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MOTIVES AND CONSTRAINTS IN THE IMPLEMENTATION OF ARGENTINA'S 2017 TAX REFORM

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ABSTRACT

This paper examines the motives, constraints, and sequencing behind Argentina's 2017 tax reform, drawing on the authors' direct involvement in its design and implementation. We document how a large inherited fiscal imbalance, a disinflation program that mechanically raised real pension spending under the pre-existing indexation rule, minority status in Congress, and limited administrative capacity jointly narrowed the feasible policy set. Within those constraints, the reform aimed to be near-revenue-neutral while rebalancing the system toward investment and employment: phasing down corporate rates with dividend taxation and inflation adjustment, reducing the labor wedge at the bottom via a per-worker deduction, rationalizing VAT and excises (including carbon and health-motivated taxes), and coordinating with provinces to cap and de-cascade the turnover tax (ISIB) through a Fiscal Consensus. We trace how coalition politics and sectoral vetoes reshaped the package, why forward guidance and escape clauses were embedded ex ante, and how the 2018 sudden stop, followed by policy reversals, limited the reform's realized growth dividend. We draw four lessons: credibility is a fiscal instrument; provincial coordination beats technocratic perfection; discretionary levers invite rent-seeking; and targeting informality and compliance margins yields higher returns than blunt rate changes. The analysis offers a pragmatic template for tax reform under macroeconomic fragility, federal fragmentation, and state-capacity constraints.

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1 Introduction

In this paper, we aim to shed light on how policymakers interact with the constraints and restrictions that shape policy outcomes. We focus on Argentina's 2017 Tax Reform as a case study that illustrates how political realities, and the inertia of the status quo limit the set of feasible policies. As members of the team of economists responsible for designing the reform, we describe the hidden tensions that underline economic policymaking: from the trade-offs we faced when drafting the initial proposal, to the conflicts, bargaining, and modifications introduced during congressional debate, and finally to our role in implementing the law once enacted.[2]

The Macri administration assumed office in December 2015 confronting a fiscal disequilibrium of unprecedented magnitude that fundamentally constrained the feasible policy space for macroeconomic stabilization. The inherited fiscal position, when subjected to rigorous methodological corrections for accounting irregularities and hidden obligations, revealed a consolidated primary deficit of approximately 6% of GDP and a financial deficit exceeding 8% of GDP (Galiani, 2019; 2020)[3]. These figures substantially exceeded official estimates of 4.5% and 6.1% respectively, highlighting how unreliable fiscal accounting can be, at least to measure the true size of the fiscal burden inherited.

The Central Bank Governor independently established a monetary policy framework, formalized in 2016 with inflation targets declining to reach 5% annually, creating an additional fiscal constraint through Argentina's pension indexation mechanism. The previous mobility formula (Law 26.417) incorporated a complex maximum operator structure (similar to, but more complex, than then better-known UK's triple-lock) that generated systematic upward bias during disinflation periods because the formula was completely tied to activity levels, specifically linking pension adjustments to both wage

[2] The 2017 tax reform bill, the fiscal pact with the provinces, and the pension reform were prepared by the Ministry of the Treasury in collaboration with other departments of the Executive Branch. The Treasury team was led by Minister Dujovne and coordinated by the Secretariat of Economic Policy, the Secretariat of the Treasury, the Undersecretariat of Public Revenues, and the Legal and Administrative Secretariat. The Office of the Chief of Cabinet and the Ministry's Office of the Chief Advisers also participated in the project. Most technical design work on these reforms was carried out by the Secretariat of Economic Policy under Sebastian Galiani, in close collaboration with his chief of staff, Santiago Afonso, and the Undersecretary of Microeconomics, Mariano Tappata. An exception was the financial-assets tax, developed by the Office of the Chief of Cabinet and the Ministry's Office of the Chief Advisers.

[3] The methodological corrections applied to obtain reliable fiscal measurements encompass several critical adjustments: the reversion of foreign exchange control-related tax collections accumulated as forced lending during 2012-2015; the recognition of obligations deliberately deferred in late 2015 to artificially improve fiscal statistics; the incorporation of holdout debt settlement interests; real exchange rate corrections for foreign currency obligations; and the reclassification of Priority Investment Plan expenditures previously recorded as financial assets. As then-Finance Minister Alfonso Prat Gay would acknowledge in March 2016, the initial cash-basis deficit estimate of 3.8% of GDP was subsequently revised to 5.2% of GDP.

evolution and tax collection performance through extensive backward-looking reference periods. The mechanism operated by taking the higher of wage growth or tax revenue growth over multiple semesters, meaning that during successful disinflation episodes, pension adjustments continued reflecting nominal wage increases from previous high-inflation periods even as current inflation declined. This created a perverse dynamic where monetary policy success automatically generated fiscal expansion, as real pension spending increased precisely when fiscal consolidation was most critical for macroeconomic stability.

The administration's initial policy responses paradoxically ran counter to its medium-term consolidation objectives. Reductions in income taxes, the elimination of export duties, and a range of fiscal concessions reflected President Macri's policy priority of lowering the tax burden on productive activities, yet these measures generated immediate revenue losses at a critical moment of macroeconomic stabilization. Simultaneously, the incorporation of the Historical Reparation Program, where the government compensated retirees for past inadequate adjustments, added 0.4% of GDP in pension spending during 2017[4], non-existent in 2015-2016, further straining fiscal resources during the stabilization period. This apparent contradiction between short-term fiscal expansion and medium-term consolidation targets underscores the complex political economy constraints confronting a minority government attempting to advance comprehensive economic reform while maintaining coalition support and addressing historical social debts.

The transition from Alfonso Prat-Gay to Nicolás Dujovne at the end of December 2016 marked a strategic pivot toward more aggressive reform implementation. Dujovne's team began to reduce public expenditures in earnest, implementing the gradual fiscal adjustment program announced at the start of the administration. Within this framework, and taking as given the inflation-reduction targets adopted by the Central Bank, the team quickly realized that it was essential to change the indexation formula for pensions and retirements. Under the existing scheme, disinflation substantially increased real expenditures, rendering the program fiscally unviable. This critical link had not been taken into account when the administration launched its inflation-targeting regime. Had the formula been revised in 2016, when the government implemented the "historical reparation" for retirees, pension spending in 2017 would not have risen as it ultimately did.

President Macri believed that restoring economic growth required a comprehensive tax reform that would not only eliminate the most distortive taxes but also reduce the overall tax burden. Dujovne's team, however, prioritized achieving fiscal equilibrium. Within the framework of the gradualist program adopted to reach that goal, they concluded there was little room to reduce the overall fiscal pressure—at least at the federal level. Their compromise was to propose a fiscally neutral reform at the federal level, focused on

[4] The total cost of disinflation to reach an annualized 5% rate embedded in the pension indexing formula was 1% of GDP in additional annual pension spending.

improving tax design, while simultaneously negotiating with the provinces for a gradual elimination of their most harmful taxes, especially given that provincial governments had benefited from increased transfers at the beginning of Macri's administration. The underlying idea was that a gradual reform preannounced many years in advance—even if it entailed a modest annual fiscal cost—could stimulate growth in the short run by improving resource allocation and attracting foreign direct investment (FDI). In this way, the reforms we analyze in this paper were conceived as complementary to the fiscal consolidation embedded in the disinflation program (particularly pension reform): they aimed to improve the tax system at low fiscal cost, support economic growth essential to the gradualist strategy launched in 2016, and simultaneously satisfy the president's supply-side policy preferences.

Within its gradualist strategy, the Macri administration judged that deep structural reforms required political capital it lacked in 2015 and would not fully accumulate by 2017, but might marshal after a presidential reelection. Following the midterm victory in 2017, Congress approved the tax reform, the fiscal pact with the provinces, and the new pension indexation formula. At that point, as Sebastian Galiani concluded his leave from his U.S. academic post and left government service, Minister Nicolás Dujovne—at President Macri's request—asked him to draft comprehensive pension and labor reform proposals to be submitted in 2020. The sequence reflects a sober appraisal of available political capital and a deliberate staging of the reform agenda to track its anticipated evolution.

The paper is organized as follows. Section 2 sets the macro-fiscal and federal context confronting the incoming administration and clarifies the binding constraints (disinflation with pension-rule feedbacks, minority status in Congress, and administrative limits). Section 3 diagnoses the pre-2017 tax system—its revenue evolution, distortions (ISIB, bank debits/credits), and the role of inflation—while outlining the optimal-tax benchmarks adapted to a high-informality setting. Section 4 details the reform blueprint: corporate income tax, VAT and excises (including carbon and health taxes), payroll-tax relief focused on low wages, capital-income taxation, and the design choices for the self-employed and the super-simplified regime. Section 5 explains the federal strategy—the Fiscal Consensus to cap and de-cascade ISIB and to modernize cadastres and property valuations—plus revenue-sharing and rule-based fiscal anchors. Section 6 recounts negotiations across ministries, provinces, and interest groups, the translation of the Treasury's draft into the Executive's bill, congressional bargaining, and the resulting departures from ex-ante neutrality. Section 7 covers implementation, escape clauses, the 2018 sudden stop, and the aftermath, including partial rollbacks and policy drift. Section 8 develops the political-economy interpretation of these outcomes. Section 9 concludes with actionable lessons on credibility, intergovernmental coordination, discretion management, and targeting the margins that matter for growth and formalization.

2 The context of the reforms

From 1989 to 2015, Argentina was governed primarily by the Peronist party, interrupted only by the brief two-year administration of the Alianza between 1999 and 2001. Yet economic policy shifted markedly with each president: the 1990s leaned toward market orientation, while from 2002 onward the country moved toward a closed economy sustained by a large and growing public sector. By December 2015, per capita GDP had fallen back to the level first reached in 2007 and had been contracting for five consecutive years. The economy was weighed down by dual exchange rates, massive energy subsidies, widening fiscal and current account deficits, and the loss of access to international capital markets. Growth was constrained not only by these macroeconomic imbalances but also by sector-specific policy failures—such as poorly designed pension rules, excessive regulation, and entrenched rent-seeking. Highly inefficient taxes further depressed activity, while a large primary deficit (6% of GDP in 2015) and rigid spending commitments left little fiscal space for necessary corrections.[5]

The new president, Mauricio Macri, leading the Cambiemos coalition, sought to stabilize the economy through a strategy centered on reducing both the fiscal deficit and the size of the public sector, lifting burdensome regulations, and restoring the role of market mechanisms in resource allocation. His administration's first decisive step was to remove capital controls, thereby eliminating the economy's most pervasive distortion. Other reforms, however, would require a more gradual approach and time to take effect.

Argentina is a federal democracy in which sparsely populated provinces are heavily overrepresented in both chambers of Congress—making it one of the most malapportioned national legislatures in the world (Kamahara & Kasuya, 2014; Samuels & Snyder, 2001). For instance, sparsely populated Santa Cruz province (0.6% of national population) holds the same Senate representation as Buenos Aires province (nearly 40% of national population) Because provincial institutions are often captured by entrenched elites (Gervasoni, 2018; Meloni, 2022), most representatives from the smaller provinces come from Peronist backgrounds. Building a congressional majority is further complicated by Argentina's staggered electoral cycle: only one-third of Senate seats and half of the Chamber of Deputies are renewed every two years. As a result, at Macri's inauguration the seven parties that made up the Cambiemos coalition controlled just 19 percent of the Senate and 34 percent of the Chamber of Deputies—well short of the majorities required in both chambers to pass legislation.

As a result, the president pursued a gradual path of economic change, hoping to build political support over time for more ambitious reforms. The Cambiemos coalition gained ground in the 2017 midterm elections, but the slow pace at which Congress is renewed left it short of a majority, with only 33 percent of the Senate and 42 percent of the Chamber of Deputies. This necessitated complex negotiations with dozens of legislators representing

[5] Adjusted for accounting methodology changes — see Galiani (2020).

diverse parties, provinces, and special interests. Still, the midterm outcome strengthened the administration by giving it a clearer mandate and, in turn, fostering greater willingness among parts of the opposition to support much-needed reforms.

Despite these difficulties, by the end of 2017 the government succeeded in passing a comprehensive Tax Reform, together with reforms to the fiscal rules and institutions governing federal–provincial relations (the Fiscal Consensus and the Federal Fiscal Responsibility Law[6]), as well as a partial reform of the pension indexing system. The first two measures aimed at an efficiency-enhancing tax reform to be phased in gradually over five years, covering both federal and provincial taxes, with caps on provincial spending helping to finance the transition. Old-age spending, which in Argentina was far higher than in comparable countries, was expected to decline relative to GDP under the new pension indexing formula, which also helped finance the tax reform. The change ensured that benefits, previously linked to volatile tax revenues, would instead be indexed primarily to inflation (70 percent) and wages (30 percent), thereby reducing volatility while modestly improving purchasing power over time. At the same time, the productivity gains achieved through the tax reform and other simultaneous policy measures would no longer be fully and immediately translated into higher pension benefits, thus creating much-needed fiscal space.

The global trend toward corporate tax rate reduction during 1980-2015 reflects intensified international tax competition for mobile capital (Devereux et al., 2002). This competitive dynamic constrains national policy autonomy, particularly for countries like Argentina seeking to attract foreign direct investment after extended periods of capital controls and macroeconomic instability.

The empirical literature on tax competition effects demonstrates economically significant responses to international tax differentials. Hassett and Mathur (2006) estimate that a 1 percentage point increase in corporate tax rates reduces wages by 0.5-0.6%, suggesting that corporate tax incidence falls substantially on immobile factors. This finding implies that Argentina's above-average corporate tax rates not only deterred investment but also reduced real wages relative to counterfactual scenarios with competitive tax rates.

Argentina's position within Latin American tax competition required careful attention to regional benchmarks. Chile's corporate tax rate of 27%, Brazil's complex but effectively lower rates for many sectors, and Uruguay's aggressive use of tax incentives for specific activities created competitive pressures for Argentina to rationalize its corporate tax structure. The administration's diagnosis that Argentina had become uncompetitive in

[6] Although these were two distinct agreements, because they were negotiated in tandem we will refer to them jointly as the Fiscal Consensus, except where the context requires distinguishing between them.

corporate taxation reflected genuine economic constraints rather than ideological preferences.

The theoretical literature on reform implementation in federal systems emphasizes the difficulty of coordinating changes across multiple jurisdictions with heterogeneous preferences (Weingast, 2009). Argentina's extreme malapportionment exacerbates these coordination problems by amplifying the influence of economically peripheral provinces with preferences systematically divergent from national efficiency considerations.

The median voter in Argentina's federal system represents a province with below-average per capita income and limited exposure to international trade, generating systematic bias toward redistributive policies and protectionist measures rather than efficiency-enhancing reforms. This political economy configuration explains the persistence of inefficient tax structures despite their obvious economic costs.

Gervasoni's (2018) analysis of subnational authoritarianism in Argentina provides additional insight into reform resistance. Provinces with limited economic diversification and weak civil society often develop patron-client relationships between governors and federal legislators, creating stable coalitions resistant to reforms that might reduce federal transfer flows or eliminate rent-seeking opportunities.

The 2017 reform's emphasis on prior negotiation with provincial governors reflects recognition of these political economy realities. Rather than pursuing technically optimal reforms through federal legislation alone, the administration adopted a second-best strategy emphasizing political feasibility through side payments and gradual implementation schedules.

The decision to accelerate fiscal consolidation through tax reform in 2017 reflected the interaction between deteriorating external financing conditions and domestic inflation persistence above target ranges. Argentina's access to international capital markets, restored through the 2016 debt normalization with holdout creditors, faced increasing strain as global monetary conditions tightened and country risk premiums expanded.

The Central Bank's inflation targeting framework faced credibility challenges from persistent fiscal dominance concerns. Financial markets' skeptical assessment of the government's commitment to fiscal consolidation generated risk premiums that complicated monetary policy implementation, creating feedback loops between fiscal performance and inflation expectations that constrained policy flexibility.

As analyzed in detail by Galiani and Afonso (2023), the old pension mobility formula established a complex dual-track mechanism where pension adjustments were completely tied to economic activity levels. The formula operated by calculating two separate adjustment factors and applying whichever generated the higher pension increase: the first track combined tax revenue evolution and wage evolution in equal proportions, weighing

between INDEC salary measurements and RIPTE wage indices, while the second track applied a fixed multiplier to available fiscal resources.

The critical design flaw lay in the extensive backward-looking reference periods stretching several semesters. During disinflation episodes, the wage component continued capturing nominal increases from previous high-inflation periods, while the tax revenue component reflected fiscal collections from earlier quarters when nominal economic activity was expanding rapidly due to inflation. This created a systematic bias where pension adjustments were calculated based on historical high-inflation data even as current inflation rates declined substantially.

When the Central Bank's disinflation program began reducing current inflation rates, these backward-looking mechanisms continued generating substantial real pension increases precisely when fiscal consolidation was most critical. The quantitative impact proved substantial during 2017, when successful disinflation generated approximately 0.3% of GDP in additional pension spending beyond what would have occurred under a contemporaneous indexation system, creating fundamental inconsistency in the macroeconomic stabilization program.

Budget constraint arithmetic revealed the impossibility of achieving sustainable debt dynamics without either accelerated fiscal consolidation or unsustainable reliance on Central Bank financing. The administration's commitment to avoiding monetary financing of fiscal deficits - a key component of the anti-inflation strategy - necessitated front-loading fiscal adjustment despite political costs and short-term output effects.

3 The tax system up to 2017

By 2017, high tax rates on highly mobile bases were generating severe distortions in economic activity. The corporate income tax rate of 35 percent—well above the regional average of approximately 27 percent—, penalized investment and had become uncompetitive after repeated tax cuts abroad. The system also lacked key distortion-mitigating features, such as accelerated VAT rebates on capital goods purchases or inflation adjustments in the corporate tax—even though annual inflation hovered around 25 percent. In their search for easy revenue, provincial governments relied on cascading turnover taxes that discouraged formal transactions and encouraged informality. The resulting heavy fiscal burden translated into widespread labor market informality, which fell most heavily on unskilled workers.

Tax design flaws compounded these distortions through notched rate structures, breaking the VAT chain, segmenting labor markets, and creating large disparities in effective tax rates among similar taxpayers. In addition, many taxes bore the imprint of rent-seeking, with special treatments carved out for particular industries or regions.

