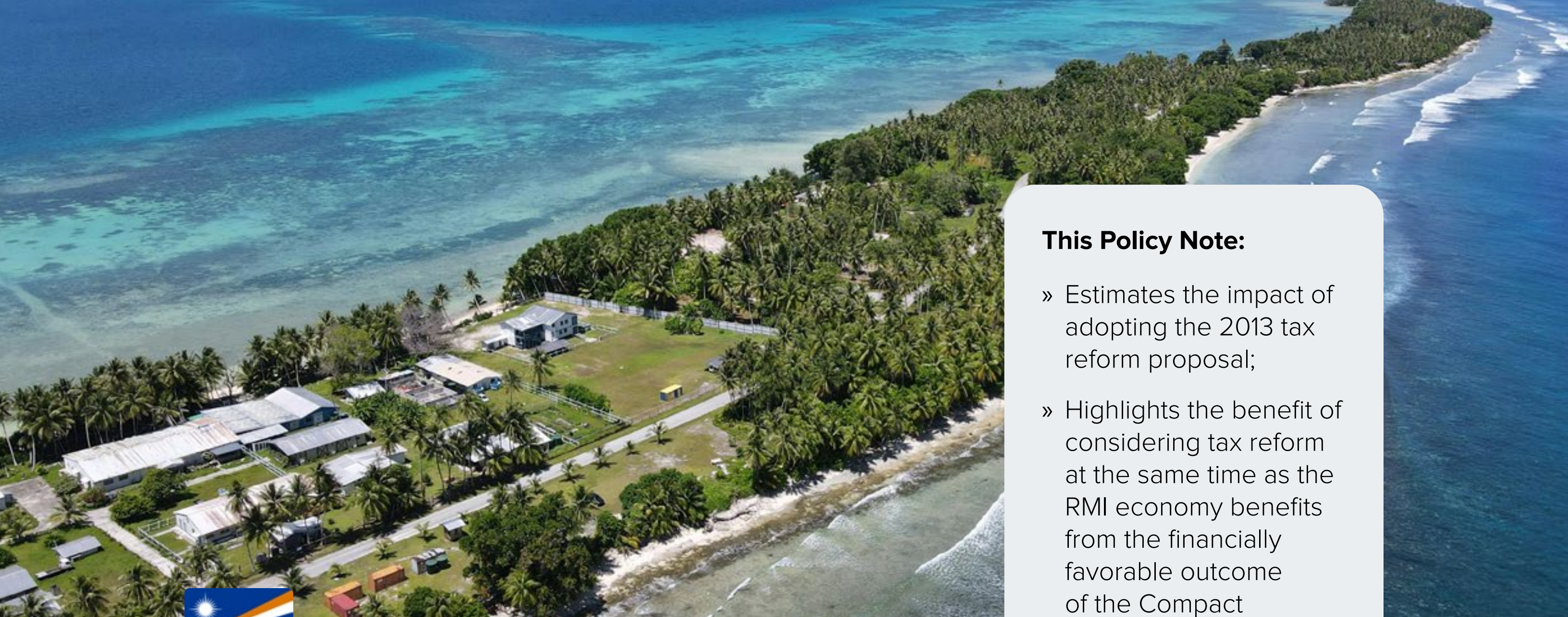

RMI Policy Note

Tax Reform Options for the RMI and Estimation of Fiscal and Economic Impact

1. Summary

The RMI has considered reforming its outdated tax regime on several previous occasions. These reforms were often designed in response to periods of fiscal stress: due to real reductions in Compact funding or a weak economy, as during the Global Financial Crisis. At present, with the financially favorable outcome of the Compact negotiations, additional revenues, and strong performance from sovereign rents, the timing is ideal to initiate tax reform. The absence of fiscal stress should make a tax reform package designed to modernize and improve efficiency easier to achieve. Further, the new administration is considering a series of social policies to benefit the less advantaged parts of the community through an increase in the minimum wage and introduction of some type of Universal Basic Income. Reform of the tax regime will thus complement the existing focus of reform.

At this time, we are not, repeat NOT, recommending all of the specific rates and elements of a best practice tax reform package; rather, we are providing the rationale for reform and estimating the revenue impact of a specific reform package as a starting point for our policy advocacy. More specifically we have created an accessible policy modeling tool—The Tax Reform Impact Calculator (TRIC). Our team genuinely looks forward to sharing the tool with policymakers—thereby enabling them to try different rates and combinations to: (i) better understand the effects of rate and element changes; and (ii) ultimately have greater ownership of the eventual chosen tax reform package enabling more informative public education sessions with stakeholders.

This Policy Note:

- Estimates the impact of adopting the 2013 tax reform proposal;
- Highlights the benefit of considering tax reform at the same time as the RMI economy benefits from the financially favorable outcome of the Compact negotiations and strong performance in sovereign rents;
- Complements the administration's current reform initiatives, such as increasing minimum wage and adopting a Universal Basic Income (UBI);
- Attempts to achieve fiscal revenue neutrality through the tax reforms, while increasing real incomes for most households;
- Identifies a shift in the burden of taxation on households through reforms that modestly increase the burden of taxation on businesses and visitors; and
- Most importantly, launches the Tax Reform Impact Calculator (TRIC), enabling policymakers to simulate tax rate and reform combinations to achieve the administration's objectives.

This Policy Note has been prepared by the Graduate School USA's (GSUSA) Economic Monitoring and Analysis Program (EconMAP). A digital copy of this note, and additional information on the EconMAP program, is available online at ***https://econmap.org***.

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So, we start with a specific package knowing full well modifications will be enabled through use of the TRIC. The comprehensive tax reform effort undertaken in 2013 provides an excellent starting point and is outlined in this note with minimal modification. The essence of the reforms is to:

1. Replace the BGRT and general import taxes with a modern broad-based consumption tax, to eliminate cascading, strengthen compliance, and simplify the tax system;
2. Introduce a net profit tax for large businesses while retaining the BGRT for small businesses;
3. Replace the existing specific import duties and local government taxes on alcohol, tobacco, motor vehicles, and fuel with similar excise taxes; and
4. Modify the wages and salaries tax by broadening the tax base, expanding the current tax-free threshold, and introducing a higher tax rate for high-income earners.

It is intended that the revenue impact of the proposed tax reform impact will be neutral; meaning the introduction of a modern regime with new taxes replacing the old regime with virtually zero impact on fiscal balance. A Marshall Island Consumption Tax (MICT) of 10 percent on goods and services is proposed. The wages tax will be reformed with an initial tax-free deduction of $4,160 for all wage earners. The current Business Gross Receipts Tax will be eliminated for any business with annual turnover above $100,000 and replaced by a business profits tax of 20 percent[1]. Local government will be included in the reforms, and sales taxes will be abolished and replaced with an equivalent amount through revenue sharing of the MICT. Inclusion of local government in the reforms will improve efficiency and avoid subjecting local government to the MICT.

The revenue-modeling results suggest that the impact on inflation and on the Consumer Price Index will be minor. Importantly, the combination of the introduction of the MICT and wage tax reforms will significantly increase real household incomes by an average of about 5 percent. Under the existing tax regime Marshallese households make the largest contribution of 67 percent of total tax collections while businesses contribute only 11 percent. Under the proposed reforms the tax burden on Marshallese households will be reduced to 53 percent while that of business will increase to 23 percent. Thus, the reform package produces a more equitable distribution of the overall tax burden.

Implementation of the reforms will require updating the set of legislation prepared as part of the 2013 proposed tax reforms. Cabinet approval will be required before submission of the draft legislation to the Nitijela for consideration. Donor support will be needed for legal drafting and provision of a project manager/tax administrator to drive the process. Public hearings will be required, presentations made, and briefing notes distributed. A new tax IT system will be required to ensure the benefits of a modern tax system are fully captured. It is anticipated that redrafting and passage of the reformed laws could be completed by the end of 2024. Implementation can be undertaken in 2025 with the objective of a go-live date in early 2026.

