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CHAPTER ___

REFORM OF MUNICIPAL INDIRECT TAXES, SERVICE TAXATION AND STAMP DUTIES

Malcolm Gillis

To be Included in: Fiscal Reform For Colombia, The Final Report and Staff Papers of the Colombian Commission for Tax Reform

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I. Municipal Indirect Taxation - The Industry and Commerce Tax

A. Defects of the Present Tax

Colombian muncipalities have the right to impose (although not all do) a tax upon all businesses located within their boundaries. In all municipalities, this tax is called the Industry and Commerce Tax (Impuesto Sobre Industria y Comercio), but the similarity between the various forms of the tax in the various jurisdiction ends here.

The tax is without question an inequitable and unworkable anachronism for a nation at Colombia's stage of development. The major defects of the Industry and Commerce Tax may be summarized as follows:

1. The tax is badly designed and poorly administered. For the various municipalities now making an attempt to collect the tax, liability is calculated on the basis of a curious blend of physical and financial evidence. For example, in Bogotá, tax liability for industrial concerns is determined on the basis of average monthly sales and installed horsepower. For commercial enterprises, the tax is levied on the basis of average monthly sales and the value of rent paid per month (presumably imputed rent in cases where a firm occupies its own building). In Medellin, tax liability is determined solely on the basis of gross sales, but there are 122 different basic sets of tax rates applicable to different types of industrial and commercial undertakings.[1] Similar

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1. According to one Medellin administrator, the existence of such a large number of rates on gross sales represents an attempt to tax the profits of the various firms on a roughly equal basis.

variations occur in the structure of the tax throughout the nation.[2] For example, in Armenia, industrial firms are taxed at progressive rates on gross sales while commercial enterprises are taxed solely according to monthly rent. In other municipalities, tax is determined on the basis of square feet of plant space employed by firms, in addition to gross sales, rent and installed horsepower.

Most municipalities attempt to include all firms, no matter how small, within the scope of the tax, although most of the taxes employ a complex maze of exemptions and provisions for reduced rates for various types of activities. As with other features of the tax, the exemption structure varies considerably from one jurisdiction to another.

The administration of the tax is further complicated by the use of exceedingly detailed criteria designed to define various types of taxable commercial and industrial undertakings and by cumbersome methods of declaration and payment. In view of these considerations, it is not surprising that evasion is uncommonly high, as perhaps 80% of liable firms do not pay the tax at all.[3] In addition, the arbitrary

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2. The structure and nature of tax rates is even more diverse. Some municipalities impose the tax at ad valorem (progressive and proportional) rates on both gross sales and monthly rent, but employ specific (but variable) rates upon installed horsepower rates. Other jurisdictions employ some combination of specific and ad-valorem rates for some activities and variable license fees for other.

3. Richard Bird, Taxation and Development (Cambridge: Harvard University Press, 1970), p. 98. This study was in manuscript form at the time of the commission investigations in the summer of 1968 and was kindly made available by the author.

manner of imposing the tax creates substantial opportunities for corruption among municipal tax inspectors, as interviews by the author with several concerned parties have confirmed. Because of these features, the tax is considered to be an unmitigated nuisance by the business community, if we may take the periodic pronouncements concerning the tax by Fenalco (The Colombian equivalent of the National Chamber of Commerce) at face value.[4]

2. The distribution of the burden of the tax, although impossible to estimate given the highly arbitrary nature of the tax, is almost surely quite regressive in character. More will be said on this later. Considerations of income distribution aside, it is alleged that an inordinate share of the tax is paid by industrial firms whereas the liability of commercial concerns such as wholesalers and service establishments, even quite large ones, is typically very light. In addition, the tax does not apply to the operation of the rapidly growing cooperatives. Repeal of the industry and commerce tax would at least place private retailers on a more equal footing with the cooperatives, which presently enjoy marked tax preferences of several types.[5]

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4. It is not known how much of the opposition to the tax is traceable to opposition to taxes in general, but knowledgeable members of the business community indicate that almost any other form of municipally-levied tax would be preferable to the Industry and Commerce Tax.

5. Cooperatives have been set up by various institutions such as the Central Bank, Avianca, the National Police and such large private firms as Baveria. Such cooperatives make sales not only to employees of the sponsoring firm or agency but to the general public as well, and are able to sell at substantially lower prices, since the locale is provided without cost and they are exempt from all national taxes (except the sales tax). Many are large enough to obtain substantial quantity discounts from suppliers.

3. The rationale for taxation of business activity as such by municipal governments is not by any means self evident. As Netzer has noted, local government taxes measured on such a peculiar basis, such as the Colombian industry and commerce tax, lack any theoretical basis, and may well lead to distortions in decisions concerning the location of business activity,[6] especially if the taxes of the tax are increased during future periods of municipal fiscal pressure. If the tax is retained, resort to higher rates to support the growing level of municipal expenditures (especially in the largest cities) is virtually certain, given the very low revenue elasticity of the typical municipal tax base.

All considerations point to the desirability of immediate abolition of this highly defective tax. But repeal of the Industry and Commerce tax would involve a substantial loss of revenue for many municipalities, especially the four largest. Revenues from the industry and commerce tax accounted for 21% and 23% of country-wide municipal tax revenues (6% and 7% of total current municipal revenues)[7] in 1966 and 1967, the picture was somewhat different for the four largest cities (Bogota, Cali, Medellin, and Barranquilla), where the yield from the tax constituted 23% and 27% of their combined tax revenues for the same period. The tax was especially

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6. Dick Netzer, "Some Aspects of Local Government Finances," Report No. 51, Economic Development Series, The Center for International Affairs, p. 89.

7. The low share of industry and commerce tax revenues in total municipal current revenues provides a very misleading impression of the importance of the tax. The relative revenue importance of the tax would be far greater if income from municipal enterprises (water, electricity, and telephone companies) were repoted on a net basis. At present such revenues are reported on a gross basis, and most municipal enterprises operate with very large deficits. In view of this consideration, it is evident that industry and commerce tax revenues consitute a large portion of general government revenues over which the municipalities have some discretion concerning their use.

important as a revenue source for Barranquilla and Medellin in 1966-67, as it accounted for nearly half of all taxes for Barranquilla and about one third of all taxes in Medellin over the period.[8,9]

Per capita collections provide another measure of the importance of the tax in various parts of the country. For the four largest cities, per capita collections in 1966 was P 30, but was only P 5 for the next 11 largest cities, P 6 for that part of the department of Antioqua outside Medellin, and only P 2 for the rest of the country.[10,11]

Some further notion of the importance of the industry and commerce tax in total municipal tax revenues may be gleaned from the fact that in 1966 the yield of the tax was second only to the real property tax as a source of tax revenue for all municipalities together. In the larger cities the yield of the industry and commerce tax is, on the average, about 60% of the revenues from the property tax. In the rest of the country revenue from the tax is only about one-third of that of the property tax.[12]

In view of the figures cited above, it must be concluded that the industry and commerce tax cannot be simply abolished, because it is too

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8. Data supplied by the National Budget Office, Bogota.

9. Projections for 1968 indicate a further rise in the relative importance of the tax in all major jurisdictions imposing it, mainly because of widespread rate increases.

10. Dick Netzer, "The Industria y Comercio Tax as a Source of Municipal Revenue," Typewritten, June 22, 1963.

11. The four largest cities together accounted for about 60% of nationwide collections from the tax in 1966 and nearly 82% of the total in 1967.

12. Ibid., p. 3.

important as a revenue source in the large cities; rather it must be replaced by another, more rational form of tax that will provide at least an equivalent amount of revenue.

A number of possible alternatives to the tax have been examined, including: the conversion of the tax to a base consisting entirely of gross sales, a low rate municipal supplement to the national sales tax, a municipal surcharge on the national business income tax, and a low rate retail sales tax. The next section discusses the relative merits of each of the potential replacements.

B. Possible Alternatives for Replacing the Tax

1. Conversion of the Tax to a Gross Sales Base

A previous study[13] recommended that the tax should be converted into a uniform rate levy based entirely on gross sales instead of the present combination of gross sales, plant space, rent and horsepower. This particular study also suggested that the tax could be made more productive of revenue simply by raising the rate.

Although almost any other form of tax would be preferable to that now employed, this proposal should never be seriously considered, as conversion of the tax base to that of gross sales would amount to the creation of a very crude multiple stage turnover tax -- one of the worst taxes ever conceived.

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13. Milton C. Taylor and Associates, Fiscal Survey of Colombia. (Baltimore: Johns Hopkins press, 1965) p. 220.

2. A Low Rate Municipal Supplement to the National Sales Tax

Replacement of the industry and commerce tax by a low rate supplement to the national sales tax does not appear feasible as long as the present manufacturers form of sales tax is retained.

If this alternative were to be adopted, revenues derived by each municipality would depend solely upon the volume of sales within the municipality that is taxable under the national sales tax. It should be recalled that the present national sales tax is by no means a general levy: food, drugs, and textbooks are exempt, and a large proportion of taxable activities is unevenly concentrated among municipalities.

Most small municipalities have virtually no manufacturing activity subject to the national sales tax hence they would derive very little benefit from a supplementary rate on the national sales.tax. Even if we disregard the problems of the small jurisdictions (who are not collecting the industry and commerce tax to any extent anyway) adoption of the proposal would give rise to arbitrary variations in revenues from such a supplement as between the larger municipalities that are now collecting the industry and commerce tax, as municipal revenues from this source would be dependent upon the relative distribution of taxable and exempt activities as between municipalities.[14]

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14. Adoption of this alternative would be a boon for Bogota, since about half of national sales tax collections arise in this jurisdiction. A city such as Bucaramanga, which is responsible for over 1/3 of national cigarette production, would derive massive benefits from this scheme because an important taxable activity happens to be located there. If the national sales tax is imposed upon imports in the customs house, as recommended in the previous chapter, disproportionate amounts of revenue would accrue to the port cities of Cartagena, Santa Marta, Barranquilla and Buenaventura.

Any attempt to allocate revenues from the supplement on the basis of consumption of taxed items (i.e., on a destination basis) would be out of the question for administrative reasons. Collection of the supplement by the national government with later remittance to the municipalities on some simple basis such as population would substantially erode municipal financial autonomy.[15] In addition, it is unlikely that the municipalities now relying heavily upon the industry and commerce tax would accept such a solution, given the great disparity between per capita collections for cities of different size mentioned above.

Finally, if changes in sales tax rates recommended in a previous section are adopted, there will be rather marked increases in the height of a number of them. Problems of combatting evasion and smuggling will be difficult enough in the presence of higher national rates even without supplementary rates for the municipalities.

3. A Municipal Surcharge on the National Business Income Tax

On the surface, the possibility of replacing the revenues that would be lost by abolition of the industry and commerce tax by adoption of a municipal surcharge on the national business income tax would appear to possess notable advantages. Such a surcharge would undoubtedly constitute a far more elastic revenue source than the present tax, and would likely be acceptable to the larger municipalities, provided proceeds from the surcharge were returned to the area of origin.

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15. For an extensive discussion of the need for decentralization in government activity and the preservation of some degree of local fiscal autonomy, see Bird, op. cit., pp. 147-155.

However, this alternative should be considered as a second or third best solution for a number of reasons.

First, rapid growth in revenues from the industry and commerce tax (due mainly to enactment of higher rates) in the last three years would mean that the rate required for any compensating surcharge on the business income tax would have to be quite high. As Table 1 indicates, the level of the surcharge that would have been required in the years 1965 through 1967 would have been 12.8%, 13.9% and 9.1% respectively. Projections made by the Finance Ministry Budget Office of business income tax yields and industry and commerce tax revenues indicate that the surcharge required in 1968 would have to be on the order of 13%, due to a large projected jump in revenues from the latter (because of enactment of higher rates) and only a moderate advance in the former.

A surcharge of the order required to compensate for repeal of the industry and commerce tax is not likely to be acceptable nor advisable, especially if there is no change in the differential treatment of corporations vis-a-vis limited liability companies under the business income tax.[16] Corporations already bear a disproportionate amount of the burden of the business income tax and would incur much greater increases in tax liability because of the surcharge than the already favored limited liability companies.

There would also be a very thorny question concerning the manner in which revenues collected by the surcharge would be allocated to the

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16. See Richard Slitor, "Reform of the Business Tax Structure," which appears as Chapter __, Part II of this volume, Section IX-A.

Table 1

Business Income Tax Surcharge Required to Compensate for Repeal of Industry and Commerce Tax

(Peso figures in millions)

	1965	1966	1967
A. Total Revenues, Industry and Commerce Tax	116.3	146.1	123.4
B. Total Revenues, Business Income Tax	906.5	1,045.0	1,362.1
C. Level of Surcharge on Business Income Taxes Required to Compensate for Repeal of Industry and Commerce Tax (Row A as percentage of Row B for each year)	12.8%	13.9%	9.1%

SOURCE: Data supplied by the National Budget Office, Ministry of Finance, Bogota.

different municipalities. The allocation would be administratively workable only if the repeal of the industry and commerce tax coupled with the establishment of the surcharge were desired in order to redistribute income among municipalities. If this were the case, then some simple formula such as population per municipality could be employed as the criteria for allocation.