Perhaps the most unusual—and certainly one of the most regressive—features of the system by 2016 was its reliance on the so-called “inflation tax,” which accounted for around 2 percent of GDP. Beyond its direct consequences, inflation also undermined the tax system more broadly: it fueled bracket creep in the personal income tax, eroded the real value of fines for noncompliance, penalized investment by preventing inflation adjustment in the corporate income tax and in VAT credits for capital goods, and made it nearly impossible to tax income from capital.

3.1 Foundations of Optimal Tax Theory

Optimal tax theory provides the normative benchmark for evaluating tax systems: design instruments that raise a given revenue while minimizing efficiency costs and achieving distributional aims. The modern canon runs from Ramsey (1927) and Mirrlees (1971) to the comprehensive treatment in Mirrlees et al. (2011). Authoritative surveys such as Mankiw et al. (2009) synthesize the main results, and Boadway (2012) reminds us that first-best prescriptions collide with real-world frictions—administrative limits, political economy, and institutional constraints—that often make second-best the relevant frontier.

A useful organizing distinction—emphasized by Slemrod (1990)—is between the design of a single instrument and the optimization of the system as a whole. The latter must reckon with interactions across bases, general-equilibrium feedbacks, and enforcement technology. Within that system perspective, the Diamond–Mirrlees (1971) production efficiency theorem shows that, under standard conditions (competitive firms, no intermediate-goods taxation, and no other market failures), optimal taxation avoids distorting production; revenue should be collected on final uses and factor supplies with relatively small elasticities. The Atkinson and Stiglitz (1976) result then adds that, if preferences satisfy separability conditions and the government has access to a non-linear income tax, differentiated commodity taxation is generally unnecessary; neutrality across organizational forms and financing margins follows as a corollary of minimizing avoidable wedges.

Modern extensions fold in heterogeneity, information constraints, and behavioral responses. The sufficient-statistics approach surveyed in Mankiw et al. (2009) and the progressive-taxation formulas in Diamond and Saez (2011) make the central prescriptions concrete: target inelastic bases; avoid cascading structures that induce inefficient vertical integration; and keep the tax system neutral with respect to legal form and financing so as not to steer firms or households into privately beneficial but socially wasteful avoidance.

The reach of production efficiency is, however, explicitly conditional. In developing-country settings with limited administrative capacity, high informality, and weak third-party reporting, the relevant trade-offs shift. Best et al. (2015) formalize the core insight: when enforcement is scarce, the revenue-efficiency frontier can dominate the production-

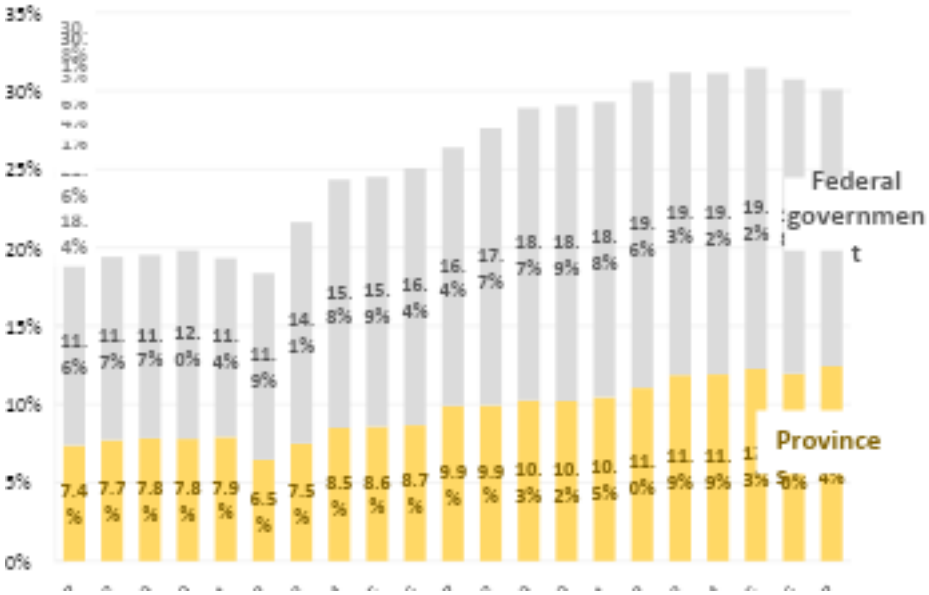
efficiency ideal, making some otherwise “distortive” instruments optimal because they are easier to monitor or harder to evade. Gordon and Li (2009) similarly explain why many low- and middle-income countries tilt toward taxes that piggyback on financial intermediation or border flows and why broad-base VATs outperform turnover-style levies only when invoice-matching and refund administration are credible.

These lessons map directly onto Argentina’s constraints. High evasion elasticities and uneven enforcement shrink the feasible set: they favor taxes that can be anchored in third-party information (e.g., VAT with effective invoice chains; withholding at source) and penalize designs that rely on self-assessment by hard-to-monitor actors. They also raise the welfare cost of cascading turnover taxes (which encourage vertical integration and input self-production), strengthen the case for payroll-tax relief at the bottom of the wage distribution where formalization elasticities are largest, and underscore the value of inflation adjustment to preserve neutrality across financing choices in high-inflation environments. In short, once administrative reality is taken as a constraint rather than an afterthought, optimal-tax principles do not disappear; they re-rank policies. Production efficiency remains a north star, but revenue efficiency and enforceability determine the navigable route.

3.2 Evolution of tax revenues

By 2017, Argentina's tax structure reflected the cumulative impact of uncoordinated, ad hoc changes driven largely by the government's growing financing needs. The tax burden - measured as the combined collections of the national and provincial governments relative to GDP- had climbed from about 19 percent to 31 percent since the regime shift of 2002 (Figure 1). This twelve-point increase excludes the inflation tax, meaning the true burden was even higher during 2007–2017, when annual inflation averaged 26 percent. The distortions created by this evolution fueled demands for reform, which the Cambiemos administration sought to address.

Figure 1 — Tax burden as a % of GDP by recipient level of government.



Note: *Net of reimbursements to exporters, the tax burden is presented by the level of government that is the final recipient of the funds collected. It excludes national taxes not collected by AFIP (such as the Special Tobacco Fund, electricity surcharges, and the Air Ticket Tax), as well as revenues raised directly by municipalities.*
Source: *Ministry of Finance.*

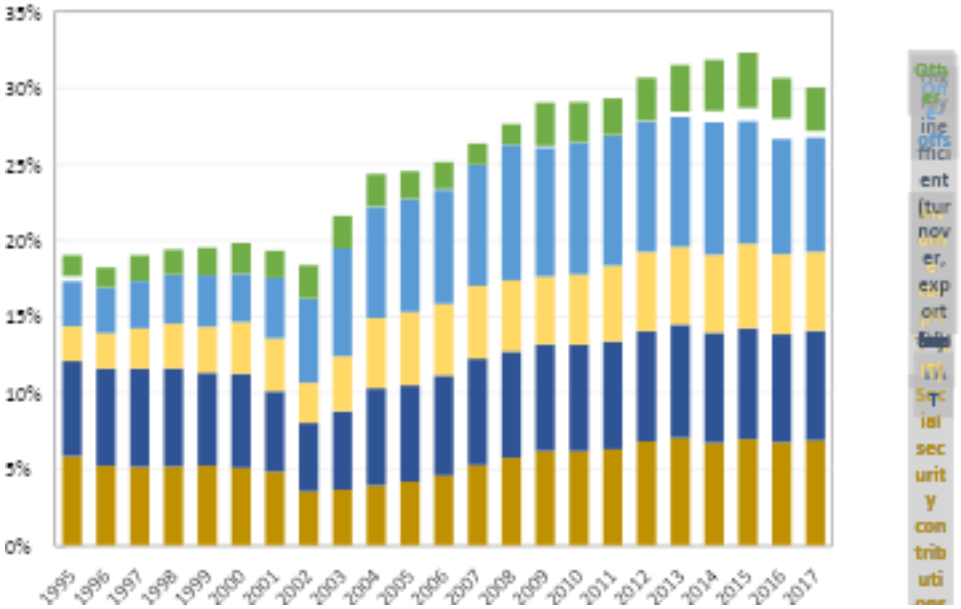
During the 1990s, the tax-to-GDP ratio remained relatively stable at under 20 percent. Beginning in 2000, however, two distinct episodes drove revenues to higher levels. The first came between 2000 and 2004, when the ratio rose by 5.4 percentage points with the introduction of high-yield emergency measures such as the tax on bank credits and debits ("cheque tax") and new export taxes, especially on the agricultural sector. The second episode, roughly spanning 2006 to 2015, added another 7.3 points of GDP. This time, no major new taxes were introduced; instead, collections grew through rate hikes in existing

levies—including the provincial turnover tax ("ISIB"), stamp duties, export taxes, and the expansion of the personal income tax along both the intensive and extensive margins.[7]

The increase in the tax burden during the first two decades of the century was disorderly and inefficient, as shown in Figure 2. Between 1998 and 2015, the tax-to-GDP ratio rose by 13.7 percentage points, including the estimated contribution of the inflation tax. Roughly half of this increase came from highly inefficient or inequitable sources, such as cascading turnover taxes and the inflation tax itself (Table 1). Over the same period, revenues from the tax on bank credits and debits rose by 1.7 points of GDP, while provincial levies—mainly ISIB and stamp duties—added another 2 and 0.1 points, respectively.

[7] Agricultural export taxes were introduced by Decree 310/02 in February 2002, initially set at 10 percent for wheat and corn and 13.5 percent for soybeans and sunflowers. Just two months later, in April 2002, the rates were raised by 10 percentage points across the board, while soybean and sunflower meal and oil were taxed at 20 percent. Beginning in 2007, export taxes on cereals and oilseeds were increased further, eventually reaching 25 percent for corn, 28 percent for wheat, 32 percent for sunflower, 35 percent for soybeans, and 32 percent for soybean by-products—an ill-conceived attempt at industrial policy. In December 2015, with the change in government, export taxes on wheat, corn, and sunflower were eliminated, and the soybean rate was cut immediately by 5 percentage points. The Macri administration also established a schedule of gradual monthly reductions of 0.5 percentage points, aiming to bring the soybean export tax down to 18 percent by December 2019. This trajectory, however, was interrupted and partly reversed in response to the 2018 sudden stop.

Figure 2 — Tax burden as a % of GDP, by tax.



Note: *"One-offs" (extraordinary taxes) include revenues from voluntary disclosure programs and personal income tax withholdings on foreign exchange and tourism services purchases; these withholdings are deducted from income tax revenues. The group of distortionary taxes covers the tax on bank credits and debits, ISIB, stamp duties, the alternative minimum corporate tax on assets, trade taxes, and real estate transfer taxes. National taxes not collected by AFIP are also included.*
Source: *Ministry of Finance.*

Table 1 — Changes to the tax-to-GDP ratio, 1998-2015

	1998	2015	Δ 98-15 (pp)
Total	19.4%	33.1%	13.7
(+) Net ordinary taxes	19.4%	32.0%	12.6
(+) "Inflation tax" [1]	0.0%	2.0%	2.0
(-) Extraordinary taxes [2]	0.0%	0.9%	0.9
Nation [3]	11.7%	20.6%	8.9
Provinces [3]	7.7%	12.5%	4.8
Highly inefficient taxes [4]	3.2%	8.2%	5.0
PIT + social security	4.3%	10.3%	6.0
VAT, CIT, and others	11.9%	14.6%	2.7

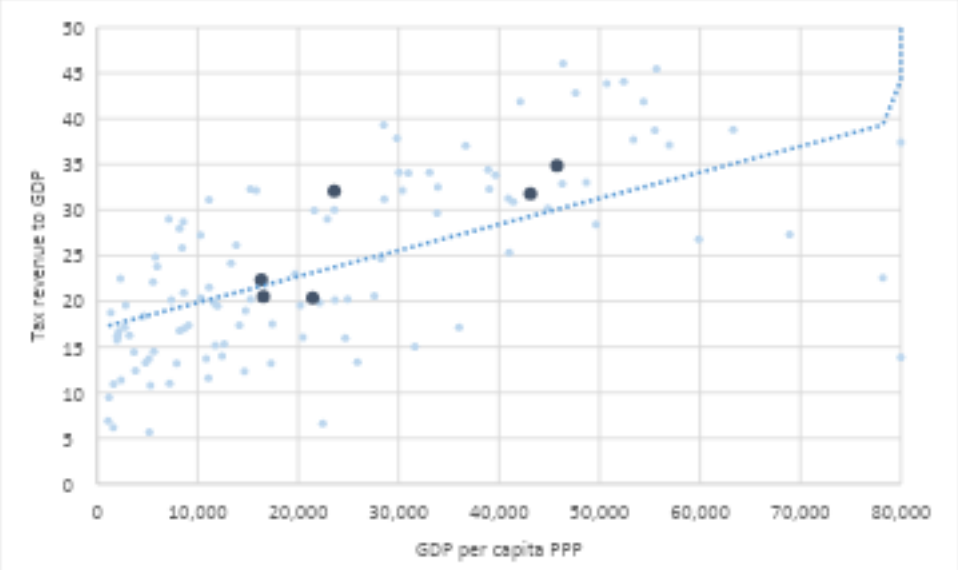
Note:
[1] The inflation tax is calculated as the previous period's real balances (monetary base over GDP) multiplied by the inflation rate.
[2] "Extraordinary taxes" include tax regularizations not assigned to specific taxes and temporary revenues from capital-levy like PIT withholdings on foreign exchange and tourism service purchases; amounts withheld between 2012 and 2015 were refunded to taxpayers in 2016.
[3] Tax resources are classified according to the recipient of funds, not by the authority responsible for collection or legislation.
[4] Distortionary taxes include the tax on bank credits and debits, ISIB, stamp duties, the alternative minimum corporate tax on assets, trade taxes, and real estate transfer taxes. It does not include the "extraordinary taxes" nor the "inflation tax".

Source: Ministry of Finance.

3.3 General tax structure

Overall, tax revenues in Argentina stood about seven percentage points above the Latin American average at the time of the reform (see Figure 3). Given the country's high levels of evasion, however, the effective burden on compliant taxpayers was even greater. In fact, Argentina recorded the second-largest VAT gap in Latin America and the third-largest CIT gap in 2016–2018 (Longinotti, 2022). While aggregate revenues were only about six percentage points below the European average, the true burden on those actually paying taxes was likely higher than in Europe, precisely because of Argentina's lower compliance rates.

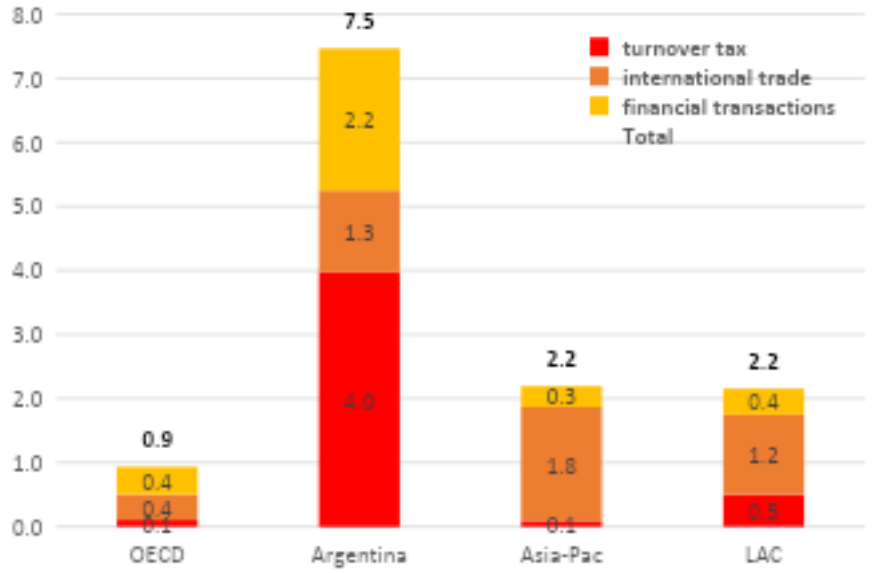
Figure 3 — Tax revenue to GDP by income level, 2017.



Sources: IMF WEO October 2023, OECD GRS 2023.

Argentina's tax structure relies heavily on transaction taxes, particularly distortive turnover-type levies. Revenues from these taxes amounted to roughly 7 percent of GDP more than the OECD average and about 6 percent more than in Latin America and the Caribbean or Asia-Pacific countries (Figure 4).

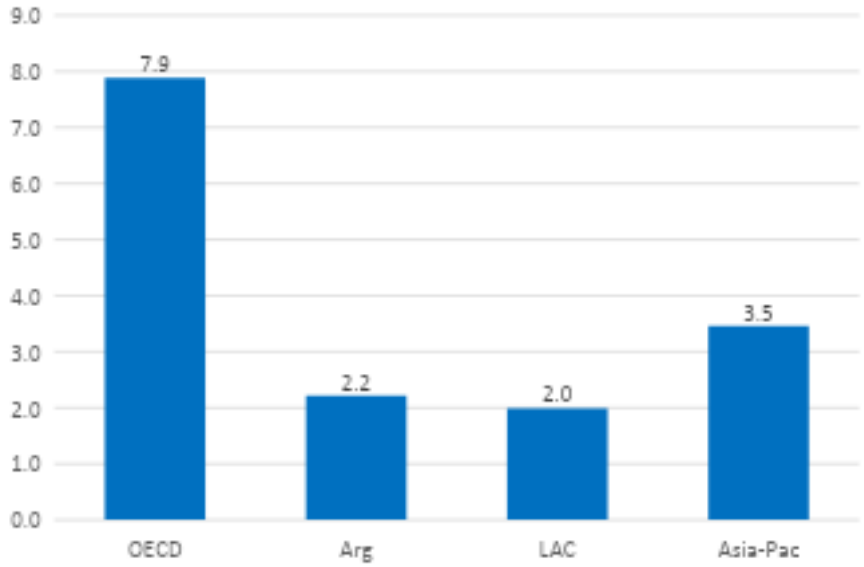
Figure 4 — Highly inefficient tax revenue as a % of GDP, 2017.