2. Background

The RMI, in common with her sister states in the FSM and Palau and other US territories, inherited a tax regime from the Trust Territory days. However, this regime has long been recognized as being inefficient, outdated, and inappropriate to the modern economy of an independent nation. Attempts to modernize the RMI tax regime extend back to the mid-1990s, when in response to a reduction in Compact funding, an ADB reform project proposed the adoption of a value- added tax, reforms to the

1 This is one element of the 2013 package that we believe should be modified; best practice argues for the net profits rate be set at the top marginal rate of the wages tax—or 16 percent.

wages tax, and introduction of a business profits tax[2]. Legislation was passed, but the reforms were never implemented, and the law was repealed.

TRAM initiated, and PFTAC prepares tax reform agenda. In response to the Global Financial Crisis in 2008 and tight fiscal position, the minister of finance set up the Tax and Revenue Reform Modernization Commission (TRAM) to make recommendations to reform the revenue collection system and to strengthen the capabilities and effectiveness of the Division of Revenue and Taxation (DRT). To assist the TRAM in its deliberations the RMI requested PFTAC to prepare a tax reform proposal.[3] Following the standard tax reform model developed by the IMF for small developing economies, PFTAC made the following major proposals:

1. Replacing the BGRT and general import taxes with a broad-based consumption tax, to eliminate cascading, strengthen compliance, and simplify the tax system;
2. Introducing a net profit tax for large businesses while retaining the BGRT for small businesses;
3. Replacing the existing specific import duties and local government taxes on alcohol, tobacco, motor vehicles, and fuel with similar excises; and
4. Modifying the wages and salaries tax by broadening the tax base and expanding the current tax-free threshold and introducing a higher tax rate for high-income earners.

In March of 2010 the TRAM finalized its report and made a series of recommendations to the minister.[4] In broad terms, the Commission members agreed with the conclusions of the PFTAC Report, although several minor adjustments were proposed to make the reforms more appropriate to the RMI.

Laws drafted for a reformed tax regime. In 2012, a tax reform advisor was recruited under AusAID for a two-year period. A series of 6 laws was drafted with support from the IMF, and an implementation plan was established together with a series of public briefings and publications outlining the reforms:

1. Marshall Islands Consumption Tax Act,
2. Marshall Islands Import Duty (Amendment) Act,
3. Marshall Islands Revenue Administration Act,
4. Marshall Islands Revenue Authority Act,
5. Marshall Islands Excise Tax Act, and
6. Marshall Islands Net Profit Tax Act.

Unfortunately, the tax reform initiative lost momentum and no further action was taken. A series of administrative reforms and strengthening was initiated in 2020 at the start of the COVID pandemic with support from AusAid through the provision of a tax advisor.

3. Favorable timing creates a new opportunity for tax reform

With a favorable financial outcome of the Compact negotiations and strong revenue performance from sovereign rents, the timing is appropriate to reinitiate the tax reform process. With the advent of the 2023 amended Compact agreement, C-23, the timing is ideal to consider comprehensive tax

2 See Policy Advisory Team ADB TA, Taxation Issues, paper # IB1Taxnissu2, Majuro, October 1995.
3 PFTAC Republic of the Marshall Islands: Reforming the Tax System, Suva Fiji, Sept 2009.
4 Tax and Revenue Reform and Modernization Commission Republic of the Marshall Islands, Republic of the Marshall Islands: *A Holistic Approach to Reforming the Tax and Revenue System*, Majuro, March 2010.

reform. In the previous efforts to create a modern and efficient tax reform regime, the RMI economy was in recession and fiscally compressed. In the mid-1990s the economy was experiencing of the second step-down in Compact funding. For the initial period of the amended Compact C-04 and during the global financial crisis of 2008/2009, the economy stagnated, and the fiscal situation was severely constrained. However, at the current time with the favorable growth in sovereign rents from both fishing fees and the ship registry, coupled with a significant expansion in Compact resources, the economy will experience a period of strong growth. Promotion of tax reform is thus unlikely to be met with the strong headwinds the RMI had experienced in the previous attempts. Furthermore, with the introduction of ASYCUDA (Automated System for Customs Data), which was developed by UNCTAD, a significant part of the tax regime and administration will have been upgraded and will form a sound foundation for the implementation of a new tax system.

Tax reform coupled with the increase in minimum wage and introduction of a Universal Basic Income (UBI) would form a solid platform for a new administration seeking reform. Implementation of the tax reform proposal should not be considered in isolation; rather it would best be part of the overall reforms currently under consideration in the Marshall Islands. The new reform-minded administration is initially promoting changes to the minimum wage to bring it into line over a period of time with the basic needs poverty line.[5] In addition, the 2023 Amended Compact allows for a Universal Basic Income to be funded from the Compact Trust Fund. Policies to implement a UBI will need to be discussed and developed over a period of time; although expectations have been raised within the RMI for early introduction of the UBI. Reform of the tax system, while promoting growth and development, will complement the minimum wage policy and UBI to ensure equity and protection for the lower income and disadvantaged members of the community.

The former tax reform initiative remains a sound basis for reform. It is not the intent of this policy note to reinvent the wheel with any new tax reform proposals. Rather, the former tax reform proposals developed for the RMI provide a sound basis for reform. In this note a brief overview of the existing tax regime will be undertaken; its weaknesses will be noted, and a discussion will follow regarding the main features of the proposed reform agenda. This will be followed by an estimation of the economic and fiscal implications of the proposed reforms and concluded with an outline of the next steps forward.

4 The Current Tax Regime

The current tax regime is based on a system that is simple to administer, which was inherited from Trust Territory days and implemented in the US-affiliated territories in the Pacific. It was based on four basic taxes: (i) a tax on wage income, (ii) a gross receipts tax levied on business turnover, (iii) duties on imports, and (iv) sale taxes.

The wages tax

The wages tax creates distortions and needs reform to reflect current living costs. Under the current system, which has been in existence for over 30 years, the first $1,560 of wages is exempt from tax. Between $1,561 and $5,200 a tax is levied at 8 percent, with an allowance that the first $1,560 is not taxed. However, above $5,200 and below $10,401 all income is taxed at 8 percent. This creates an anomaly that someone earning between $5,200 and $5,337 will receive less take home pay than somebody earning $5,200. Wage earners earning more than $10,400 are taxed at 12 percent. In FY23 the wages tax represents the major share of national government taxes with collections of $16.2 million or 46 percent

5 See, Graduate School USA, *Estimating an Appropriate Minimum Wage in the Republic of the Marshall Islands (RMI) Based on a Basic Needs Poverty Line*, see also ***https://econmap.org***, Honolulu, March 2024.

of total taxes. The buoyancy of the wages tax, the ratio of the change in wage tax collections to the change in nominal cash GDP (excluding offshore fishing), was 1.37 (FY10–FY22) but just 0.99 over the longer period FY04–FY22. While further analysis is required, the increase in the later period suggests an increase in the number of wage earners crossing the tax boundary from 8 to 12 percent and suggests the need to modify the tax boundaries (brackets).