However, it should be recalled that the primary concern in this particular case is to provide those municipalities that have been relying on the existing tax with a new tax source of at least equal revenue yield. Allocation of the surcharge on a per capita basis would certainly be resisted quite strongly by the four largest cities, especially Medellin (which tends to be quite jealous of its fiscal perogatives), since the present tax has furnished such a large proportion of its total tax revenues for quite some time. Therefore, allocation of any business tax surcharge on a population basis does not appear feasible.

If some simple criteria for allocation, such as population, cannot be used, alternative formulas will certainly involve significant administrative difficulties. A large portion of nationwide business enterprises, in particular large industrial concerns and most large distributors, file their income tax declarations on a consolidated basis in Bogota (Sears, Bavaria, Vida, Tia, Tampico, etc.) Medellin (Tania, Ley, Caravana, Drogueria Neuva York) and Cali (Carvajal, Belmonte). That is, income tax on the nation-wide operations of these firms is declared and paid mainly in the three largest municipalities. The existence of this pattern of payment casts doubt on the feasibility of employing a business income tax surcharge as a replacement for the levy in question. How would the

broader, more income elastic base, revenues from the retail levy will rapidly come to exceed that now obtained from the industry and commerce tax.[17] Apart from the greater revenue elasticity of the tax, which will substantially bolster the fiscal capacity and hence strengthen the autonomy of municipal governments, there are a number of other major advantages of this reform, of which the following appear to be most important:

(a) Under the new approach it will finally be possible to include a number of services within the indirect tax system on a rational basis. Unless the retail tax is adopted, expanded coverage of service-type expenditures will be possible only if a series of municipal or department excise levies upon services are established. The distributive and allocative arguments for including services in the tax base, as well as particular services appropriate for inclusion in the scope of the retail tax, are discussed in a subsequent section and need not be restated here. There is, in addition, an administrative argument for including services in the base of a retail tax, also discussed in a later section.[18]

(b) The new tax will contribute toward a more equitable tax structure since its impact will almost surely not be as regressive and erratic as the industry and commerce tax. That is to say, there is good reason to believe

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17. See Appendix 1 of this chapter for revenue estimates for a possible municipal retail sales tax.

18. See Section II of this chapter.

that a retail tax with food exempt and certain income elastic services taxable, will (under reasonable shifting assumptions) not only be not regressive, but most likely at least slightly progressive. No concrete statements can be made concerning the probable distributive impact of the existing tax, since it is levied in such an arbitrary manner and since the base varies so widely between municipalities. However, it is known that the present industry and commerce tax is levied upon a large number of retail grocery stores, food wholesalers, and processors of food products. For example, in Bogota in 1966 almost one half of the taxpaying firms in the "commerce" category were classified as retail food firms. Fully two thirds of these firms were of the small, family operated variety. In the "industry" category, 666 firms in Bogota were manufacturers or processors of food and drink products.[19] It is impossible to calculate how much of the taxes paid by these firms is typically shifted forward to consumers, but to the extent forward shifting takes place, the tax has significant regressive characteristics on the income uses side.

(c) On the administrative front,[20] adoption of the retail tax in place of the existing tax municipal tax authorities would be dealing with a far fewer number of taxpying firms than is the case with the existing tax and with firms significantly larger on the average than at present.

For example, there were 38,239 firms paying industry and commerce tax in 1966 in Bogota alone. Of this number, roughly one half paid less than

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19. Distrito Especial de Bogota, Anuario Estadistico 1966, pp. 129-134.

20. See Malcolm Gillis, "Sales Tax Reform," Section VI-2, Chapter __, of this volume for a discussion of the administrative feasibility of employing retail taxation in developing economies.

P 50 per month[21] (approximately U.S. $3.00 at 1968 exchange rates).

It is certain that the number of taxpaying firms would be drastically reduced if a retail tax of the type proposed were adopted to replace the present highly defective levy. Rough calculations indicate that if food were exempted and certain services taxable, and if very small firms were excluded from the scope of the tax,[22] the number of taxpaying firms in Bogota would be in the neighborhood of 6,000 to 9,000, instead of the nearly 40,000 now subject to the industry and commerce tax.

If we may assume that little or no reduction would be made in the number of persons now responsible for administering the present tax, inspectors would be able to devote substantially greater amounts of time in assessment and audit activity to each firm coming under the scope of the new tax. On the other hand, the number of inspectors could be markedly reduced and the training and salaries of those remaining could be considerably improved without increased administrative outlays. Furthermore, inspectors would not be collecting a tax that is completely strange to them, as they are (in most jurisdictions) at present faced with the necessity of determining gross sales for each firm for purposes of the existing tax.

An additional administrative argument in favor of the retail tax as a replacement for the present tax is that a number of other already existing municipal indirect taxes, such as that upon admissions, could be easily incorporated into the retail tax.

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21. Distrito Especial de Bogota, op. cit., p. 135.

22. The removal of small vendors from the scope of the tax renders invalid the traditional objection to retail taxes in developing nations that of alleged administrative infeasibility.

(d) The new tax will bring valuable experience which then will be applied to the operation of the national sales tax once it is shifted toward the retail level. The municipal tax would not be abolished in this event, but would be imposed at supplementary rates to the national levy, with consequent economies in both administration and compliance.

(e) Unlike the industry and commerce tax, the proposed retail levy will provide some slight incentive to save more and consume less, since a given consumer may decrease his tax liability by reducing his taxable consumption. However, at low rates of tax this influence is not likely to be particularly strong, given the presence of exemptions and the apparent extent to which saving in Colombia is made for purposes of financing future consumption.

2. The Structure of the Tax

a. General Features

The revenue from the proposed retail sales tax should accrue to those municipalities in which it is collected, and responsibility for its administration should rest with the municipalities. However, the structure of the tax should be uniform for all municipalities in which it is imposed, although the level of tax rates actually employed could, within limits, be left to the discretion of the various jurisdictions. Application of the tax, at least at the outset, should be confined to the larger municipalities, as for example, those with more than 50,000 or perhaps 100,000 inhabitants.[23] Because the industry and commerce tax is not now effectively collected by the smaller municipalities, this restriction would involve no significant revenue loss for them.

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23. If the tax were confined to those municipalities with population of 50,000 or more, this would mean that nearly 40 of them would levy the tax. There are at least eleven municipalities with population in excess of 100,000.

b. Taxable Products

All products sold at retail should be subject to tax unless specifically exempted. The most important exemption that should be made is food,[24] but not food sold in taxable restaurants. The exemption of food is designed to prevent the tax from being regressive in its incidence. In addition, certain items now exempt from the national sales tax, such as drugs and textbooks, might be exempted so as to be consistent with other objectives of public policy.

c. Exclusion of Small Firms

Firms having no paid employees and with monthly sales of less than say 3,000 to 5,000 pesos should be excluded from the scope of this levy, since effective collection from such enterprises is not feasible in the context of a single stage retail tax. A large number of such firms would automatically be exempt by virtue of the exemption of food.

Fear is sometimes voiced that the expediency of exempting small firms from the scope of a sales tax is inherently anti-developmental, since these firms are likely to be less efficient than their larger counterparts. Experience in other countries indicates that this fear is largely unfounded,[25] as the process of development itself tends to erode the number of small firms in any case.

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24. Food should be defined in the same way as is recommended for the national sales tax. See Chapter __, Part II of this volume, Section IV-A.

25. C.f., Malcolm Gillis, Sales Taxation in a Developing Economy, The Chilean Case (Unpublished PhD Dissertation, University of Illinois, 1968), p. 371.

d. Rates

The tax should be imposed at a general flat rate of 2% on all taxable products, although a higher rate of perhaps 10% could be applied to certain specifically enumerated services.[26] In view of the fact that higher manufacturers tax rates on luxury products have been recommended, national tax policy requires that some attempt be made to impose something approaching the retail equivalents of the rates on such products to the consumption of luxury services.[27] Otherwise, consumers will have a strong incentive to divert more of their expenditures toward purchase of such items, thereby thwarting the aims of luxury taxation and further warping the allocation of resources.

e. Nature of Taxable Services

Only specifically enumerated services would be included in the base of the tax, in contrast to the treatment for products (where goods not specifically exempted would be taxed). Only those services of a consumption nature and rendered by commercial establishments should be included within the scope of the tax. A later section of this chapter deals with the types of services suitable for inclusion in the retail tax base.

f. Other Considerations

Although it would be inappropriate at this time to enter into a detailed discussion of the various administrative techniques and minor structural provisions that would help to insure smooth operation of the tax, it is worthwhile to indicate the nature of some of the types of questions that will have to be considered.

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26. While it is absolutely imperative that all taxable products be subject to one basic rate under the retail tax, no serious difficultion should arise if certain services rendered by specialized service establishments were subject to a higher rate.

27. See below, Section II-A, for a discussion of the precise nature of "luxury services."

(i) The tax should apply on an accrual basis. That is, liability for tax would be incurred during the period in which sales are made, rather than when payment is received.

(ii) For larger firms (such as Sears, Tic, Ley, Caravajal, etc.) bimonthly declarations and payment might be required. Consideration might be given to allowing, at least initially, quarterly declarations for smaller firms subject to tax in order to minimize the strain on working capital caused by the combination of use of the accrual basis and the existence of substantial accounts receivable.

(iii) The tax should be applicable to the total net selling price rather than price inclusive of tax. Careful consideration should be given to the matter of whether the tax is to be quoted separately from selling price. The arguments in favor of such a provision have been previously cited and will not be recanted here.[28]

II. The Taxation of Services

A. The Case for Heavier Taxation of Certain Services

A rather heavy premium should be attached to the incorporation of a far greater number of services, especially luxury services, within the scope of indirect taxation than is the case at present.[29] Several arguments can be

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28. See the preceding chapter, section VI-2.

29. It may be helpful to refer once again to the definition of the word luxury as employed in the commission report and staff papers. See, for example, Malcolm Gillis, ____, "Objectives and Means of Indirect Taxation," which appears as Chapter ___, Part II of this volume.

marshalled in favor of such a step.

First, the extension of the scope of indirect taxation so as to include a greater number of service expenditures would without question enhance the overall revenue elasticity of the tax system, thereby advancing one of the prime objectives of the tax reform. Levin's ingenious study[30] of the effects of economic development upon sales tax bases clearly indicates that the inclusion of services in general (utilities, rent, recreation and amusement, transportation excluding automobiles and miscellaneous services) may be expected to significantly contribute to the long run revenue elasticity of a sales tax in an economy such as that of Colombia. Although the results of any study based on cross-sectional comparisons of consumption on an international scale should, as Levin warns, be interpreted with care, they do lend additional empirical support to the oft-repeated belief that the inclusion of services enhances the revenue elasticity of indirect taxes.

The consequences for revenue elasticity of the inclusion of services within the scope of Colombian indirect taxation should be ever more favorable than suggested by Levin's analysis, because the primary emphasis of the proposals discussed below is upon income elastic services of a luxury nature, rather than services in general. For example, such services as utilities and rent would not be brought within the indirect tax base.

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30. Jonathan Levin, "The Effects of Economic Development on the Base of a Sales Tax: A Case Study of Colombia," International Monetary Fund Staff Papers, March 1968, pp. 48-53. Levin indicates that as nations rise from the lowest to the highest per capita income categories, the income elasticity of consumption for services in general may be placed at about 1.2, meaning that expenditures on these items rise by 12% for each 10% increase in per capita income.

The accent upon incorporation of more luxury services in the tax base is also designed to build a greater degree of progressivity into the fiscal system, one of the principal goals of the overall tax reform.[31]

In addition, a number of the service type expenditures that have been selected for heavier taxation and/or inclusion in the tax base for the first time, are characterized by a very high import content, particularly telephone service, foreign travel and the services derived from automobile ownership. Reasons for the advisability of discouraging import-intensive consumption in Colombia have been discussed previously and need not be restated here.[32]

The imposition of new or heavier taxes upon many services may also be justified as a means of improving resource allocation. The imposition of the national sales tax upon a wide variety of commodities almost certainly had the effect of deflecting some demand to the largely untaxed services

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31. See Malcolm Gillis, "Objectives and Means of Indirect Tax Reform," which appears as Chapter __. Part II. However, care should be taken not to exaggerate the contribution that the inclusion of services in the indirect tax base can make to a more equitable tax structure. Recent research indicates that including services in the tax base of state retail taxes in the United States increases the progressivity of the sales tax by only insignificant amounts, especially if utilities and medical services are not exempted. See David G. Davies, "The Significance of Taxation of Services for the Pattern of Distribution of Tax Burden by Income Class." Paper presented at the 62nd Conference of the National Tax Association, Sept. 1969. Notwithstanding this finding, the very sharp class-differentiated consumption patterns in Colombia, typical of both products and services, insures that selective inclusion of certain services in the tax base will enhance progressivity.

32. Ibid. section _____.

sectors, and adoption of higher sales tax rates proposed in the previous chapter may be expected to create further pressures in this direction, should the tax treatment of services remain unchanged.

In addition, should the commission accept the proposal for a municipal retail sales tax, and/or if the national sales tax is moved toward the retail level, there will be a strong administrative argument for taxation of many services. Inclusion of certain services simplifies the administration of such taxes, especially in cases where firms (such as repair shops) engage in both the sale of commodities as well as the rendering of services. However, the problems caused for a retail tax by failure to tax services is not confined to those associated with repair shops.[33]

Finally, although it has already been noted that incorporation of more services into the tax base would enhance the long run revenue elasticity of the indirect tax system, it is important to emphasize that the immediate revenue consequences of such action will not be inconsequential. Greater reliance upon the taxation of services will contribute significantly to closing the projected massive fiscal gaps facing both the municipal and departmental levels of government, to whom most of the additional service taxation revenue would accrue.