Source: *OECD Global Revenue Statistics Database. See Table 1 Note [4].*

On the flip side, compared with countries that devote a similar share of GDP to government spending (such as the OECD average), Argentina collects about 6 percent of GDP less from the income tax (Figure 5). This shortfall reflects a mix of factors: a very high non-taxable income (NTI), broad exemptions for capital income, widespread avoidance, preferential treatments, and other loopholes. This imbalance is a defining feature of Argentina's tax system. The state has struggled to raise revenue through efficient and transparent taxes, instead relying on opaque, hidden, and highly distortive instruments—at the cost of lower productivity and slower growth. A similar pattern is evident at the provincial level, where over the past two decades direct property taxes have been eroded and replaced with cascading turnover taxes.

Figure 5 — Taxes on income, profits and capital gains of individuals as a % of GDP, 2017.



Source: *OECD Global Revenue Statistics Database.*

3.4 Provincial taxes

Argentina's tax system by 2017 exhibited multiple characteristics antithetical to optimal taxation principles, reflecting the interaction between federal institutional arrangements and a development model emphasizing import substitution over export competitiveness. The system's fundamental pathology derived from systematic penalization of activities with comparative advantage through export taxes while subsidizing inefficient domestic production through cascading provincial taxes and regulatory protection.

The provincial gross income tax (*Impuesto sobre los Ingresos Brutos*, ISIB) constitutes the most economically distortive element of Argentina's tax architecture. Unlike VAT systems that achieve production efficiency through destination-based taxation with border adjustments, the ISIB operates as a gross receipts tax imposed at each production stage without credit mechanisms for taxes paid on inputs. This generates powerful incentives for vertical integration to avoid repeated taxation, creating allocative distortions that reduce aggregate productivity and limit scale economies.

Between 2002 and 2015, political competition revolved around expanding public spending, which in turn drove up the provincial tax burden. Provinces increased their gross income tax (ISIB), a non-salient cascading turnover tax, as well as their stamp duties. ISIB rates were extended to exports, and provinces set higher rates on sales by out-of-province vendors—creating de facto internal customs and maximizing inefficiency. Successive reforms also eroded salient land and property taxes, further reducing overall efficiency. Provinces acted without coordination, producing a patchwork of rates applied to the same tax base. Each jurisdiction also introduced its own withholding mechanisms, adding significant compliance and financial costs for taxpayers.

Beyond the well-known inefficiencies of cascading taxes (Keen, 2013), Argentina's provincial turnover tax introduces additional distortions through a particularly intricate system of administration. In Argentina's federal context, 24 separate ISIB systems with different rate structures, exemptions, and administrative procedures further fragmented the national market through regulatory balkanization. Tax rates differ across provinces, and the tax base must be apportioned between the jurisdictions of production and consumption. This complexity necessitates a centralized clearing mechanism—the Multilateral Agreement—to manage interprovincial transactions. Further complicating the landscape, provincial governments have adopted aggressive withholding and collection regimes. These have transformed the system into a bureaucratic labyrinth for taxpayers, driving up compliance costs and rendering dispute resolution with tax authorities both slow and onerous.

These problems greatly increase compliance costs for taxpayers. Bureaucratic hurdles to obtain refunds for incorrect or excessive withholdings have created large balances in taxpayers' favor that are difficult to recover and quickly lose value in an inflationary environment. As a result, effective tax rates are higher than the legal or nominal rates. This has become a major obstacle to market competition, since compliance and financial[8] costs now represent a significant barrier to entry for small and medium-sized firms seeking to operate in new jurisdictions.

Secondly, by 2015 competition for tax revenues had led many provinces to impose higher rates on firms not established within their borders, effectively creating an "internal customs" system. This distorted firms' location decisions, encouraging the concentration of production and consumption in the most populated jurisdictions. Given the prevailing rate structure and the distribution of consumers, it was only natural for companies to concentrate their plants in those markets.

The federal coordination problem exhibits classic common-pool characteristics identified in the fiscal federalism literature (Rodden, 2006). Provincial governments, particularly those with limited economic bases, face incentives to maximize transfers from the federal coparticipation system while imposing locally optimal tax rates that ignore spillover effects

[8] Amounts withheld were systematically above assessed taxes during this period.

on neighboring jurisdictions. The constitutional assignment of broad tax powers to provinces, combined with federal transfer mechanisms based on relative need rather than fiscal effort, creates moral hazard in provincial fiscal management.

Meloni's (2022) analysis of Argentine federalism identifies systematic biases favoring smaller provinces through malapportioned representation and transfer formulas. This political economy configuration generates coalitions supporting inefficient tax systems, as representatives from economically marginal provinces benefit from federal transfers financed by distortive national taxes while maintaining autonomy over locally imposed taxes that primarily affect mobile capital and labor.

A consensus mechanism was needed, which addressed the fundamental coordination problem in Argentine federalism by creating explicit linkages between federal tax reform and provincial policy adjustments. Rather than imposing uniform solutions, the agreement allowed flexibility in implementation timing and methods while establishing binding commitments to achieve specified outcomes.

The design ought to incorporate numerous side payments to secure pivotal votes. Negotiating exemptions for specific sectors to address concerns from legislators representing affected constituencies. This targeted approach can prove essential for achieving provincial support. While maintaining flexibility on second-order taxes, the government ensures achieving macroeconomic objectives, contrasting with previous failed reform attempts, where the central government maintained rigid positions on all aspects of proposed legislation.

3.5 Taxes on labor and personal income

Structural changes in the labor market following the 2002 regime shift fueled strong growth in both social security contributions and the personal income tax. Social security revenues rose from 4.8 percent of GDP in 1998 to 7.1 percent in 2017, largely because of increases in formal employment and real wages, especially up to 2011 (Blanco et al., 2019). This expansion occurred despite already high statutory rates—the highest in Latin America (OECD et al., 2016)—and particularly heavy burdens on low-wage workers (Alzúa & Pacheco, 2021). Personal income tax receipts also grew for similar reasons, but their rise was amplified by policy choices that expanded the base on both the extensive and intensive margins. The marginal rate schedule, however, remained unchanged between 2000 and 2017, despite cumulative inflation of more than 2,100 percent, resulting in severe “bracket creep.” Standard deductions also eroded in real terms, with significant year-to-year volatility driven by political considerations (Afonso, 2022).

The personal income tax became one of the most contentious issues during the 2015 presidential election, largely due to the severe distortions introduced by earlier politically motivated reforms (Afonso, 2022; Tortarolo, 2018; Tortarolo et al., 2019). All major candidates—including both Peronist contenders and Mauricio Macri—pledged to exempt all

wage income from the tax, a move that would have effectively restricted its scope to high-income independent professionals and sole proprietors. However, the gravity of the fiscal crisis rendered this promise unfeasible. In the first two months of the new administration, a partial reform was enacted by decree under delegated legislative powers. While this reform addressed the most glaring horizontal inequities in the existing tax structure, it did so at the cost of massively expanding the number of taxpayers—by several hundred thousand.[9]

Throughout 2016, Cambiemos struggled to find politically acceptable ways to backtrack on its pledge to eliminate the income tax on wages. The opposition, for its part, continued to demand the full elimination—or at least a substantial reduction—of the tax. The standoff culminated in a contentious congressional debate in December 2016, which ultimately produced a negotiated compromise with the Peronist opposition. The Executive's original proposal was significantly amended in the process.

In December 2016, Law 27,346 introduced modifications to the income tax that partially addressed its most pressing flaw: the outdated marginal rate schedule. Although the schedule was updated, the adjustment fell short of what was necessary or desirable to establish a sufficiently gradual income gradient. Basic deductions, meanwhile, remained roughly constant in real terms. The reform also introduced new deductions—such as those for high-income retirees and workers in Patagonia—that were difficult to justify on either equity or efficiency grounds. At the same time, it eliminated outdated deductions for dependents like grandparents, grandchildren, and sons-in-law, which had lost relevance with the expansion of the social safety net.

Equally significant, the reform established that deductions, the rate schedule, and all other tax parameters would henceforth be indexed to the previous year's inflation—marking the most substantial adjustment of the income tax system to high inflation since the 1980s. However, it "froze" the system with high deductions and a marginal rate structure that remained overly steep. The reform came at a high fiscal cost—reducing personal income tax revenues by 0.7% of GDP—precisely when the administration needed to shrink the fiscal deficit, not expand it. And despite this cost, the improvements to the tax design were limited. In the end, the government accepted the compromise not because it offered a sound policy solution, but because it allowed the issue to be politically neutralized.

Unfortunately, given the political and fiscal costs of the 2016 reform, the administration ruled out another major overhaul of the personal income tax in the broader reform effort the following year. As a result, the 2017 agenda left the personal income tax largely untouched, incorporating only minor adjustments. The government had already spent significant political capital on the issue and absorbed a substantial revenue loss, leaving little room for further change. Indeed, when the team led by Minister Dujovne attempted to

[9] Eliminating horizontal inequities without increasing effective tax rates would have required setting the non-taxable threshold at a very high level—substantially reducing the tax liabilities of inframarginal taxpayers and resulting in significant revenue losses.

reopen discussions on changes to the personal income tax in 2017 with the non-Kirchnerist Peronists—a group with whom the Macri administration had managed to reach agreements, albeit always at a high fiscal cost, in order to legislate—they insisted that it had been agreed during the 2016 reform that the personal income tax would not be part of the 2017 reform.

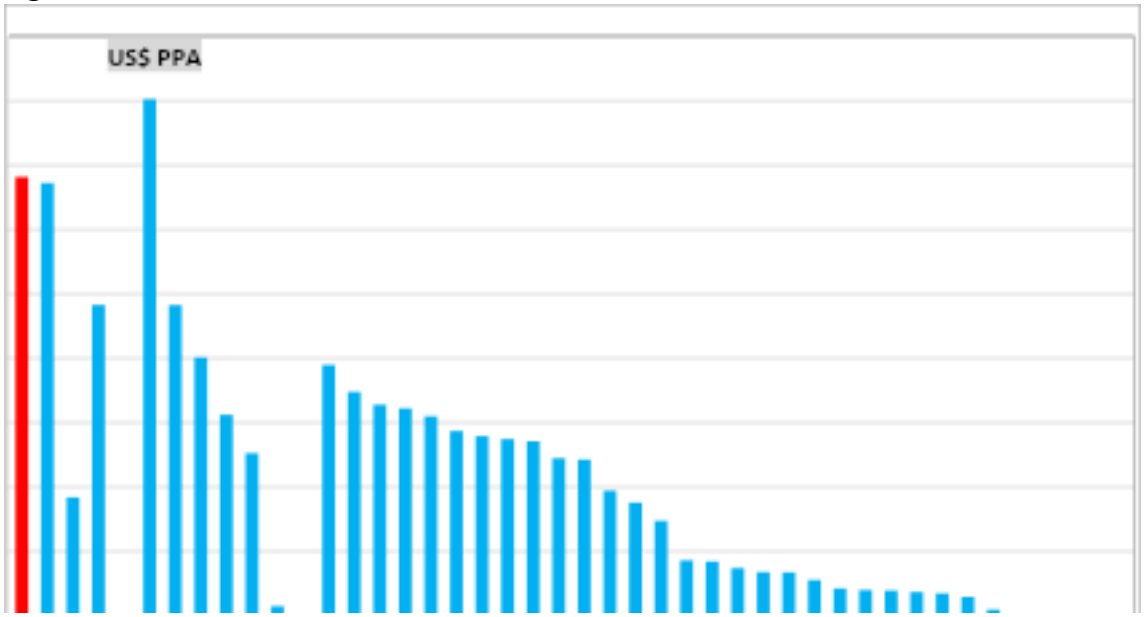
Personal income tax collections in Argentina are lower not only than in developed countries but also compared with peers at similar levels of development. The primary reason is that the tax falls on a relatively narrow share of the population. As shown in Figure 6, Argentina's non-taxable income threshold ranks among the highest in the world. The counterpart to this narrow base is a steep marginal rate structure: once taxpayers fall within the system, rates escalate rapidly. This burden weighs particularly heavily on the self-employed, whose deductions are more limited than those available to wage earners—though still comparatively generous by international standards.[10]

Personal income tax revenues in Argentina have stagnated since around 2010. Since then, the political system has struggled to expand the tax on either the extensive or intensive margin. Successive, often highly contentious reforms and counter-reforms -such as the one in 2016- have reflected the deep political sensitivity surrounding the tax. On two occasions prior to 2016, Peronist administrations introduced highly distortionary reforms aimed at exempting lower-wage earners, which resulted in extremely high effective marginal tax rates for those remaining in the tax net[11]. The same pattern repeated in 2021 under another Peronist government (see Afonso, 2022). Then, in 2023, under pressure to deliver a campaign success, the administration once again dismantled the tax, this time to such an extent that only around 90,000 high-income wage earners remained liable.

[10] The social contribution burden for independent workers in Argentina is significantly lower than for salaried employees. These workers typically pay fixed monthly amounts equivalent to the contributions and taxable base of roughly half the minimum wage. This arrangement is also highly unusual by international standards. In most countries, self-employed individuals face social security contributions that are broadly comparable to those of employees, both in terms of rates and the income base on which they are assessed.

[11] Which are also the taxpayers most reactive to taxation.

Figure 6. Personal income tax. Non-taxable income[12] in USD PPA, 2016.



Source: *Ministry of Finance based on OECD (2016), SIPA.*

3.6 Personal income tax on capital income

One important reason for Argentina's comparatively low personal income tax revenues is that most forms of capital income—such as interest and capital gains on domestic financial assets including bank deposits, public and private debt instruments, and equity—were exempt from the tax. This stood in contrast to standard practice not only in developed countries but also in Latin American peers such as Brazil, Chile, Colombia, Peru, Mexico, and Uruguay. In Argentina, returns on bank deposits, debt instruments, mutual funds, dividends, and capital gains on stocks and real estate were excluded from the PIT base. Instead, the tax was primarily levied on labor income, earnings from nonfinancial investments, and income derived from assets held abroad.

3.7 Payroll taxes

Argentina combines a high share of informal workers with the highest pension contribution rates in Latin America, alongside design features that generate significant distortions (OECD et al., 2016). For administrative reasons, the country sets minimum tax bases that result in high effective tax rates for low-skilled, part-time employees. By contrast, most other countries' tax systems aim for zero or even negative effective tax rates for the lowest-income workers, who typically display higher taxable income elasticities due to both avoidance and real behavioral responses. At the same time, Argentina's public sector maintains the super-simplified regime as a parallel, much cheaper mechanism for registering employment.

[12] Non-taxable income.

Table 2 — Mandatory social security contributions and other tax-wedge-like concepts.

Concept	Employer	Employee	Total
Old age, disability, and child benefits	16.0%	11.0%	27.0%
Old age health insurance	2.0%	3.0%	5.0%
Health insurance (active workers)	6.0%	3.0%	9.0%
Employment programs	1.5%	-	1.5%
Mandatory public total	**25.5%**	**17.0%**	**42.5%**
Mandatory life insurance	Typically 0-3% depending on industry		
Occupational risk insurance	1-17%, typically around 3%, depending on industry		
Union fees	Typically 2-3% depending on industry		

Source: *Ministry of Labor (https://argentina.gob.ar/trabajo/buscastrabajo/conocetusderechos/salario, accessed 2024-02-16).*
Note: *these are the headline and modal rates. There is, however, a wide variety of preferential treatments based on industry, location, company, and worker characteristics. Legal rates vary widely as a result.*

It should be noted that the largest contributor to Argentina's abnormally high labor costs is not its (also unusually high) payroll taxation but rather the employment regulations, which by 2017 combined the expectations of European-style protection with the pervasive rent-seeking practices characteristic of a Latin American economy.

3.8 Super-simplified tax

Two main factors explain the adoption of simplified tax regimes in middle-income countries: the need to drastically reduce compliance costs by simplifying general taxation, and the need to tailor tax rates to taxable income and labor supply elasticities, given both real and evasion responses, particularly among the self-employed. In Argentina, this rationale led to the creation of the *super-simplified tax*[13]. By 2017, some 3.5 million individuals were registered under this scheme, typically facing an effective income tax burden ranging from 0 to 5 percent, while also gaining access to subsidized health insurance, subsidized pensions, child allowances, and other benefits. Taxpayers are assigned to one of eight categories based on gross income declared in the previous year and are reclassified every six months. Instead of paying the personal income tax, VAT, health, and pension contributions separately, they make a single fixed monthly payment—at a vastly lower effective tax rate than either a general-regime self-employed worker or a formal dependent employee. For comparison, the combined effective PIT and social security contribution rate for formal dependent workers amounts to around 49 percent of total compensation costs to the firm, once employer contributions are included.

Table 3 — Super-simplified regime categories for service providing workers, 2017.

		Effective rates by component			
Category	Max yearly gross revenues as multiples of wages [1]	Tax	Old age and disability	Health insurance	Total
A	0.3	1.0%	4.3%	6.0%	11.2%
B	0.4	1.2%	3.1%	4.0%	8.4%
C	0.5	1.6%	2.6%	3.0%	7.2%
D	0.8	1.8%	1.9%	2.0%	5.6%
E	1.1	2.5%	1.6%	1.5%	5.6%
F	1.4	2.8%	1.4%	1.2%	5.3%
G	1.6	2.9%	1.3%	1.0%	5.2%
H	2.3	4.8%	1.0%	0.7%	6.5%

Notes: *[1] Max yearly gross revenues expressed as multiples of the average yearly formal dependent wages of stable workers (RIPTE).*

Beyond the distortion created by allowing workers to register under multiple regimes with sharply different effective tax rates, the design of the super-simplified tax raises several additional concerns. Its notched structure generates substantial bunching at the thresholds, particularly in the highest category, where exceeding the limit entails a significant loss of after-tax income. Moreover, the sheer number of participants makes effective auditing virtually impossible—a fact well known and actively exploited by taxpayers.

[13] "Monotributo" or "régimen simplificado".

