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SUBJECT - Tax Administration Project No. 526-51-790-018.1

REFERENCE -

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Attached is **PROP** for subject project. The paper has been prepared in accordance with the approved reorganization plan for projects. (See TOAID A-257, 8/21/69 and TOAID A-285, 9/18/69).

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Attachment: a/s

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Noncapital Project Paper

9/30/69

PAGE 1 OF 1 PAGES

DRAFTED BY

APOPE:CDodson:ys

OFFICE

Program

PHONE NO. DATE

10/13/69

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Tax Adv:WFlaherty (draft)

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Act. DIR:DFLisberg (draft)

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NONCAPITAL PROJECT PAPER

Country: PARAGUAY

Project No. 526-51-790-018.1

Submission Date: September 30, 1969

Project Title: TAX ADMINISTRATION

U.S. Obligation Span: FY 1965 through FY 1975

Physical Implementation Span: FY 1965 through FY 1975

Gross life-of-project financial requirements:

U.S. Dollars	\$651,000	
COP Contribution	43,000	(in kind) (equivalent)
GOP-owned PL 480	<u>20,000</u>	
	<u>\$714,000</u>	

A. SUMMARY DESCRIPTION OF PROJECT

1. Project Justification: The need and justification for a project for an improved tax administration system in Paraguay is identified in the FY 1970 Program Memorandum Appendix A and the FY 1971 CFS Appendix C, as well as in the PAI dated January 14, 1969. High priority is assigned to the project because of its relevance and significance in furthering the U.S. objective of helping Paraguay to increase its capacity to more effectively mobilize its financial resources and to increase central government savings. Maximum impact of the project on the above objective will continue to depend to a large degree on top-level coordinated policy action on the part of the USAID, the U.S. Embassy, and international agencies, working within the context of the approved strategy of using CIAP self-help requirements for extracting improved GOP fiscal performance. In implementing this policy, it should be noted that USAID tax administration activities under this project are being closely coordinated with OAS tax assistance in the field of legislation and tax policy.

2. Project Goals and Targets: Over the projected 11-year implementation period of the project, the following major goals and targets are identified:

a. Development and institutionalization of substantially improved systems and procedures in tax administration.

(1) Preparation of written manuals to reflect procedures, forms, prescribed methods for receiving and processing documents, position descriptions and functions, and the like.

(2) Organization and institutionalization of in-service training programs for Ministry of Finance technical and administrative personnel so that training courses will routinely be made available to new employees and to employees changing to new technical or administrative positions.

(3) Development of a centralized planning function for monitoring the written procedures and making periodic review of internal and external forms, and personnel and financial budgets.

b. Increased voluntary compliance with the country's tax laws, resulting in an estimated 10% annual increase in collections (under existing tax laws) of indirect taxes, sales taxes, and taxes on income and real property.

c. Improved administrative provisions in new and revised tax legislation. (This target to be achieved through coordination of USAID activities and those of OAS advisors).

3. Plan of Action

a. Major U.S. and GOP Resource Inputs: The major U.S. contribution over the entire implementation period of the project will be the technical services of U.S. Internal Revenue Service advisors, including both full-time and short-term specialists. U.S. funds also are provided for participant training in the U.S. and 3rd countries, invitational travel, and for limited amounts of commodities required by the U.S. advisors to carry out the project. The GOP contribution consists of "in-kind" facilities and services for logistical support of the project. A small amount of GOP-owned PL 480 funding also is budgeted for supplies and equipment.

b. Major Requirements for GOP Self-Help Actions: The principal requirement is the establishment of a healthy climate for tax administration in which improved techniques may be incorporated not only in the present administrative structure but also may survive succeeding administrations. Political considerations having an adverse effect on project implementation should be reduced to a minimum. (See Part III of PAR, January 1969, for more detailed discussion of both positive and negative aspects of the role of the GOP). Also, the GOP will be required to take specific self-help actions within the context of the CIAP recommendations, including preparation and enactment of new and revised tax legislation.