Import duties

Import duties lack buoyancy. Import duties are the second most important tax item in the RMI. In FY23 $9.4 million was collected (27 percent of domestic tax collections). General imports are taxed at a rate of 10 percent with food items at 6 percent. Other import duties are levied on sin tax items such as alcohol and tobacco at varying higher rates. Fuel taxes are levied on a specific or volume basis at low rates and well below their carbon content or environmental cost. Soft drinks are also taxed at higher rates to protect the nation's health. Transport vehicles attract differential rates. Estimation of the buoyancy of import taxes is difficult given the variability of rates and unreliability of the estimation of import values in the RMI. For example, during the period FY04–FY23 import taxes recorded a very low buoyancy ratio of 0.08, reflecting significant changes in tax rates during the early period. More recently, during the FY10–FY22 period, the buoyancy ratio rose to 0.81, a period over which tax rate changes were minimal.

The import regime is inefficient, has many exemptions, and is not compliant with international trade agreements. The import duty regime is relatively simple and free of protective tariffs, but a variety of exemptions exist. Imported inputs used for manufacturing or packaging and labelling are allowed to be imported duty free. However, given the underdeveloped nature of the economy and lack of manufacturing, distortions due to protection are minor. Fuel imported by MEC (Marshalls Energy Company) for power generation is exempt from duty, and while reducing costs to consumers encourages the use of fossil fuels and carbon emissions. Exemption of duties is provided on fuel imports by MEC for resale to fishing vessels, as well as with fishing equipment imported to the RMI for the use on licensed fishing vessels. The later exemptions are justifiable on the grounds of enabling domestic entities to remain competitive in export markets. Lastly, renewable-energy equipment for the purposes of power generation and energy efficient equipment, together with renewable-energy vehicles, are allowed duty free. As a result of the import tax regime and differential taxes on domestic production, the RMI does not qualify for participation in international or regional trade-related organizations such as the WTO or the PICTA/PACER regional trade arrangements.

Business Gross Receipts Tax (BGRT)

The BGRT is highly inefficient and distortionary. The BGRT is levied at 3 percent and is intended as a proxy income tax, although the base of the tax is gross turnover and, as such, is a de facto sales tax. The tax suffers from the well-known cascading effect, such that each sale from one business to another multiplies the total tax intake. Thus, the more businesses there are in the supply chain, the higher is the effective tax rate on the final product. The lack of equivalence of tax rates between one business and another or between different industries in the economy distorts production incentives and resource allocation. A further adverse effect of the BGRT is that the rate of tax is the same regardless of the level of profit and, for example, a loss-making concern is still subject to tax despite having no net income. The benefit of the tax is that it is broad based and simple to administer. However, the adverse effects are well known and disliked by the business sector. The RMI economy has progressed significantly since Trust Territory days when the tax was first introduced, and the time is right to repeal and replace the BGRT with a more modern and efficient tax regime.

Exemptions provided to the SOE sector introduce economic distortions. In FY23 BGRT collections were $8.2 million and represented 23 percent of domestic tax collections. In terms of buoyancy the BGRT ratio of the increase in BGRT tax collections to nominal GDP was 0.89 during the longer FY04–FY22 period but just 0.86 in the more recent period of FY10–FY22, suggesting stability in terms of predictability compared with the wages and import tax. The provision of services delivered by SOEs of electricity, water, sewerage, telecommunications as well as domestic air transport and copra production are exempt from the tax thereby introducing distortions to the economic system. Fish and fish products have been exempted from the BGRT to enable the fishing sector to remain competitive in international markets.

Local Government Sales Taxes

Local government sales taxes were an issue of contention in earlier reforms. The final element of the RMI tax regime is the sales taxes levied by the local governments of Majuro (MALGOV) and Kwajalein (KALGOV). MALGOV levies a rate of 4 percent on all retail sales and collects revenues of $2.8 million. Likewise, KALGOV levies a sales tax of 10 percent and collects $1.2 million. Both governments also collect taxes based on sin goods and fuel. Both governments and the national government also levy taxes on daily hotel room rates. While local government taxes are relatively minor, the governments closely guard their right to impose taxes, which, during the previous attempts at tax reform, was an issue and point of contention.

5 The Tax Reform Proposal

Tax reforms are designed to be revenue neutral. The tax reform proposal developed in 2013 was supported by the IMF, PFTAC, and a resident tax advisor in the RMI for a two-year period. Laws were drafted and ready for consideration by the Nitijela. The proposal formed a sound basis for tax reform and is replicated in this policy note. The intent of the reforms is designed to be revenue neutral. That is, the total impact of the changes is not designed to levy additional tax on the community. That said, the estimation of tax collections under a reformed system is based on the existing tax regime. The current regime is known to be inefficient, and tax avoidance is suspected to be large. It is thus anticipated that additional revenues are likely to be generated although the size of the increase is unknown at this stage.

The centerpiece of the tax reform is the Marshall Islands Consumption Tax (MICT). The main feature of the proposal is to replace and repeal the existing general import duties and BGRT with a broad-based consumption tax (Marshall Islands Consumption Tax or MICT) and business profits tax (BPT). The new consumption tax is a value-added tax. The tax is collected at each stage of the supply chain in proportion to the value added at each stage and is in effect passed down the line to the final consumer. Each registered taxpayer gets a credit for the MICT paid on inputs of goods and services purchased from other suppliers and collects MICT on sales paid for by the consumer. Registered businesses thus pay taxes on neither input nor outputs. Rather, it is the final consumer, or non-registered MICT businesses that are subject to the tax. This is predominantly households, tourists, and nonprofits.

Tax reform will convert remaining specific import duties to excises. In addition to the introduction of the MICT, the tax reform proposal includes the provision for conversion of existing “sin” taxes levied on alcohol and tobacco, soft drinks, et cetera into excises. Excises are imposed equally on both imports and domestic production and create a level playing field between domestically produced items and imports. The existing fuel tax will be converted into a carbon tax and levied in proportion to the carbon emitted. The few remaining import taxes would also be converted into excises.

Local government sales taxes will be abolished but revenue benefits will be shared among different layers of government. Local government sales taxes will be abolished as part of the reforms, but the new regime would include a revenue-sharing formula to compensate local governments for the loss of revenue. This provision in the earlier 2013 reform proposal proved particularly contentious, reflecting local government's desire to maintain an independent revenue policy. However, the normal recommended treatment between different layers of government in the case of introduction of a VAT is for all governments to collectively reap the benefits of an efficient revenue regime and to share the benefits among the affected parties.

Tax reform is economically efficient. A critical principle behind the tax reform is the concept of economic efficiency. This means that taxes are levied in a non-distortionary way, and no producer has preferential treatment to another. This means that investors make decisions on the merits of investing in different industries and is not affected by the choice of differential effective tax rates. A key result of the tax reform is that there is no advantage provided to either imports or domestically produced items. This means that the RMI would be eligible to join and take advantage of the benefits of international trade organizations such as the WTO, PICTA, and PACER.

The second key piece of the tax reform is the introduction of a business profits tax. To create a level playing field and preserve equity through the tax system between businesses and consumers, the tax reform includes the provision of the Business Profits Tax (BPT), a tax on business profits that are registered for the MICT. This replaces the existing BGRT. The business profits tax is based on the normal concept of income tax paid in most jurisdictions by corporations, partnerships, sole proprietors, and other business formations. Businesses are allowed to deduct all normal business expenses from gross income and the remaining profit is subject to BPT. Unlike the current BGRT, businesses only pay tax when they create positive profits. Since the BPT is paid on profit and not turnover, it does not cascade through the system.

Reduction in the rate and removal of distortions in the wages tax. To support government policy for social protection (an increase in the minimum wage and introduction of UBI), it is intended to provide a minimum tax-free allowance or deduction against total wage income that is not subject to tax. While this will benefit low-wage earners it will also benefit all wage-earning groups and reduce the overall burden of wage taxes. It will further compensate low-income earners for the regressive or negative impact of the introduction of the MICT. A further characteristic of the current wage tax regime is the tax-free allowance for wage earners less than $5,200, but those above this amount are subject to tax at 8 percent. Thus, some wage earners on higher incomes above $5,200 will receive less net pay than those below the threshold. This is clearly distortionary and has been removed in the tax reform proposal.