3.9 Inflation tax

Inflation functions as an *unlegislated tax* that enables the government to finance part of its fiscal deficit without formally creating new taxes or raising existing rates. In Argentina, the dynamics between 2007 and 2015 reflected a persistent excess supply of money: inflation rose sharply because the government printed money beyond the demand for real balances, with the aim of covering an expanding fiscal deficit. This excess liquidity generated mounting inflationary pressures, which in turn required further monetary issuance by the central bank, reinforcing the cycle.

Inflation generates distortions at both the macroeconomic and microeconomic levels. Yet one of its most damaging features is its asymmetrical impact on households. Lower-income families, with zero or very limited savings, see their entire wages held as monetary balances throughout the month, fully exposed to the erosion of purchasing power caused by inflation.

Argentina's political dynamics have historically driven spending levels that far exceed what taxes alone can sustain. The resulting gap has been financed either through debt issuance—periodically resolved through restructurings and haircuts—or through monetary expansion. This pattern has fueled chronic inflation, which by the end of 2023 had reached an annualized rate of 1,427 percent. Since 2003, the last year of price stability, inflation has followed an inexorable upward trajectory, interrupted only by brief and fragile respites.

3.10 Other distortions created by inflation

High inflation has distorted the functioning of Argentina's tax system in multiple, interrelated ways. Most directly, tax parameters—such as income tax deductions, thresholds, caps, and fines—experience large real fluctuations due to imperfect indexation. One of the few surviving provisions from the 1990s institutional framework, which had successfully ended the hyperinflationary era and ushered in a decade of price stability, was the prohibition of indexation. Although severely weakened, this prohibition remains formally in place. Over time, successive governments resorted to alternative mechanisms to mitigate the impact of inflation: first through ad hoc adjustments, later through annual updates, and eventually through more frequent legislative changes or other convoluted formulas that avoided explicit CPI indexation while nonetheless referencing price levels indirectly. The incentive to rely on such opaque methods was compounded by the manipulation of official inflation statistics between January 2007 and December 2015 under the Kirchner administrations. Still, in a context of high and volatile inflation, any backward-looking indexation mechanism produces significant real variability, which directly feeds into distortions in tax parameters.

Although "bracket creep" is a well-known phenomenon, Argentina's personal income tax offers a striking case study. Between 2000 and 2017, the marginal rate schedule was left

unchanged despite cumulative inflation of more than 2,140 percent. As a result, by the end of this period nearly all taxpayers were either exempt or subject to the top marginal rate of 35 percent. From 2017 onward, the schedule was updated annually according to changes in nominal wages between October of year *t–2* and October of year *t–1*, in order to allow time for publication of the necessary statistics and regulations. This mechanism, however, introduces considerable real volatility: since 2002, the average absolute difference in year-on-year inflation rates for October has been 12.1 percentage points, rising to 18.2 points since 2015. Added to this is the volatility of real wages themselves, which have fluctuated between –13 percent and +21 percent on an annual basis over the past two decades.

What happened to deductions is even more striking. Although their nominal values were periodically adjusted, these updates consistently lagged behind inflation, producing a clear long-term downward trend marked by significant variability. This erosion in the real value of deductions gradually expanded the personal income tax to a larger share of the population, though coverage still remained low relative to Argentina's level of development and international benchmarks. Parameter adjustments were often not debated in Congress but instead enacted through executive decrees under delegated legislative powers. The politically sensitive nature of drawing vast numbers of new taxpayers into the system led successive governments to introduce highly complex and distortive mechanisms to segment taxpayers, with the explicit aim of exempting those with the lowest average effective rates, who placed strong political value on not being considered taxpayers at all. These measures often generated effective marginal tax rates in excess of 100 percent. Macro volatility and shifting political pressures further produced one or more ad hoc updates each year to deductions and brackets, even after the adoption of the current wage-based indexation formula. These episodes are described in detail in Afonso (2022).

Other taxes adopt the same complex pension indexation formula, which is itself based on changes in earmarked tax revenues and social security contributions per beneficiary, as well as wages. This layering further increases the lag in adjustment and, in turn, amplifies the real volatility it generates.

Tax administration has also been undermined by the real variability of tax parameters. Penalties for failing to file tax declarations were left unadjusted and thus eroded to trivial levels. Withholding and reporting regimes, too, became distorted as their nominal thresholds failed to keep pace with inflation. More broadly, the task of assessing a taxpayer's actual liability becomes exceedingly difficult when inflation is running at 6 or 7 percent per month.

A second channel through which inflation distorts the tax system is by altering effective tax rates in the absence of adequate inflation adjustment. Outdated valuations of assets and liabilities on corporate balance sheets lead to the taxation of shareholders' equity through inflation-exposed items such as cash holdings. With proper inflation adjustment, firms

would record losses on their cash balances and therefore face a lower corporate income tax liability. Without it, however, effective tax rates can become substantially higher than those prescribed in the legislation.

The corporate income tax's imperfect inflation adjustment also reduces the real value of depreciation allowances and taxes nominal capital gains. This creates all sorts of distortions: between debt and equity financing, between current and future consumption/investment, between different asset types, between companies with markedly different seasonal operations, between projects with different risk profiles but similar expected returns, etc.

Property taxes are also affected if there is no methodology in place for the frequent market-rating of valuations. Updating valuations is politically costly. In Argentina, properties are valued at the maximum between purchase prices and (severely outdated) fiscal valuations. This creates a dispersion in effective tax rates between newly and previously purchased properties, among other distortions.

An important derivation is that taxing real rather than nominal returns on financial assets is made almost impossible given the high and variable inflation, which partly helps explain why most returns on financial assets are exempt from the personal income tax. Argentina is an outlier in terms of the small share of tax revenues explained by the personal income tax, to which the difficulties with dealing with inflation contribute.

A third type of distortion is the erosion of the value of the money owed to the government because of taxes. Whether the government is 'long' or 'short' inflation depends on which responds faster to it: revenues or expenditures[14]. The corporate income tax is the fiscal 'item' with the slowest response, as the firm's liabilities are calculated and due six months after finishing the fiscal year. Assuming uniformity throughout the year, earnings are outdated by 9 months on average by the time they are due, and are not updated at all for inflation.

To mitigate this depreciation, the government has established prepayments: a company's corporate income tax liability[15], calculated on May of year *t* on the basis of year *t-1*'s profits, is the basis for the monthly payments between June of year *t* and April of year *t+1* on account of the liabilities to be determined on May of *t+1* for the operations during year *t*. Any difference[16] is canceled upon filing the tax declaration in May.

[14] Either by indexation or by contract renegotiations.

[15] Assuming that the fiscal and calendar years coincide for this firm.

[16] The advance payments can be adjusted by the firm if the business is doing badly, if there are legal tax rate changes, and for other reasons. They are also adjusted for withheld amounts, changes to deductions, and other changes to tax policy parameters. However, the earnings are estimated to be the same in nominal terms as in the previous years.

Inflation also affects the value of government liabilities to the taxpayers, which are typically not adjusted. Such is the case of VAT credits for inputs and capital goods purchases, which depresses investment below optimal levels, especially in capital intensive industries with long repayment periods. The same lack of adjustment affects carryover losses in the corporate income tax, which disincentivizes growing firms, particularly startups. It is also generally true of withheld amounts for all taxes. During both 2012-2015 and 2020-2023 the government established high withholding rates on the purchases of foreign currency and emissive tourism services on account of the personal income tax, which can be claimed by the taxpayers -at the historical, unadjusted value- in March of the following year.

As a reference, the sums owed by the federal and provincial tax administrations to taxpayers, and subject to inflation devaluation, has averaged 4% of GDP in recent years.

A fourth way in which inflation distorts the tax system by affecting its design. Some taxes require being set in real amounts per quantity to achieve economic efficiency. An example would be a carbon tax, which must be set at an inflation-adjusted value per quantity of emitted greenhouse gases. This factor increases the use of suboptimal ad-valorem tax designs. The distortion is larger when there are extra-fiscal needs for a minimum tax, as is the case of tobacco taxes.

Planning with such macroeconomic volatility and in a context of low state capacity is made much more difficult than otherwise. The fiscal risks are much greater on all sides: revenue, expenditure, and financing. This creates uncertainty on tax rates, which disproportionately affects risky projects. But more importantly, this fosters the delegation of legislative powers by Congress to the Executive, who often is bestowed with the ability to rewrite major tax legislation provisions suddenly and with no deliberation. Of course, inflation can also lead to higher tax rates due to the erosion of the real value of taxes between the creation of the liability and the payment.

Similarly (fifth), as tax incentive programs are often made conditional on the volatile fiscal outturns, explicitly through rationing or implicitly through delaying refunds, they are often of uncertain value and thus turned into windfall gains when received by the beneficiaries.

Sixth, litigation. The distortions of the lack or imperfect inflation adjustment on the corporate income tax create large incentives to seek judicial relief. Thus, some firms are awarded what amounts to preferential treatments by the judiciary, for example enabling them to fully inflation-adjust their statements. Firms awarded with rulings will enjoy a lower tax burden than their competitors. This also biases overall revenue lower, as only the firms to benefit from the full inflation adjustment will sue – firms benefited by *not* inflation-adjusting their statements (those with a negative equity in inflation exposed assets and liabilities) will just enjoy the reduction in their effective tax rates.

Seventh, whenever a government relies heavily on printing money, stringent capital controls typically follow, with a regulated "official" exchange rate mandated for international trade and other activities. Parallel free markets for foreign exchange appear, whether legal or not, and a gap emerges between the free and the regulated prices of the currency. This distorts effective tax rates, as taxes on foreign currency denominated flows or stocks are assessed at the official exchange rate.

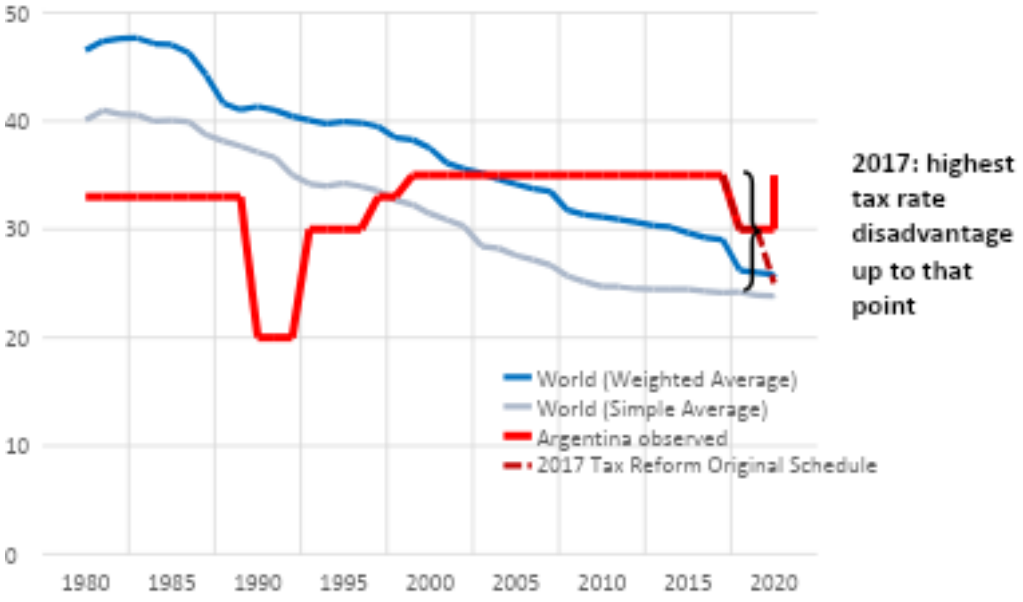
The size of the distortion in the exchange rate varies with policy objectives and economics shocks. If the government decides to stem central bank reserve losses, it could transitorily ease controls and reduce the currency gap. In this scenario the real exchange rate assessed at the parallel, free currency values would not change, but it would rise at the official exchange rate — a devaluation in the regulated transactions markets, such as international trade. This creates volatility in the real exchange rate calculated at the official regulated foreign exchange rates. As taxes are assessed using this rate, large gains are losses are imputed to firms for their foreign currency denominated positions and activities, even if businesses take the free market rate as reference and no actual economic gains or losses occur.

3.11 Taxes on corporations / investment

Although the corporate income tax rate has remained stable, the rates in the rest of the countries have been significantly reduced, leaving the rate in Argentina high and uncompetitive compared to other countries. Moreover, other features of the tax system such as the lack of inflation adjustment in the corporate income tax, the lack of refunds on VAT credits for investments, etc., also created distortions against investment. This, together with the increase in inefficient taxes described above, could help explain the country's low private investment rate, among the lowest in the world[17].

[17] Continued macroeconomic instability and a poor business environment are also leading factors.

Figure 7 — Headline corporate income tax rates in Argentina vs the World.



Source: *Tax Foundation Database.*

Besides the headline 35% rate, a 10% tax was levied on dividends between 2013 and 2015, which put the rate on distributed earnings at 41.5%. In 2016 the tax on dividends was repealed.

OECD countries typically apply lower rates on corporations, but higher overall rates on distributed earnings via the personal income tax[18]. The international fiscal competition for investments drove rates lower over time[19]. In Argentina, the uncertain economic incidence of the corporate tax (considered by many to fall exclusively on the owners of capital) and the reticence to raise the PIT (even if for dividends) combined with the need to finance ever growing redistributive spending. This indirectly led to increases in effective rates, because of the rising inflation and the lack of adjustment in the CIT.

3.12 Tax on bank credits and debits

A 0.6% tax was levied on bank credits and debits – a tax on registered payments[20] that incentivizes firm informality. There is a long list of preferential treatments and exemptions, the most important being that of the savings accounts used for employee and pensioners income. The tax raised significant revenues: 1.6% of GDP. It operated as a turnover tax, with

[18] Harding (2013) documents the different ways to structure the taxation of dividends observed in OECD countries.

[19] Besides headline rates, other countries also aggressively used CIT incentives (accelerated depreciation, R&D, industrial policy programs, etc.) to drive effective rates lower at a faster rate than headline rates.

[20] By "registered payments" we mean "not in cash". Registered payments are not necessarily neither "formal" or "informal", in the sense of being invoiced and declared to the tax administration, but higher registered payments are associated with higher levels of formality.

firm-to-firm transactions paying 1.2%. This was on top of the ISIB – the provincial turnover tax which shared some of its negative traits such as cascading.

A share of the charge[21] could be used by firms as a payment on account of the income tax. This partially gave the tax the character of being a withholding mechanism on the income tax, or (put differently) a minimum CIT typically employed for tax administration reasons (Best et al., 2015). Along with the provincial ISIB, this tax was often identified as one of the main culprits behind the high levels of firm informality. However, it also helps raise taxes from registered noncompliers. The 2016 Small and Medium Businesses Law delivered several benefits to these firms, among which was computing 100% of the tax paid on credits and debits on account of the income tax.

3.13 Taxes on wealth

As part of the attempt to fund the transition period until a budget balance was achieved, the Macri administration adopted a broad tax amnesty in early 2016. It was a success — assets equivalent to 20.7% of GDP were disclosed and 1.8% of GDP in one-off taxes were collected from 0.1% of the adult population, mostly during 2016, with 80% of the base hidden abroad.

The newly disclosed assets had an enduring effect on the "wealth tax" collection. The *impuesto sobre los bienes personales* (BBPP) was levied on the taxpayers' gross value of their assets since 1991. The only liabilities that can be deducted are bank-originated mortgages. Depending on the year, there was either a general personal deduction or an exemption for taxpayers under a threshold. Few assets were exempt: local savings accounts, term deposits, rural land, and most notably public debt instruments issued by Argentina's public sector. While some assets were assessed at outdated fiscal valuations (local real estate) the rest of the asset types were considered at market values. By 2015, the rates schedule when from 0.5% to 1.25%[22] [23]. In a zero percent real rates environment, the rates were higher than the real income derived from the assets.

Along with the biases against investment in the CIT and VAT[24], BBPP was seen as a major obstacle in renewing interest for investments in the country. It was also seen as preventing the tax amnesty. A large portion of the previously undisclosed assets would be "unfrozen"

[21] 34% of the tax paid on credits, which translates to 17% of turnover on firm-to-firm transactions.
[22] The official exchange rate was used to value assets in pesos for the tax assessment. As this was set below the market rate via government interventions, the effective tax rates were lower that the headline rates for all foreign and most local assets. The top effective rate was 0.9% in 2014 and would have been approximately 0.8% in 2015, although the exchange rate controls were lifted in mid-December 2015.
[23] A more detailed description of the tax and its reforms can be found in (Londoño-Vélez & Tortarolo, 2023).
[24] CIT: high headline rates, lack of inflation adjustment. VAT: no immediate refunds for VAT credits on capital goods, lack of inflation adjustment.

by the 2016 tax amnesty and enabled to fund real investments. But the large BBPP rates would have deterred taxpayers from participating. Thus, the same April 2016 law that approved the amnesty also laid out a gradually decreasing flat rates: 0.75% in 2016[25], 0.5% in 2017, and 0.25% in 2018. Given this, the 2017 tax reform would not propose further changes to the BBPP tax, despite the known biases and distortions that this kind of tax design imposes (OECD, 2018; Perret, 2019).

3.14 Federal revenue sharing agreements and tax expiration dates

A highly complex set of laws governs the revenue sharing agreements between the federal government and the provinces in Argentina, and is beyond the scope of this document[26]. However, in what amounted to a high-profile political statement, the Peronist-dominated Supreme Court issued a ruling in late November 2015, days before the inauguration of the new administration, that effectively reassigned 0.8% of GDP in revenues from the Federal to the Provincial government[27]. Thus, the provinces were in a very comfortable financial position, as they had not yet permanently increased spending levels. The provinces also collect their own taxes, chief among them the ISIB, over which they have (almost) complete jurisdiction on taxable bases, rates, and procedures.

Argentina's Constitution mandates that federal tax revenues be shared with the provinces according to a general revenue sharing agreement. Taxes can be earmarked, though, within set time limits. One large earmark that benefited the federal government, of the tax on bank credits and debits, was set to expire by the end of 2017, with the provinces aiming to reclaim those funds. This would have meant a reallocation of funds from the federal governments to the provinces of 0.7% of GDP, additional to the 0.8% of GDP mandated by the Supreme Court in November 2015, which required immediate action by the federal government. This was an additional incentive to push for a tax reform.