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33. The taxation of such services avoids the vexing problem of separating the commodity and service element in price. This difficulty arises either when only the commodity element or the service element is taxable. Aside from repair shops there are numerous instances in which the actual sale price of a product includes service elements such as advertising, transportation and installation charges. If services as such are not taxable, they would not be taxed if sold by an independent firm whose sole activity consists in the rendering of services, but they would be taxed if sold by firms providing such services in conjunction with the sale of commodities. Attempts by the latter type of firm to separate the service element from the price of the commodity leads to endless complications for both vendors and tax administrators. See John F. Due, State Sales Tax Administration Service, 1963), pp. 162-171.

B. The Present Tax Treatment of Services

1. Taxed Services

At present virtually no services are taxable, whether of a "luxury" nature or not. Those that are subject to tax generally bear very light levies imposed by the national government, and to a lesser extent, the municipal governments. The following service-type activities are subject to various miscellaneous taxes.

a. Admissions

This category includes cinemas, cockfights, bowling alleys, plays, bull fights and sports events, activities which are now subjett to a confusing variety of permanent and transitory national, departmental, and municipal taxes.[34]

b. Transient Accommodations

There is a 5% national tax on hotel bills that exceed P 10 per day. Proceeds of the tax are earmarked for promotion of tourism.

c. Foreign Travel

Foreign travel is now subject to a national P 500 stamp tax that must be paid by each Colombian national departing for a foreign country (other than Ecuador and Venezuela). In addition there is a 5% tax upon the purchase of all airline tickets having a destination outside Colombia; proceeds of the latter tax are earmarked for the Colombian Airport Authority (ECA).

d. Domestic Air Travel

Intra-country travelers must pay a P 15 national tax upon each round trip flight; proceeds are earmarked for airport maintenance and construction.

34. See Section D-2 below.

e. Repair Work Incorporating New Materials

Repair work of all types is, in principle, subject to the national sales tax, but taxation of this type of activity has proven unenforceable except in the case of tire-recapping. All other repair work is effectively outside the scope of taxation.

f. Residential Building Contracting

This activity is subject to tax (in the form of a levy on building permits) in a number of municipalities, but the levy is universally quite weakly enforced. Rates vary considerably for the different municipalities employing the tax.

2. Untaxed Services

The following service activities are at present subject to no indirect tax whatsoever:

Beauty parlors

Turkish and sauna baths

Services of domestic servants

Social clubs

Professional services (medical, dental, legal and brokerage services

Parking lots

Telephone service[35]

Photofinishing

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35. In Bogota only, there is a temporary tax of P 3 per phone per month. The entire proceeds of the tax is earmarked for the promotion of sports (principally to cover expenses abroad of sports teams representing Colombia).

Services rendered by commercial laundry and dry cleaning establishments

Automobile service (brake inspection, repair involving only labor, lubrication, etc.)

Private education

Rentals of tangible personal property (autos, television sets, etc.)

Tailoring services

Restaurants and night clubs

Public utility service other than telephones (electricity, water)

Minor repair activities (shoe, watch, and appliance repair)

Freight

Radio, television and newspaper advertising

Printing shops.

Most of the above services are suitable candidates for inclusion in the tax base, and their taxation would be well within the limits of administrative feasibility. A large number of these items are essentially luxury in nature in the Colombian context. However, the taxation of some of the services listed above would be inadvisable for administrative reasons, while others should be excluded because they are primarily rendered to business firms, and still others might be excluded for reasons of general social policy or to avoid introducing regressive elements in the taxation of services. The treatment of still others that are already taxed should be modified.

C. Services Inappropriate for Taxation

It is generally agreed that only those services rendered by commercial establishments and primarily of a consumption nature should be included

within the scope of indirect taxation.[36] On the basis of this widely accepted rule of thumb, together with other special considerations relevant in the Colombian context, we may conclude that a number of the services cited above cannot be feasibly taxed. In addition, a number of the following services would most likely fall within anyone's definition of luxury services as far as Colombia is concerned, but taxation of them is deemed inadvisable because of administrative difficulties.

a. Services of domestic servants.

Even if administrative difficulties involved in any attempt to tax this item of expenditure could be surmounted, it is quite likely that the tax would be reflected primarily in reduced wages for already low-paid domestic servants, given the market for such services in Colombia.

b. Professional services (those rendered by doctors, lawyers, dentists, brokers, etc.)

If we accept the principle that taxation should be confined, insofar as possible, to those services rendered by commercial concerns rather than individuals, there is little else to add. In the case of physicians and dentists, there are probably strong social reasons for excluding their services from the scope of indirect taxation. With respect to brokers, fear is often voiced in Colombia that extension of tax to brokerage services at this time would severely inhibit the development of the embryonic money and capital markets emerging in Bogotá and Medellín.

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36. For the best statement of the reasons underlying this dictum, see John F. Due, Sales Taxation, pp. 374-376.

c. Services rendered by tailors, leather, watch and appliance repair shops

The only serious objection to taxation of services rendered by these firms lies in the administrative sphere. In Colombia virtually all these activities are one-man operations; therefore attempts to include them within the scope of service taxation would involve a very large number of small taxpayers who maintain almost no records.[37] If in the future the possibilities for bolstering both the quantity and quality of resources at the disposal of tax administration are vastly enhanced, consideration might be given to subjecting such services to tax.

d. Private education

Non-parochial private education, as well as a large proportion of parochial education, is almost exclusively a prerogative of upper-middle and upper-income groups in Colombia, and a portion of this type of expenditure might be considered a form of luxury consumption. However, expenditures of this type are best viewed as a form of investment in human capital, and in the interests of development should not be taxed.

Other types of services are rendered primarily to business firms and should not be subject to tax.[38] These include freight, radio and television advertising, and services rendered by printing firms.

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37. For the same reason, barber shop services should perhaps not be subject to tax in the rural areas and in small cities. However, in the larger cities, especially Bogota, Cali, Medellin and Neiva, a number of barbers are typically employed in one easily identifiable shop, and the quality of record keeping is reasonably good. One-man barber shops would automatically be excluded in any case under the retail tax.

38. The arguments against taxation of such services are well known and therefore are not repeated here. See Due, Sales Taxation, pp. 374-375.

In addition, a case might be made, on grounds of avoiding regressivity, for excluding the services rendered by small restaurants from tax. This possibility is discussed in greater detail below.

D. Municipal Service Taxes

If the commission decides to accept the staff proposal for replacing the municipal industry and commerce tax with a low rate retail sales tax, it will be feasible to include a number of presently untaxed services in the base of the tax, as well as several services already lightly taxed. In general, the rate applicable to taxable commodities should also apply to taxable services. However, the tax rate could be higher for a number of services rendered by firms that engage exclusively in service activity. If the retail tax is rejected, a new municipal tax called the Impuesto Municipal Sobre Servicios (Municipal Tax on Services) could be established instead. The base of this alternative form of tax would include all the items listed below.

1. Services Not Previously Taxed

The following untaxed services should be brought within the scope of the retail tax:[39]

(a) Beauty and barber shop service;

(b) Turkish and sauna baths, services of health clubs;

(c) Rentals of tangible personal[40] property (automobiles, etc.);

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39. Recall that small firms (those with no paid employees and sales of less than P 3,000 or P 5,000 per month) would not be subject to the retail tax.

40. Such rentals are not at present an important activity in Colombia, although car rental firms are very much in evidence in some of the large cities. As income levels rise, this type of activity will likely become increasingly more predominant, and forward-looking tax policy should take this likelihood into account.

(d) Laundry and dry cleaning services rendered by commercial establishments;

(e) Photofinishing and photographic services in general;

(f) Automobile services (repair and maintenance);[41]

(g) Night clubs and cabarets;

(h) Parking lot services;[42]

(i) Restaurant services.

Items (a) through (h) are fairly obvious candidates for inclusion within the scope of the municipal retail (or special service excise) tax. However, some special comments may be in order concerning the proposed inclusion of restaurant services. Such expenditures are normally viewed as rather income elastic in nature. However, it is recognized that especially in the large urban areas, there are a large number of small restaurants that cater to very low income individuals who find it necessary (due to travel problems) to obtain lunches and dinners in these establishments during working hours. For this reason, and because any attempt to extend tax to all restaurants would involve so many taxpayers as to create intractable administrative difficulties, it is worth repeating that all concerns operating with no paid employees and with monthly sales inferior to, say, P 3,000 or P 5,000, should be exempt from tax.

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41. See Chapter ____, Charles E. McLure, Jr, "Automotive Taxation" pp. ___ to ___, for a discussion of a proposed automobile registration tax.

42. A tax on parking lot fees (which will surely be vigorously criticized in the automobile-owning Bogotá press) is also justified on grounds that it would amount to a tax on congestion. However, it would have to be imposed at rates substantially higher than the general retail rate in order to have any appreciable effect upon the reduction or urban congestion.

2. Services Presently Taxed

In addition to those items listed above, the base of the municipal retail sales tax (or alternatively, the special municipal service excises) should reach a number of services already taxed by various levels of government, including the municipal level. Taxes now collected on these items by other levels of government would not necessarily have to be abolished, except in certain cases.

These services would include:

(a) transient accommodations;

(b) admissions (Espectaculos publicos);

(c) domestic air travel.

Because each of these items is now subject to taxation by other levels of government some further discussion of the possibilities of including them within the base of the proposed municipal taxes is required.

The retail tax should include transient accommodations and should apply to the total bill paid by each guest including meals and other services performed by such establishments.[43] The present 5% national tax might have to be abolished, since different levels of government are, at least in principle, prohibited by the Constitution from employing the same tax.[44] However, imposition of tax by more than one level of government has

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43. Fear of losing the North American tourist dollar should not deter adoption of this tax. (This has been a favorite argument of the Colombian Hotelmens Association.) Other nations that compete with Colombia for tourists impose transient accommodations taxes as high as 15% (Chile) and 20% (Ecuador) without any noticeable effect upon the tourist trade.

44. Colombian hotels are classified into four categories: luxury, first class, second class, and "other." The national tax applies only to the first three categories.

been allowed in the case of other taxes (auto registration, admissions).

At the present time, the most important taxes on admissions are levied by the municipal governments and the national government,[45] although a few departmental governments have been empowered to employ such taxes from time to time.[46] In addition temporary taxes have been used by the national government for brief periods, the proceeds of which have been earmarked for special purposes.[47] The regular national taxes are imposed at rates of 2.5% on admissions to light "cultural" entertainment (movies, soccer games, etc.).[48] Municipal tax rates applicable to admissions generally do not vary by type of function, and range from 2% to 10%, depending on the jurisdiction. In the past the municipal taxes could be deducted from the national tax, but this arrangement is no longer in force.

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45. The combined yield of the municipal taxes was P 14.1 million in 1966. National government admissions taxes amounted to P 25 million in the same year.

46. In 1967 the departments of Valle and Tolima were granted the right to impose a special 10% on admissions for purposes of financing construction of facilities for the sixth Pan-American Games in Cali in 1971.

47. For example, there was a special 10% tax on admissions that was collected for four months in 1967 for purposes of providing funds for the reconstruction of Quibdo, a community devastated by an earthquake in that year. There is also a special national tax levied on movie admissions for purposes of financing the activities of the agency that classifies films on the basis of suitability for viewing by various age groups.

48. By providing for lower rates upon admissions to "cultural" events patronized almost exclusively by the educated urban elite, the national tax is even more regressive in its impact than a flat rate tax on all admissions (given the very great extent of movie-going on the part of both the urban and rural poor). The differential rate structure, like most schemes to encourage "art" through the fiscal system should perhaps be viewed as an indirect subsidy to "cultured" upper income groups, unless it can be shown that campesinos and other low income groups derive a far greater psychic income from attendance by the patrons of cultural events than the patrons themselves. Of course the sentiments expressed in this footnote are philistinic in tone.

A strong case can be made for national government abandonment of this revenue source and the transferral of all admissions taxes to the municipal governments.[49] As noted in a previous study, a tax on entertainment and public shows appears particularly appropriate for the use of the municipalities, and it was probably a mistake for the national government to enter this field.[50]

The existence of the present national government earmarked tax of P 15 on domestic airline tickets may preclude the possibility of inclusion of this service in any municipal service tax structure. But aside from legal restrictions, there is no reason why the municipal retail sales tax (or the municipal service excises) should not apply to the sale of airline tickets for travel within Colombia. In any case, consideration might be given to the application of tax to the gross receipts of travel agencies, in lieu of a tax on domestic airline tickets.

E. Proposed Departmental Service Taxes

Two new sources of revenue from the taxation of services are proposed for the departments: a telephone tax and a tax on social clubs.[51]

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49. The national taxes on admissions were ceded to the municipalities by Law 33 of December 1968, after this recommendation was accepted by the Tax Commission.

50. Taylor, op. cit., p. 220.

51. In a sense, the benefits derived from the ownership of automobiles could be viewed as a form of luxury service consumption. A previous chapter has proposed the creation of a new automobile registration tax, which would replace the existing municipal and national taxes, the revenues of which would accrue to the departments. See McLure, Automotive Taxation, Chapter ___, pp.

