ISSN 0738-3185

PN-ABB-947
60125

Monograph No. 16
Grenada Tax Project
Comprehensive Fiscal Reforms For Grenada: Directions For Research and Technical Assistance

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September 1984

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COMPREHENSIVE FISCAL REFORMS FOR GRENADA: DIRECTIONS FOR RESEARCH AND TECHNICAL ASSISTANCE

I. The Problem

The Grenadian fiscal system is in need of a comprehensive reform. In a nutshell, taxes are too high and the government share of GNP too large to accommodate a growth led by increased private sector domestic and foreign investment. The fiscal reform needs to be comprehensive rather then piecemeal, it calls for a different tax policy than presently exists, and it must include a program of deficit reduction.

Grenadian current expenditures have grown at about the same rate as GNP during most of the past decade and, by 1983, accounted for one-fourth of total national product. This is a high percentage, even by comparison with other LDCs. Grenada's current expenditure increases have been largely uncontrolled--budgetary planning is not well developed--and the focus seems to have been as much on sustaining the public employment budget as on stimulating economic development activities. Capital spending has increased at an even faster rate than current expenditures, to its present level of about 30 percent of GNP. Given the small size of the domestic economy, it has taken a very high level of taxation and foreign assistance to support this spending program.

The tax system has developed in an ad hoc manner, largely to meet the revenue demands of rising current expenditures. As in most cases where revenue generation is the driving force benind discretionary tax changes, other desirable attributes of the tax structure have been sacrificed: the

present system is not hospitable to increased investment or risk-taking; it is unfair in taxing some types of purchases and income-generating activities (imported goods, exports, dividend income, wage and salary income) more heavily than others; and little public savings have been generated. All of these problems have been exacerbated by a steadily deteriorating quality of tax administration.

The major structural problem with the Grenadian tax system is clear: the nominal tax rates are too high. The personal income tax reaches a marginal rate of 65 percent at about 3 times the average family income; the company tax rate is 55 percent; and the average tax rate on import value is 53 percent. In virtually every country where tax rates reach such high levels. there is pressure on the government to provide special exemptions; the rate of illegal evasion rises; elaborate schemes are hatched to avoid payment, for examples, the creation of quasi-governmental corporations, and the payment of grocery allowances in lieu of wages; and smuggling and underdeclaration of import values increase. The net effect of these actions is to further narrow the tax base, force the nominal rates to rise even higher, bring even more pressures on government to provide exceptions, and on it goes. This is exactly the pattern that has developed in Grenada. By 1984, the tax system had become a formidable obstacle to private sector-led development.

The problems that lie ahead are not too difficult to identify. The fiscal deficit of 1984 will grow, under almost any circumstances, during the next few years. The major pressures on expenditure growth cannot be

eased overnight. The involvement of U.S. assistance in capital investments will not likely be reversed or slowed, hence the substantial recurrent cost commitments associated with new capital investments will materialize,[1] and a national unemployment rate in the 30 percent range makes it unlikely that massive public employee layoffs can occur immediately.

Elimination of the deficit in the next year simply will not happen. The more relevant question is whether steps will be taken now to plan a longer run program of deficit reduction, or whether the GOG will continue to make year-to-year, ad hoc adjustments. The long-term, planned adjustment is clearly the only way to go. Otherwise, the future pattern is likely to be one of yearly negotiation with the IMF, World Bank, and US government about which taxes can be raised and which expenditures can be cut. The result of this pattern, in so many countries, has been piecemeal adjustments to the tax system which have piled new distortions upon old distortion. There is an opportunity for comprehensive tax reform in Grenada in 1985, and this opportunity may not soon present itself again.

II. Objectives

A comprehensive fiscal reform program for Grenada might take four objectives as basic. The first is to establish a long run (5 year) fiscal plan to find a balance between expenditure needs and tax requirements, and to set appropriate revenue targets. Since high tax rates are the major fiscal issue in Grenada, the first problem to be dealt with is the need to

control and slow the growth in expenditures while providing for adequate recurrent cost coverage on new capital projects. The institution of budget planning and control mechanisms, reconsideration of the GOGs public enterprise role, and the institutionalization of a fiscal planning model are all central to achieving this objective.

The second goal is to reform the tax system so that its rate and base structure will be conducive to a private sector led economic development strategy. This reform will involve a program of income tax rate reduction and broadening the tax base, but it also will involve structural reforms to reconsider if not eliminate the distortions or biases in the present system, for examples, the bias against dividend distribution and in favor of retained earnings, the protection of certain but not other domestic production activities, the absence of any taxation of property wealth, and the effective exclusion of capital gains from the tax base. These distortions may be corrected by structural reforms of the tax system, depending on the kinds of tradeoffs the GOG is willing to make between economic development, equity, and revenue yield goals. To determine whether such tradeoffs are desirable, one needs to carefully study the potential response of investors, workers, and producers to alternative tax structure changes.