New dividend and interest tax. The new tax regime will introduce a withholding tax on dividend and interest income.

New Customs and Revenue Authority. A new Revenue Authority will be established, like MISSA, to administer the new tax regime. This will permit a more efficient administration, improved customer service, revenue sharing to the two local governments, and greater tax compliance under an incentivized culture.

6 Principles of tax policy.

In section 3 a description of the existing tax regime was outlined, and in section 4 the key elements of the new reformed system were presented. Before providing a discussion of tax rates and impact of the proposed reforms, the old and new regimes are compared against the principles of taxation[6]:

6 Pacific Financial Technical Assistance Centre, PFTAC, IMF, *Improving Revenue Collection and Capacity in Forum Island Countries, Suva*, Fiji, September 2010.

» **Efficiency/Neutrality**. Taxes should be raised, as much as possible, in a non-distorting fashion, leaving economic choices the same as they would have been without taxes.

» **Simplicity and transparency**. Simple taxes are good taxes. A tax with simple rules, few and low rates, minimal exemptions, as well as a clear, wide, measurable base provides more revenue and less opportunity for evasion.

» **Equity/Fairness**. In general, individuals with similar incomes should pay similar taxes (horizontal equity) and individuals with higher income should pay more taxes (vertical equity).

» **High revenue-generating capacity**. The tax system should be able to supply the government with the resources it needs and as the economy grows to meet its spending obligations on a sustainable basis with minimal volatility.

» **Harmonization with international trade**. Less reliance on distortionary trade taxes and greater reliance on domestic taxes such as VAT and excises, which tax all goods and services regardless of their origins, helps countries to obtain the benefits of free trade, as well as to prepare for WTO entry.

» **Feasibility**. The design of taxes should be aligned with the capacity of tax administration to actually implement and collect tax revenue.

» **Integration**. All main taxes should be consistent, in terms of thresholds, rates, and regulation, in order to ensure fair treatment of all taxpayers and minimize administrative costs.

The Business Gross Receipts Tax. Looking at each tax in turn, Box 1 below provides a summary of the benefits and costs of the existing and proposed tax regimes. The existing BGRT, due to its cascading nature, is a highly inefficient tax; it creates distortions in the economy and biases resource allocation against low margin products and favors the converse. However, it is simple to administer and without exemptions has been a transparent tax in the RMI. While the tax is broad based, it has little capacity for high revenue generation due to its distortionary nature. Due to the large differences in effective rates of tax on domestic products and imports, it is not consistent with international trade regimes. Due to the simplicity of administration, it has been effectively implemented at low cost. Overall, it has been accorded a score of 0.

Import duties. Import duties generally fare poorly on most fronts. Import duties are both distortionary and lack transparency, with both large numbers of exemptions, smuggling, and avoidance. Revenue generation is frequently weak due to exemptions, and customs duties are mostly inelastic with respect to GDP and clearly not in accord with international trade organizations. Trade taxes are frequently implemented due to easy identification of cross-border flow of goods and transactions. Import taxes have the lowest score of all 5 taxes at -3.

Wages tax. The wages tax is a tax on income and as such does not impact resource allocation or economic efficiency. It is also relatively simple to implement and is the largest tax revenue source in the RMI. It also scores high on equity grounds and is a progressive tax. That said, the tax as it currently stands is distortionary due to the discontinuity at the $5,200 tax band as described above. With reform this imperfection can be rectified. In its current form it is easy to administer and scores well on achievement of tax principles and ranks at the top with the MICT. The wages tax has the highest score of existing taxes at 4.

Marshall Islands Consumption Tax. The MICT scores very well on economic efficiency and on neutrality. While it is sometimes considered to be difficult to understand, it is in effect a simple and transparent tax if implemented in a "clean" fashion without differences in rates on different products. Its weak point is on equity grounds that poor households pay a higher proportion of their income due to lower savings rates. Due to the wide base of the tax, it has a large revenue-generating capacity and is harmonized

Box 1: Comparison of Palau's tax regime with tax-reform principles

	Existing taxes			Tax Reform	
	GRT	**Import taxes**	**Wages tax**	**VAT**	**Business Profits Tax**
Efficiency/Neutrality	-1	-1	0	1	0
Simplicity and transparency	1	-1	1	1	-1
Equity/Fairness	0	0	1	-1	1
High revenue generating capacity	0	-1	1	1	0
Harmonization with trade	-1	-1	0	1	0
Feasibility	1	1	1	1	1
Score	0	-3	4	4	1

with international trade agreements, reflecting its non-distortionary nature. It is generally considered a simple tax to administer and by its nature contains an implicit incentive for compliance. In addition to the principles identified, a VAT also encourages both exports and investment as these categories are "zero-rated" and attract no tax. Due to the highly desirable economic and administrative characteristics it forms the basis of nearly all modern tax regimes.[7] Overall, it has been accorded a score of 4.

Business Profits Tax. The BPT, like the wages tax, is a tax on income and as such does not impact resource allocation, economic efficiency, or trade relations. It is also considered a complex tax, and while it is simple in principle to understand, its application is often far from simple. Like the wages tax it is considered to be an equitable tax and balances the regressive nature of a VAT. Given the undeveloped nature of the business sector in the RMI, it is not anticipated to be a buoyant tax. Finally, while administration is more complex, the availability of accounting firms enabling implementation provides tax thresholds that are not set too low. Overall, the BPT is scored 2.

Tax reforms and proposed rates for 2013 are re-simulated for FY22 and found to be slightly revenue negative. In this policy note the tax rates proposed for the 2013 tax reform initiative have been adopted as the base.[8] The original proposal was intended to be revenue neutral, which means that estimated total tax collections after implementation of the reforms should be the same as before the reforms. The impact of the changes in tax rates and introduction of new taxes is simulated in this paper and is found to be slightly revenue negative based on FY22 collections and structure of the economy.

GSUSA has prepared a tax reform model to simulate the impact of the tax reforms. Accompanying this policy note the GSUSA has prepared an Excel workbook, Tax Reform Impact Calculator (TRIC), which can be used by policy makers to simulate different assumptions, estimate the impact, and align with policy objectives. The TRIC not only estimates the revenue impact of the reforms but also the impact on wage earners, inflation, and the different institutions in the economy.

Income taxes. The 2013 reforms proposal eliminates the $5,200 tax band distortion with the following rates and bands:

$0 - $4,160	Untaxed
$4,161 - $10,400	8%
$10,401 - $20,800	12%
>$20,800	16%

7 The US is the only major developed nation that does not have a VAT.
8 The views of the GSUSA are thus not included in the simulations.

For the BPT and businesses with a turnover greater than $100,000 a rate of 20 percent was selected. In some economies, such as Palau, the BPT is set at the top marginal rate. This procedure ensures equality between business owners and the highest group of wage earners. A further consideration is that the OECD has indicated that a minimum business tax rate of 15 percent is sufficient to avoid a jurisdiction being classified as a tax haven.

For a small business with a turnover less than $10,000, an annual presumptive tax of $80 per quarter applies and for amounts between $10,000 and $100,000, businesses are subject to a 3 percent tax similar to the existing BGRT.

Marshall Islands Consumption Tax. A rate of 10 percent was selected for the MICT. Only businesses with a turnover greater than $100,000 per annum would be subject to the new tax. The 2013 tax reforms made provision for electricity and water to be "zero-rated" and thus the final consumer would not be subject to tax on these items. This policy note strongly recommends implementation of a "clean" tax regime. Zero-rating electricity is highly distortionary and negates the principle of economic efficiency and administrative simplicity. Recognizing that power is an important element of household consumption and that the MICT might incur additional costs on low-income households, the tax reform has been designed to include offsets to assist disadvantage groups. Namely the reduction in wage taxes, increase in the minimum wage, and UBI will all assist in compensating low-income households. Further the MEC could provide low-income households with a reduced tariff that is financed through a community service obligation of CSO.