NONCAPITAL PROJECT FUNDING (OBLIGATIONS IN \$000)

Table 1
Page 1 of 2
Country: PARAGUAY

PROP DATE
Original 9/30/69
Rev. No.
Project No. 526-51-790-018.1

Project Title: TAX ADMINISTRATION

Fiscal Years	L/G	Total	Cont ^{1/}	Personnel Serv.			Participants		Commodities		Other Costs	
				AID	PASA	CON	U. S. Agencies	CONT	Dir U.S.Ag	CONT	Dir & U.S.Ag ^{2/}	CONT
Prior through Act. FY 69	G	212	-	-	182	-	19	-	11	-	-	-
Oper. FY 70	G	70	-	-	60	-	2	-	8	-	-	-
Budg. FY 71	G	101	-	-	90	-	6	-	5	-	-	-
B + 1 FY 72	G	105	-	-	96	-	4	-	5	-	-	-
B + 2 FY 73	G	113	-	-	105	-	4	-	4	-	-	-
B + 3 FY 74	G	91	-	-	85	-	4	-	2	-	-	-
All Subs. 75	G	<u>59</u>	-	-	<u>53</u>	-	<u>4</u>	-	<u>2</u>	-	-	-
Total Life	G	651	-	-	571	-	43	-	37	-	-	-

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ASSUMPTION

- ^{1/} Memorandum (nonadd) columns
- ^{2/} \$8,000 for "other costs" for full time PASA Advisor is included in the Personnel Services Column.

Table 1

Page 2 of 2

Exchg rate \$1 = 126 Guaranis ^{2/}

Project No. 526-51-790-018.1

Fiscal Years	AID-controlled Local Currency		Other Cash Contribution Cooperating Country ^{4/}
	U.S. owned	Country owned ^{3/}	
Prior through Act. FY 69	-	-	15
Oper. FY 70	-	8	3
Budg. FY 71	-	-	5
B + 1 FY 72	-	-	5
B + 2 FY 73	-	12	5
B + 3 FY 74	-	-	5
All Subs. 75	-	-	<u>5</u>
Total Life	-	20	43

^{2/} As of preparation date^{3/} PL 480 funds^{4/} Ministry of Finance office, staff and facilities support.

B. SETTING OR ENVIRONMENT

As pointed out in the PAR of January 14, 1969, the role of the GOP has been of key significance in terms of both its positive and negative factors affecting the overall environment. During the three-year period 1965-68, GOP political considerations resulted in a lack of support for the IRS Advisor's recommendations in the real estate tax area and put this phase of the program substantially behind schedule. Also, the threat of adverse political action from the business community and other groups during the 1968 GOP presidential election period was one of the main causes for the Ministry of Finance's suspension of the special three-year audit program for income tax. During the latter part of 1968, however, the situation improved. In September 1968 the Minister of Finance made important changes in key leadership positions in the Ministry, i.e. the Sub-Secretary of the Ministry and the Secretary General, with the new officials being younger professionally-trained tax economists with important previous experience in the Department. Most of the political problems in the real estate area also were solved when the former Director of the Real Estate Tax Department died and a new Director was appointed who is more progressive and receptive to recommendations for improvements.

The threat of a serious GOP budgetary deficit crisis in 1968 was the major issue in the CIAP meetings in August/September 1968, with the final CIAP recommendations including specific self-help fiscal requirements to be met by the GOP. To date, GOP performance in meeting these requirements has been commendable. In December 1968 and in March 1969, for example, the GOP enacted the first six tax measures recommended by CIAP, and these measures are expected to produce at least an additional \$500 million in tax revenues for 1969.* (For more detailed discussion of GOP self-help performance in the fiscal area, see TOAID A-198, June 20, 1969)

In summary, as shown above, the overall setting for the adoption of procedures and other recommendations for improving the level of tax administration in Paraguay has improved considerably in the last year, and it is expected that the GOP role will continue to make an increasingly positive impact on the achievement of project targets in 1970 and future years.

Below the level of the Minister of Finance the USAID Tax Advisor has four principal counterparts, the Directors of the three tax offices with which he's primarily concerned (Indirect, Real Property, and Income and Sales Tax) and the Inspector General of the Ministry of Finance. All are competent administrators and, except for the Director of the Real Property Tax Office, all have had considerable, successful experience as government administrators.