Third, it is an important objective to make the reform program a lasting one. This means that a set of administrative procedures must be put in place and made operational, and that a well-trained staff be left behind to carry on the work. Too often in the past, the technical assistance programs have been short term, and the advisors did not stay

in-country long enough for the reforms to "take." The 1981 income tax administration assistance, customs administration training in 1980, the property valuation exercise in 1981, and the financial management assistance provided in 1979 are all examples of technical assistance programs which did not lead to permanent improvements. The reason for this failure, we think, is that the advisors did not stay with it long enough to see the programs through to implementation. This is why we stress the need for long-term technical assistance in the administration area.

Fourth, technical assistance in the area of tax and expenditure reform must be coordinated. If the reform is to be truly comprehensive, and if all the pieces of the program are to fit together, it is essential that the technical assistance advice be carefully planned. For example, one does not want to invest in improving the administration of some component of the tax system that will be scrapped by structural reform. The program of purely administrative reforms must not get out in front of the structural reform program. It is also essential that the fiscal reform and the reform of economic policy be carefully integrated. The fiscal and economic policy changes cannot take place independently. For examples, one must coordinate any change in import tax rates with changes in the foreign trade regime, and the income tax treatment of interest depends in part on changes in the usury laws. Another kind of necessary coordination is that which must take place among the donors of the technical assistance, at least USAID, the IMF, and the World Bank. Finally GOG tax reform cannot take place in isolation from the other Caribbean countries with which it shares a common external tariff and currency union.

III. Technical Assistance Needs

We might break the technical assistance needs into three general areas:

- tax structure;
- tax administration and training;
- expenditure planning and control.

Several careful studies of particular aspects of the fiscal system are called for. These analyses, based on study of available data, the laws, observation of the operation of the system, interviews, and/or survey research are indispensable in formulating the right structural reforms. In other cases, the technical assistance will require day-to-day advice, on-the-job training, and a rewriting of job duties, office procedures, etc. The former usually do not have to be carried out by full time resident staff. The latter clearly do.

Tax Structure Studies

The common goal in the tax structure studies will be to redesign the current tax system to be simpler, more easily administered, and more conducive to promoting private sector involvement in economic development. One approach to this goal--the right one, we think, based on our initial work--is to move toward broader-based, flat rate (or "flatter" rate) structured taxes with a heavy emphasis on improved administration. The following general discussions are indicative of the kind of work which needs to be done. (More detail on the general setting for the structural studies is provided in Fiscal Memorandum No. 4.)

Personal Income Tax. The personal income tax can play a more important role in the Grenadian tax structure. As detailed in Fiscal Memorandum No. 5, the present system is defective in the areas of tax base, rate structure, and administration.

The base of the tax has been narrowed by unwarranted exemptions (e.g., interest income), generous deductions, and considerable tax evasion by the self-employed. To control this latter problem, there is a clear need to upgrade skills in the Inland Revenue Department in techniques such as field auditing. (Administrative reform issues are discussed below and in Fiscal Memorandum No. 13.) But the problem is more than simply administration; it is also a legal structure that is unfair and likely an impediment to economic growth.

The steeply progressive tax rate structure, with marginal tax rates of 65 percent for taxable incomes above EC$30,000, has created powerful disincentives to work effort, private investment and risk-taking. Such distortions run counter to the main government policy objective of rapid economic growth led by the private sector. High rates have also discouraged compliance, damaging the horizontal and vertical equity of the tax.

Besides studying the most appropriate tax rate structure, there are other aspects of the personal income tax that will require further thought. For example, at present, capital gains are not taxed, but some form of their inclusion in the tax base would be desirable. Income averaging procedures and inflation adjustments of the tax to avoid arbitrary real burden increases produced by inflation should be

incorporated in the tax law. The present tax ignores these issues. It would also be desirable to study the provision of a general standard deduction and simplified tax form as an alternative to the present itemized-deductions-only approach.

Structural study is necessary to understand the revenue yield, incidence, and economic development impacts of a more flat rate tax structure, indexation, various changes in deductions, credits, etc.

Company Income Tax. The company tax has gradually diminished in relative importance in recent years. By 1983, it represented only 11.4 percent of total tax revenue. This performance is to a large extent a reflection of the poor business climate of the last few years, to which the company tax itself may have contributed.

As in the case of the personal income tax, the present company tax is characterized by a deficient design of the tax base, a discouragingly high tax rate (55 percent), and poor administration. Administrative issues are discussed in Fiscal Memorandum No. 13.

The impact of the company tax on incentives to invest and on risk-taking is of crucial significance to GOG economic development objectives, since the largest share of private investment takes place in the company sector. To create a favorable climate to investment, the tax rate should to be lowered. But there is also a list of important structural issues, discussed in some detail in Fiscal Memorandum No. 6, that need to be considered prior to reforming the company tax. Some of these are:

- Whether firms should be allowed to use accelerated depreciation methods, in addition to the straight line method currently used.

- Whether firms should be allowed to depreciate at replacement cost or some other inflation-adjusted method and what is the proper inventory accounting method.

- Whether a longer loss-offset period than the present 3 years should be granted.

- What is the most desirable way to integrate the company and personal income taxes to avoid double taxation of dividends.