Local government and revenue sharing. The tax reform proposal also proposes that the local government sales taxes are abolished and are treated as registered taxpayers for MICT purposes. Being treated as registered taxpayers, local governments would be required to collect MICT on sales of any goods and services but would more importantly be eligible for a MICT tax credit on purchases. The loss of sales taxes is intended to be compensated by a revenue share of 25 percent of MICT collections for MalGov and 10 percent for KalGov. These revenue shares have been estimated to ensure full compensation for the loss in local government revenues. Under the current regime, local government would not be MICT registered and would be liable to pay national government taxes on purchases of goods and services. Treatment of local government as an MICT-registered taxpayer is thus consistent with the principle that lower levels of government are not subject to taxes imposed at the national level[9].

Excises and other taxes. In the reforms the general import tax rate of 8 percent is abolished as is the 5 percent import tax on food. All other import taxes are converted into excise equally applied whether the good is domestically produced or imported. The new taxes on interest earnings and dividends are proposed to be at the low rate of 3 percent.

7 Impact of the tax reforms.

The impact of reforms on inflation is slightly deflationary. The design of the 2013 tax reforms was intended to be revenue neutral. When the reforms and tax rates proposed in 2013 are updated to FY2022 values, the latest available, it was found that a tax loss of $1.8 million was incurred (4.7 percent of the original tax effort). However, while the reforms remain broadly revenue neutral, the changes in the impact and incidence on the distribution of income are significantly different. In terms of inflation, the introduction of the MICT, repeal of the BGRT, food taxes, general import taxes, and local government sales taxes has a small deflationary impact on prices of 0.4 percent. Given that the reforms are projected to be revenue negative, a small reduction in prices is to be anticipated. However, these projections assume no change in behavior of agents in the economy. Most importantly they assume

9 The impact of these arrangements is simulated in the TRIC.

that private businesses do not use the reforms as a justification to raise profit margins. In Palau, the experience was that the private sector increased profit margins by the full amount of the Palau Goods and Service Tax (VAT) on top of existing purchaser prices. In essence the private sector internalized in their profit margins the former BGRT and general import taxes that had been repealed. The introduction of the reforms was thus accompanied by an increase in prices. With awareness of change in private sector behavior, the RMI is forewarned and in a position to take remedial action.

National government revenues are projected to fall by $2.1 million but local government makes a small gain. The overall impact on fiscal revenues for the national and local governments is shown in Table 1. The change in wage tax allowances and rates comes with a significant revenue loss. However, this is more than offset by new revenues from the MICT and Business Profits Tax. The reforms come with the repeal of the BGRT for registered MICT taxpayers and the removal of import duties from food and general items of 5 percent and 8 percent respectively. Other import taxes, mostly sin taxes, are replaced by matching excises. Local government sales taxes are repealed and replaced by revenue sharing of the MICT with the national government. The net result is that the national government loses $2.1 million in revenues with a small gain for local government of $0.3 million.

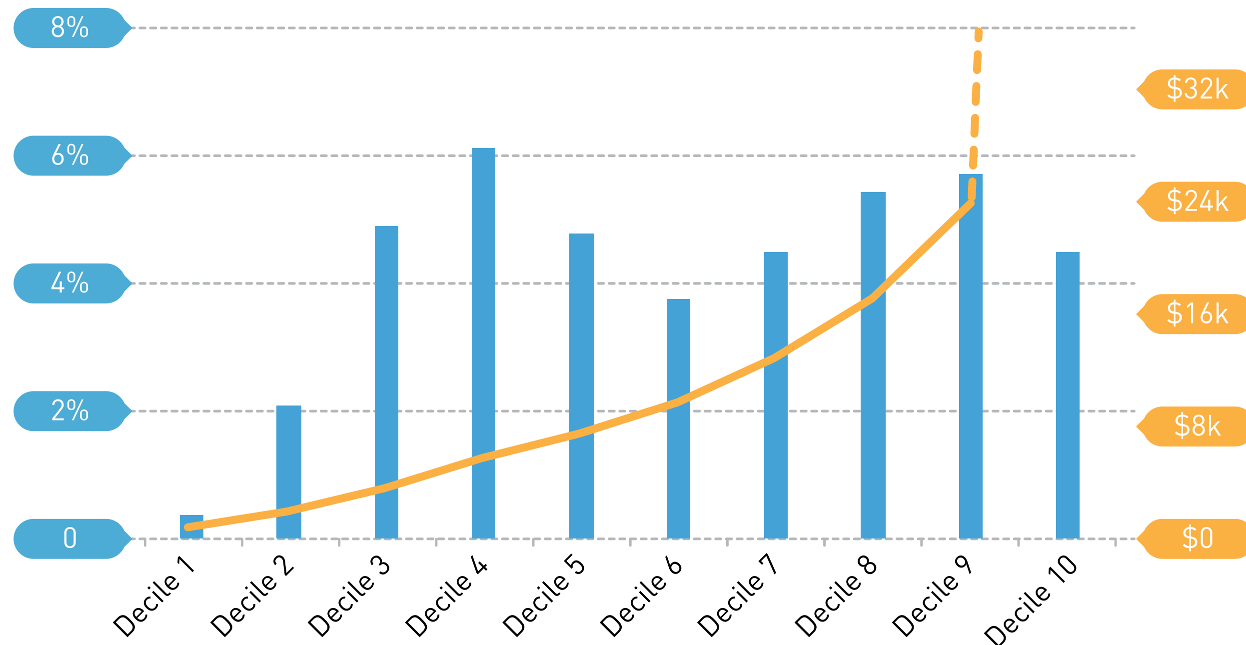
The impact of the reduction in wages taxes after allowance for changes in prices due to the MICT is an increase in real wages. The distribution of wage earners and impact of the reforms by decile group are shown in Figure 1. The figure indicates that 50 percent of wage earners earn less than $8,000 a year and 90 percent earn less than $24,000. The range of wage earners is thus concentrated in a small range of income levels. For the first two deciles, incomes are less than $4,000 per annum and less than the minimum wage. Rather than indicating that workers are paid less than the legal minimum wage, the

Table 1: National and Local government tax collections and transfers

National Government	FY22 Actual	Reform	Difference
Wages Tax	$16.7	$11.2	-$5.5
Marshall Islands Consumption Tax	-	$12.2	$12.2
Business Profit Tax	-	$7.5	$7.5
Gross Revenue Tax	$7.1	$0.3	-$6.9
General Import Taxes	$5.1	-	-$5.1
Other Import Taxes	$5.0	-	-$5.0
Excise Taxes	-	$5.0	$5.0
Miscellaneous Taxes	$1.0	$1.0	
Transfers to Local Governments	-	-$4.3	-$4.3
Total Collection	**$35.0**	**$32.9**	**-$2.1**

Local Governments	FY22 Actual	Reform	Difference
Sales Tax	$4.0	-	-$4.0
MICT Revenue Shares	-	$4.3	$4.3
MICT Payments	-	-	-
Total Collection	**$4.0**	**$4.3**	**$0.3**
General Government (National+Local)	**$39.0**	**$37.1**	**-$1.8**

Figure 1: Impact of wage tax reductions on real households incomes by decile



data more likely reflects that this group of workers are employed for less than full-time.[10] For the upper eight deciles the tax reforms indicate a substantial increase in real wages. The variation on real wage increases between deciles reflects the wage bands before and after the reforms.

