of this type of measure have not been studied in full, it is difficult to gauge their impact on future compliance and to what extent they have been more or less effective in terms of encouraging taxpayer compliance than more commonly used types of amnesty programs.