



## FISCAL AFFAIRS

# Progressive VAT\*

TECHNOLOGY FOR MORE TARGETED VAT/GST RELIEF

OECD GLOBAL FORUM ON VAT

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Artur Swistak, Deputy Division Chief, IMF FAD Tax Policy 2 Division  
Rita de la Feria, Professor of Tax Law, University of Leeds;

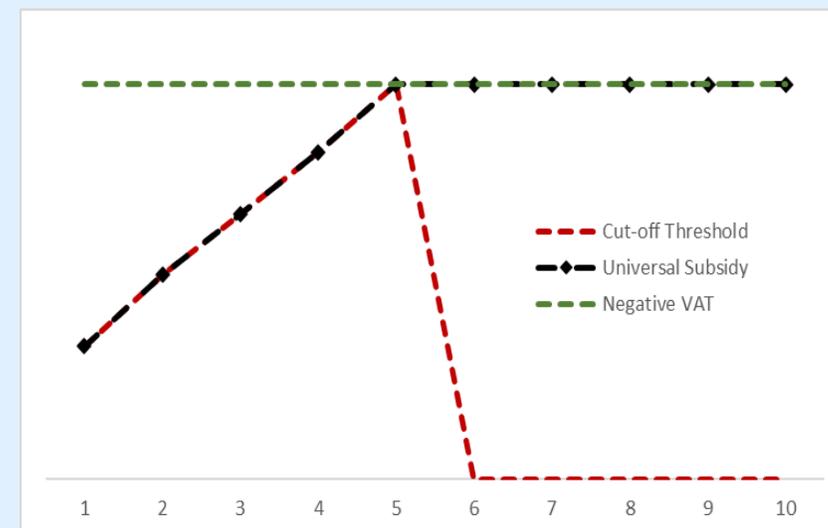
\* IMF Working Paper No. 2024/078, available at: <https://www.imf.org/-/media/Files/Publications/WP/2024/English/wpia2024078-print-pdf.ashx>

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# What is a Progressive VAT?

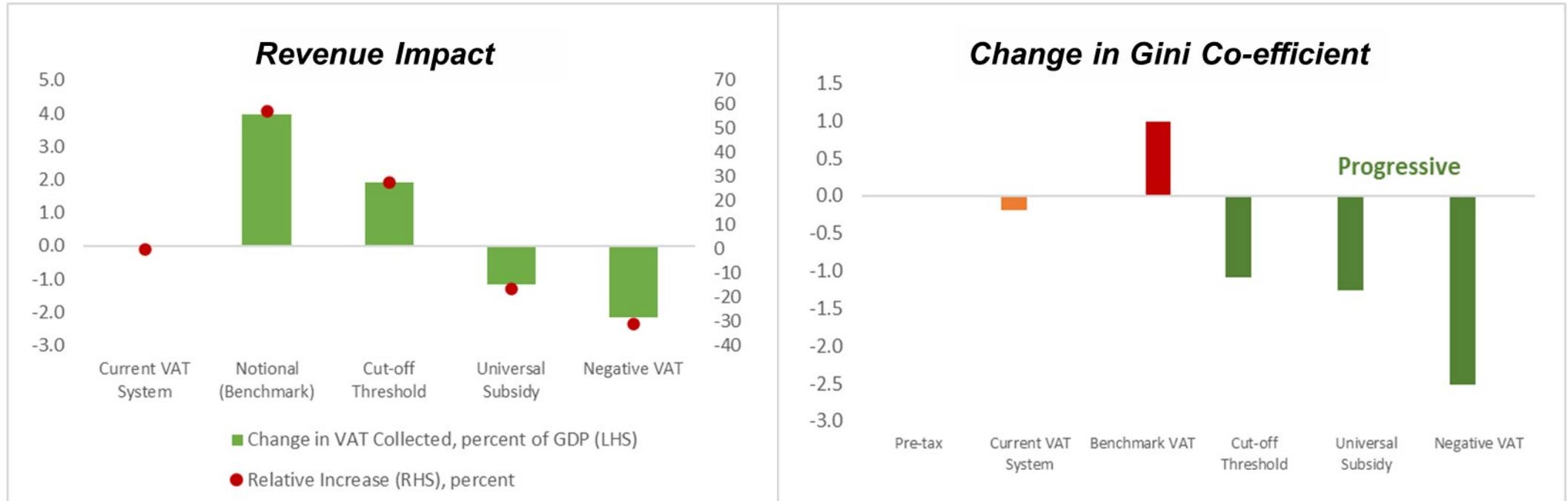
- **Alternative policy response** to addressing (perceived) VAT regressivity, different from:
  - Traditional approach (exemptions)
  - Modern approach (transfers)
- **Progressive VAT concept:**
  - Not progressive *de jure* (no graduated rates), but progressive *de facto*
  - Universal coverage (no special registration)
  - Single rate / no exclusions from the base
  - **VAT compensation in real-time** to low-income individuals (real-time software systems, mobile/digital money)