Tax reform encourages a more equitable distribution of income and a level playing field between households and businesses. Figure 2 indicates some important changes in the distribution of the tax burden before and after the reforms. Before the reforms most of the incidence or burden of taxation fell on the household sector. The share of taxes paid for by the business sector was 11 percent while the share of the Marshallese households was close to 67 percent. The reform of the tax system results in a significant shift in the distribution of income, which reduces the share of Marshallese households to 53 percent and increases that of businesses to 23 percent. The tax reform encourages a more equitable distribution of income and a level playing field between households and businesses.

8 Implementation

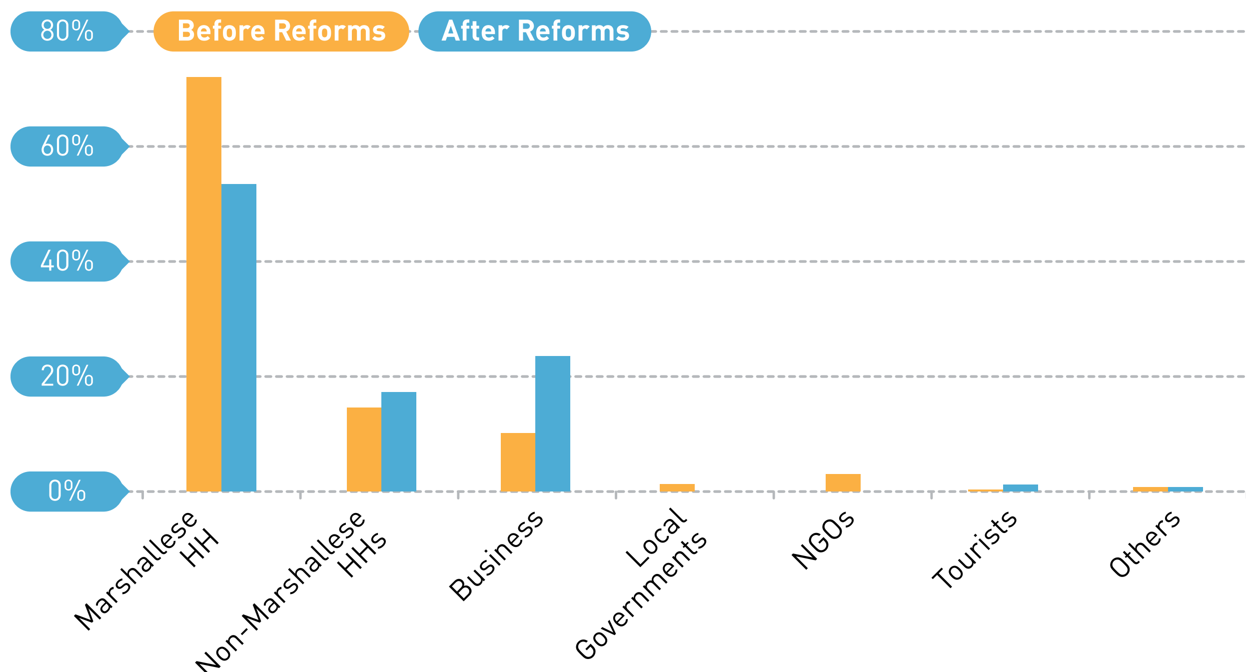
In this section a few important considerations are indicated for the implementation process. Initially, a cabinet decision will be needed to indicate the government's intent to adopt the forms. Several key ingredients will then need to be set in motion:

1. **Request for donor support**. Assuming the government intends to follow the reform program discussed here and outlined in 2013, a request will be required to seek donor support. A request to the IMF and PFTAC will be the starting point. The existing legislation provides an excellent set of bills to work from. However, these will need to be updated to reflect changes in best practice since the original drafting.

2. **Recruitment of a project manager**. A long-term project manager and tax administrator to oversee the reform implementation will be needed for a period of two years. Donors such as the ADB or

10 The wage data is based on quarterly returns to MISSA and thus includes workers who are less than full-time, see appendix for greater detail.

Figure 2: Share of tax burden by institutional sector, pre and post reform



World Bank would be an excellent source to backstop the reforms. In addition, bilaterals such as Australia and the Australian Tax Office have provided key support in the tax reform progress in other Pacific Island states.

3. **IT systems**. A key element of the reforms is the selection of suitable IT software. It is usually indicated that the duration of implementation of the tax reform process is determined by the IT selection and setup. There are two main approaches: (i) Commercial off-the-shelf software or (ii) custom-made or bespoke systems. The former approach has the advantage of a large user base and well-developed IT solutions. However, the system may impose certain institutional constraints reflecting the structure of the software. Bespoke systems are more flexible and may better fit the jurisdiction but will be unlikely to be developed as well or support a wide user base. In the case of the Marshall Islands with very limited IT skills, the use of a well-established COTS system would be highly recommended.

4. **Passage of legislation through the Nitijela**. With the reform proposal well developed and legislation updated, a steering committee will need to be established to drive the process. Public hearings will be required, presentations made, and briefing notes distributed (a series of excellent briefing notes were prepared as part of the original 2013 reform process). With a well-briefed public and private sector, the legislation will need to be passed by the Nitijela.

5. **Implementation**. Once the legislation is passed into law, a steering committee is established, a project manager put in place, and software selected, then implementation can proceed. It should be possible with commitment from the government to complete the initial steps during 2024 and initiate preparation during 2025 for a go-live date in 2026.

6. **Order of reform implementation**. The process normally recommended and followed in the recent example of Palau, was for the MICT or VAT to be implemented first, with the concurrent repeal of the BGRT, and general import taxes. At this time the reforms proposed to the wage tax can also be adopted to offset any regressive impact on low-income households. Premature

reform of the wages tax might risk the implementation of the MICT without any compensating action. Lastly, the Business Profits Tax can be fully implemented a year after the introduction of the MICT. However, in the interim to preserve government revenues, BPT progress payments can be made and adjusted at year-end to reflect actual outputs.

Technical Appendix: Estimating the Impact of the Proposed Tax Reform on RMI Government Revenues, Prices, and Wage Distribution

1 Impact on Revenue Collection

Marshall Islands Consumption Tax

The calculation of the impact on government revenues resulting from the proposed Marshall Islands Consumption Tax (MICT) starts with the estimation of the consumption tax base. This requires the identification of the total expenditure of each user in the economy, the expenditure on nontaxable items, and the gross revenue taxes (BGRT) and import duties on the items consumed (Equation 1).

$$\begin{aligned} MICT\ Base = & \ Expenditure - Expenditure\ on\ Nontaxable\ Items \\ & - GRT\ on\ Consumed\ Items - Import\ Duties\ on\ Consumed\ Items \end{aligned} \quad (1)$$

In this exercise, the expenditure of each final user[11] in the economy for FY22 from the RMI national accounts was utilized. In addition, financial services, domestic help, and overseas travel are considered tax-exempt, hence the consumption expenditures on these items are removed from the estimation process.

The BGRT for each final user is removed from the estimates by multiplying each user's expenditure with the current BGRT rate of 3 percent. The small difference between the estimated BGRT and the total BGRT collected was then allocated proportionally to each user to match the total actual collection. The total customs duty collected on food imports was proportionally allocated among households and tourists based on their FY22 expenditure, while the total customs duty collection on general imports is distributed to households, NGOs, investment, and exports based on their FY22 expenditure. Table A1 provides a breakdown by user of the BGRT, duties, and the MICT base.