3.15 Policy changes during the first year

We have already touched on some tax policy changes undertaken during the first year of the administration. The policy changes were unsystematic and responded to political demands and instincts, not optimizing for overall efficiency or fiscal sustainability.

[25] The initial rate was close to the effective top rate for the top taxpayers — see footnote 33.
[26] Grossly simplified, revenues are apportioned using fixed share coefficients first between the Federal government and the provinces, and secondly among the provinces.
[27] The 2006 law that earmarked those revenues to the federal government was ruled unconstitutional. The Supreme Court had almost a decade to decide on the issue but decided to do so just days prior to the start of a new administration of the opposing party. The ruling was of immediate application for 3 provinces. The Macri administration reached an agreement in May of 2016 with the remaining 21 provinces, which had yet to receive a ruling (but eventually would). The revenues would be gradually reassigned over 5 years. The 0.8% of GDP figure corresponds to the 2019 run-rate of the full reassignment.

The main changes, by fiscal impact were the changes to the personal income tax (described in §3.4), the tax amnesty and related changes to taxes on net wealth (§3.12), the dismantling of capital controls, and the reduction in export taxes. Also relevant during 2016 were the effects of the November 2015 Supreme Court decision on the revenue sharing agreement, described in (§3.13).

As part of the previous administration's capital controls, withholdings were levied on purchases of foreign currency, air tickets and tourism services. The withholdings, normally tax administration measures, functioned as unlegislated taxes, as they were unrelated to the tax code's taxable events, generated large balances in favor of the taxpayers, and were seldom refunded. The administration decided to refund all the balances to the taxpayers at the start[28].

Fulfilling campaign promises, the Cambiemos administration eliminated taxes on exports for all products except for soybeans and its subproducts[29], Argentina's main export product. For these, an immediate 5 percentage points reduction was adopted from the starting 35% rate, and a further gradual reduction of 0.5 percentage points per month was scheduled to start in January 2018[30]. At the time, the Executive enjoyed of powers delegated by Congress to freely set the rates.

Several other changes were made during 2016. The dividends tax was abolished, to be later reinstated by the 2017 Tax Reform. The Minimum Presumptive Corporate Income Tax was repealed[31]. "Industrial policy" / rent seeking laws created new benefits for the automotive and tourism industries. Another law and related regulations created sizable tax benefits for all Small and Medium Businesses in the country. Tax incentives for the adoption of electronic payments were introduced.

Overall, during 2016 the tax policy changes accounted for a recurrent, yearly loss of 1.2pp of GDP in tax revenues. Additionally, that year's one-off changes added up to +0.7pp: 1.4pp for the tax amnesty (with a further 0.4pp to be collected in January 2017) and -0.7pp for the refunds related to the capital controls. The policy mix included questionable cuts to the personal income tax and new industrial policy / rent seeking benefits, put too much emphasis on export tax cuts, and did nothing for the severe tax distortions depressing investment and formal employment. It would have been unsustainable to continue to

[28] It also wished to refund all VAT balances, which surpassed 2% of GDP. The administration was eager to immediately fulfill all campaign promises as early as possible. The promises were completely inconsistent with the declared goal of a rapid fiscal consolidation, yet the political leadership did not internalize the contradictions.

[29] And a few other minor ones like leather and wool. These were industrial policy / rent seeking policies that ostensibly sought to foster the local industrialization of these products.

[30] This was short lived, as export taxes were raised during 2018 due to the sudden stop balance of payments crisis.

[31] This was a tax levied on firm assets and 100% applicable as a payment in account of the Corporate Income Tax. In effect, it was a tax avoidance policy measure, similar to the Alternative Minimum Tax seen in the US and comparable schemes in other countries. At the time it was seen as costly and unfair.

operate in this manner for the remaining three years of the administration. A properly planned, comprehensive Tax Reform was needed to bring order to the tax system.

3.16 Taking stock

Argentina's tax system had evolved into a structure characterized by an elevated tax burden and a large presence of highly inefficient taxes. The principles of economic theory and the realities of global tax competition made it necessary by 2017, after the initial macroeconomic stabilization efforts, to shift towards a structure with lower charges on exports, greater coverage of personal income tax and property taxes, greater collection of *Pigouvian taxes*, reduced investment disincentives through elimination of highly distortive instruments (ISIB and the tax on bank credits and debits).

Cross-country empirical evidence consistently demonstrates substantial departures from optimal taxation principles, particularly regarding corporate income taxation in developing countries. The canonical work of Cummins et al. (1996) established through careful comparison across multiple OECD economies that corporate tax reforms generate significant responses in aggregate investment behavior. Their analysis of tax changes across nine countries reveals that reductions in the effective tax burden on capital systematically raise investment rates, with user cost elasticities in the range of -0.5 to -1.0. This consensus finding, subsequently confirmed by Hassett and Hubbard (2002) in their authoritative survey of the investment literature, indicates that a 10 percentage point reduction in the effective corporate tax rate generates approximately 2 percentage points of additional investment relative to GDP. The mechanisms operate through standard neoclassical channels: lower tax rates on capital income reduce the user cost of capital, thereby increasing the profitability of marginal investment projects and expanding the capital stock.

Argentina's position in the international distribution of effective corporate tax rates—with statutory rates exceeding 30% and effective rates substantially elevated by limited depreciation allowances and lack of inflation adjustment—placed the country among the high-tax jurisdictions analyzed in the comparative literature. This elevated tax burden on formal sector capital reflected not only suboptimal policy design but also the structural constraint imposed by extensive labor market informality. With approximately one-quarter of economic activity operating outside formal tax collection mechanisms, the effective tax base for corporate income taxation was substantially narrower than aggregate economic activity would suggest. This informality constraint forced reliance on higher statutory rates on the formal sector to achieve revenue targets, creating a vicious cycle where high corporate tax rates further incentivized informal operations, thereby eroding the tax base and necessitating even higher rates on compliant taxpayers.

Regional evidence from Latin America provides particularly relevant benchmarks while highlighting Argentina's unique constraints. Bustos et al. (2004) analyze Chile's tax reform experience in a context of lower informality rates and more diversified tax bases,

demonstrating reform dynamics that proved less applicable to Argentina's constrained fiscal environment. While Cummins et al. (1996) provide foundational evidence that corporate tax reductions generate capital formation increases, their analysis assumes functioning formal economies where tax base erosion through informality remains limited. Desai and Dharmapala (2006) further demonstrate that in contexts with substantial informal sectors, the distortions from corporate income taxation become magnified, as firms face not only the direct cost of taxation but also the incentive structure favoring informal operation to avoid tax obligations entirely. Argentina's challenge was more complex: achieving revenue adequacy while reducing distortions in an economy where optimal taxes like corporate income tax and VAT faced severe collection constraints due to widespread informality and limited administrative capacity.

These revenue constraints explained Argentina's persistent reliance on theoretically suboptimal yet administratively feasible instruments. Cascading taxes like the provincial gross income tax (ISIB) and the bank debit and credit tax, while creating severe allocative distortions through vertical integration incentives and formality disincentives, remained fiscally indispensable. As emphasized in Mankiw et al. (2009), optimal tax theory presumes administrative capacity to implement sophisticated instruments and broad compliance across economic sectors. Argentina's reality in 2017 was that exclusive reliance on first-best taxes - corporate income tax, VAT, and personal income tax - would have generated insufficient revenue given evasion rates and informal sector size. The tax system's apparent irrationality reflected second-best optimization under binding political and administrative constraints rather than ignorance of optimal taxation principles.

During 2016, the Cambiemos administration implemented large cuts to export taxes on agricultural products and the personal income tax, both focus of widespread demand for a lower tax burden. Those changes were, however, reactive to political demands and disregarded the functioning of the system as a whole and the underlying revenue constraints imposed by informality. While tax revenues decreased considerably (0.5% of GDP), the most severe growth-depressing distortions on employment and investment remained unaddressed, and the fundamental tension between revenue needs and efficiency remained unresolved.

4 The Tax Reform Draft and its constraints

The Treasury’s Tax Reform Draft mainly aimed to increase efficiency by broadening tax bases, reducing compliance costs and distortions, mostly by aligning tax rates with (lower) international benchmarks. The Tax Reform Draft was conceived to be broadly revenue-neutral for the public sector as a whole, with the new taxes and the broader tax bases compensating lower rates elsewhere.

The set of the three initiatives (the Tax Reform, the Pension Indexing Reform, and the Fiscal Consensus) was intended to be almost neutral in terms of the budget balance. The Tax

Reform would reduce the federal government's revenues, but the shortfall would be covered by the reduced spending in terms of GDP caused by linking pensions to inflation, rather than to tax revenues. The provincial governments would see increased revenues thanks to the Supreme Court's decision, compensating the mild primary deficit observed by 2017. The Fiscal Consensus would lead to reduced provincial tax revenues, to be offset by the spending limits set for the provinces by the Federal Fiscal Responsibility Law. At the end of the road, the provincial governments would see a primary surplus. Both levels of government would reduce taxes and spending at approximately the same rate, without impacting on the ongoing fiscal consolidation program of the federal government[32].

The reforms' main proposals involved aligning the taxation of investment to international practices, reducing the tax wedge for unskilled workers, and reducing the effective tax wedge of the turnover tax that affected formal transactions.

The Draft reflected the team's view of a path towards an ideal system from an "optimal taxation" perspective. It internalized budgetary constraints (aiming for neutrality) and the constitutional limits to the federal government authority on fiscal issues over the provinces, while also being free of political requirements. The goal was to avoid internalizing politically mandated distortions such as benefits to specific sectors or constituencies at an early date in the process as much as possible. However, the team correctly anticipated a sequential negotiation process with a large number of stakeholders, and sought in some cases to make an "opening bid" that left sufficient room for concessions without compromising the core of the reform. The set of reforms left some margin of error for deviations of the implementation path.

4.1 Gradual implementation

The team judged that maintaining the country's tax take at around 32% of GDP—excluding the inflation tax—was only sustainable if revenues were raised through better-designed, more efficient taxes. At those levels, Argentina relied on highly distortionary instruments that impeded growth. Expenditure was even farther above international benchmarks, and needed to fall to create the fiscal space required to reform the tax system. Budgetary constraints were severe, and limited voting power in Congress precluded a faster pace of fiscal consolidation.

Thus, the tax reform had to be implemented gradually. Ideally it would be fiscally neutral—or close to it—but if the political equilibrium ultimately implied a net revenue reduction of about 0.2–0.3% of GDP, that was still consistent with the broader consolidation program. The timeline would allow independent spending measures already underway to generate the necessary fiscal space.

[32] Closing the deficit would be achieved by spending rationalization elsewhere, such as curtailing energy subsidies and other wasteful spending at the federal government level.

On the revenue side, tax increases were likewise phased in over 3 to 10 years to avoid sudden disruptions. By providing forward guidance embedded in law, the administration aimed to spur private investment and hiring on the basis of the future tax schedule. Gradualism also gave the authorities room to monitor outcomes, reassess underlying projections, and correct course as needed.

4.2 Taxation of personal income

Early on, politics restricted the set of addressable policies, vetoing some of the team's desired changes. Although there were some important distortions in the personal income tax deductions, the Reform ended skirting that due to previous political agreements of 2016, which had led to a fiscally expansive compromise solution.

The Draft, however, called for the gradual implementation of changes that would have brought the tax in line with international benchmarks.[33] The deductions were to be kept fixed in nominal terms, with their real value constantly eroded by inflation. The marginal rates schedule's thresholds would have raised each year in real terms. Thus, the speed of the transition was not preordained but rather depended on the speed of the disinflation[34]. Complementary reforms were proposed for the taxation of the self-employed, which would eventually have closed the gigantic gap in effective tax rates between the regimes.

4.2.1 Taxation of the self-employed

The super-simplified tax reform was also removed from the Draft as its very low effective tax rates, lowered compliance costs and almost complete lack of oversight from the tax agency made it very popular. The Draft sought to phase out the super-simplified tax over eight years, except for those under the "social" subregimes. That time was deemed enough to lower the effective combined marginal tax rates for low-income formal workers[35] and for the tax administration to implement simplified and fully automated tax returns for the VAT and PIT, which would render the need for the super-simplified tax moot.

Starting from the highest gross income category, each would be sequentially subjected to the same sequence of events: first, new registrations would be banned; second, and a year later, legacy taxpayers would be enrolled into the general social security and PIT regimes for the self-employed; finally, two years later, these taxpayers would be enrolled into the VAT.

[33] This replicated the Executive's mid-2016 proposal, which was abandoned during negotiations for the Compromise solution of December 2016.
[34] If the inflation targets were met, it would have taken in the order of 15 years to bring the deductions in line with OECD standards.
[35] Due to the combined effect of the gradual changes to the employer's social security contributions tax base deductions and the gradual "flattening" of the then steep PIT rate schedule.

Table 4 — Super-simplified regime phase-out schedule, by category.

Category	H, I, J, K	G	F	E	D
Number enrolled (2017)	124k	101k	168k	172k	426k
Revenue ceiling in multiples of average wages	2.3 to 3.3	1.6	1.4	1.1	0.8
Inscriptions end	From the start	End of year 1	End of year 2	End of year 3	End of year 4
PIT + Social Security mandatory enrollment	End of year 1	End of year 2	End of year 3	End of year 4	End of year 5
VAT mandatory enrollment	End of year 3	End of year 4	End of year 5	End of year 6	End of year 7

Other alternatives were also considered, such as raising the fixed monthly payments and setting permanence limits on the super-simplified regime. However, from a political economy point of view it was considered preferable to treat all the taxpayers with the same set of rules under a unified regime that was simpler and with gently increasing marginal tax rates for all, preventing the possibility relaxing the super-simplified tax eligibility rules in the future resulting from the political process.

Changes to the general regime for the self-employed were considered as well. Demands for tax relief were intense and had swayed the Cambiemos administration, with several small step-changes being approved in the years before and after the reform. However, the income tax deductions for the general regime self-employed were already elevated by international standards. The Draft thus focused on reducing compliance costs, which for these taxpayers were severe, and extending several social security benefits that this group was not eligible for[36], disincentivizing registration.

These Ministry's Draft proposals were dropped from the Executive's. However, the Presidency assured Ministry officials that the reforms to personal income taxation would be undertaken after reelection.

4.3 Capital income taxation

The low levels of proceeds from the taxation of capital income were as anomalous even in comparison with the other large or high-income Latin America countries. The team believed in the necessity of redressing the situation on equity and efficiency grounds, helping normalize the tax system structure seen on Figure 7. More importantly, it would also make the whole Reform more politically acceptable. The Cambiemos administration was (wrongly) perceived as promoting the interests of the rich, and the Reform concentrated on reducing distortions on taxes with a legal incidence on firms. Taxing capital income was one

[36] The general-regime self-employed were excluded from the direct transfer child benefits. They did enjoy an income tax deduction, but as deductions were high they only were of significance to 95+ percentile individuals by income. The lower income general-regime self-employed also couldn't access subsidized health insurance as the super-simplified tax participants did. Along with compliance costs, these design features created a strong disincentive to enrolling in the general regime above the differential tax rates, which also were considerable.

important proposal of the Peronist opposition during the presidential campaign and would become their main demand during the Reform negotiations. Thus, to further bolster the support for the Reform and improve the optics, the proceeds were to be earmarked for boosting the pension system's finances[37].

Argentina's macroeconomic volatility posed challenges for the design of capital income taxation. The valuation of financial assets varied widely – the country risk premia ranged from 346 bps (Dec. 2017) to 1348 bps (Nov. 2012) since 2011. This created large capital gains or losses from year to year that demanded a careful design of carry forward provisions balanced with the usual base erosion limitations.

A bigger issue was inflation, which averaged 31% over the preceding five years. One of the few remaining institutional legacies of the last successful macroeconomic stabilization program, 1991's Peso Convertibility regime, was a general prohibition of the indexation of contracts. By 2017 this had been somewhat relaxed, but there were still three methods of guarding from inflation in widespread use: dollar denominated contracts, CPI-indexed contracts, and contracts with high-nominal coupons that took account of expected inflation. Peso-denominated debt instruments thus had correspondingly high nominal interest coupons – an instrument with an ex-ante real yield of 2% would pay 27.5% in interest. This also happened with short-term "bullet" bonds, issued at low parities that internalized expected inflation. The challenge was to find a mechanism to tax real returns, however designated (as interest or capital gains), in a context of high and volatile inflation.

The widespread dollar denominated contracts also had to be considered. Taxes are normally assessed in pesos. A dollar contract would show gains due to inflation, even if the real exchange rate remained constant from year to year.

These issues constrained the design of the tax, which we knew would be suboptimal from the start. As is common practice in other countries, the taxable base was to be subjected to a flat rate below the top marginal rate for general income (35%). "Hard currency" or inflation protected instruments were to pay 15% on interests and capital gains. Peso denominated contracts would pay 3% initially (when inflation was still high) and 5% later on. Mutual funds with mixed contract types (such as dollar and peso denominated bonds) would be taxed at the weight average rate.

The rates on peso-denominated assets implicitly assumed that the inflation targets of each year would be met, as the real effective rates would end up being too high if inflation overshot them. The design of the tax was complicated enough, and trying to precisely tax real rates of return would have made tax administration and compliance too impractical. We were also not aware of any tax system that has successfully resolved these issues (crucial under Argentina's volatility) and that we could take as an example.

[37] This was of little actual consequence, as Argentina has a defined benefit pension system with large deficits covered by the Treasury and earmarked revenues are fungible.

The changes included a yearly deduction from the tax base of 52k ARS (3k USD) to avoid taxing small savers who would presumably have a high elasticity of taxable income and could be driven away from the formal market. Thus, effective rates gently increased from 0% to the marginal rates of Table 3 above.

The team considered several risks stemming from the proposal, the most important being that it could make financing more expensive for the government. Correspondingly, it would disincentivize savings and credit. We expected the tax to improve the primary fiscal balance but leave the overall balance unchanged or slightly worsened. To manage these risks, we decided to keep the exemption for non-residents on capital income originated from public bonds. The capital income derived from the instruments the Central Bank uses to conduct monetary policy was crucially exempt as well. This way, the tax would have only applied to capital income from domestic sources and received exclusively by local residents, not affecting the government's ability to tap international markets for funding, as it had been doing so in the prior two years, 2016 and 2017.