*Stylized VAT subsidy amount*



***Umbrella concept:** Various possible design options regarding **eligibility, compensation amount, ceilings, tapering, payments, etc.***

# Balancing Revenue and Equity Objectives



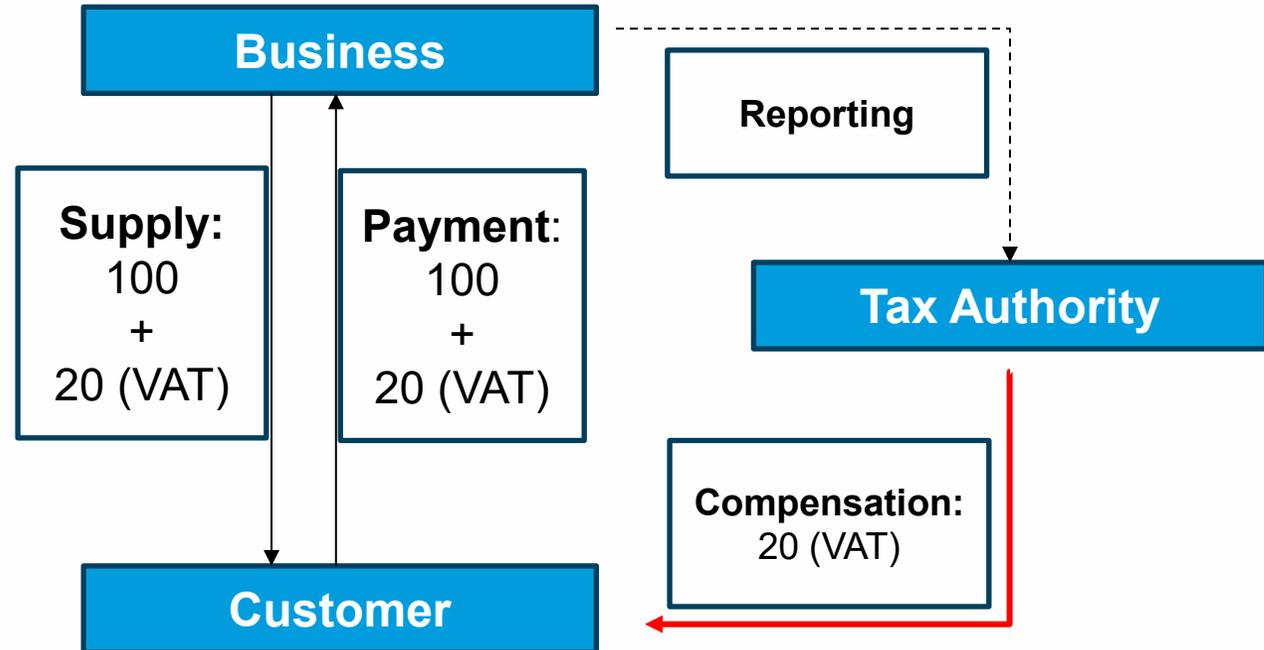
**Actual design needs to balance revenue and equity objectives:** the more revenue is forgone, the higher levels of progressivity can be achieved

# Leveraging Technological Advances

- **Targeting has significantly improved** worldwide, assisted by technology:
  - Most low and middle-income countries have unconditional cash transfer programs (Warwick et al., 2022)
- Use of technology by tax administrations is spreading:
  - **Real-time software systems** – data warehousing – used primarily for anti-fraud purposes
  - **Mobile / digital money** – the impact of the pandemic experience