Mathematically for each final user, the total MICT collection is estimated as follows:

$$MICT\ Collection_j = (1-\gamma)(1-\varepsilon)\tau_{MICT} Base_j \quad (2)$$

where:

γ is the turnover of non-MICT registered businesses, calculated to be 9.8 percent,

ε is the allowance for error, assumed to be 10 percent, and

τ_{MICT} is the MICT rate.

Assuming a 10 percent MICT rate, Table A2 illustrates the estimated MICT collection for each user. Notably, households will be the largest source of MICT collections given that it has the largest tax base with the anticipated collection in the reform scenario at $12.2 million.

11 Refers to households, government, NGOs, capital formation, exports, and imports of tourism services.

Table A1: BGRT and Foodstuff and General Imports Duty Allocation by User (in USD)

	BGRT	Foodstuff Duty	General Imports Duty	MICT Base
Government	797,831	-	-	52,064,224
Households	4,498,102	2,734,660	1,509,855	140,273,279
NGOs	89,494	-	-	5,840,110
Investment	345,297	-	388,889	-
Exports	1,417,277	37,825	475,730	1,940,226
Imports	-	-	-	4,440,669
Total	**7,148,000**	**2,772,485**	**2,374,473**	**204,558,510**

Source: EconMAP calculations.

Table A2: Estimated MICT Collections (in USD)

	Collection
Households	11,249,917
NGOs	468,377
Investment	-
Exports	155,606
Imports	356,142
Total	**12,230,042**

Source: EconMAP calculations.

Local Government Sales Taxes

Currently, the Majuro Atoll Local Government (MALGOV) and the Kwajalein Atoll Local Government (KALGOV) levy 4 percent and 10 percent tax on sales, respectively. As part of the tax reform, these local government sales taxes will be abolished, and both MALGOV and KALGOV will be considered registered taxpayers for MICT purposes. This would imply that both would be able to collect MICT on sales of any goods and services and would be eligible for a MICT tax credit on purchases. With the loss of revenues from sales taxes, the national government could compensate local governments for revenues from the MICT tax collection.

In determining the appropriate revenue share of the local government, the percentage share of each local government has been set to exceed the ratio of their current collection to the estimated MICT collection. Thus, ensuring that local governments are fully compensated for the loss of their sales taxes. Calculations show that the share of MALGOV needs to be larger than 23.2 percent of the total and larger than 9.5 percent for KALGOV to recover the loss in revenues.[12]

For the current exercise a revenue share of 25 percent was adopted for MALGOV and 10 percent for KALGOV, respectively, Table 3 shows the estimated impact on local government revenues. As observed, local governments will incur a net benefit with the tax reform if they opt to be MICT-registered.

12 MALGOV share = 2,834,449/12,230,042 = 0.232; KALGOV share = 1,164,915/12,230,042 = 0.095

Table A3: Estimated Revenues for the Local Governments (MICT-Registered)

	Actual	Reform	Difference
Local Sales Taxes	**3,999,364**	**-**	**-3,999,364**
Majuro Atoll Local Government	2,834,449	-	-2,834,449
Kwajalein Atoll Local Government	1,164,915	-	(1,164,915)
MICT Revenue Shares	**-**	**4,280,515**	**4,280,515**
Majuro Atoll Local Government	-	3,057,510	3,057,510
Kwajalein Atoll Local Government	-	1,223,004	1,223,004
MICT Payments	**-**	**-**	**-**
Total Revenues	**3,999,364**	**5,445,430**	**1,446,065**

Source: EconMAP calculations.

Nevertheless, should local governments be exempt from MICT and retain their sales taxes, both local governments would be required to pay MICT on purchases of goods and services. The prevailing rate of MICT would then need to be adjusted as the additional revenue needed to compensate local government would no longer be needed. A new effective MICT rate of 6.5 percent would result (Equation 3) and total MICT collections are recalculated as follows in Table A4.

$$Effective\ MICT\ Rate = (1 - rev\ share_{MALGOV} - rev\ share_{KALGOV})\tau_{MICT}$$

With local governments remaining non-registered in the reform scenario, both MALGOV and KALGOV would incur a net loss due to additional MICT payments on their purchases of goods and services (Table A5).

Wages and Salaries Tax

In estimating the revenue from the proposed income tax reform, a dataset containing quarterly gross earnings from the Marshall Islands Social Security Administration (MISSA) was used. The dataset contains information for 11,355 filers of which 9,888 are Marshallese while 1,467 are non-Marshallese.

Table A4: Estimated MICT Collections when Local Governments are non-registered

	Collection
Households	7,312,446
Local Governments	566,489
NGOs	304,445
Investment	-
Exports	101,144
Imports	231,492
Total	**8,516,016**

Source: EconMAP calculations.

Table A5: Estimated Local Government Revenues (non-MICT registered)

	Actual	Reform	Difference
Local Sales Taxes	**3,999,364**	**3,999,364**	**-**
Majuro Atoll Local Government	2,834,449	2,834,449	-
Kwajalein Atoll Local Government	1,164,915	1,164,915	-
MICT Revenue Shares	**-**	**-**	**-**
Majuro Atoll Local Government	-	-	-
Kwajalein Atoll Local Government	-	-	-
MICT Payments	**-**	**566,489**	**-566,489**
Total Revenues	**3,999,364**	**5,445,430**	**1,446,065**

Source: EconMAP calculations.

Marshallese Income Tax

For Marshallese taxpayers, the quarterly gross earnings of each taxpayer for FY22 were used to derive annual gross earnings regardless of whether the taxpayer worked for only part of or all of the entire fiscal year. Depending on the estimated gross annual income of each filer, the current tax rates as prescribed in the Income Tax Act 1989 were applied. Aggregating, the total tax paid for each Marshallese filer in the dataset yields an estimate of total collections (Table A6).

Table A6: Actual vs Expected Marshallese Wage Tax Collection in the Current Tax System

Actual Collection FY22	$11,649,000
Expected Collection	$12,802,930

Source: EconMAP calculations.

Table A6 suggests that the estimated collection is larger than the actual collection, implying a collection efficiency ratio of 0.91. Tax collections were then estimated using the proposed reform income tax rates from the same dataset. Assuming the same collection efficiency, Table A7 shows the estimated revenue with the new Marshallese income tax rates. Table A7 suggests that the national government will lose about $4.4 million in revenues due to the tax reform, which is, conversely, the total nominal tax savings of Marshallese taxpayers.

Table A7: Actual vs Estimated Marshallese Wage Tax Collection in the Proposed System

Actual Collection FY22	$11,649,000
Reform Collection	$12,802,930
Difference	($4,439,792)

Source: EconMAP calculations.

Income Tax for Expatriates/Non-Marshallese

Expatriates in the Marshall Islands are also subject to income taxes. While expatriates working outside Kwajalein are subjected to the same rates as Marshallese taxpayers, foreigners working in the Kwajalein base are eligible for a reduced income tax rate of 5 percent.

Given that expatriates in Kwajalein do not file returns at MISSA, it is assumed that non-Marshallese filers in the Social Security dataset are those who are subjected to the standard rates. The current and proposed systems are then applied to the individual annual income of non-Marshallese reported from the Social Security data (**Table A8**).

Table A8 shows that the actual collection of wage taxes for expatriates in Marshallese tax rates is less than estimated, implying a collection efficiency ratio of 0.933. Using proposed tax rates for each individual, the estimated total tax paid is derived. The total collection is also multiplied by the collection efficiency ratio, which yields the estimated collection for non-Marshallese.

As in the case of Marshallese taxpayers, the national government is expected to lose about $1.1 million in revenues due to the proposed reforms (**Table A9**). The foregone revenues will also translate to the total increase in nominal after-tax income for expatriates in the Marshallese wages tax system.