1. A Departmental Telephone Tax[52]

This new tax is proposed as a departmental levy both because of the severe revenue crisis at the departmental level of government and because the tax could be administered more easily by the departments than the municipalities, since the public telephone enterprises usually serve several municipalities in the same department.

A tax on this service is particularly appropriate in Colombia because residential telephone service is consumed almost exclusively by upper income groups in Colombia. The fact that telephone companies are publicly owned in Colombia does not constitute an argument against this tax in any way.

It is to be emphasized that the case for a telephone tax has nothing to do with the fact that telephone tariffs are at present far below the level that would be required to avoid deficit operations by the public telephone companies. In other words, the proposed tax should not be viewed as even a partial substitute for increases in telephone service rates. If and when these rates are increased sufficiently to bring them more nearly in line with costs, the case for the proposed tax will be just as strong; that is, telephone service is now completely free of tax (except for the P 3 tax in Bogotá) although a wide range of commodities is subject to the sales tax. Therefore, consumption of this highly import-intensive untaxed service is heavily favored relative to consumption of taxed commodities. In any case, the adoption of even higher rates of telephone tax than proposed in this section may not be expected to significantly discourage consumption of

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52. This section was prepared in cooperation with Charles E. McLure, Jr.

this service.[53] and would certainly exert a little pressure in the right direction, as far as resource allocation and the total charges paid by telephone users are concerned.

The tax should be imposed at ad-valorem rates on all telephone bills, whether for residential or commercial use.[54] Coin operated public telephones could be exempt, in order to avoid curtailment of a service that is likely enjoyed primarily by lower income groups, especially in rural areas.

Rates for the proposed tax could be set at 10% to 25% of monthly charges to customers. The tax would be collected for the departments by the various public telephone enterprises. For interdepartmental calls, revenues would accrue to the department from which the call originates.[55]

Revenues from the tax would be quite substantial, and would provide significant relief from the critical revenue difficulties now facing the departments. Moreover, the revenue elasticity of the tax will almost certainly exceed that of the present major departmental revenue sources (taxes on beer, cigarettes and liquors).

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54. Administrative considerations dictate that the tax should apply to business as well as residential telephone service. It may be argued that business telephone service should not be taxed, for the same reasons that freight services should not be subject to sales tax, and because forward shifting of the tax by business firms would render the telephone tax regressive. This last argument is not very persuasive in the Colombian context, since such a large portion of the budgets of low income families is spent on unprocessed food items that do not go through manufacturing stages and are not distributed by commercial establishments. In any case, any attempt to distinguish between business and residential telephones for tax purposes would invite wholesale evasion or result in the tax not being collected at all.

55. Calls abroad are handled by Telecom, the national telecommunications entity, and users receive a separate bill for such calls from this agency.

Table 2 below indicates the gross receipts of telephone companies in the years 1962-66, by department, and the potential revenues from the proposed tax at a rate of 10% or 25%, 1966 only. Receipts from coin operated telephones are assumed to be a minute fraction of the total.

A rough projection of the potential revenues that would arise from the proposed tax for the years 1967-1971 can be made if we can assume that the gross receipts of the telephone companies will grow at least as rapidly (22% per annum) in this period as they did in the previous five years. This assumption appears to be reasonable, if overly conservative, since the National Association of Telephone Enterprises announced in July of 1968 that the stock of telephones in the country would be augmented from its present level of 500,000 to 1,500,000 units by 1978.[56]

Given a rate of growth of 22% per annum in the gross receipts of the phone companies, the potential revenues from the tax for the period 1967-71 would be indicated in Table 3 below.

For a typical Bogota upper-middle income household (income of between P 10,000 and P 13,000 per month) owning a telephone in 1968, the tax would have amounted to about 4 - 5 pesos per month under the 10% rate and 11 - 12 pesos per month under the 25% rate (about U.S. 23¢ and 71¢ respectively).

Had the tax been in existence in 1965 at a 25% rate, its importance as a source of tax revenue would have been exceeded only by the departmental beer and tobacco taxes. Even at a rate of 10% it would have been fourth in importance in the departmental tax structure.

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56. El Tiempo, Bogota, July 17, 1968.

2. A Proposed Departmental Tax on Social Clubs[57]

One of the most conspicuous forms of luxury consumption in Colombia is participation in a wide variety of social clubs. At present these clubs (their assets, shares, sales, and other income) are entirely exempt from tax of any kind.[58, 59] The services rendered by such entities satisfy consumer wants in the same way as the consumption of taxable products or other taxable services and should not be excluded from the indirect tax base. Services provided by these organizations include meals, entertainment and other recreation, lodging, use of club equipment, as well as the highly regarded prestige benefits attached to club membership in Colombia.

In addition there are other arguments in favor of enactment of a tax upon services rendered by social clubs. The tax would be borne by those with the greatest financial capacity and therefore would introduce an additional element of progressivity into the tax system. The proposal may also be justified on the somewhat esoteric ground that it would constitute a tax upon a leisure-complement, with presumably salutary effects on work effort. Finally, the departments critically need new sources of revenue, and could most effectively administer the tax, since the clubs

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57. This section prepared in cooperation with Charles E. McLure, Jr.

58. The clubs are required to file income tax returns.

59. See Chapter __, Andrew Quale, "Reform of the Net Wealth Tax," for proposals for including the shares of social clubs in the base of the net wealth tax.

TABLE 2

Gross Receipts of Telephone Companies, 1962-1966, and Potential Revenues from a Telephone Service Tax at Rates of 10% and 25%, 1966
(millions of pesos)

	Gross Receipts by Department[a]					Tax Revenue at 10% rate (column 5X 10%)	Tax Revenue at 25% rate (column 5X 25%)	Percent of Revenues Accruing to Each Department
Year / Department[b]	1 1962	2 1963	3 1964	4 1965	5 1966	6 1966	7 1966	8
Antioquia	22.7	25.1	25.8	37.9	40.6	4.1	10.2	19.0
Atlantico	7.9	10.4	11.9	15.7	13.5	1.4	3.4	6.3
Bolivar	2.0	2.9	3.7	5.6	8.8	0.9	2.2	4.1
Caldas	4.9	5.3	9.6	9.6	9.6	1.0	2.4	4.5
Cauca	0.4	0.4	0.4	0.5	1.6	0.2	0.4	0.7
Bogota, D.E.	34.2	39.5	44.2	56.3	72.4	7.2	18.1	33.9
Cundinamarca	0.6	1.6	1.1	1.8	3.8	0.4	1.0	1.8
Huila	----	----	----	----	0.2	---	0.1	0.1
Magdelena	0.4	0.7	1.0	1.8	2.0	0.2	0.5	0.9
Quindio	----	----	----	----	3.0	0.3	0.8	1.4
Santander	0.5	1.0	0.6	2.4	3.5	0.4	0.9	1.6
Tolima	0.5	1.3	2.0	2.5	2.9	0.3	0.7	1.4
Valle	21.3	25.7	30.0	43.9	52.0	5.2	13.0	24.3
Totals	95.4	113.8	130.4	178.1	213.8	21.4	53.5	100%

(a) Source: Data compiled by Mr. Jaime Vasquez of the Finance Ministry from unpublished information supplied by the National Association of Telephone Enterprises.

(b) Does not include the recently created departments of Cesar, Risaralda and Sucre. Data for the departments of Choco, Cordoba, Guajira, Meta and Norte de Santander were not available, but telephone service is quite limited in these departments, all of which have very low per capita incomes.

TABLE 3

Estimates of Revenues for a 10% and a 25% Ad-Valorem Tax on Telephone Service, 1967-71

(millions of pesos)

Year	Tax Revenue at a 10% Rate	Tax Revenue at a 25% Rate
1967	26.1	65.
1968	31.8	79.5
1969	38.8	97.1
1970	47.4	118.4
1971	58.0	143.5

typically are located either outside or just within the boundaries of the larger municipalities, and can not easily be hidden from the view of the departmental tax administration.[60]

The tax should take the form of a luxury excise levied at a rate of perhaps 20% on the gross receipts of the most important (in terms of assets) clubs in the country. Gross receipts should be defined so as to include any and all receipts, including sales of meals, beverages, products, annual and monthly membership fees, and perhaps receipts from the sale of bonds and debentures.[61] For the sake of administrative feasibility, the tax should apply only to clubs above a certain size. Size would be defined in terms of gross receipts or volume of assets.[62] Information concerning both magnitudes is readily available, by virtue of the fact that the clubs must file income tax returns (although they are not subject to income or net wealth tax) and could be required to report assets or receipts, as many do at present. This information could easily be made available to departmental tax administrators.[63]

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60. Indeed, most are located near major highways and are impossible to ignore. There were over 20 such clubs, having 1966 assets in excess of P 100,000 within a 10-mile radius of Bogota alone and six had assets exceeding P 5 million in the same year.

61. Gross receipts used for charity, if any, might be excluded from taxable gross receipts. If this is done, care must be taken to insure that "charities" are strictly defined so that this provision is not used for wholesale tax evasion, especially given the high incidence of top-notch lawyers in the memberships of the clubs.

62. For administrative reasons the tax could not apply to clubs provided by companies for their employees. There are a number of such clubs, including those established by Bavaria (the largest company in Colombia) and Avianca (the national airline). Some consideration should be given to the taxation of these clubs by other means. One possibility would be to disallow expenses of this type as a deduction under the business income tax.

63. If there is some concern that the tax would apply to fairly large service clubs performing useful social functions (such as aid to the blind by the Lions Clubs throughout the country) these essentially middle class organizations could be excluded by a provision restricting the tax to clubs with

Should the scope of the tax be restricted so as to include only the receipts of those clubs above a certain size, a reasonable level below which clubs would not be taxable would appear to be on the order of P 100,000 in assets or P 50,000 in annual receipts.[64] The asset limitation would be the most workable, since assets would not fluctuate as much as gross receipts from year to year and hence there would be less movement of clubs from taxable to exempt categories over a period of years. If exemption from tax is defined in terms of asset size, there is a very real possibility that directors of large clubs would find numerous ways of changing financial practices or modes of operation so as to escape the proposed tax. For example, if taxable clubs are defined so as to include those with total assets exceeding P 100,000, there would be ample opportunity, unless proper safeguards are taken, for clubs to sell assets to either members or non-members and then leasing them back.

It was not possible to obtain data from all regional offices of the national tax administration that could be used for estimating the potential revenues of the proposed tax on a country-wide basis. However, sufficiently detailed information was available from the Bogota national tax office to enable revenue estimates for Bogota-Cundinamarca for 1966, had the tax existed then. The estimate will be a conservative one, since not all clubs

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assets (or gross receipts) per member exceeding some arbitrarily determined level. In such a case the definition of "membership" should be carefully constructed to prevent clubs from artificially inflating membership rolls. Membership could be defined in terms of households rather than individuals, so as to exclude the possibility of counting small children.

64. Exemptions set at these levels would automatically exclude all service clubs in Bogotá, such as the various Lions and Rotary Clubs.

filing income tax returns complied with the asset and receipts reporting requirement. In addition the 1966 returns of a few clubs were unavailable, so that 1965 returns had to be used for them. Both factors should result in a strong downward bias in the revenue estimates, in addition to that arising from possible under-reporting of assets and sales by the clubs themselves. Data from the returns of twenty-six clubs were inspected, and the gross receipts of seventeen having assets greater than P 100,000 were included in the basis for the revenue estimates.[65] As indicated in Table 4 below, application of a 20% tax to the gross receipts of these clubs alone would have yielded about P 5.3 million in 1966. The corresponding figures for 1968 should be considerably higher, since a number of clubs have apparently grown substantially since that time. If we follow the traditional (but crude) rule of thumb that Bogotá accounts for about half of all types of tax collections, nationwide revenues from the tax would have been about 11-12 million in 1966, derived from perhaps 30-35 taxpayer clubs on a nationwide basis.

F. A National Tax on Foreign Travel

1. Present Treatment of Foreign Travel

Heavier taxes upon foreign travel than presently exist may be justified in order to: introduce more progressivity into the tax system; to help conserve foreign exchange; and for revenue purposes. Even if the need

65. It is to be emphasized that the estimate does not include the receipts of all social clubs in the Bogotá area, nor even all of the largest and most opulent, since information on a number of others could not be obtained before the Commission deliberations. It is known that there are at least by actual count, 40 large social clubs within the Bogotá special district alone, and several more in Cundinamarca outside the special district.