An additional concern was that the government's credibility would be negatively affected by introducing the tax so soon after the tax amnesty program that ended only a few months prior. This seemingly opportunistic behavior could increase the expectations on the frequency and direction of future tax reforms, harming the incentives to invest by firms, contrary to the goals of the Reforms.

Despite the risks, the tax was a blocking issue politically. There would be no Reform without implementing some sort of tax on capital income, as demanded by the Peronist opposition on distributional grounds. In the end, the Ministry believed[38] that the tax would be limited enough to contain the risks.

The tax was forecast to yield up to 0.26% of GDP in revenues, with over half of that going to the provincial governments due to the standing revenue sharing agreements. This was a small fraction of the ~2% of GDP in supply side tax cuts that needed to be offset with higher personal income taxes. Again, the main (but not exclusive) driver of the inclusion in the Draft proposal was the political capital that it would confer to the process. Although Congress removed the exemption on the Central Bank policy instruments, increasing the tax base, for a number of reasons[39] the tax only yielded 0.06% of GDP during 2018, and a similar level during 2019. This serves as an example of the bias identified by Hines (2018) in the forecasts of tax reform impacts.

[38] The Ministry's political staff was divided on the convenience of pushing for this change, with the authors being against the proposal.
[39] Including the lack of capital gains as asset prices collapsed since early 2018.

Table 5 — Fixed income asset returns before and after tax, 2020 rate schedule as set by the 2017 Tax Reform, at 2017 market conditions.

			Effective rates for investments of…			
			USD 50k		USD 500k	
Instrument type	Marginal rate (2018)	Returns, before tax	Returns, after tax	Effective rate	Returns, after tax	Effective rate
Peso	15%					
Lebac 1m	"	27.2%	26.1%	3.8%	25.8%	4.9%
Certificate deposit 1y	"	20.0%	19.3%	3.5%	19.0%	4.9%
2026 Treasury bond	"	15.0%	14.6%	3.0%	14.3%	4.9%
CPI indexed	5%					
Discount 2035	"	5.4%	5.4%	0.0%	4.7%	12.7%
Certificate deposit 1y	"	0.0%	0.0%	0.0%	0.0%	0.0%
Dollar	5%					
Par 2038	"	6.9%	6.7%	2.9%	5.9%	13.8%
Discount 2035	"	6.3%	6.3%	0.0%	5.5%	13.1%
Bonar 2024	"	4.1%	4.1%	0.0%	3.7%	11.2%
Certificate deposit 1y	"	0.5%	0.5%	0.0%	0.5%	0.0%

Note: *this is a simplified presentation. Considers reinvesting for shorter dated securities. The returns of the dollar assets are denominated, those of indexed securities are expressed in constant-value pesos, and the unadjusted peso assets are denominated in pesos.* ***Source:*** *Ministry of Treasury.*

Some hard to justify income tax savings incentives were added to the Executive's Draft fulfilling requests from the Ministry of Finance. Careful impact evaluations show that these incentives fail to promote savings (Chetty et al., 2014; Friedman, 2017; Ramnath, 2013). The same occurred with the mortgage interest deduction (Fatica & Prammer, 2018; Gruber et al., 2017; Hanson, 2012; Sommer & Sullivan, 2018; Valentin, 2023).

4.4 Payroll taxes

Addressing informality and employment of the unskilled was the main goal of the proposals related to the payroll tax. Plus, the investment-stimulating reforms to the corporate income tax would primarily benefit the skilled workers, providing an additional income distribution motivation to focus the benefits on lower-wage workers. The Draft proposed a per-employee, per-month deduction of the employer's social security contributions' tax base. The deduction would max out at a value equivalent to the minimum wage at the time of the Reform[40], zeroing-out the employer's social security contributions up to that level. Thus, the Reform focused the benefits on those at the margins of the formal labor market[41]. This was a costly investment and, to partially offset the costs, the marginal employer's social security contribution rate was raised from 17.0% to 19.5%—but average effective rates would only

[40] It would however be indexed to the CPI, not the minimum wage, to avoid perverse incentives in the setting of the latter.

[41] Those entering the market, the unskilled, the marginally attached to the formal market, people close to their retirement, women on the verge or some time after childbirth, people with disabilities. The Reform was particularly beneficial for part-time workers.

raise for the highest income workers, those benefitted by their complementarity with the Reform-induced investments. The Reform chose to reduce the *employer's* social security contributions, rather than the *employee's*, to concentrate the impact on formal employment. With inflexible minimum wages, the alternative would have improved the wages of the already-formal employees with little to no benefit to the outsiders.

Still, these changes would create 1.2% of GDP in annual foregone revenues (static scoring[42]). As with most of the Reform changes, these would be phased in gradually (and linearly) over 5 years. Given that the defined-benefits pension system is administered by the federal government, the full cost of the changes would be borne by it. Of all of the changes proposed by the Draft, this was the one with the largest fiscal impact.

Although the reform's aim was to improve the employment prospects of low-skilled workers—by raising wages and/or formalization—it had to be layered onto dozens of special regimes accumulated over the years. Some of these programs targeted minority or disadvantaged groups; others funneled benefits to narrowly defined industries born of rent-seeking or industrial policy; still others subsidized marginal jobs in small firms expanding their payrolls. Any change to tax rates and deductions creates winners and losers and typically brings transition relief, most commonly by grandfathering existing preferences. Argentina's payroll tax regime is no exception, and the reform did not depart from that practice. While, on efficiency grounds, replacing all prior preferences with a single, uniform payroll deduction would have been preferable, it was likely indefensible in court and—so we judged at the time—prohibitively costly politically.

There was, however, an ill-designed tax benefit that could be modified to further offset the fiscal impact of the changes, called Decree 814/01. This was a remnant of the political compromises reached during two prior macroeconomic stabilization plans, during the Convertibility regime of 1991 to 2001. The benefit allowed some firms to take their payroll taxes as payment on account of the VAT, effectively lowering labor costs. The eligible jobs were those located at some distance from the country's capital, with higher benefit rates for localities farther away and with smaller populations. There was no cap, however, on the benefits. This resulted in extractive and/or conclave industries located in isolated areas (i.e., with labor market power) accounted for almost all the tax expenditure.

As was the case when the benefit was implemented and then when it was reformed, the beneficiaries commanded an important lobbying power. First, most provinces, other than Buenos Aires, had some firms receiving benefits, often the province's largest employer, and that made their representatives sympathetic to the program. Second, these firms tended to be members of powerful industrial lobbying groups, which have successfully conditioned Argentina's trade openness throughout its history. Despite this, the resistance phasing out this subsidy was lower than expected, although still significant. The payment on account

[42] I.e. assuming no behavioral responses.

amounted to 0.3% of GDP in annual tax expenditures. Thus, on an aggregate level, the cost of the reforms to payroll taxation netted out to 0.9% of GDP by the fifth year of the fully implemented Reform, using static scoring.

4.5 Tax on bank credits and debits

The Draft scheduled a gradual (over 5 years) increase the share of the tax paid on credits and debits that medium and large firms could compute as a payment on account of the income tax[43].

The Draft enabled the Executive to suspend further share increases at any moment over the 5-year schedule if the fiscal consolidation program was imperiled for any reason. This was one of the "exit clauses" that the Team built into the Draft in case unforeseen circumstances like the 2018 sudden stop threatened to derail the macroeconomic stabilization efforts.

4.6 Taxes on corporations / investments

The Draft put great emphasis on eliminating investment-depressing distortions in the tax system. It proposed refunding VAT credits on capital goods purchases, although the tight fiscal space conditioned the mechanism beyond the optimal[44].

Extensive changes were proposed for the CIT. The Draft incorporated inflation adjustment according to international norms[45]. The headline rate, 35%, would be lowered to 30% during the initial two years, and later be set to 25%, closing the gap with the international benchmarks at the time. A new tax on distributed dividends was also proposed, keeping the combined rate at the prevailing 35% rate.

Ever increasingly outdated fiscal valuations, mainly of real state properties, meant that holdings would be recorded at close to no value in the balance sheets. Owners enjoyed lowered tax liabilities each year. But it also led to "stranded assets", as sales (recorded at market values) would incur in a huge tax penalty. The Draft proposed a voluntary one-off revaluation, enabling taxpayers to compute asset costs at market values[46] in exchange for paying a tax on the revaluation. This partially compensated for the previously lowered tax liabilities, with tax rates between 8-15% for most cases.

Several anti-abuse changes were introduced to the CIT. The "base erosion and profit shifting" OECD recommendations were adopted. Fiscal transparency regulations for trusts and similar devices were implemented. The regulations regarding transfer pricing, excessive leveraging, and transactions involving low-tax jurisdictions were strengthened. Other

[43] Micro and small businesses already enjoyed that benefit due to a 2016 Law.
[44] VAT credits on investments have macroeconomic proportions, so a cap would be set each year on the Federal Budget Law. Refunds would proceed on a first-come, first-served basis, with a preference for SMEs.
[45] IAS 29 Financial Reporting in Hyperinflationary Economies.
[46] Or using a predetermined price index.

loopholes were closed as well. This was the most technically complex and lengthy portion of the draft.

4.7 VAT

As is common in most countries, the VAT had preferential treatments that generated tax expenditures of about 1.0% of GDP. Argentina's exemptions are not atypical[47], and the largest ones are explained by the usual merit goods (foodstuff, housing, medicine, education, etc.).

These tax expenditures were regressive in distributional terms. Reduced rates on foodstuff and housing, for instance, create larger tax expenditures in absolute value for the well off than for the poorer people. Additionally, several smaller tax expenditures could only be understood as crystallized rent seeking behavior, such as the exemption of racehorse breeding. And, over recent years, lobbies had managed to secure new exemptions or reduced rates, as is the case of media conglomerates. The Draft proposed a comprehensive re-evaluation of these preferential tax treatments. Those that couldn't be justified from a merit goods perspective would be abolished. The rest, then implemented as differential tax rates, would be replaced by targeted transfers, which do not distort consumption decisions and allow for savings by curtailing leakage to the well-off. The new direct transfers would have been targeted to minimum and non-contributory pension beneficiaries, as well as the recipients of child benefits[48].

The headline VAT rate was 21%, with reduced rates of 10.5% and exemptions. That was above the values then observed in countries comparable by income. This is a case where the exacting demands for tax cuts of the Executive had to be managed, in this case with a proposal conditional on fiscal performance. The Executive originally pushed for dropping the headline rate to 16% with no offsetting reductions in the VAT's tax expenditures. The Executive probably saw that this chapter of the Draft was easier to capitalize than the changes to corporate taxes or the provincial turnover tax.

The Team didn't view further reductions to the VAT as among those with the highest efficiency returns per unit of political capital spent, and the changes would have made the Reforms more expansionary. An internal compromise solution was reached. The Draft proposed a 5-year gradual convergence towards a unified general rate of 18%, eliminating tax expenditures, which would have implied a slight loss of tax revenues on static terms. The Draft also proposed delegating the authority to the President to further decrease the

[47] Argentina's tax expenditures on general consumption taxes appear to be below-average (Longinotti, 2019, 2021, 2022).

[48] All children under 18 are entitled to child benefits, which are income-tested but remain relevant to all but the tenth decile.

headline rate to 15% if a fiscal surplus was achieved ahead of the fiscal targets[49]. The team viewed this chapter of the Draft as unlikely to survive the coalition's political review — eliminating the preferential treatments for foodstuff, medicines, education, health, housing, etc. was too politically costly, even if welfare enhancing and redistributive. Soon enough, a senior member (a governor) vetoed it.

The Draft put a great deal of emphasis on simplification and other tax administration improvements that would lead to lower compliance costs. In particular, it pushed for the full implementation of the digital VAT books, which at the time were still far from being a reality. The objective was to allow self-employed workers to carry out their basic accounting, complying with the requirements of the general regime without needing to resort to professional assistance. The Draft also proposed to levy VAT on digital services rendered by foreign companies and consumed locally, eliminating a distortion against local providers.

4.8 Federal excise taxes

The Draft also strove to make excise taxes more efficient and more clearly define their role as Pigouvian taxes, eliminating rent-seeking preferential treatments. Except for the effects of the tax on greenhouse gases in the long term, the excise tax increases were inconsequential in terms of revenue. Despite this, several reasons led the team to focus on these issues. First, these taxes were plagued by design issues that originated from rent-seeking activities, and a wholesale tax reform was a unique opportunity that we couldn't let pass to improve the system.

Secondly, and most importantly, these taxes target production that is concentrated on a few provinces in each case, with strong connections to local political power. A set of a few provinces are involved in hydrocarbon extraction and production. A different set of a few provinces is involved in the production of sugar for sugar sweetened beverages, and yet another different set is involved in the production of alcoholic beverages. This significantly helps the creation of transitory voting alliances in Congress whenever one of those activities is involved, with enough power to veto parts or all of any reform. These activities are linked to the provinces' identities, and any attempt to change their regulations or taxes is bound to be very salient. For these reasons, local elites value their contribution to economic activity at a significant premium. For the reform team, this meant that we could expand our room for negotiations by threatening to impose these Pigouvian taxes. The plan was to trade these reforms, highly valued by the representatives of the affected provinces' elites, for their support in passing the core of the Reform unchanged. But things would turn out differently.

[49] The combined effect of the changes would have had a null distributive impact, as assessed by changes to the Gini coefficient.

4.8.1 Health Pigouvian taxes

Such was the case with alcohol taxes, which had important carveouts for local producers. Alcohol taxes had important carveouts for local producers (wines were completely exempt while others of lower alcohol-by-volume were taxes); the Draft hoped to align the ad-valorem tax rates with the alcohol-by-volume informed by each product's label[50]. It would also raise rates on high alcohol content beverages, as they were below OECD benchmarks.

It also proposed to gradually reduce, over a 6 year-period, the excise tax on electronic goods not produced in the Tierra del Fuego province, one of the most onerous rent-seeking preferential treatments in Argentina's tax system[51].

Tobacco taxes were also set to be overhauled by the draft. A complex system of ad-valorem taxes was levied on tobacco products[52], but despite the high rates affordability continued to be high compared to other countries. The tax rates were increased in 2016 by a presidential decree that used delegated powers confirmed by Congress from 60% of the wholesale price to 75%, or from 150% from the net-of-tax price to 300%; the changes increased real tax revenues by 50% (González-Rozada, 2019). However, that delegation only allowed for transitory changes to tax rates, and the decree was on tenuous legal grounds. Thus, the Draft sought to overhaul the system of taxes by implementing the minimum set of changes that would allow cigarette prices to increase. We proposed a fixed minimum tax per pack, while codifying the 70% tax rate (or 233% of the net-of-tax price). These changes were calibrated to keep tobacco tax revenues unchanged. Yet the new provisions gave the Executive branch the power to further raise the minimum tax by 25%, and the indexation mechanism would have raised the real value of the minimum tax as the economy's inflation receded[53].

The Reform Draft also put forth a sugary drinks tax that aimed to raise revenues and fight obesity. The proposal was to tax the added-sugar content of beverages with a fixed amount per gram, with a (low) exempt minimum[54] that encouraged the input substitution for non-caloric sweeteners; this.

[50] Based on the WHO's recommendations (Sornpaisarn et al., 2017).
[51] It creates yearly revenue losses of 0.3% of GDP.
[52] Simplifying the tobacco taxes system would have implied the discussion of the revenue sharing agreement that applied to each and the ensuing redistribution of tax revenues away from the tobacco producing provinces that benefitted from earmarks in those agreements. The seven tobacco producing provinces had an important voting power in Congress, and the changes were deemed to be politically too costly even at the stage of the Reform Draft.
[53] This also applies to all the other indexed tax parameters – as the indexation used lagged past inflation, whenever a parameter is updated it rises in real terms above the previous update's level.
[54] Normalized by volume.

4.8.2 Carbon and fuel taxes

A broad-based carbon tax on each equivalent ton of CO_2 from almost all hydrocarbon energy uses was proposed, at the rate of 25 USD/tnCO_{2e}, with a gradual adoption over 10 years. The proposal had strong political support from the Minister of Energy, as it believed that the scheme could bring order to a myriad of policies with differing implicit carbon prices. As effective carbon tax rates were already amongst the highest in the world for liquid fuels, we transformed the existing ad-valorem tax to two indexed per-quantity taxes at the same overall effective tax rate[55]. In the case of natural gas and other previously exempt products such as mineral carbon, the tax was to be adopted following the complete withdrawal of energy subsidies to be completed by 2019. The Team expected Congress to approve a wide-based tax of around 10 USD/tnCO_{2e}, after the negotiations.

The Team believed that a widespread carbon tax would lead to a better allocation of scarce investments. Graduality would ensure that preexisting projects would not be significantly harmed, already battered by years of macroeconomic volatility and interventions by the previous administration. The Ministry of Environment did not request nor participate in the design of this tax or any other, despite being invited to by the Treasury. The Team also believed that it was going to help in signing the Mercosur-EU trade agreement, allaying some of the European objections on environmental grounds.

A secondary reason for the Ministry of Energy's support for the tax was the demand for a fuel price stabilization mechanism – oil prices were twice as high by late 2017 as they were in early 2016. The Ministry of Energy agreed to replace the ad-valorem taxes with an indexed fixed amount as a substitute for their preferred, more ambitious solution. The Draft's design also satiated the demand for fuel tax cuts, as it was believed that oil prices would continue to rise and thus lower effective tax rates at the pump.

4.9 Other federal taxes

The transaction costs for trading property were very high in Argentina, leading to a misallocation of the housing capital stock. In addition to the costs of property brokers and notaries, provincial and federal taxes added to these costs. The Fiscal Consensus addressed the provincial stamp duty tax on property deeds. The Reform proposed that the federal tax on the gross income from property sales be replaced by a 15% capital gains tax, adjusted for inflation. The change would only apply beginning with the second time a property was traded after the reform. The new tax served as an incentive for taxpayers to provide fair assessments of their property purchases, as it would have decreased their liability down the line. On the contrary, the existing arrangement incentivized underreporting, with

[55] Other unimportant taxes revenue-wise were also folded into the carbon tax, such as the tax on compressed natural gas for automotive use, simplifying the tax system.

repercussions on other tax bases (the provincial property tax and the federal tax on personal assets).