Table A8: Actual vs Estimated Non-Marshallese Wage Tax Collection in the Old System

Actual Collection FY22[1/]	$3,259,308
Expected Collection	$3,492,554

1/ Actual collection for expatriates in Marshallese tax rates is obtained by multiplying the total expatriates' tax collection for FY22 with the ration of the FY12 total collected tax from expatriates in Marshallese tax rates to the FY12 total wages tax collected from expatriates.

Source: EconMAP calculations.

Table A9: Actual vs Estimated Non-Marshallese Wage Tax Collection in the Proposed System

Actual Collection FY22[1/]	$3,259,308
Expected Collection	$2,154,093
Difference	($1,105,215)

1/ Actual collection for expatriates in Marshallese tax rates is obtained by multiplying the total expatriates' tax collection for FY22 with the ration of the FY12 total collected tax from expatriates in Marshallese tax rates to the FY12 total wages tax collected from expatriates.

Source: EconMAP calculations.

Taxes on Business Profits

Ideally, to estimate the collection of taxes on profits, the proposed 20 percent business profit tax (BPT) rate would be multiplied by the profit of every firm with an annual turnover larger than $100,000. For those businesses earning between $10,000 and $100,000 during the year, the existing 3 percent BGRT will remain in force. However, in the absence of detailed data on the profits of firms in the RMI, anonymized data on gross revenue for FY22 from the Ministry of Finance, Taxation, and Revenue was used to estimate the impact of the proposed tax reform.

Based on this dataset, 94.1 percent of the entire reported business revenue in the RMI is accounted for by firms earning larger than $100,000 in FY22 while those with turnover between $10,000 and $100,000 collectively generated $9,898,109 in gross receipts.

Using this information, the estimated government collection on the taxation of business profits is summarized in Equation 4:

$$Collection_{BPT} = \begin{cases} \tau_1 . Revenue, & \$10{,}000 < Turnover \leq \$100{,}000 \\ (1-\delta)(1-i)(1-\mu)\tau_2 \omega OS, & \$100{,}000 < Turnover \end{cases} \quad (4)$$

Where:

δ is the depreciation rate = 20 percent,
i is the allowance for interest and bad debts = 5 percent,
μ is the factor for non-compliance = 20 percent,
τ_1 is the 3 percent BGRT,
τ_2 is the business profit tax rate,
ω represents the share of the revenue of firms earning beyond $100,000 to the total business receipts, and
OS is the operating surplus estimated from the national accounts.

Equation 4 shows that for businesses with turnover between 10,000 and $100,000, revenue is directly multiplied by the BGRT rate of 3 percent. For businesses with revenues exceeding $100,000, given that data on profits is not available, the FY22 current price private sector operating surplus derived from the national accounts is used as a proxy for profit. The operating surplus is then multiplied by the share of the revenue of the firms earning beyond $100,000 to the overall revenues (ω) to capture only the proportion of the profit of the base that will be taxed. The collection is further adjusted to account for depreciation, noncompliance, interest, and bad debts. Table A10 provides the estimated revenue collection on the proposed taxation on business profits.

Table A10: Estimated Revenue Collection on the Proposed Taxation on Business Profits

	Actual	Reform	Difference
Business Profits Tax	-	$7,472,123	$7,742,123
Hotel and Resort BGRT	$83,000	-	($83,000)
BGRT on Business with Turnover Between $10,000 and $100,000	$7,065,000	$296,943	($6,768,057)
Total	$7,148,000	$7,472,123	$621,066

Source: EconMAP calculations.

2 Impact on Prices

The first step in measuring the impact of the tax reform on consumer prices is to estimate the MICT impact on each item on the CPI basket. There are 61 items in the basket, of which 16 are domestic and 45 are imported. In addition, three items in the basket are considered tax-exempt: off-island travel

expenditures, hospital visits, and tuition fees. For each item i in the basket, the estimated impact on its price is governed by Equation 5.

$$MICT\ Impact_i = \begin{cases} 0, & tax\text{-}exempt \\ \left[1 - \tau_{loc} - \frac{(1+m_d)\tau_{GRT}}{(1+\tau_{GRT})} - (1-m_d)\tau_{im} - \tau_{eIT} - \ell\right](1-\tau_{MICT}) - 1, & otherwise \end{cases}$$

where:

τ_{loc} is the local government sales rate,
m_d is the distributor's margin,
τ_{GRT} is the current BGRT rate,
τ_{im} is the import duty,
τ_{eIT} are the embedded indirect taxes, and
ℓ is the loss on the producer input tax

Equation 5 posits that the impact of the reform on tax-exempt items will be zero. On all other goods, the local government sales tax rate, BGRT, and embedded indirect taxes are removed and then replaced with the MICT. When a good is imported, a 5 percent duty for foodstuff and 8 percent for general imports are additionally removed. In cases where the good is domestically produced in the RMI, a reduction in the producer BGRT and losses in producer import taxes are accounted for.

Aggregating the weighted MICT impact on each item i, the total impact of the tax reform on consumer prices is derived (Equation 6).

$$Total\ Impact = \sum_{i=1}^{61} w_i MICT\ Impact_i \qquad (6)$$

where:

w_i is the weight of good i in the consumption basket.

In the reform case and where local governments are registered for MICT purposes, the estimated impact on consumer prices is slightly deflationary. On the other hand, when governments remain non-registered and continue to impose their own sales taxes, there is a slight increase in consumer prices (Table A11).

It must be noted that the analysis of the change in prices is static and does not account for any behavioral changes in the agents in the economy.

3 Impact on Marshallese Wage Distribution

Estimation of the impact of the tax reform on the Marshallese wage distribution groups taxpayers in the Social Security database by deciles based on their gross earnings. In the distribution (Table A12), the earnings of tax filers in the lowest deciles tend to be low since most taxpayers in these groups only work part of the fiscal year. In addition, 50 percent of the distribution earns less than $8,000 per annum.

Nominal tax savings are derived as the difference between the wage taxes paid under the current and reformed regimes. Real tax savings (in pre-reform prices) are derived by subtracting the original after-

tax incomes from the reformed after-tax incomes adjusted for the inflationary impact of the MICT.[13] Table A12 shows that all income groups are likely to gain in the tax reform with an average increase in real incomes of 4.2 percent.

Table A11: Impact of the Tax Reform on Consumer Prices

	CPI Impact (%)
Local Governments: MICT-registered	-0.4
Local Governments: non-MICT registered	0.1

Source: EconMAP calculations.

Table A12: Nominal and Real Tax Savings for Each Decile

	Annual Income Cut-off ($)	Nominal Tax Savings ($)	Real Tax Savings ($)	Percent Change in Real Income
Decile 1	850	0	3	0%
Decile 2	1,987	34	41	2%
Decile 3	3,600	163	176	5%
Decile 4	5,760	333	353	6%
Decile 5	7,515	333	359	5%
Decile 6	9,777	333	367	4%
Decile 7	12,947	537	580	4%
Decile 8	17,173	875	931	5%
Decile 9	24,002	1,293	1,370	6%
Decile 10	181,247	7,583	8,135	4%

Source: EconMAP calculations.

This Policy Note has been prepared by ***Dr. Richard Sturton*** and ***Michael Barsabal*** of the Graduate School USA's (GSUSA) Economic Monitoring and Analysis Program (EconMAP). EconMAP is supported by the U.S. Department of the Interior's Office of Insular Affairs, and the Asian Development Bank. The analysis, opinions and recommendations presented in this document are solely those of the author(s) and should not be interpreted as the official position of GSUSA, its sponsoring entities, or the government of the Republic of the Marshall Islands.

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13 To adjust the reformed after-tax income for the price impact, it is divided by $\sum_{i=1}^{61} w_{i,j} MICT\ Impact_i$ where $w_{i,j}$ is the weight of good i in the consumption basket of decile j.