TABLE 4

Estimates of Revenues from a 20% Tax on the Gross Receipts of Large Social Clubs in the Bogotà Area, 1966[a]

Name of Club	Reported Total Assets (Pesos)	Reported Gross Receipts (Pesos)
Country Club	12,603,415	7,310,785
Jockey Club	10,144,572	3,000,000[b]
Club Los Lagartos	9,606,601	2.000,000[b]
Club La Colina	8,400,483	1,215,553
Carmel Club Campestre	8,003,591	1,121,553
Club Campestre El Rancho	6,087,068	547,021
Club del Comercio de Bogotà	3,533,933	760,032
San Andres Golf Club	2,680,091	1,355,051
Club de Contadores Publicos	2,113,059	42,232
Club Campestre de Ingenieros	1,808,464	588,940
Club Campestre Fontanor	1,500,095	391,987
Club de Abogados	1,434,144	614,307
Club Deportivo Los Millionarios	1,371,958	4,465,505
Gun Club de Bogota	639,000	350,000[b]
Santafe Club	487,860	3,031,193
Club Social Olimpico	361,945	32,560
Club de Tenis el Campin	143,914	123,982

Total Gross Receipts:	26,599,901
Tax Rate	20%
Potential Revenues:	5,319,980

a. Source: Tax Returns filed in the Bogotà tax office, 1965 and 1966. Data in this table was compiled by Mr. Jaime Vasquez of the Ministry of Finance.

b. Estimated on the basis of the relation between assets and gross sales of clubs of comparable size and activity.

for heavier taxation of this item of consumption[66] is not conceded, it is still evident that the existing tax treatment of foreign travel and other measures designed to restrict foreign travel should be placed on a more rational basis. This point is taken up later. There is also some danger that in the absence of the acceptance of a workable well designed proposal by the Tax Commission, the government will adopt a number of ill-conceived, arbitrary measures designed to curb the drain on exchange reserves arising from travel abroad by residents.[67]

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66. It is explicitly recognized that the consumption element may not constitute 100% of the motivation for foreign trave. Some (for example, the three major newspapers in Bogotá and the association of travel agents) object to any taxation of foreign travel on the grounds that it discourages an activity that is not only "educational" but which leads to generally more "well rounded individuals" and helps to develop a more cosmopolitan outlook' on the part of the citizenry. Although others may question the priorities of those who insist that this type of educational activity (which is almost exclusively undertaken by wealthy Colombians) should be encouraged while other, perhaps equally "educational" activities available to lower income groups (such as movies, and even radio and television) are taxed relatively heavily, this is not at issue here. The fact remains that expenditures for foreign travel represent an especially appropriate index of ability to pay in Colombia (if any expenditures can be viewed in this way). In addition, failure to tax this item of consumption while imposing heavy taxes upon the consumption of products and other services provides an artificial incentive in favor of increased outlays on this most import-intensive of purchases.

67. The administration evidently views this drain with great preoccupation. During the latter part of July 1968 the government announced its intention to curb the outflow of tourist dollars through three separate measures. The first would involve an increase in the 90 day previous deposit requirement necessary for the purchase of dollars by Colombian tourists. Enactment of this proposal would only serve to stimulate the black market in dollars, would provide no revenue to the government (the government may not make use of the deposit funds on hand) and the brunt of the burden would fall on those least able to finance the deposits (those lacking preferential access to credit sources). The second proposal would have had the effect of requiring nearly 1000 students studying abroad to return home. This would be a highly arbitrary action and would penalize such persons all out of proportion to their contribution to the drain on exchange reserves. The third proposal involved an increase to P 1,000 in the present P 500 stamp tax on international departures. This action would be subject to the same objections as apply to the existing P 500 tax discussed below.

At present there exists a P 500 stamp tax that must be paid by each Colombian national departing for a foreign country.[68] There is also a 5% tax that must be paid on the value of each airline ticket having a destination outside of Colombia. The latter is an earmarked tax, the proceeds of which accrue to the Empresa Colombiana de Aeropuertos, and is used for airport construction. No alternation is proposed for the ad-valorem tax.[69]

The P 500 stamp tax suffers from the limitation that it represents a significant disincentive for short trips relative to longer trips, and is unrelated to expenditures abroad by Colombian tourists. A person embarking on a four day business trip to Santiago or Lima pays just as much travel stamp tax as a well-to-do family that spends several weeks on a vacation trip to Europe or the United States.

The government also attempts to limit spending by Colombians abroad by supplying restrictions to the amount of dollars they may legally purchase for this purpose.[70] This limit is ineffective except for the

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68. Other exemptions include: airline and ships crews, persons authorized to engage in frontier trade with Venezuela, Ecuador, Peru and Brazil, and students officially approved for study abroad.

69. A special tax on P 75 must be paid by all passengers (Colombian and otherwise) embarking from a Colombian airport to a foreign destination. Revenues are earmarked for airport maintenance and construction.

70. In 1968 each Colombian national was allowed to purchase $30 (dollars) for each day he planned to spend abroad, with a yearly limit of $1,350. Persons traveling abroad for business purposes were allowed somewhat larger dollar purchases.

infrequent traveler lacking access to the black market in dollars. It fails to limit spending by those persons able to finance extended trips abroad by drawing down on illegal dollar deposits held in foreign countries (and which are almost impossible to discover). Any alteration in the tax treatment of foreign travel should be designed so as to allow the discontinuation of this measure.

2. A Proposed Tax on Foreign Travel

The proposal outlined in this section consists of a combination of three distinct levies, two of which are already in existence. It is designed to tax more heavily a highly income-elastic expenditure item that cannot be easily reached under broad-based income or sales taxes and to bring the tax burden on expenditures for foreign travel more in line with proposed higher taxes on expenditures for income-elastic products. Furthermore, the proposal is intended ts a partial replacement for the complex maze of restrictions placed on foreign travel through previous deposits requirements, limitations on exchange purchases and the arbitrary actions of various government agencies. The proposal seeks to curb the growth of foreign travel by increasing the direct costs of expenditures on this item rather than by restricting foreign travel by relying on ineffective administrative methods that have the added defect of raising no revenues for the government. In addition, adoption of the proposal would allow repeal of a troublesome and unevenly enforced aspect of the income tax law, the 15% income tax surcharge on absenteeism.[71]

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71. This surcharge is imposed on the Colombian income of nationals residing abroad continuously for over six months in any taxable year. The administrative efforts devoted to enforcement of this provision is all out of proportion to the revenues it yields, as collections of this surcharge amounted to less than 1/10 of 1% of personal income tax revenues in the period 1964-66 (about 0.002% of national tax collections).

Specifically, it is recommended that the existing P 500 stamp tax be retained, along with the 5% ad-valorem tax on airline tickets. The latter may be viewed as an acceptable, although imperfect form of user charge on airline travelers[72] and is collected and remitted efficiently by the various travel agencies and airlines. The existing stamp tax may be retained, as there is no good reason to discard it as long as it remains at 500 pesos, especially since the real burden of the tax has been and will be steadily eroded as a result of inflation.[73] Further, the tax is not an insignificant source of revenue, as its 1967 yield was on the order of P 24.4 milion, or almost 1/2 the yield of the national automobile registration tax and P 1 million more than the national surcharge on the property tax. Finally, under the new travel tax system the existing stamp tax will serve as a minimum levy on this type of expenditure, guaranteeing that travelers pay no less than P 500 for each trip.

The characteristics of the new portion of the travel tax would be as follows:

(a) The tax would be levied on the basis of the number of days spent abroad by Colombian tourists, so as to discourage extensive stay and drain of limited exchange resources. Since there is ample reason for believing

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72. If the proposal outlined in this section is rejected, then consideration might be given to increasing the 5% tax to 10% and applying it both to airline and ship travel. This step would be preferable to any increase in the P 500 stamp tax, as it would at least bear a closer relation to overall foreign travel expenditures than would a higher stamp tax levied at the same rate on all trips abroad.

73. The P 500 tax was adopted in 1966. Since that time inflation has reduced its real burden so that its equivalent in 1966 pesos is about P 325.

that time spent abroad is highly correlated with exchange spent, the per diem tax would more closely approximate a levy on expenditures than any other realistic form of tax (given the undesirable stimulus to black market operations involved in applying a regular ad-valorem tax to purchases of exchange from official sources). Further, the imposition of the per diem portion of the travel tax would insure that those persons able to finance extended trips abroad by drawing down on illegal dollar deposits held in other countries would at least have to pay for this privilege.

(b) Trips of not more than six days duration would not give rise to tax liability under the per diem portion of the new travel tax. This exemption is designed to simplify administration and to free the majority of business and "scientific" trips (at least the non-consumption portion of such trips) from tax. Besides, a disincentive to short trips is already provided by the flat P 500 tax.

(c) The rate structure for the new portion of the tax might be as follows:[74]

(i) 50 pesos per day for the first seven taxable days (i.e., between the 7th and 13th day inclusive);

(ii) 100 pesos per day for each subsequent day spent abroad.

(d) The new tax should apply comprehensibly to all travel. The travel of public officials should be included,[75] as this will result in a more

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74. Alternatively the existing stamp tax could be viewed as an advance payment of travel tax and could be credited against per diem tax liability.

75. Alan Peacock convinced the author of the desirability of this provision.

careful scrutinizing of the real costs and benefits of such trips and would have the added advantage of making the tax more palatable to the private sector.[76] For business firms, the entire amount of the tax should, contrary to present practice, be allowed as a deduction under the business income tax.

(e) Aside from trips of no more than six days duration, the only other exemptions would be:

(i) Students approved by ICETEX (Instituto Colombiano Para Estudios en el Exterior) for study abroad.

(ii) Travelers with diplomatic passports, and airline and ships crews.

(iv) Those persons who present a work visa from another country together with proof of gainful employment in that country.

(v) Children under the age of 12 years.[77]

(f) The per diem portion of the travel tax should be collected at the time of return from abroad and should be based on the most recent exit date of the traveler's passport. The travel stamp tax would continue to be paid at the time of departure. Since travelers returning from abroad are likely to be illiquid at the time of reentry into the country, some consideration might be given to the possibility of allowing returnees to sign a statement committing themselves to payment of tax plus interest

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76. For travel of government officials, the nominal cost of the tax would be paid by the government agency sponsoring the trip. Trips not taken by government officials because of the influence of the tax presumably should not have been taken in the first place.

77. Consideration might be given to taxing households traveling abroad as a unit. For example, the rate normally applicable to persons traveling alone could be reduced by one half for each adult member of the household traveling abroad as a unit.

within a specified period, rather than paying at customs.[78]

Although the revenue implications of the tax do not constitute the principal rationale for the tax, the estimated additional yield from this proposal should not be insignificant. Data necessary for a refined estimate of the yield of the tax are unavailable, but an approximation based on some rather arbitrary assumptions can be made for 1966 and then projected to 1971.

In 1966, the last year for which complete data is available, a total of 63,230 Colombian residents (not including airline crews) traveled by air to other nations.[79] Of this number 5,013 stayed outside the country for more than one year. It seems reasonable to assume that the greater part of the exempt travel of students and diplomats fell into the latter category. Assuming that of the remaining 58,217 travelers, perhaps 8,000 were traveling for official government business and perhaps another 5,000 would have been exempt by virtue of possessing work visas, there would have been roughly 45,000 taxable travelers. If we further assume that one-third of this number took trips of less than seven days duration, this leaves a core of some 30,000 taxpayers. If the average duration of

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78. Under this proposal a returning Colombian tourist that had spent 28 days outside the country would have a total travel tax liability of P 2,350 (assuming a six day exemption). He would have paid P 500 on departure, so that the balance owed in tax would be P 1,850 (exclusive of the 5% tax on airline tickets, had he traveled by air). If he had spent $30 per day, the maximum now allowed (the peso equivalent of $30 in August 1968 would be P 492), then the effective tax rate on his expenditures abroad would be about 16%, or some four to eight percentage points less than the retail equivalent of the 50% manufacturers tax rates proposed in the previous chapter.

79. Data furnished by Avianca. Sea and overland traffic is ignored because of a complete lack of data. In any case, air travel is by far the principal mode of foreign travel for Colombian tourists.

trips taken by these travelers were three weeks, then potential revenues from the per diem portion of the travel tax would have been P 52.5 million had the tax existed in 1966.[80] This of course assumes that the tax, had it existed in 1966, would not have significantly diminished the number of Colombians traveling abroad. Although nothing is known concerning price elasticities of demand for foreign travel, an assumption of a high degree of elasticity does not appear unreasonable, since such cost-increasing measures as the enactment of the P 500 stamp tax and other restrictive steps apparently have had little effect in curbing the growth of foreign travel, as witnessed by the extreme preoccupation of the government over the outflow of tourist dollars in 1968 cited previously.

If the stamp tax had been allowed as a credit against per diem tax due, the net addition to government revenues would have been P 37.5 million in 1966 (P 52.5 million minus P 15 million). Assuming the number of non-exempt Colombians traveling abroad increases at 2.5% per year (slightly less than the rate of population growth) revenues from the tax would be about P 60 million in 1971 if the stamp tax is not allowed as a credit against the per diem tax and P 45 if it is allowed as a credit.

Whatever the revenue results, the proposed travel tax appears to be the most feasible means of imposing an expenditure tax on foreign travel that would be in line with the proposed taxes on consumption of other

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80. Calculated in the following manner:

P 10.5 million	-- revenues for the first taxable week (30,000 travelers at P 50 per day)
P 42.0 million	-- revenues for the next two taxable weeks (30,000 travelers at P 100 per day)
P 52.5 million	Total

income elastic goods and services, and would surely be a much more efficient and rational method of curbing foreign travel than the present restrictions intended to achieve this purpose.