* Of the six measures, the two most important are the sales tax which is expected to produce more than \$300 million and the increased stamp tax rate which should generate about \$140 million.

The Real Estate Tax Department, which a year ago was the most resistant to changes, is now the most active department of the Ministry in adopting and implementing new procedures that will undoubtedly lead to better service to taxpayers and increased tax collections. The Income/Sales tax office now has operating a program for examining tax returns. This has been incorporated in an annual work plan, and promises to bear its greatest fruits following the expected enactment of a new income tax law at the beginning of the year.

Cooperation from the Director of the Indirect Tax Office is excellent. The USAID Tax Advisor has been invited by that Director to accompany him on field trips designed to open necessary new sub-offices to improve taxpayer service, and to pave the way for including Real Property/Income/Sales Tax functions within the Regional Offices now supervised by the Director of Indirect Tax Office.

The Inspector General is a dynamic, enthusiastic individual who has always cooperated with the USAID tax project.

At the top, the Minister of Finance, earlier this year, approved, almost 100% of the USAID tax project's suggested work plan for CY 1969 for the tax offices.

The foregoing is not to say there are still no problems. There is a pressing need, for example, for the creation of the office of Director General of Revenues so that the efforts of all the sub-offices may be coordinated. To date, the Minister has given this proposal no support, preferring that the counterparts mentioned report directly to him. Also, there is no centralized planning function for the Ministry. In the present climate however, we are hopeful that this office will be established. The Minister does not favor sending his executives to specialized training courses in the U.S. and other countries. He would prefer that the foreign countries send experts here to direct such courses. However, we're ^{PERSONALLY} optimistic that we'll see an early change in this attitude.

Political considerations, especially where the ruling Colorado party is involved, often override otherwise seemingly logical courses of action. However, in spite of the foregoing, Paraguay is changing its attitudes toward not only the necessity for adequate and efficient administration of its taxes, but also toward the necessity for providing an adequate across-the-board system of raising sufficient revenues to meet the country's heavy fiscal obligations. A new sales tax law was enacted earlier this year - the first in Paraguay. Several beneficial changes were made to existing real property laws. The tax on imported cigarettes was increased substantially. A tax observation group composed of Paraguayan congressmen and the Minister's Technical Advisor has just completed a four-country tour, studying existing income tax systems. All of these men will be key figures in the writing and enactment of the new income tax law - expected to be passed by CY 1970. The Ministry's attitude is positive toward USAID recommendations for effective administration in all of these areas. The USAID's appraisal would be, therefore, that while the setting in Paraguay for the

adoption of more modern tax administration procedures and practices is far from perfect, it is considerably better than it has been in the past.

C. STRATEGY

As stated in the preceding summary, a maximum impact from the USAID's tax administration assistance will continue to depend to a large degree on coordinated policy action and support of the USAID Director, the U.S. Embassy, and international agencies in implementing the CIAP strategy for obtaining GOP action on recommended fiscal recommendations. Within this overall context, the main thrust in USAID's operational strategy will be the persistent pushing, implementation, and follow-up of project activities leading to planned objectives.

Additionally, plans are now being made by the AID tax advisor to meet periodically with members of the Paraguayan Congress, particularly members of the Committee on Finance, to exchange views on administrative implications in the very important income tax law now being proposed. A paper setting forth some of his views has been made available to the Minister of Finance, members of the previously mentioned tax observation group, and the Director of the Income Tax office.

D. PLANNED TARGETS, RESULTS, AND OUTPUTS

Over the 11-year implementation span of the project, now scheduled to terminate at the end of FY 1975, the general objective of the AID tax administration effort in Paraguay is to assist the Ministry of Finance in the development and institutionalization of substantially improved systems and procedures in tax administration. Institutionalization contemplates that by the time the project is terminated, procedures, forms, prescribed methods for receiving and processing documents, position descriptions and functions, and the like, will be reflected in written manuals, subject to periodic review and revision. It also contemplates that training programs will be organized, centralized and routinely made available to new technical employees and to employees changing to technical or administrative positions. During the life of the project such training is expected to be supplemented by AID sponsored courses in the U.S. and other countries for supervisors and executives.

