TAX POLICY APPROACHES

International Growth Centre

WHEN THIRD-BEST IS BEST

FIRST-BEST

First-best approaches form a 'perfect' tax system, with no barriers to information or enforcement. In practice, these are not used as they are impractical and inequitable (e.g., lump sum tax).

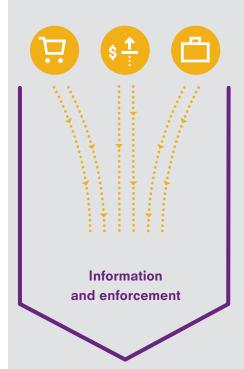
SECOND-BEST

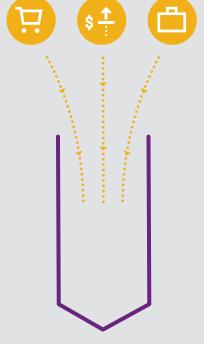
High-income countries use second-best approaches to tax collection to maintain production efficiency. With good information and enforcement, they can collect 30–40% of GDP in revenue.

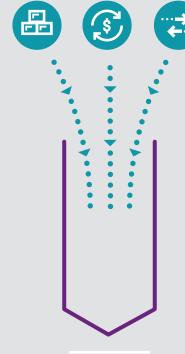
Low-income countries use the same approach. But a lack of information and enforcement capacity means that they can typically generate only 10–15% of GDP in revenue.

THIRD-BEST

In many low-income countries, a **third-best approach**, which addresses limits to information and enforcement, could reduce tax evasion and generate more revenue.











(%GDP)