III. Stamp Tax Reform[81]

A. Introduction

The British economist Hobson observed in 1910 that "stamp duties are for the most part cumbersome relics of a past haphazard method of catch-penny improvisation which has no place in any scientific system of finance."[82] The existing Colombian system of stamp taxes and stamped paper is truly a fossil of past decades. Most of the virtually innumerable stamp taxes are characterized by inordinately high costs of collection,[83] infinitesimal yields, uncertainty concerning application of the tax and extreme complexity. A previous study emphasized the regressivity of the stamp tax system as a whole and noted that the taxes fall quite arbitrarily on consumers of

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81. The work necessary for the construction of a proposal for stamp tax reform for the Tax Commission was immensely simplified by previous work done by Richard Bird in this area and published in the June 1967 issue of the Bulletin for International Fiscal Documentation, "Stamp Tax Reform in Colombia," pp. 247-255. The author also owes a great debt to Drs. Juan Zorro and Harold Sanchez of the Colombian Finance Ministry for their diligent efforts in securing hard-to-obtain information upon which estimates of revenue loss arising from stamp tax reform could be based.

82. J. A. Hobson, Taxation in the New State (London Metheun, 1919) p. 125, cited in: Alan R. Prest, Public Finance (Chicago, Quadrandle Books 1960) p. 358.

83. It has been estimated that the cost of printing stamps and stamped paper alone amounts to about 1% of total collections and that overall collection costs are perhaps four to five times higher than for most national taxes. Bird, "Stamp Tax Reform," p. 249.

particular products, besides being of low revenue productivity.[84] Compliance costs per peso of tax paid by business firms and individuals are surely far higher for this set of taxes than for any other levy in the tax system. Without question the majority of the largely archaic stamp duties are nuisance levies whose potential for obstructing business and delaying completion of transactions far exceed the marginal contributions they make to the public treasury. For example, a single simple transaction may involve substantial time lost in trips to the stamp tax vending offices and in waiting in yet other interminable lines at government offices in order to purchase stamps.[85] Return trips are often necessary especially in rural areas where stamps, especially stamps of the right denomination, are often unavailable. A number of firms maintain at least one person whose principal task is that of standing in line at stamp vendor offices or otherwise attend to stamped paper and stamp needs.[86] Evasion of stamp and stamped paper requirements in alleged to be far more common than compliance, partly because the basic validity of documents is (fortunately) not voided by improper stamping or failure to employ stamps, and since penalties are nominal. Casual observation easily supports Bird's contention that stamp taxes are often evaded on small transactions and only nominal tax is paid on large ones, and in

84. Taylor, op. cit., p. 203.

85. The author was able to appreciate more fully the wastes involved in the form of sacrificed opportunities (and perhaps output) in the existing stamp tax system (and the endless other activities in Colombia involving long queues) by virtue of his attempt to obtain stamps necessary for the validation of birth documents. In this case the effort to secure one P 10 stamp involved 4 hours of waiting in line and 2 separate trips to the stamp vendor.

86. Information supplied by Fenalco (Federacion Nacional de Comerciantes).

many cases they may be avoided completely by altering the form of the transaction, since it is the form and not the fact that is the object of many of the important stamp duties.[87]

Little would be gained by presenting a detailed description of the present stamp tax system, since Bird's recent paper provides an excellent summary of the major features of this set of levies as well as a discussion of its most glaring defects. Therefore this section will be confined to proposals for reform of the system and the revenue consequences thereof.

The recommendations are conditioned by recognition of the severe revenue constraints facing all levels of government in Colombia. The general presumption is that virtually all of the existing stamp duties would be subjected to the ultimate reform, that of abolition. However, as Table 5 indicates, the revenue consequences of such a step would not be trivial. Therefore some premium should be attached to alternatives that would enable the repeal of the most objectionable aspects of the stamp tax system, while keeping those that are either significant revenue producers that serve useful purposes and those that may be incorporated into a system of rational fees and user charges.

As Table 5 shows, the system of stamp taxes (and stamped paper) furnishes a non-negligible proportion of central government tax revenues, as collections averaged 5.7% of total taxes over the past seven years and 5.4% for the past three years. By way of comparison, the relative revenue importance of the stamp tax system has been about half that of

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87. Bird, op. cit., p. 251.

TABLE 5

Stamp Tax and Stamped Paper Revenues: Absolute Yields and Yields as a Percentages of Total Central Government Tax Revenues, 1962-68 [a]

Year	Yield (Millions of Pesos)	Stamp Duties as % of Total Central Government Tax Revenues
1962	140.6	7.3
1963	168.9	5.6
1964	227.1	5.5
1965	234.8	5.5
1966	328.3	5.2
1967	410.1[c]	5.9
1968[b]	223.1[c]	5.0

a. SOURCE: Minihacienda, Informe Sobre Recaudos. Years 1962-67, January-June 1968.

b. January through June only.

b. Revenues reflect the full effects of the introduction of several new taxes in 1966.

the sales tax and about 2-1/2 times that of the estate tax in the period 1966-1968. Although stamp tax yields have consistently averaged between 5% and 6% of total tax collections, the relative importance of the tax has been maintained by frequent rate increases and the enactment of new taxes in recent years (such as the travel tax and the automobile ownership tax) and not by virtue of an inherent high degree of ex-ante revenue elasticity.

The recommendations outlined below are designed to permit drastic improvements in the operation of the stamp tax system, with consequent high benefits to government (in the form of reduced administrative costs) and taxpayers (in the form of vastly reduced compliance costs) with minimal sacrifice of revenue. Where information is available concerning the possible revenue consequences of each recommendation, these are discussed in conjunction with each. At the end of the section an attempt is made to summarize the revenue results of the proposals as a whole.

For purposes of selective reform the existing stamp tax system has been divided into four categories.

(1) Those that are objectionable on almost all counts (either on grounds of their nuisance aspects, regressivity, small revenue yield, complexity, high rates of evasion and high administration and compliance costs) and which should be abolished outright.

(2) Those that are questionable on grounds of economic effects or administrative feasibility and which should be considered as possible candidates for abolition.

(3) Those that are essentially in the nature of payments to the government for services performed by the public. These should be retained

but placed on a cost-of-service basis. It is emphasized, however, that the levies that remain as fees need not necessarily be collected by means of stamps.

(4) Those which actually represent taxes unrelated to services rendered by the government but which have some merit as elements in the tax structure and which thereby should be retained. Here again, these levies need not be collected by means of stamps.

B. Candidates for Immediate Abolition

1. Official Stamped Paper (Papel Sellado)

A very strong case can be made for the abolition of this relic of the 19th century. This aspect of the stamp tax system is an unmitigated nuisance which serves no useful purposes. Evasion is widespread, since failure to comply with the complex stamped paper requirements does not invalidate the legality of a document, and penalties are very light.[88] The law pertaining to stamped paper is exceedingly complex; it is difficult for the taxpayer to know exactly which and when documents must be recorded on stamped forms. For example, there are over 32 classes of exemptions from the stamped paper requirement, with various sub-classes within classes.

The minor revenue importance of stamped paper is evident from the figures for total collections in 1966 and 1967. In both years, revenues from stamped paper at P 13.1 million and P 15.7 respectively amounted to less than 4% of total stamp tax collections.

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88. At present there is a one-peso charge for each sheet, and a three peso charge for failure to comply with stamped paper requirements.

It is not unlikely that printing and other administrative costs involved in the sale of stamped paper exceeded revenues. In any case, net revenues for the government are probably nil. Without question the social gain from the abolition of stamped paper in the form of reduced compliance costs, diminished taxpayer aggravation and removal of impediments to transactions, will infinitely exceed the small amount of revenues lost. One argument that has been employed in defense of the retention of stamped paper is an extremely weak one: that because stamped paper has a 40% rag content, while most "common" paper does not. The use of stamped paper insures that "records" will not deteriorate with age. But even this argument is no longer valid, because at the beginning of 1968 the rag content of stamped paper was reduced by one-half.

2. The Stamp Tax on Public and Private Appointments

It is difficult to imagine what could have been the rationale for the establishment of this particular tax unless it grew out of the spoils system of allocating public jobs and represented an attempt to recapture some of the spoils for the public treasury. At present, new public (and a limited number of private) appointments give rise to a stamp tax liability which must be paid by the employee on assuming his duties,[89] the basis of the tax being his first month's salary. Even if pay scales for public employees were commensurate with those of the private sector, and even if all government salary checks arrived punctually, this tax would

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89. If monthly salary does not exceed P 1,000, the tax is 2%. If monthly salary exceeds P 1,000, the tax is 4%. If all salary is contingent, a tax of five pesos is paid. The tax also applies to interim appointments.

make little sense. As it happens pay scales are low in comparison with the private sector, and an employee receives his first check (with luck) some months after beginning work. In the meantime he is required to pay the tax several months before receiving income. As Bird noted, "it is so difficult already to hire and keep capable people in the public service that it seems ridiculous to place even minor obstacles in the process."[90] There is abundant support for this contention. Unfortunately the requisite data required to estimate the possible revenue loss arising from abolition of this portion of the stamp tax is not readily available. However, the revenue that would be foregone from such a step would almost certainly be inconsequential. In any case the argument for abolition of the tax is so strong that it should be repealed forthwith.

3. The Tax on Income Tax Declarations

At present there is a P 10 stamp tax on income tax declarations (P5 for each of two copies, P 20 for late returns). There are a number of objections to this particular aspect of stamp taxation:

a) If the government truly desires to encourage the filing of income tax declarations (even when no tax is due) the tax is irrational since it not only automatically creates a tax liability for the declarer whether he has income tax liability or not, but also makes the process of declaration more burdensome and time consuming, given the necessity of standing in yet another line to obtain stamps.

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90. Bird, op. cit., p. 252.

b) The tax is clearly regressive in its incidence. It is estimated that only slightly more than 1/2 of those who filed income tax returns in 1966 paid any income tax, while according to Bird, 1/3 of those who filed taxable returns in Bogotá paid more in stamp tax than in income tax.[91] It has been argued that "since so many of those who declare income are exempt from tax or have liabilities inferior to 10 pesos, the existence of this particular stamp tax is justified as a contribution to help defray the high cost of handling and processing tax-exempt returns."[92] (Indeed, the minimum cost of processing returns, even the simplest ones, is estimated to be at least seven pesos.) In reply to this contention it may be noted that a simple and more rational solution to this problem would be to raise the level of filing requirements. This would have the added advantage of allowing more careful policing of taxable returns via the release of administrative personnel into more productive activity.

Even though the initial motive for adopting the tax was primarily that of gaining more revenue, yields in 1966 and 1967 were barely greater than the cost of processing all the tax-exempt returns. Total revenues (nation-wide) from this provision were (including the additional 10 peso stamp tax on late returns) only P 12.3 million in 1966 and P 20.8 million in 1967, the only years for which figures were available.

Abolition of this particular tax would thus involve minimal revenue sacrifice. Further, if the commission adopts the proposals concerning changes in the level of filing requirements[93] (which would be raised from

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91. Bird, op. cit. p. 252.

92. Typewritten comments by Ruben Gonzalez Lago, Lawyer for the National Tax Administration, May, 1967.

93. See Melvin White and Andrew Quale, "The Colombian Individual Income Tax," Part II, chapter ___ of this volume.

the present P 2500 level to at least P 5,000 and possibly P 10,000, depending upon which plan the commission accepts), revenues from the stamp tax on income tax returns will fall in any case, so that revenue loss from abolition of the tax will be perhaps only 2/3 of the amount that would be lost in the absence of changes in filing requirements.[94]

Furthermore, the net revenue loss to the government would be still less if many remaining stamp taxes were disallowed as deductions from the income tax. At present any and all stamp taxes paid are eligible for deduction. Consistency with respect to other taxes would require that deductibility should be allowed only for those stamp taxes that represent necessary expenses in earning income. The proposals outlined in this paper will, if accepted, eliminate a large number of stamp taxes that are both nuisances and directly and vaguely related to the earning of income. The elimination of deductibility of all the remaining stamp taxes should be considered in order to minimize the central government revenue loss from abolition of many of the stamp taxes, and to simplify income tax returns. One of the most often voiced complaints against the income tax at present is the extreme complexity of the returns.

It is recognized that some small violence to horizontal equity would result from abolition of deductibility for all stamp taxes. Therefore, it is suggested that if the above suggestion is not accepted, only a few specifically enumerated of the remaining stamp taxes that are obvious expenses of earning income be allowed as deductions. Examples might be:

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94. Rough calculations indicate that if filing requirements had been P 10,000 in 1967 rather than P 2,500, revenues from this particular stamp tax would have been about P 14 million instead of P 20.6 million.

certain stamp taxes which are actually surrogates for licenses, such as the taxes on firearm sellers, certificates of air and seaworthiness and health, etc. In any case, more limited deductibility of stamp taxes would reduce overall revenue loss. Certainly the abolition of dozens of stamp taxes, as recommended here, would in itself automatically lead to marginal increases in income tax yields because all are now deductible. If all stamp taxes had been disallowed as deductions in 1967, we can roughly estimate that income tax revenues might have been some ₱ 40 million more in 1967 than they actually were.[95]

Elimination of the deductibility feature would, therefore, allow greater freedom from revenue constraints in stamp tax reform.

4. Stamp Tax on Matches

This is clearly a petty tax that is easily evaded and which is not very productive of revenue. The present provision requires that a .02 centavo stamp (about 1/10 of 1 U.S. cent) be affixed to each and every box of matches sold. Cost of printing, selling and policing (if any) of this antiquated tax, when combined with compliance costs of match-makers (almost all of which are large enough to be reached effectively under the sales tax) must surely exceed the meager revenues from this levy. For 1966 and 1967, yields were only ₱ 6.0 and ₱.6.8 million respectively.