For monitoring the written procedures and making periodic review of internal and external forms, personnel and financial budgets, a centralized planning function will be required.

Attainment of the principal goal, an overall improvement in the level of tax administration in Paraguay, should assure a sharp increase in the area of the most important by-product of good tax administration, i.e. voluntary compliance with the nation's tax laws. This, of course, would normally be accompanied by increases in collections of tax revenues in areas of concentration that would exceed, relatively, annual increases in the gross national product.

Any estimate for projected increases in tax revenues will obviously be affected by new revenue laws, amendments to existing laws and fluctuations in the value of the national currency (among other considerations) as well as through improvement in the quality of tax administration in Paraguay. Collections in the area of the tax project's principal effort were as follows for 1968 (Source: Dept. of Economic Studies, Central Bank of Paraguay):

Indirect taxes	\$ 1,901,800,000
Income (Profits) taxes	\$ 730,000,000
Real Property taxes	\$ 351,400,000
Sales taxes	(Passed Feb. 1969)

An annual increase approximating 10% a year, without regard to the non-administration influences, previously mentioned, should be easily attainable, if administration-improvements recommended by the AID tax team are adopted. Further, increased income tax revenues that would average considerably more than 10% over the life of the project would almost certainly be realized, particularly if three or four of the key, administratively desirable, articles recommended by the tax team were incorporated into the proposed new income tax law (projected for passage early in 1970).

The general objective of the tax project is reflected in more detail in the specific objectives included in the following Section E. of this PROP.

E. COURSE OF ACTION

Specific activities will be aimed at realizing specific targets, all of which will be directed toward the ultimate goal of institutionalizing tax administration modernization in Paraguay. This will require identification of the required activities and monitoring not only their installation but also their effectiveness once installed. The latter can be partially done during the life of the project through a constant follow-up by the USAID Tax Advisor. However, to assure their continuation specific Paraguayan officials must be responsible eventually for the monitoring and effective function/of the whole tax administration effort. It is contemplated therefore that when this project is terminated not only will the desired administrative changes have been adopted, but effective written procedures for monitoring, evaluating and altering them will be an integral part of the resulting tax administration system. This would involve not only the incorporation of new procedures, forms and attitudes, but also routine training courses for all technicians and supervisors, and hopefully, the beginnings of the establishment of something akin to a civil service commission to the end that the granting of government jobs would be more objective and less restrictive than at present. (For example, through a system of job descriptions and salary classification)

Implementation of the general course of action to achieve the tax administration project objectives will revolve mainly around the services of USAID-funded IRS advisors. A "staffing pattern" for these services is shown in Table No. 2.

Table No. 2TAX ADMINISTRATION STAFFING PATTERN

(USAID-financed services of U.S. Internal Revenue Service Advisors)
(FY 1965-1975)

Fiscal Year	'65	'66	'67	'68	'69	'70	'71	'72	'73	'74	'75
Senior Tax Advisor (Full-time Team Leader)	X	X	X	X	X	X	X	X	X	X	X
Real Property Tax Advisor (Short-term six weeks)	X										
Real Property Tax Advisor (Full-time two years)		X	X								
Data Processing Specialist (TDY four months)						X					
Collections Specialist (TDY four months)						X					
Collection/Processing Advisor (Full-time two years)							X ^{a/}	X ^{a/}			
Real Property Tax Specialist (TDY three months)							X				
Data Processing Specialist (TDY three months)								X			
Audit Advisor (Full-time two years)									X	X	
Intelligence Specialist (TDY three months)									X		
Collections Specialist (TDY three months)											X

a/ Present OPRED requirements preclude recruitment of this full-time advisor but the position is included in the staffing pattern because of its high priority in achieving effective implementation of project activities and the possibility that circumstances may change so as to permit filling the UNCLASSIFIED position at a later date.

There is a high priority need in FY 1971-72 for a Collection/Processing Advisor, especially in the area of current and delinquent accounts in the Real Property Tax Office. Also, after passage of revised legislation for the income tax law, and the writing of the administrative regulations pertaining to the law, and implementation of an effective system for selecting and examining tax returns, a full-time Audit Advisor will be needed, not only to assist in the establishment of needed audit programs in income tax and other areas, but also to assist in the preparation of required procedural manuals, as well as internal and external audit forms.