A clear example of rent-seeking was a 5% tax on cellular telephony bills partially earmarked to finance Argentina's Olympic committee. This earmark was replaced by a budget allocation, hoping that in the future this expenditure's merit would be judged against other programs and reviewed.

An ad-valorem tax on "luxury cars", defined as those above a threshold set by the Ministry of Production by its own discretion, was a disguised protectionist policy. The Treasury sought to remove this discretion and transform it into a Pigouvian tax assessed on vehicle age and weight, also inviting the provinces to reform their car registration fees in the same manner, although this proposal was internally challenged and didn't make it to the Draft.

The Draft also proposed to reduce other ad-valorem taxes on specific transactions, such as insurance premiums, hard to justify from a public economics perspective.

4.10 Provincial taxes[56]

4.10.1ISIB

Even though constitutionally the provinces have full autonomy on tax bases and rates, the federal government can negotiate and push for changes through voluntary "fiscal agreements"[57]. In parallel with the 2017 Tax Reform, the 2017 Fiscal Consensus was a landmark agreement between the federal government and the provinces. Its main provisions involved the provincial gross income tax, whereby provinces committed to eliminating the so-called "internal customs" and levying the tax on exports. They also agreed to tax rate caps which gradually decreased over a five-year period, being only marginally binding in the first year (2018), eventually reaching 0% for upstream and intermediate activities by the fifth year. The aim was to transform the tax into a final gross sales tax and eliminate the vertical integration incentive.

The preferred direction for the tax reform would have been to differentiate tax rates according to whether the purchaser in a transaction was a final consumer or a firm. But tax administration and firm systems were not suited to implementing such changes in the short term. The path of least resistance was to do a variation on the usual year-to-year changes to

[56] The Fiscal Consensus also capped or eliminated other less significant taxes and attempted to create a unified database of municipal taxes.

[57] Here we're using "agreements" as a generic term. Past agreements were either titled "Pacts", "Accords", or (during the Cambiemos administration) "Consensus".

the provincial tax codes[58]. Each year the prevailing tax rates, set per industry[59], were slightly tweaked. At the time, the provinces used custom 6-digit classification tables based on (but different than) the national classifier. The Team also did not have access to micro or statistical data to precisely estimate the desired impacts, as the centralized system for processing the ISIB tax returns was controlled by a member of the Peronist opposition not aligned with the reform proposal. We could only perform rough calculations using similar but not identical tax bases. And there was not even a unified database of all the nominal provincial tax rates available. All these constraints led the Team to adopt a known design[60] that imposed gradually decreasing caps on upstream economic activities as a way to avoid taxing intermediate transactions. This was an adequate approach to the taxation of agricultural and industrial activities, for example, but had shortcomings when addressing professional services.

The reforms attempted to claw back the 0.8% of GDP in additional tax revenues that the Supreme Court granted to the provinces in November 2015. The tax reform, which originally included an expansion of the PIT, would be revenue neutral on the federal taxes that are shared between the federal government and the provinces. However, the Fiscal agreements would lead to a decrease of 1.1pp in provincial tax revenues through the ISIB rate caps[61]. Thus, most of the decrease in overall tax revenues was to be financed by the provinces. This also concentrated the fiscal effort on one of the worst taxes in the system regarding efficiency.

4.10.2 Property taxes

The existing revenue sharing agreement of the federal tax on personal assets created incentives for the provinces to race to the bottom on the fiscal valuation of urban and rural property. A coordination mechanism was needed so that all closed the gap to market valuations at a similar pace. By the Fiscal Consensus, the federal government agreed to create a property valuations agency charged with adopting methodologies to perform objective mass appraisals based on market valuations, and the provinces agreed to participate and adopt those procedures, ensuring access to cadastral and related registries. The aim was to increase proceeds by 0.4% of GDP.

[58] There would only be a few days between the enactment of the Fiscal Consensus and the new rates entering into law, so the changes needed to be minimally disruptive for both the tax administration and the taxpayers.

[59] Several other conditions affected tax rates. Each province varied rates according to firm revenue brackets, and taxes did sometimes change according to the customer or the specific goods sold, even within the same industry code.

[60] It was used in the 1993's Fiscal Pact that similarly tried to reign in the ISIB.

[61] The ISIB rate caps would generate a revenue loss of 1.5pp of GDP, partly offset by higher property taxes. The Fiscal agreements included the adoption of the federal property valuations agency that would help the provinces close the gap between fiscal and market assessments, both technically and politically.

4.10.3 Federal revenue sharing agreement earmarks and tax expiration date

The Fiscal Consensus also mostly upheld the preexisting allocation of federal taxes between the federal and provincial governments. The federal government would have relinquished its earmark of the tax on bank credits and debits (0.7% of GDP) if no action was taken. Overall, the provinces made large concessions (tax cuts, expenditure reductions, no changes to earmarked taxes shares, dropped court claims, and others) without any significant compensation from the federal government[62].

The simultaneous Fiscal Responsibility Law established fiscal rules for both the federal government and the provinces. The federal government has very weak enforcement instruments over the provinces, mostly limited to approving or not credit lines with multilateral institutions and restricting discretionary transfers from the federal government[63]. The main fiscal rule was capping the increases in recurrent spending to inflation, and capping total primary expenditure increases to inflation if the province records a primary deficit and/or is highly indebted[64]. The rule was set to ease growing spending along with nominal GDP from 2020 onwards for overall budget surplus provinces. Capping growth to inflation, the expected real GDP growth for the following years, and the decrease in the tax burden mandated by the Fiscal Consensus would combine to help deflate the provincial government size. As part of the Fiscal Consensus, the provinces also agreed to drop 56 demands against the federal government for alleged noncompliance with past revenue sharing agreements. The demands amounted to 7% of GDP (stock).Things the Draft skirted

[62] The Federal government did agree to one long standing claim by the Buenos Aires province. In the 1990s, due to the close political alignment with the Federal government it received a preferential share of the income tax proceeds. The province was removed from the shares-based revenue split, and was instead given lump sum transfer fixed in nominal pesos. This benefited the province during the deflationary context of the late 1990s, but by 2017 their effective share of the income tax proceeds had fallen close to zero, exacerbating its general disadvantaged position in the general revenue share splits due to malapportionment. Given that this rule was called *the Buenos Aires Metropolitan Area fund* and that the province was governed by *Cambiemos*—the first non-Peronist provincial government since 1987 in Buenos Aires—it became politically untenable not to address the situation. At the same time, it is politically impossible for the governor of any other province to agree to resource concessions seen as coming from their treasuries destined for Buenos Aires. The smaller provinces carry historical grievances from two centuries ago—at this point a core part of their political identity—against the larger one, despite it being severely disadvantaged in the federal revenue share splits over the last half a century. Thus, the face-saving transaction for all the parties was for the smaller provinces to agree to some concessions to the Federal government, and for the Federal government to compensate the Buenos Aires province. This resulted in no significant transfers between the Federal government and the aggregate of the provinces.

[63] Most transfers are automatic, daily, and according to the revenue sharing agreements whose legal status is below the Constitution but above regular federal legislation. No government has dared intervene with this mechanism so far.

[64] Additional rules limited personnel roster increases to the population growth rate, among others.

The Team at the Ministry designed the Reforms while operating relatively free of political constraints. A few key areas were, however, outside the scope of the Reforms. We have talked previously about the political agreement blocking a personal income tax reform (§4.2). A related issue was the mandatory health insurance scheme. The main source of financing is a 9% tax on the wages of formal dependent workers[65]. The mandatory health insurance providers are managed by the unions — a remnant of a 1960s political bargain. This is a vehicle for the rent seeking of the unions' leadership[66] to which sheer inefficiency must be added on top, resulting in an expensive system. Any attempt to streamline the sector to ultimately reduce the distortion of the labor market would immediately be blocked by the unions. Thus, the government declined to pursue this reform from the beginning.

The Cambiemos administration quickly dismantled a myriad of quantitative barriers to international trade (Bernini and Lembergman, 2020), reducing rents. However, the taxes on imports remained unchanged, for the most part[67]. Changing the Mercosur's Common External Tariff demands unanimity between the member countries.

5 Negotiations with stakeholders – Congress, other executive branch ministries and business interests

The three Peronist administrations that preceded Macri's raised the tax burden, as indicated by the tax revenues/GDP indicator, by 12 percentage points between the years 2001 and 2015. The increased distortions caused by this growth led to a demand for tax reform, which the Cambiemos administration channeled. Thus, almost no tax hikes were considered politically tenable by the administration, regardless of whether Argentina's parameters were below international standards, Pigouvian efficiency reasons, or of the efficiency-increasing tax cuts that they could enable elsewhere in the tax system.

5.1 Changes to the Treasury's Draft

The Ministry of Treasury's draft tax reform underwent significant changes before the president submitted it to Congress. The process resembled a sequence of negotiations with various veto players—other ministries, the president, coalition leaders, and ultimately congressional blocs. While the team anticipated some modifications, we were surprised by the extent to which the final version reflected demands from the Executive rather than from Congress.

Consultations with the Executive began soon after the Treasury finalized its draft in June 2017. From that point, political considerations began to constrain the menu of feasible

[65] With higher effective rates for the lower skilled and part time employees due to minimum tax bases.
[66] Union leaders often outright own the hospitals and other providers contracted by the insurers.
[67] The Mercosur's tariff exceptions list to the Common External Tariff was used, however, replacing low-volume items (such as sparingly used industrial inputs) with high value ones (like notebook computers).

reforms, blocking several of the team's preferred measures. Although the personal income tax system exhibited notable distortions, by August the Executive's version had sidestepped the issue entirely. Political agreements reached with the opposition in 2016 had produced an unstable compromise that could not be reopened, and which effectively required full exemption for all workers. Another major change was the removal of the proposed super-simplified tax regime. Despite its low effective tax rates, reduced compliance costs, and minimal oversight by the tax agency, it had become extremely popular among the government's electoral base—making it politically untouchable.

The Treasury's full draft was kept on a need-to-know basis until three weeks before it was made publicly available for comment. Minister Dujovne presented the reform at a press conference [add date], earlier than the team had anticipated. The government's resounding midterm election victory had emboldened the political leadership to accelerate the reform's unveiling. However, this left only a narrow window for public discussion, as the bill was scheduled to be submitted to Congress two weeks later. Anticipating fierce resistance from other government stakeholders—particularly the Ministries of Production and Agriculture—the Treasury sought to minimize the time available for lobbying efforts.

Yet the intensity of the opposition was underestimated. The Ministry of Production swiftly mobilized affected special interest groups to obstruct key provisions. One striking example was the excise tax reform on alcoholic beverages. Rather than rationalizing tax rates, the final version increased distortions in favor of wine producers (concentrated in Mendoza and other provinces). Congressional lobbying also introduced a preferential rate for vaguely defined "artisanal beers"—a loophole later exploited by medium-sized producers—and blocked the planned rate hike on high-alcohol-content beverages. The Ministry of Agriculture, for its part, successfully secured a VAT reduction for poultry and pork products.

The Ministry of Production also warned energy-intensive industries about the proposed carbon tax, contributing to its dilution. More critically, opposition arose from within the Executive itself. The government had previously made a major political and fiscal bet by offering substantial investment incentives for developing the Vaca Muerta shale formation. Despite the Energy Minister's support for the reform, the proposed tax rate was cut from USD 25 to USD 10 per ton of CO_2-equivalent. Anticipating such pushback, the Treasury had deliberately chosen a rate that left room for negotiation within the Executive and Congress. Nonetheless, the final changes went further than expected, fully exempting natural gas from the tax. On the other hand, new products such as coal and fuel oil were ultimately included. As a result, Argentina established an explicit tax on the carbon content of fossil fuels—one that could be expanded in the future either by revisiting the natural gas exemption or by raising the carbon price. Politically, this would be more feasible than increasing existing taxes.

As later explained by Galiani in a public lecture[68], the reform's has also a political objective. At the time, Mercosur was negotiating a free trade agreement with the European Union—an agreement that was signed in 2019 but never ratified by the respective parliaments. Introducing a carbon tax was an important step in aligning Mercosur's climate policies with EU expectations. Indeed, when the agreement was announced, European officials praised the inclusion of commitments to improved environmental standards by Mercosur countries, including the development of carbon pricing instruments.

The industry-leading multinational soft drink companies responded positively to the Draft Reform's proposal for a sugary drinks tax, while also suggesting pragmatic modifications. The bill included an ad-valorem tax that mirrored the structure of the existing tax regime, since the team's preferred alternative—a fixed levy per gram of sugar—had not met the internal deadline for inclusion. Interestingly, the multinationals proposed a similar framework, as they anticipated being better positioned than local competitors to reformulate their products with reduced sugar content, gaining market share in the process.

In contrast, local beverage companies—and more significantly, domestic sugar and sweetener producers—focused their lobbying efforts on Congress. These groups ultimately succeeded in removing the proposed tax from the bill. This reversal, however, occurred with the tacit approval of the reform team. In fact, Minister Dujovne and Secretary Galiani met with the governor of Tucumán—the country's main sugar-producing province and a Peronist stronghold—to strike a political deal. In exchange for the support of Tucumán's senators for the pension reform, specifically the new pension indexation formula, the government agreed to drop the sugar tax provision from the legislation. Given the fiscal importance of the pension reform, the team chose to prioritize it over the sugary drinks tax.

The Ministry of Finance successfully lobbied for the inclusion of personal income tax deductions for insurance premiums, aiming to promote growth in the insurance industry. However, there was no solid economic rationale for this tax expenditure, given that insurance payouts were—and remained—exempt from taxation. The broader "industrial policy" justification was even weaker. Nonetheless, the deduction carried a relatively low cap of approximately USD 3,000, in line with most itemized deductions in Argentina, and thus had a negligible fiscal impact.

By contrast, the Executive's most fiscally significant interventions were of a broader nature. The VAT refund scheme for capital goods purchases was expanded, and the corporate income tax rate reduction schedule was accelerated—shortened by one year—thereby increasing the short-term revenue cost of the reform.

[68] https://www.youtube.com/watch?v=ITfx0pJICJk&list=PLE3QeoHcHATCHu13cwZynER142FPoRr73

5.2 Changes in Congress

Several provisions of the reform were ultimately dropped during congressional negotiations. Each of these proposed changes adversely affected constituencies geographically concentrated in a small number of provinces. Notable examples include the proposed tax on sugary drinks, the elimination of the corporate income tax exemption for mutual savings institutions, the removal of tax subsidies for the electronics industry, and the elimination of bonus personal income tax deductions for public employees and the oil sector. The reform's comprehensive approach—aiming to address multiple distortions and preferential treatments simultaneously—ironically made it easier for affected interest groups to coordinate their lobbying efforts and successfully block these changes.

Congress also introduced several additional measures, though most had limited fiscal impact. These included a reduction in personal income tax for self-employed workers entering the general regime, increased export refunds for small and medium-sized enterprises (SMEs), and new VAT refunds for beneficiaries of federal grants targeted at low-income students and other vulnerable groups. In a further concession, utility companies were exceptionally allowed to claim VAT credits on their purchases in excess of their VAT debits—a measure justified, in part, by the persistence of substantial energy subsidies, which still accounted for 1.3% of GDP in 2017.

5.3 Revenue neutrality and expected results

The reform ultimately lost its fiscal neutrality, as Congress approved nearly all proposed tax cuts while rejecting most tax increases. Nonetheless, the short-term revenue impact for the federal government remained limited due to the reform's gradual implementation—estimated at 0.4% and 0.5% of GDP in 2018 and 2019, respectively, in static terms. A conservative general equilibrium simulation, which incorporated gains from improved resource allocation and enhanced tax administration, estimated the net revenue loss for the consolidated public sector—including provincial tax cuts—at 0.2% and 0.3% of GDP for 2018 and 2019, respectively. These figures remained well within the fiscal consolidation path, given the projected pace of expenditure reductions.

More importantly, the reform's net fiscal impact was also lower than the revenue losses the federal government would have incurred under a "business as usual" scenario. In particular, without the reform, the 0.7% of GDP in earmarked revenues from the tax on bank credits and debits would likely have reverted to the provinces, restoring their historical share. From this perspective, the reform—when accounting for all effects—may not have cost the federal government any revenue at all. Indeed, it arguably left the Treasury in a better position than it would have faced had no reform been enacted and the provinces successfully reclaimed those tax revenues.

Most of the changes to the reform were made before the bill was sent to Congress, largely in response to requests from within the government. Crucially, the core components of the

reform—those with the greatest fiscal implications if altered—were approved without modification. These included reforms to payroll taxes, the corporate income tax, and the tax on bank credits and debits. In contrast, legislators chose to expend their political capital on provisions that, while relatively minor in revenue terms, had significant symbolic weight for their provincial constituencies. A prime example was the tax on sugary drinks. These adjustments helped offset the political costs of broader compromises. By the end of the process, nearly all the "room for concessions" that the Treasury team had strategically built into the draft had been exhausted.

In addition to assessing each amendment's partial fiscal impact, we evaluated the reform's effect on long-term economic growth using a computable general equilibrium (CGE) model. The baseline model assumed an elastic labor supply, real wages growing in line with real GDP, and investment behavior following Tobin's Q framework. Under these assumptions, the model estimated that the economy would be approximately 5% larger by the fifth year relative to a no-reform scenario. Importantly, the model captured only a subset of the dynamic effects and likely underestimates the full growth acceleration that the reform could trigger.

5.3.1 Escape clauses

The reform package included several built-in "escape clauses" to safeguard the fiscal consolidation program in the event of adverse shocks—an eventuality that materialized with the sudden stop in capital flows in 2018. These clauses granted the Executive delegated powers to modify tax rates, postpone the implementation of scheduled rate reductions, or adjust other parameters across various taxes. While such delegation is a longstanding practice in Argentina, successive Supreme Court rulings over the past two decades—prompted by past Executive overreach—have progressively narrowed its scope.

One of the most significant levers for fiscal flexibility was the tax on bank credits and debits. The Executive retained the authority to suspend the portion of this tax that could be credited against corporate income tax (CIT) liabilities. Reversing this credit mechanism would have yielded a static revenue gain of approximately 0.7% of GDP, shared across federal and subnational governments.