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95. Stamp tax revenues were slightly greater than 400 million pesos in 1967. To calculate the effects of elimination of their eligibility for deductions, we would need some information on marginal tax rates of those taking stamp taxes as deductions. This we do not have. However, as a rough approximation we can use the average rate paid on taxable returns, which was about 11% in 1964. Assuming this figure is reasonably accurate for 1967, and applying it to overall stamp tax collections, we obtain an approximate figure of ₱ 40 million. Of course, a significant portion of stamp duties were probably paid by persons paying no income tax in 1967.

Thus very little revenue would be foregone if this tax were repealed, while at the same time efforts to simplify administration and compliance would be well served.

5. Stamp Tax on Playing Cards

This is another example of a nuisance levy which produces almost no revenues and which is apparently evaded on a large scale. The regulations require that a 40 centavo stamp be affixed to each pack of cards. Revenues from this provision were only P 124 thousand in 1966 and P 80 thousand in 1967, so that revenue loss from abolition of this remnant of colonial times would be insignificant.

6. Stamp Tax on Greases

The present provisions call for a 80 centavo stamp on each gallon or fraction of a gallon of nonedibile grease. This levy serves only to delay distribution of the product and is also quite easily evaded and unproductive of revenue. Yield figures for the nation as a whole are not available, but estimates based on Ecopetrol and Intercol remittances of the tax indicate that for 1966 and 1967 collections were about P 5.4 million and P 4.9 million respectively.

7. Stamp Taxes on Petitions to the Government

Petitions to the government for the purpose of seeking exemption or reduction of taxes or customs duties, as well as several other types of petitions, must pay a P 10 stamp tax. This provision appears to be among the most objectionable of all the stamp taxes. As was noted in an earlier study, such petitions should be viewed as a right for citizens in a democracy and should not be discouraged by a fee.[96] Abolition of this archaic levy

96. Taylor, op. cit. p. 203.

would indicate a more positive attitude on the part of the government toward its constituents and would help moderate the sometimes extreme adversary stance characteristic of relations between government and private citizens. Although revenues from this provision could not be obtained, it is highly doubtful that abolition of this levy would involve more than 100 thousand pesos at most.

Other documents or other written proceedings presented to most government agencies carry a P 1 tax. This is yet another petty tax that increases the cost of doing business with the government, not so much because of the 1 peso tax but because of the time and trouble involved in ascertaining whether the tax should be paid, buying stamps, having them cancelled, etc. Revenue losses are inestimable but would almost certainly be inconsequential.

8. Stamp Tax on Books of Account Registered at a Chamber of Commerce

This tax, levied at 20 centavos a sheet, has no evident rationale whatever unless it is that of providing make-work for clerical employees of the chambers of commerce who must affix stamps to each page. Quite by chance, I am personally aware that this requirement is almost never followed. Evasion of this levy is freely admitted. No information can be obtained concerning collections from this tax, but considering the comments above, revenue losses from abolition would be nil.

9. Stamp Tax on Payrolls Presented for Payment by Government Employees

Public employees must pay each month a stamp tax of 20 centavos per P 100 of salary. Here is a case of the use of a captive group of taxpayers by the government. Public employees are already grossly underpaid

and must pay a significant stamp tax when hired.[97] Also, unlike their more fortunate counterparts in the private sector who find it much easier to evade income tax (being either self-employed or having access to unpoliced expense accounts), public employees typically pay the full amount of taxes due on their salaries.

Abolition of this provision would have cost the government P 280 thousand in 1966, the latest year for which comprehensive salary figures paid by the government are available. A yield of this magnitude hardly justifies the additional bookkeeping work required to collect the tax.

10. Stamp Tax on Certain Documentary Evidence

This is essentially a tax of 25 centavos per 100 pesos of value indicated on documents[98] presented in evidence in proceedings to obtain payment of debts, either in civil suits or administrative proceedings. This provision only makes the collection of debts more cumbersome and expensive. It should be abolished and if charges are to be levied, a fixed percentage of the contested indebtedness should be charged to the debtor, if he is adjudged in arrears (as in small claims courts in most U. S. states). No basis for estimates of revenue loss is available.

11. Contracts; Agreements to Enter into a Contract.

Contracts must pay 25 centavos per P 100 of value or P 20 where value is indeterminate; agreements to enter into a contract are subject to a tax of P 10. This levy amounts to a considerable burden on personal and

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97. In 1966, 63% of all public employees (excluding police and the military) received salaries inferior to P 1,000 (about U.S. $70).

98. Where the value is indeterminate, the tax is 30 pesos.

business transactions and could be defended only in terms of revenue needs. Since the revenue productivity of this levy is insignificant, there is no argument for retaining it, as the tax is inconsistent with modern business methods. Furthermore, there are so many exemptions from this provision that it is nearly impossible to know when a contract is taxable.

12. Stamp Taxes on Bills of Lading, Drafts, Bills of Exchange, Warehouse Receipts, Leins

A) Bills of Lading. Domestic bills of lading or any other freight documents pay a tax of 5 centavos per P 100 charge. Foreign bills of lading pay a P 5 tax plus P 2 per extra copy (payable at $1.00 U.S. = 1 peso).

These charges impede the orderly conduct of financial activity and freight transfer. In an economy where significant delays in execution of transaction are plentiful enough, no further obstacles should be raised. Revenues are insignificant, especially given the ample opportunities for evasion of this provision and lack of (fortunately) policing efforts.

b) Drafts, Bills of Exchange and Promissory Notes

Taxes on these items are levied at 25 centavos per P 100 value. These taxes on credit instruments should be abolished for the same reason the stamp tax on contracts should be repealed.

c) Warehouse Receipts. Insofar as this is a tax (20 centavos per P100 value) in addition to warehouse charges for use of government warehouses, it should be abolished as a nuisance. If the tax is imposed in

lieu of charges, it should still be abolished and charges placed on a cost-of-service basis.

13. Flight Documents

This stamp tax is payable at P 10 per page of flight documents (payable at U.S. $1.00 = 1 peso). This is another nuisance tax that impedes orderly business operations, except this one is hardly even applied since all Colombian airlines and a number of foreign ones are exempt. Therefore, revenue loss will be nil if the levy is abolished.

14. Stamp Tax on Various Forms of Certificates

Except as noted below in the section dealing with present stamp taxes that can be converted to a fee basis, all stamp taxes on certificates should be abolished because of the miniscule revenues they entail.

15. Stamp Tax on Parcels

This tax applies to declarations made by individuals to the post office concerning the value of parcels whose contents are subject to duty. The three-page declarations made for parcels sent abroad are taxed at P 2 per sheet. Packages sent anywhere within Colombia carry a 20 centavo tax in addition to postage stamps. The only purpose served by this set of stamp taxes is that of requiring the expenditure of at least one hour of additional time in the post office in order to send a package.

C. Possible Candidates for Abolition

1. Stamp Tax on Issuance of Bonds

This tax is levied at 1% of the nominal value of the bond if it is registered. Bearer bonds (unregistered bonds) pay 2%. Given the still

quite embryonic nature of money and capital markets in Colombia, any tax that inhibits the issuance of debentures, however slightly, should be viewed with some reservation. However, a case can be made for the continuation of the 2% levy on bearer bonds unless other means are found to limit the use of this substantial avenue of income tax evasion.[99] Data required for the estimation of the revenue loss that would arise from abolition of this duty are unavailable.

2. Stamp Tax on the Issuance, Assignment or Transfer of Corporate Shares

This portion of the stamp tax is levied at 4% on the issuance of both registered shares and bearer shares. Transfer of registered shares gives rise to stamp tax liability of 2% of the previous month's market value of the share, and transfer of bearer shares requires payment of stamp taxes equal to 3% of the value of the share, as determined by the National Tax Administration.

The tax on the issuance and transfer of shares has been severely criticized for a number of reasons.[100] First, the existence of the tax has often been used as an argument against a full-fledged capital gains tax that would include capital gains in its base. Second, the tax is a poor substitute for a capital gains tax, falling as it does on loss as well as gain transactions. In addition the tax violates generally accepted principles of equity, as it is unrelated to the size of any gain or to the income

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99. See Part II of this volume Chapter ____; Richard Slitor, "Reform of the Business Income Tax" Section _____.

100. See Bird, "Stamp Tax Reform," pp. 252-253 for a more detailed discussion of these criticisms.

of the recipient. Finally, the tax may have impeded the development of the embryonic private capital market by lowering the price and volume of traded assets.

For these reasons, serious consideration might be given to repeal of the issuance and transfer taxes on registered shares, especially if the Commission adopts the staff proposals for the capital gains tax.[101] However, as in the case of bearer bonds, the tax on bearer shares should not be repealed at the present time. It does not appear that there exists any other method for reaching gains from these instruments, and they are universally acknowledged to be one of the most notorious means of evading income tax. Since the issuance of bearer shares cannot be prohibited outright because of legal constraints, the stamp tax due of their issue might be increased to at least 25% or 30%.

3. Stamp Tax on Insurance Policies and Renewals

This tax is imposed at rates from 2.5% to 4.0% of gross monthly premiums. It almost certainly inhibits the growth of the incipient Colombian insurance industry and thereby discourages this form of saving. Further, to the extent the tax impedes the development of greater insurance activity, it discourages the growth risk-spreading institutional arrangements that many believe to be critical for the process of development in nations such as Colombia.[102] A weak argument for retention of this

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101. See Andrew C. Quale Jr., "The Capital Gains Tax," which appears as Chapter ___, Part II of this volume.

102. C.f., Charles Wolf, Jr., "Institutions and Economic Development," reprinted in Bernard Okun and Robert W. Richardson, Studies in Economic Development (New York; Holt, Rinehart and Winston, 1964) pp. 355-359.

provision is that its incidence may be progressive.

4. Stamp Tax on Checks and Other Money Transfers

Under present stamp tax provisions all checks payable in Colombia must carry a 20 centavo tax. The tax is printed on the checks and paid by the depositor to the bank when check books are delivered. This tax might be considered as a candidate for abolition, as it acts as a deterrent to the increased use of this safer, more convenient and efficient means of making payment.

However, as Colombian stamp taxes go, the tax is fairly productive of revenue and is reasonably easy to pay and collect. Revenues from the 20 centavo tax (on checks only) were P 13.9 million in 1966 and P 14.5 million in 1967.[103]

For money transfers other than checks, the stamp tax should be repealed on grounds of the miniscule revenues it brings in (P 70 thousand in 1967).

D. Stamp Taxes That Should Be Retained but Placed on a Fee Basis

The guiding principle that should be followed for return of stamp taxes affecting a number of services performed by the government for individual members of the public is that the taxes as such should be abolished and charges made on a cost-of-service basis.[104] If this were done, the use of stamps would be superfluous. The only argument for

103. Estimates based on data supplied by the Central Bank on reported checks paid in the country for each year.

104. Ordinarily, charges for such services should not be made on a cost-of-service basis when a substantial and clear redistributional intent is involved in the rendering of the service, e.g., public medical care provided for indigent families.

retention of the stamp requirement is that failure to do so would invite wholesale pocketing of receipts by those public employees collecting fees for rendering the government services in question. This argument is largely invalid. Charges and fees can always be collected without stamps except in those limited cases where a stamp must be affixed in order to attest to the validity of certain certificates or documents (such as those that expire on a periodic basis), and dishonest public employees can always perform a service and pocket the fee when stamps are used if the payor does not demand a stamp each time. Certainly the affixing of stamps does not (as upper-echelon tax officials will vouch) guarantee honest fiscal administration, and the requirement builds inflexibility into charges in the face of changes in cost of service.

Some of the items listed below involve regulatory activities of the government, some entail government issuance of or validation of various documents and certificates, while others represent tangible services rendered by government agencies to benefit specific persons. In general, the pricing principle for the fees and charges outlined below should be based on the full costs of providing the services, although in the case of certain services of a non-regulatory nature some consideration might even be given to a simple form of price discrimination in favor of low income persons, or where this is not administratively feasible, charges set below costs. No attempt has been made to calculate appropriate levels of charges or fees for each activity, as this would be an impossible task in the short time available to the commission staff, although some tentative suggestions

are indicated in certain cases.[105]

Notwithstanding the lack of hard evidence concerning the extent to which the present stamp duties levied for these activities falls short of that required to cover costs of service, it is clear that some of the charges could be revised upward considerably, thereby converting them into more productive and equitable sources of general government revenue.

As indicated by Table 6 below, no less than one dozen categories of existing stamp duties could be feasibly altered to a cost-of-service basis.

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105. An excellent (and perhaps the only) guide to the construction of a rational structure of fees and user charges for various types of services rendered by government agencies may be found in Alice John Vandermeulen, "Reform of a State Fee Structure: Principles, Pitfalls and Proposals for Increasing Revenue," National Tax Journal, Vol. 17 (December 1964) pp. 402-409.