The Senior Tax Advisor will continue to supervise the entire project, and as the need arises, he would draw on his own specialties to advise in specific areas. To the extent possible, the Senior Advisor should complement with his experience the specialties of the other advisors.

Participant Training Program

A relatively small USAID-financed participant training program (\$43 thousand projected over the life of the project) is included in the overall project plan of action.* The program provides for U.S. and 3rd-country training, with emphasis on sending key personnel to the INTAX training program conducted by the U.S. Internal Revenue Service. USAID-financed invitational travel also is included in the program, with its main use being the sending of strategically-placed GOP officials and members of the GOP congress on visits to the U.S. and other Latin American countries to observe and study the operation and administration of efficient tax systems.

GOP Contributions and Self Help Actions

GOP contributions will include cash contributions from government revenues to the budget at the In-Service Training Center, government transportation for field trips to outlying offices, salary and other financial support for technicians and officials attending training schools, both in and out of the country, as well as in-kind contributions of office space, furniture and equipment.

The principle requirement for GOP self help action would be the creation of a climate within the Ministry of the Treasury (with a minimum of political interference) in which tax administration improvement techniques may be not only incorporated into

* The reason for the relatively small size of the participant resource input is the desire of the present Minister of Finance to keep his best people on the job in Paraguay and to maximize the use of local in-service training at such facilities as the In-Service Training Center of the National University.

the present tax administration structure, but also may be incorporated in such a form as to survive succeeding administrators. We have noted a very favorable change in this direction in the attitude of the Ministry during the past year.

This new interest has been demonstrated in measurable form, for example, by the Ministry's increased contributions to the budget of the In-Service Training Center and the payment of salaries, transportation and per diem costs for officials attending a course in tax administration and policy in Buenos Aires.

Also the new interest has been evidenced by the approval of, and initiation of projects included in, a work plan submitted by the U.S.A.I.D. tax project. This work plan contained, principally, objectives included with those listed elsewhere in this report, all designed to assist the Paraguayan government in modernizing tax administration in the country.

Following is a more detailed description of the general work plan for achieving the project goals described.

General Work Plan

(FY 1969-75)

1. Audit Activities: Development of a comprehensive audit program for all taxes susceptible to audits, with emphasis on increasing skills of technical employees in Income Tax office.
2. Appeals: Establishment of an equitable system of taxpayer appeals for all offices, with emphasis on development of a hearings function in the Real Property tax office and an improved appeals system in the income tax offices.
3. Initiation of needed audit and filing changes in the Indirect Tax office, including the following activities:
 - a. Develop and submit to the Minister of Hacienda a budget of personnel needed to carry out the audit mission of the Indirect Tax office.
 - b. Install a master file for all taxpayer in the Indirect Tax office.
4. Updating of taxpayer and property records in the Real Property Tax office, including property valuations, specifically including:
 - a. Initiation of procedures to bring the lists of taxpayers up to date.

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- b. Establishment of procedures for adding new properties to existing tax rolls.
- c. Updating of values of real estate in the capital.
- d. Updating of values of real estate in municipalities away from the capital.
- e. Improvement of filing system by transferring property tax records from books, as at present, to individual cards. To be limited, initially to Asunción.
- f. Development of a plan for increasing all present (1957) values, to be submitted to Minister during last half of year.
- g. Improvement of a present procedure for identifying new construction, initially in Asunción.
- h. Purging of outstanding delinquent property tax balance of amounts barred by statute of limitations, pertaining to exempt properties, below minimum tolerances, etc.

5. Creation of realistic real estate valuation divisions throughout the country with a view toward equating property assessments, including establishment of a code system for property valuation norms.

6. Development of an overall objective plan for reducing outstanding delinquent property tax balances, including:

- a. Initiation of a mailout program to delinquent property taxpayers in downtown Asunción.
- b. Initiation of a mailout program to delinquent taxpayers in urban and suburban areas of Asunción.
- c. Initiation of a mailout program to selected delinquent taxpayers outside of the capital city.
- d. Development of a plan for systematically reducing penalties on delinquent real estate taxes.
- e. Establishment of a new minimum tolerance below which tax bills will not be mailed out, nor will collection efforts be made.