Another key instrument for ensuring compliance with the fiscal consolidation path was the export tax regime. Historically, export duties have served as Argentina's go-to tool for closing fiscal gaps during crises. Until 2012, they were considered outside the scope of constitutional limitations on the Executive's power to set tax rates. Although a Supreme Court ruling that year brought them under constitutional constraints, the Executive still enjoyed considerable delegated authority over export taxes in 2018. Crucially, export taxes accrue entirely to the federal government. As such, they offer a uniquely powerful mechanism for rapidly raising revenue without prolonged legislative debate and, more importantly, without triggering disputes over federal-provincial revenue sharing. In practice,

this tool could have been used to recoup the 0.9% of GDP lost through export tax cuts implemented by the Cambiemos administration by the end of 2017.

5.4 Capital income taxation and the 2018 sudden-stop

In the final stages of the legislative process, the congressional opposition secured last-minute changes to the capital income provisions, notably the elimination of the tax exemption for nonresident investors on income from short-term instruments issued by the Central Bank (Lebacs), which were central to the conduct of monetary policy at the time. The withholding tax took effect on April 26, coinciding with a sharp ~150 basis point selloff in Lebac prices. This episode has been cited as one of two key catalysts of the broader market selloff that, compounded by a severe drought, ultimately led to Argentina's Stand-By Arrangement with the IMF in July 2018.

An internal event study conducted by the Treasury, however, suggests that the implementation of the tax had only a limited effect on asset prices. The study offers a rationale for this finding, implying that the market reaction may have been driven more by broader macroeconomic vulnerabilities than by the specific tax measure.[69]

The administration chose not to exercise presidential veto power, consistent with its broader approach during that period of refraining from vetoing legislation passed by Congress, even when it disagreed with its content. Notably, the same congressional Peronist leadership that had pushed for the inclusion of the tax on nonresident income from Central Bank instruments during the reform negotiations later moved swiftly—and quietly—to repeal it after their party returned to power in December 2019.

6 Implementation

The Executive's discretionary powers opened the door to renewed lobbying by both government stakeholders and industry groups. Although administrative law formally vested all tax policy authority in the Treasury, other agencies frequently intervened in practice—often pursuing their own agendas. As a result, several painstakingly negotiated and legislated reforms were subsequently delayed, diluted, or reversed by other ministries.

A clear example was the proposal to adopt market-based property valuations for provincial tax assessments, which would have helped offset revenue losses from less efficient subnational taxes. Despite being approved by all provinces through a binding *Fiscal*

[69] The event study conducted by the Treasury compared the yield evolution of an affected instrument—Lebacs maturing in September—with that of comparable, still-exempt bonds possessing similar risk and duration characteristics, before and after the tax was implemented. The effective withholding tax rate was 2.15%, and in many cases, investors were able to credit this amount against income tax liabilities in their country of residence. However, the timing of the tax coincided with a broader global selloff in late April 2018, rendering the results of the study inconclusive.

Consensus, the initiative was blocked by other Executive officials on ideological "small-government" grounds.

Even though tax policy was nominally under the Treasury's exclusive jurisdiction, other ministries could directly alter tax outcomes. The Ministry of Production, for instance, controlled the revenue thresholds defining Small and Medium Enterprises (SMEs). Since most taxes—and many subsidies—are notched in favor of smaller firms, Production could (and did) effectively reduce tax liabilities for a large share of companies by substantially raising these thresholds. Similarly, the Ministry of Agriculture could prompt the Executive to declare a "productive emergency," triggering tax exemptions and payment deferrals. Intended to assist in cases of severe droughts, floods, or plagues, the mechanism was often repurposed to permanently reduce tax burdens on low-productivity activities or regions by repeatedly renewing the state of emergency.

The Ministry of Labor also wielded direct influence over payroll taxation. It could approve collective bargaining agreements between unions and industry associations that reclassified portions of wages as "non-contributory," exempting them from employee and employer contributions—despite this practice being explicitly illegal. Moreover, it successfully pressured the Executive to accelerate the implementation of payroll tax deductions that were legally designed to phase in gradually over five years, granting the full benefit to over 7% of formal workers in the first year after the reform's enactment.

The reform's overarching goal had been to promote employment and investment while preserving neutrality, thereby curbing the proliferation of industrial-policy-style tax privileges. Despite the considerable political capital invested, other ministries continued to advance sector-specific tax regimes without Treasury consultation—making later reversals politically costly. The 2019 *Knowledge Economy Law* exemplified this pattern, expanding the generous incentives originally designed for software developers to encompass nearly all content-creation and professional service industries.

Along similar lines, the Treasury's draft had proposed a comprehensive overhaul of the tax administration agency's governance. The agency frequently issued regulations inconsistent with Treasury directives and without prior consultation, either raising compliance costs for taxpayers or altering effective tax rates absent any cost-benefit analysis. Despite formally reporting to the Treasury, the agency operated with near-complete autonomy, dealing directly with the Presidency and other ministries while pursuing multiple, often conflicting, objectives—effectively neutralizing efforts to coordinate tax policy.

In practice, the Treasury lacked the institutional tools to shape the agency's priorities, allocate its resources, or design performance incentives. A substantial portion of the agency's budget was devoted to developing administrative systems requested by other ministries—particularly Production, Agriculture, and Labor—to implement their

independent tax policies. Additional demands came from social policy agencies requiring constant updates to income and wealth verification systems for means-tested transfers. These competing demands, layered on top of the implementation of the tax reform itself, left little capacity for the agency to focus on core functions such as combating tax avoidance and reducing compliance costs. Consequently, progress on key initiatives—most notably the nationwide rollout of fully digital VAT records—lagged behind schedule, undermining both the reform's macroeconomic sustainability and the broader fiscal consolidation effort.

Even so, the policy drift observed during 2016–2019 likely remained less severe than what would have occurred under a "no-reform" counterfactual, given the widespread and uncoordinated pressures for tax relief the government faced during that period.

7 Aftermath of the Tax Reform

The 2018 sudden stop accelerated the need for fiscal consolidation and led to the first deviation from the multiyear implementation schedule, pausing or reversing many of the tax cuts mandated by the Reform and previous legislation. The adoption of inflation adjustment for the corporate income tax statements was deferred, and the budget for VAT credit refunds for capital goods purchases was reduced.

The following presidential administration (begun in December 2019) canceled most of the Tax Reform provisions immediately after taking office, increased rates to 2015 levels, and created new taxes. Most of the other unrelated reforms of the Macri administration were undone as well.

Something similar happened to the Fiscal Consensus. The implementation of some provisions was delayed by 1 year in 2018. The subsequent Fiscal Consensuses of 2020-22 kept the ISIB rate caps at 2019's levels rather than decreasing as scheduled. They also relaxed the caps on some activities, notably financial intermediation, financial services, internet, and cellular communications. The rate "cap" for financial intermediation, at 9% of revenues, creates a sizable distortion in an economy under a high inflation regime[70].

This highlights one of Argentina's biggest challenges: politically- and macroeconomic-instability -induced policy volatility. The 2017 Tax Reform relied on the administration's credibility to maximize the impact of the pre-scheduled tax changes on present investment decisions. The promises lasted only for about a year, as the possibility of a change in administration (and policies) became a self-fulfilling prophecy. No policy change can ever be assumed to last beyond the current administration, at most. Taxpayers rightly discount such promises rendering tax incentives ineffective. Increasingly, industries lobby for "fiscal stability" provisions that increase the burden on other industries and reduce the available

[70] When inflation tends to infinity this would be a 9% tax on the assets of financial institutions.

fiscal policy tools, providing industry-specific patches for the distortions created by the macroeconomic and political volatility.

The budget discussed in late 2018 for the following year included several tax changes that partially undid previous reforms with the objective of propping up revenues. The preset declining rates on the wealth tax (§3.12) were tripled[71]. The government thus reneged on the "promise" of low rates made at the time of the 2016 tax amnesty. Similarly, the budget set a very low cap for the refunds on capital goods VAT credits. It also stipulated that the inflation adjustment in the corporate income tax would only be computed by a third in each subsequent year, e.g. a third of 2018's inflation adjustment would be computed in each year in the 2019-2021 period, instead of all at once in 2019[72].

The budget also served as an opportunity to create several new preferential tax treatments, such as (among others) a lowered VAT rate on housing construction, and more importantly a VAT exemption for all of the supply chain of media conglomerates, newspapers, and the printing and publishing industry, as well as a preferential refund window on VAT balances not applicable to any other economic sector.

The country experienced a negative shock in 2018 – a severe drought and a sudden stop in international financing, and inflation shot upwards. This context highlighted the challenges of implementing externality correcting taxes in an inflationary context. Efficiency dictates that a fixed money amount is levied on each unit of "bad" product consumed. The carbon tax imposed a fixed amount per ton of CO2 equivalent and the minimum cigarettes tax was set per pack. These charges had to be indexed to inflation, and updated every three months according to the Reform. In a deteriorating macroeconomic and political environment, this created constant demands on the government to skip the updates, portrayed as "tax hikes".

8 Political economy lessons

The 2017 reform was as much a political coordination exercise as it was a technical redesign of tax instruments. Argentina's federal structure—highly malapportioned and populated by provinces with heterogeneous economic bases and entrenched elites—creates a setting in which nationally efficient tax design is systematically filtered through local and sectoral vetoes, side-payments, and logrolls. In such a system, the "feasible set" is defined by a common-pool problem over federal revenues, by the institutional over-representation of smaller, poorer provinces, and by the electoral cycle that only renews partial congressional shares every two years.

[71] A flat rate schedule was changed for a gradually increasing one, and a new deduction for owner-occupied housing.

[72] The inflation adjustment scheme would suffer subsequent changes in 2019 (a sixth spread over six years), 2020 (no adjustment), and 2021 (full adjustment). The criteria for triggering the inflation adjustment, based on the cumulative inflation over the prior three years, was also altered to prevent firms from claiming the benefit.

Three constraints were pivotal. First, macroeconomic stabilization created a binding fiscal ceiling. The government confronted a large inherited deficit and adopted a disinflation program that, under the old pension mobility rule, mechanically raised real spending as inflation fell. This macro/fiscal linkage narrowed the space for any reform with front-loaded revenue losses and made "near-neutral" changes the only viable path. Second, the administration's minority status in both chambers required coalition-building across multiple Peronist factions and governors whose preferences were tilted toward preserving provincial revenue autonomy and transfer flows. Third, administrative limits—widespread informality, weak enforcement capacity, and high compliance costs—meant that an "optimal tax" blueprint could not be implemented at once; the reform had to work with the state we have, not the state we wished we had.

Within this political technology, sequencing and packaging dominated. The Treasury's draft made efficiency the organizing principle (reduce cascading and notches; align CIT and VAT with international practice; narrow exemptions; introduce Pigouvian logic where applicable) and then embedded fiscal guardrails and escape clauses to protect the consolidation path. Recognizing that many upstream taxes were provincially controlled, the federal government paired the national bill with a Fiscal Consensus that capped the provincial turnover tax rates over time, dismantled "internal customs," and committed provinces to modernize cadastres and property valuations. The quid pro quo rested on two pillars: (i) provinces had enjoyed a favorable revenue shock after the 2015 Supreme Court ruling and could, in principle, finance a transition away from the most distortionary bases; and (ii) spending caps in the Federal Fiscal Responsibility Law would create the fiscal room to sustain those tax cuts.

Even so, the reform encountered textbook manifestations of veto politics. Sector-concentrated interests—alcohol, sugar-sweetened beverages, Tierra del Fuego electronics, and later portions of energy—leveraged geographic concentration to mobilize provincial delegations. The executive branch was not monolithic: line ministries with legacy industrial-policy agendas (Production, Agriculture, Labor) and discretionary levers (SME thresholds, "productive emergency" declarations, wage component reclassification, accelerated payroll deductions) diluted hard-won neutrality and increased policy drift post-law. The sugary-drinks episode is emblematic: a technically-sound excise with health co-benefits became a bargaining chip exchanged for Senate votes on pension indexation—a swap the Treasury accepted because the macro stakes of the indexation fix dominated the (modest) revenue and efficiency gains from the beverage tax.

Forecasting and credibility further complicated the coalition. Reform packages everywhere over-predict revenue from base-broadening and under-predict the political stickiness of tax expenditures (Hines, 2018). Argentina was no exception: Congress accepted most rate cuts and rejected much of the base expansion, bending the package away from ex ante neutrality. The capital-income chapter shows the double bind: politically indispensable to signal "fairness" and broaden the PIT base, yet operationally hard to implement under high and volatile inflation, with Congress adding last-minute changes (taxing nonresidents on

central-bank paper) that raised market-stability concerns during the 2018 sudden stop. Delegated escape clauses were a deliberate hedge against such asymmetries—e.g., pausing the CIT creditability of the bank debits/credits tax or altering export duties if the consolidation path came under stress—but frequent recourse to discretion carries its own political-economy cost: it invites new rounds of lobbying and weakens the commitment value of forward guidance, a major selling point of the Reform Draft.

Two broader lessons follow. First, growth diagnostics matter for reform design (Rodrik-Hausmann-Velasco, 2005). In 2016–2017 the binding constraints on investment were macro instability,policy volatility, and regulations depressing productivity of the whole economy as in the labor market, not headline statutory rates per se. When politics foreclose welfare-improving swaps that involve visible tax increases (say, broadening PIT or pruning VAT expenditures) in exchange for large efficiency gains elsewhere, a strictly revenue-neutral "surgery" on taxes may be dominated by regulatory reforms with low fiscal cost and high credibility dividends. Second, institutional control is as important as statutory content. Without unity of command over the tax administration and the line ministries that can re-create special regimes by regulation, a neutrality-oriented law will erode in implementation. In short: design travels only as far as the coalition, the macro anchor, and the administrative state can carry it.

9 Conclusions

Argentina's 2017 tax reform was conceived as a growth-friendly rebalancing under severe fiscal and political constraints: align corporate taxation with international practice, reduce the labor wedge at the bottom, unwind cascading provincial turnover taxes, rationalize VAT and excises, and begin to tax capital income—while keeping the package roughly neutral to safeguard consolidation. The strategy was explicitly gradualist and state-capacity-aware: use legal forward guidance to influence current investment and hiring decisions; synchronize provincial changes through a Fiscal Consensus; and hard-wire escape valves in case the macro turned.

The record suggests four takeaways for future reforms. First, credibility is a fiscal instrument. In high-volatility environments, the expectation that today's law will be reversed tomorrow severely discounts the impact of scheduled rate paths and weakens the investment channel. The 2018 shock and the subsequent partial rollbacks—deferring CIT inflation adjustment, capping VAT credit refunds on capital goods, reinstating higher wealth-tax rates—illustrate the cost of thin credibility. The corollary is that reforms with low discretionary content, clear automaticity, and shared enforcement across levels of government stand a better chance of surviving the cycle and delivering the promised efficiency gains. Forward guidance is of limited value if discount rates are high.

Second, coordination beats perfection. Because provinces control key distortionary taxes (provincial turnover tax, stamp duties) and property cadastres, a federal reform without a provincial pact is doomed to under-deliver. The 2017 Fiscal Consensus was directionally

right: cap and phase down the provincial turnover tax—especially on upstream stages—and modernize property valuations to backfill revenues with less distortionary bases. Where empirical precision is infeasible ex ante (no unified provincial turnover tax microdata; heterogeneous provincial classifications), simple, transparent caps and nationally visible milestones are superior to intricate but unenforceable formulas.

Third, discretion is a magnet for rent-seeking. Delegated powers and ministerial by-laws are tempting tools to manage macro risk and implementation bottlenecks, but each additional decreeable lever widens the aperture for special pleading. If discretion is unavoidable, it should be rule-bound (quantitative triggers linked to macro targets), sunsetted, and fiscally scored in the budget to raise the political cost of ad hoc deviations[73]. Strengthening governance and alignment between the Treasury and the tax administration is part of the same problem: without unified prioritization (e.g., digital VAT books nationwide, standardized refund timelines, penalty indexation), technical advances will be crowded out by bespoke regimes and compliance burdens will remain high.

Fourth, target the true margins. The combination of large informality, high compliance costs, and backward-looking indexation produces highly uneven effective tax rates. Over time, the reform frontier should move away from blunt rate changes toward measures that directly expand the formal base at low administrative cost. Here the payments and data revolution changes what is feasible relative to 2017: with widespread digital money and e-invoicing, it is now more practical to reduce the cash premium and to automate third-party reporting, narrowing evasion without punitive headline rates. A modern reform could pair (i) real-time withholding on platform-mediated transactions, (ii) standardized, automatically indexed penalties and thresholds, and (iii) simplified, pre-filled returns for the self-employed as the functional replacement for the super-simplified regime—while protecting truly low-income micro-entrepreneurs through explicit transfers rather than opaque tax notches. The payoff is a broader, fairer PIT/VAT base that allows the gradual retirement of cascading provincial taxes.

Finally, a strategic implication. When macro instability and political fragmentation are the binding constraints, the expected return to regulatory and administrative reforms (competition policy, labor-contract certainty, customs modernization, automatic and timely tax-refund, credible fiscal rules) may exceed the return to large, rate-cutting tax packages, unless those packages are tightly pay-as-you-go and institutionally insulated. The 2017 experience supports a pragmatic maxim: if you cannot control the full policy nexus—macroeconomic anchor, legislative majorities, and administrative execution—then either narrow the scope to measures with high credibility and low discretion, or sequence reforms so that credibility and capacity are built first and only then "spent" on complex tax swaps.

[73] Automatic sunsetting can be challenging when no Constitutional-level commitment devices are available — benefits then to be renewed *ad infinitum*.

In sum, the 2017 reform moved the system in the right direction under adverse conditions, but its growth dividend was capped by macro shocks, coalition arithmetics, and implementation drift. The next iteration should lock in what worked—coordination with provinces, anti-cascading logic, investment neutrality—while shifting the center of gravity toward credibility-enhancing rules, digital-era enforcement that shrinks informality, and institutional designs that minimize discretionary leakage. Only then can Argentina replace a politics of episodic tax surgery with a politics of sustained, rules-based state capacity.

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