TABLE 6

Stamp Taxes Recommended for Conversion to a Fee Basis: Present Taxes and Proposed Fees

Type of Activity or Service Affected	Present Stamp Tax Rates	Proposed Fees
1. Certificates of Airworthiness and Seaworthiness	Airplanes: P 5 per metric ton Ships: P 1 per ton or cargo capacity	Airplanes and ships: Inspection fee: P 50 per hour of inspector's time Registration fee: P 200 per year
2. Official Health Certificates	P 2	A charge sufficient to cover part of the costs of examination and recording, since a substantial portion of benefits not confined to the possessor of the certificate.
3. Tax Clearance Certificates a/ (Certificados de Paz y Salvo)	P 1	An increase to P 5 in order to more closely approximate processing costs
4. Copies of Official Publications	P 1 for publications, P 2 per sheet for official translations	Costs of publication or translation except in cases where wide dissemination is deemed essential (e.g., public health brochures)
5. Copies of certificates of marriage, death, etc.	50 centavos per copy	costs of production
6. Homestead rights.	50 centavos per hectare	costs of processing applications
7. Naturalization Papers, Passport Travel Permits and Visas	Naturalization Papers: P 500 for farmers, skilled laborers and spouses of Colombians; P 1,000 for all others Passports: P 100 upon issuance, P 20 revalidations Resident visas: P 10 Temporary visas: P 5	Same as present taxes
8. Patents and Trade Marks	Trade Marks: P 200 Patents: p 500 Renewals of either: P 200	Same as present taxes, except for foreign trade marks: P 1,000
9. Proceedings for establishment of judicial status (corporate charters, etc.)	P 100	Costs of processing and recording
10. Wills and testaments	P 20 per page	Recording costs
11. Official property appraisals	Impossible to determine	Appraisal costs
12. Consular Invoices and Certificates	Consular Invoices: US $5 per original copy; US $2 per extra copy Consular certificates: US $5	Same as present taxes

a/ These certificates are required of all Colombians planning to travel abroad and are issued only upon proof of non-delinquency in payment of national taxes. They are also required for other purposes too numerous to mention here.

E. Other Stamp Taxes

Finally, there are a number of stamp duties that are essentially taxes but which have merit on other grounds and which therefore should be retained in modified form (though not necessarily by the central government). These include:

(1) Travel tax

Under the proposal outlined in a previous section of this chapter[106] the P 500 travel stamp tax would be retained as part of a new travel tax. This is the only case where the requirement that stamps as such must be purchased should be continued.

(2) Automotive stamp taxes

The present tax varies with vehicle age, and rates range from P 25 to P 80 per month.[107] Under the proposals for reform of automotive taxation, it has been recommended in another chapter that this tax be extensively modified and given to the departmental governments.[108]

This is the only instance in which the abolition of a stamp tax would lead to a significant revenue loss for the central government, should the right to tax automobile ownership be made the exclusive property of the departments.[109] The tax has only been in existence since late 1966 and

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106. See p. ___.

107. The tax is imposed on the following basis:
(a) vehicles of model years 1950-55: P 25 per month
(b) vehicles of model years 1956-59: P 35 per month
(c) vehicles of model years 1960-63: P 50 per month
(d) vehicles of model years 1964-69: P 80 per month

108. See McLure, "Automotive Taxation," Chapter ___. Section ____.

109. However, the revenue gain to the departments would, because of alterations in the form of the tax, far exceed the revenue loss to the national government.

became effective in 1967 (except in Antioquia, where officials have refused to collect the tax). Revenues for 1967 were P 51.1 and are estimated at P 65.0 for 1968.

(3) Licenses and non-commercial permits[110]

(a) Licenses to sell firearms, ammunition and explosives

The present tax is P 500 for initial license, P 200 for renewals. This levy should be retained so as to retain some element of control over traffic in these items. However, it would be much simpler just to sell the license certificates and renewals for P 500 and P 200 respectively and dispense with the stamps.

(b) Licenses to sell in public streets and plazas

The present tax of P 200 should be retained and more strictly enforced in order to more effectively ration the number of stations available to reduce urban sidewalk congestion; and to limit outlets for small contraband articles.

(c) Permits to carry firearms

The existing P 10 tax might be increased to P 25 or P 50 as a further element of control in the use of firearms.

(4) Commercial permits and concessions

(a) Permits to exploit emerald mines

The existing stamp tax duties of P 1,000 for such permits and P 200 for renewals should, in the absence of good reasons for altering the charges, remain at present levels, as long as the government makes no attempt to

110. All three categories within the set of license-permit taxes could well be viewed as appropriate for conversion to a cost-of-service fee basis. In this case charges would be based on the costs of regulation.

restrict emerald mining through limited issue of permits.

(b) Navigation permits

The present stamp tax duty of P 5 on these permits might be increased to P 50 or P 100. An increase in this levy appears justifiable since the state furnishes valuable services to ships plying the various rivers and harbors (buoys, channel dredging, bank lights, etc.).

(c) Concessions

Present taxes on concessions are as follows:

(a) Petroleum - P 2,000

(b) Uranium - P 1,000

(c) Other mining - P 200

(d) Forest rights (over 500 hectares) - P 500

(e) Water rights - P 1 per liter per second for water use

This set of taxes should be retained in their present form although rates could possibly be increased in certain cases.

(5) Imports by travelers in excess of allowances

The present stamp duty is defined as 2% of the value in excess of travelers' allowances. Consideration might be given to increasing this tax to 10%, in order to dampen one of the principal incentives for foreign travel.

(6) Ship's manifests

The present tax is variable according to ship tonnage. Rates range from P 45 for ships under 45 net tons up to a maximum of P 150 for ships over 10,000 tons. Some consideration might be given to increasing rates, for the same reasons applicable to navigation permits.

G. Revenue Losses

Any estimate of the net revenue effects of the set of proposals regarding the stamp duties must of necessity be quite crude in nature. However, a rough idea can be gained by examining the calculable losses that would have resulted had the recommendations been in force in 1966 and 1967. The calculable loss (the losses that can be ascertained by adding up the losses from abolishing taxes for which reasonable revenue estimates exist) would have been P 45 million in 1966 and P 110 million in 1967 if the automobile tax had been ceded to the departments. If the automobile stamp tax had not been ceded to the departments, calculable losses would have been P 45 million in 1966 (the automobile stamp tax was not in effect then) and P 59 million in 1967.

No realistic estimate of the 1971 net revenue loss is even remotely possible. However, assuming that some increases in charges for those stamp taxes converted to a fee basis and those remaining as taxes are possible, it seems reasonable to place the 1971 revenue loss at between P 100 and P 150 million.

APPENDIX I

Estimates of Potential Retail Sales Tax Revenues for the Eighteen Largest Municipalities, 1966

In order to estimate potential revenues from a municipal retail sales tax of the type discussed in section C of Chapter __, it is necessary to have some idea of the magnitude of taxable retail sales in the municipalities that would be employing the tax. Such estimates are available for the year 1960 for the eighteen largest municipalities only. This study was sponsored by DANE (The National Statistical Bureau) and constitutes the only recent reasonably reliable information of any kind concerning retail sales.

In order to derive an estimate of retail sales for 1966, it was necessary to employ some rather crude assumptions; specifically it was assumed that retail sales in each municipality grew at the same rate as gross domestic product over the period in question. The use of this assumption is likely to understate the true growth of retail sales during the period for at least three reasons.

1) The process of development itself has undoubtedly drawn more and more of the population into the money economy.

2) Increasing urbanization in Colombia over the past decade has quite likely increased the percentage share of total sales at retail of the principal cities vis-a-vis the rest of the nation.

3) Many taxable services that would be incorporated in the base of the tax (beauty parlors, laundry, etc.) were not included in the original data.

Therefore total estimated retail sales for 1966 in the largest cities (especially the four largest) are probably substantially inferior to actual retail sales for these cities in 1966.

The average annual rate of annual money GDP growth for the period 1960-1966 was approximately 17.4%. Therefore, if retail sales grew at the same rate, retail sales in 1966 should have been 2.615 times thier value in 1960. If we can assume that retail sales in each municipality grew at the same rate as the national average, we can calculate estimated 1966 retail sales for each of the four large cities and for the rest of the nation as well. Then, applying a 2% rate to taxable retail sales, we may derive potential 1966 revenues for the retail tax, had it exited then. It should be noted that we are dealing only with taxable retail sales. (Retail sales in the original DANE study were classified according to types of products sold. Food sales were subtracted from aggregate 1960 retail sales reported by DANE for each municipality.)

Table A-1 summarizes the results for the 4 principal municipalities.

TABLE A-1

Hypothetical 1966 Retail Sales Tax Revenues: Barranquilla, Bogota, Cali and Medellin, and Actual Industry and Commerce Tax Collections, 1966.

(millions of pesos)

	Estimated Taxable Retail Sales 1966	Projected Taxable Retail Sales 1966	Hypothetical Retail Sales Tax Revenues Assuming a 2% Rate, 1966	Actual Industry and Commerce Collections 1966
Barranquilla	433.10	1,132.6	22.7	13.6
Bogota	2,070.50	5,414.4	108.3	28.7
Cali	655.50	1,714.1	34.3	10.9
Medellin	629.70	1,646.7	32.9	36.1
Totals			197.2	89.3

For all of the 18 largest municipalities the following picture emerges, as summarized in Table A-2.

TABLE A-2

Hypothetical Retail Sales Tax Revenues for the 18 Largest Municipalities in 1966 and Actual Industry and Commerce Tax Collections, 1966.
(millions of pesos)

18 Largest Cities; Estimated Taxable Retail Sales 1960	18 Largest Cities; Projected Taxable Retail Sales 1966	18 Largest Cities; Hypothetical Retail Sales Tax Revenues Assuming a 2% Rate 1966	Actual Industry and Commerce Tax Collections, 1966 (all municipalities)
4,892.9	12,795	255.9	146.0

Even if we explicitly recognize the rather obvious limitations of each of the revenue estimates, it is clear that the revenues that would arise from the proposed retail sales tax would easily exceed those of the present Impuesto de Industria y Commercio, even if rates for the new tax were as low as 2%. If anything, each of the yield estimates most likely grossly understate the actual revenue potential of the tax. However, no allowance has been made for potential tax evasion.

Since a high premium has been placed upon insuring that the substitution of a new form of tax for the existing industry and commerce tax will not result in substantial losses of revenue for the municipalities, alternative approaches to the estimation of the potential revenues from a retail tax may be worthwhile, as a check against the calculations above.

Two quite crude independent estimates were undertaken for this purpose. One applies to Bogota only, the other to the nation as a whole.

The estimate for Bogota employed a sample of the 10 large non-food retail vendors that make their income tax declarations in Bogota. For each of these firms, reported figures for gross sales were extracted from their income tax returns for 1966. Unfortunately, it was not possible to obtain data for other large firms having branches and selling in Bogota but filing income tax declarations in other cities.[1]

If we make the assumption that the nationwide firms that declared in Bogota made 50% of their gross sales in Bogota (this does not appear to be grossly unreasonable, since Bogota is responsible for around 50% of all economic activity, tax collections etc.) we may obtain a figure of gross estimated sales of these 10 largest firms of P 412.5 million in Bogota alone. Had a 2% retail tax existed in Bogota in 1966, revenues from these 10 firms alone would have been P 8.3 million for Bogota. Actual revenues collected from nearly 40,000 firms covered by the industry and commerce tax were P 28 million for that year. Therefore the collection potentisl for a hypothetical 2% retail sales tax levied only upon 10 firms would have been about 30% of the actualy industry and commerce tax yield.

An alternative, but equally crude approach, may be employed to estimate potential retail sales tax revenues for the nation as a whole in 1966. Levin estimated that the base of the present national sales tax was about 25% of gross domestic product in recent years.[2] The exemption struc-

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1. Included among the firms filing in other cities are several quite large retail enterprises such as Tania, Ley, Carvajal, Caravana. The firm Ley is the largest retail distributor in Colombia.

2. Jonathan Levin, "The Effects of Economic Development on the Base of a Sales Tax: A Case Study of Colombia," International Monetary Fund Staff Papers, March 1968, p. 57.

structure of the proposed retail tax would be virtually identical to that of the existing national sales tax, but a large number of services would be included in the scope of the former that are not found in the latter. Because of the inclusion of services, and because the retail tax would include wholesale and retail margins (whereas the existing tax generally does not), it appears fairly safe, even conservative, to assume that the base of the municipal retail sales tax would be at least 33% of GDP.

Assuming that this percentage relation holds for the years 1966 through 1968, we may obtain, given figures for GDP and the proposed retail tax rate, a very rough idea of the potential revenue from a retail tax imposed on a nationwide basis for these years. The calculations are summarized in Table A-3 below.

Even after allowing for rates of evasion for the retail tax comparable to those for the national sales tax (50%), and considering that the proposed retail tax would likely be levied only in cities with more than 100,000 inhabitants, it is clear that the revenues from the proposed tax would more than compensate for the abolition of the industry and commerce tax.

TABLE A-3

Estimates of Potential Revenues from a 2% Municipal Retail Tax on Nationwide Basis, and a Comparison with Actual Industry and Commerce Collections, 1966-1968

(millions of pesos, current prices)

	Gross Domestic Product [a] (1)	Retail Sales Tax Base as Percent of GDP (2)	Retail Sales Tax Base (3)	Potential Retail Sales Tax Revenues (2% of column 3) (4)	Industry and Commerce Tax Collections (5)
1966	72,021	33%	23,767	475	146
1967	80,704	33%	26,632	533	123
1968	90,550	33%	29,882	598	165 [b]

a. 1966 GDP figures from Banco de la Republica, Cuentas Nacionales (multilith. Bogota, 1968) 1967 and 1968 GDP figures based on Planeacion estimates of rates of growth in money GDP.

b. Estimated.