7. Designing of methods for facilitating administration in the real estate tax office, including:

- a. Preparation of a study of exempt properties and submission of the analysis, with appropriate observations, to congress through the Ministry.
- b. Evaluation of administrative cost of enforcing the minimum tax rate.
- c. Exploration of the possibility of locating real property tax representatives in key regional offices.

8. Establishment of procedures for assuring that the tax offices make a reasonable follow up on delinquent returns, including the following activities:

- a. Establishment of a procedure for automatically following up on Sales Tax Responsibilities who fail to file returns.
- b. Updating of a current procedure for following up on registered taxpayers who fail to present income tax returns.
- c. Establishment of a procedure for locating non filers in selected areas of the country.

9. Establishment of procedures for assuring that the government collects the maximum amounts of taxes determined to be due, and which can be collected through reasonable vigorous, administrative effort, including the following activities:

- a. Establishment of a force of tax collectors in the real property office.
- b. Preparation and implementation of a plan for collections of delinquent indirect taxes, within present budgetary limitations.

10. Installation of procedures to assure the smooth and efficacious flow of tax documents and other data through the income tax office, including the following activities:

- a. Review of procedures for receiving tax documents and payments, and recommend changes and additions in both central and regional offices.
- b. Preparation of flow charts and procedures designed to improve the flow of data through the audit section.

11. Development of control devices that will aid in minimizing accuracy of internal statistics and establish internal controls, including the following activities:

- a. Develop a technical time report for the crystallization of statistics by technical personnel.
- b. Review internal forms suggesting improvements, deletions and additions.
- c. Review the system of internal control for cash, stamps, and other valuables in the Regional offices.

12. Improved Administrative Provisions in Tax Legislation

- a. Assistance in the drafting and enactment of an Income Tax Law that lends itself to efficient administration.
- b. Establishment of necessary means to assure efficient administration of the Income Tax Law.

13. Organization and Management - Ministry of Finance

- a. Decentralization of the real property and income tax offices.
- b. Development of a planning function.
- c. Installation of the position, Director General of Taxes.
- d. Encouragement for the eventual establishment of a competitive career service in the tax offices.
- e. Assistance in the development of an efficient internal inspection function.
- f. Development of a system that will enable personnel budget planners to anticipate changes in staffing requirements.
- g. Development of procedures for compiling accurate personnel and financial budgets for the tax offices.

14. Taxpayer Education and Relations: Development ^{of} a positive attitude toward taxpayer education, information and relations in the various tax offices, including the following activities:

- a. Development of a publicity program for advising taxpayers that income, sales and property taxes can be paid in regional indirect tax offices.

b. Development of a computation table for aiding taxpayers and their employees in determining at a glance, sales tax due for various amounts of sales at various rates.

c. Development of a procedure, to be submitted for ministerial approval, for issuing "official" receipts to taxpayers in regional offices.

15. Tax Intelligence: Demonstration of the need for routine enforcement of sanctions and other remedies for discouraging tax fraud.

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SUBJECT - **Approval of Project No. 526-15-790-018.1,**

REFERENCE - **Tax Administration - Paraguay
TOAID A-317**

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The project, as defined in the PROP, has been reviewed by A.I.D./W offices concerned and is approved with the following conditions, recommendations, and observations:

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1. The project number was changed to conform with the new numbers agreed upon between the USAID and A.I.D./W. The new number also appears in the FY 1970 IAD.
2. The chart shown on Page 8 of the PROP should be enlarged upon to reflect collections for the years 1965, 1966, and 1967. By including collections for those years instead of only 1968, The USAID and A.I.D./W will be in a better position to estimate future years' collections and to see where the project is headed.
3. A.I.D./W wonders whether the 10% increase in tax revenue over the life of the project is high enough. Although the PROP indicates it would be "considerably more than 10%," A.I.D./W is interested in learning just how much more of an increase is anticipated.

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DRAFTED BY	OFFICE	PHONE NO.	DATE	APPROVED BY
BJacobson	LA/APU	23381	1-20-70	

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LA/OPNS: ABagley
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