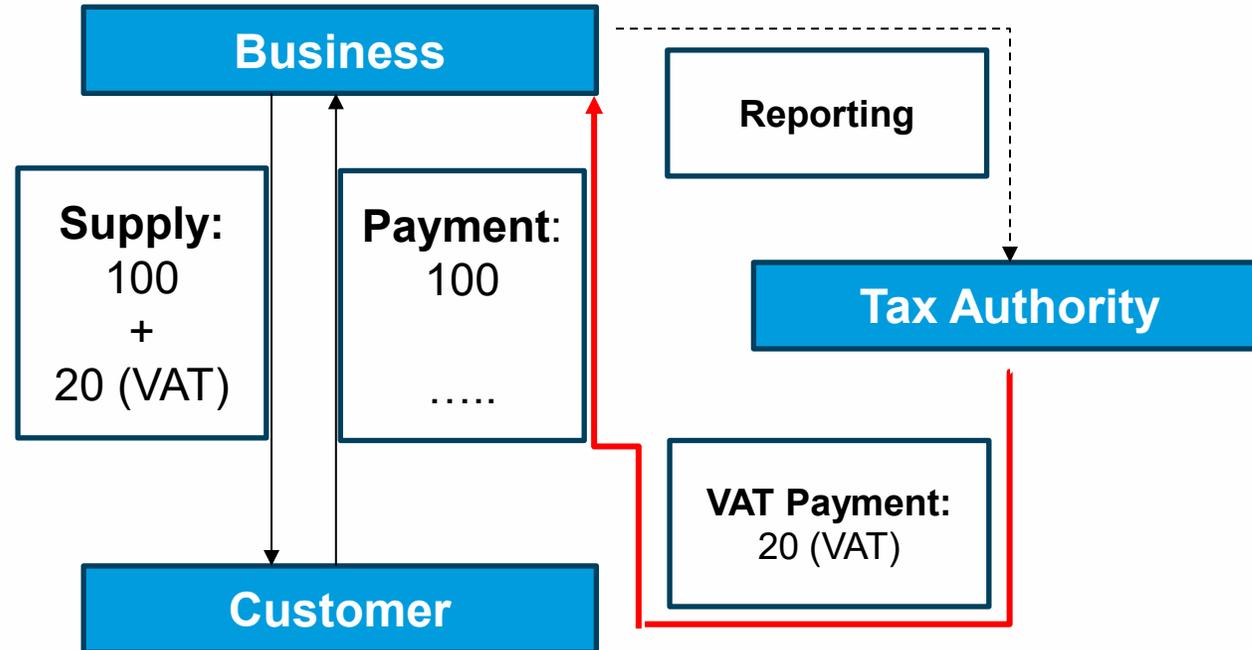
VAT-related Welfare Programs in LATAM	
Argentina	Partial VAT refund on purchases by debit card for retirees, pensioners, and beneficiaries of the Universal Child Allowance
Bolivia	Partial VAT refund for individuals on low incomes
Colombia	VAT compensation for the poorest households
Ecuador	VAT refunds for low-income older individuals and individuals with disabilities for purchase of basic-needs goods / services
Uruguay	VAT refund for households in situations of extreme vulnerability and beneficiaries of the Family Allowance program

# Payment Approaches: Single Payment



- Standard receipt
- Full payment by customer
  - *Higher cash requirement*
- Compensation not visible to businesses
  - *No risk of welfare stigma*

# Payment Approaches: Divided Payment



- Standard receipt
- Partial payment by customer
  - *Less cash required*
- Compensation visible to businesses
  - *Risk of welfare stigma*

# Progressive VAT: Key Characteristics

- Fits “personalized VAT” category, but **emphasis on vertical equity**
  - Horizontal equity could still be addressed if need be
  - Compliance enhancing cashbacks typically universal and flat (though some progressivity induced)
- **Point of sale (real-time, immediate) relief**
  - Not a subjective relief (Traditional VAT or D-VAT proposal)
  - One-step approach (**no deferred compensation / refunds**)
- **Embedded in VAT design**
  - Salient link between VAT base and compensation (tax expenditure)
  - Reduced risk of decoupling two distinct policies: base broadening and transfers
- **Neutral and “invisible” to businesses**
  - Significant efficiency gains; improved pass-through; no welfare stigma

# Main Gains and Advantages of Progressive VAT

- **Political economy gains** – increase acceptability to VAT base broadening, cashflow gains, no welfare stigma
- **Equity gains** – improved income distribution, poverty reduction
- **Efficiency gains** – reduced distortions, no tax cascading
- **Revenue gains** – eliminated ill-targeted VAT reliefs
- **Compliance gains** – reduced informality, increased self-enforcement, lower compliance cost,
- **Trade balance gains** – bias towards domestic purchases

# Limitations and Risks

- Viable option only for countries with real-time VAT invoicing technology
  - not a universal panacea yet
- Privacy risks
  - seemingly not larger than current practices
  - decentralized cloud computing potential remedy
- Fraud risks
  - limited by ceiling, counterbalanced by income taxation
- Shift towards income taxation (consumption-based income tax)
  - issues of optimal design, work incentives, etc.

**Thank you**