Property Tax. As noted in Fiscal Memorandum 7, the property tax is presently providing less than 1 percent of total revenues, and has been declining in relative importance. The major problem is administrative--the lack of a tax roll and the ability to maintain one--and this will be addressed through technical assistance, as described below and in Fiscal Memorandum No. 12. Other aspects of the problem, however, are structural. The present form of property tax is overly complex, horizontally unequal, and yields less revenue than it could. These problems, and the possibilities for reform, need to be addressed through careful study of the alternative choices for restructuring. The following questions/issues are central to such study:

- Can the differential assessment rates and progressive rate structure under the present system be eliminated?

- How many parcels need be included in the system, and how should agricultural land be treated?

- How can revaluation be efficiently accomplished and what techniques can be used to maintain revenue yield between regular revaluation years?

There also is the question of how much revenue can Grenada derive from the property tax. One could make the argument that as much as EC$4 million could have been derived in 1984, without causing undue economic distortions, had a functional property tax been in place. The level of property tax in Grenada, as a percent of GNP, is well below international norms. Using data from a recent study of fiscal systems in 55 developing countries, we can estimate that a fivefold increase in property tax revenue would be necessary to bring Grenada to the average.[2] The issue in Grenada is not just that property taxes are low, but that other taxes are levied at very high rates. One needs to explore the implications of a higher effective property tax rate in conjunction with lower income taxes, to determine if such a 'swap' would be good public policy for Grenada.

There are other forms of property taxation in Grenada that must be included in any consideration of comprehensive reform. A major question is whether the property transfer tax should be eliminated or reformed (see Fiscal Memorandum No. 8) and whether a capital gains tax on land is possible and appropriate. On the one hand, the property transfer tax does not yield much revenue and its elimination would remove some of the disincentive to understate property transfer sales values. The latter could be an important gain for property tax valuation purposes. On the other hand, as long as there is no tax on capital gains, the property transfer tax is the closest surrogate which the GOG has in place. Moreover, elimination of this tax may not lead to more accurate property value records. In this case, one might argue for a strengthened property transfer tax. Obviously, the issue calls for careful study and

coordination with reforms proposed in the areas of capital gains taxation and property valuation.

Finally, the GOG should consider the possibility of using betterment levies, or special assessments, to capture a portion of the future land value increases. This form of taxation could be quite lucrative, given the potential impact of infrastructure improvements on land values. Many countries have found effective ways to capture the land value increments associated with public improvements. Careful study is necessary to work out the best technique for Grenada.

Indirect Taxes. Indirect taxes yielded about 64 percent of all tax revenues in 1983; and import duties constituted about 93 percent of indirect taxes. The heavy reliance on taxes related to foreign trade is almost inevitable in a small open economy such as Grenada, but some shift away from this heavy reliance is necessary and possible. Especially in the longer run, as the domestic economy develops, the indirect tax system must be capable of drawing local production of goods and services into the tax system. One focus in this structural study will be on designing such a system.

There are major problems with the present system of indirect taxation in Grenada, as outlined in Fiscal Memorandum No. 10. The first is that the combined rates of tax on imports are very high, equaling 53 percent of the value of imports subject to duty, or 26 percent of the value of all imports. Basic foods carry a combined rate of over 29 percent and other foods from 37 to 86 percent. Non-food consumer goods carry rates ranging from 48 to 96 percent, with some as high as 140 percent. Thus, the level

of protection is very high and the burden on low income consumers may be quite high.

The second problem is the very great complexity of the system: there are nine different levies on foreign trade. Some apply specific rates, some apply ad valorem rates, and some apply both. The tariff rates are highly complex, difficult to administer and there is no document that shows all levies by commodity class.

The third problem is the differential treatment of various commodities and importers. While relatively few commodities are exempt from duty, exemptions to government, statutory bodies and businesses favored under tax incentive legislation resulted in 57 percent of the value of all imports entering free of duty. The result of this pattern is a narrowing of the base, perhaps unnecessarily, which leads to a higher tax rate; uneven and perhaps unintended degrees of protection; and an unfair treatment of consumers who cannot benefit from preferential tax rates on imported foodstuffs and consumer goods.

Fourth, there are relatively heavy export duties which appear to be burdening agricultural production. Clearly these duties should be phased out. There are better ways to tax profits in the agricultural sector.

Finally, there are substantial problems in the administration of indirect taxes, largely in the Customs area. These are discussed below and in Fiscal Memorandum No. 11.

A first order of business in Grenada is a structural reform of the system of indirect taxes. While the general direction of reform already

seems clear, working out the specifics will require a great deal of research. The general scope of work for this design stage would include:

- A codification of the present rates levied on different commodities.
- A unification of the present nine elements of the indirect tax structure into a common external tariff and a general consumption duty. The rate structure would also be simplified with three or four basic rates. The important problem is to select these rates and analyze the revenue and equity implications.
- Tax rates on domestic consumption should be brought in line with levies on imports to promote economic efficiency in production. Before the introduction of a domestic indirect tax policy, however, a careful study of the economic structure of the Grenadian economy is necessary to avoid cascading effects and the introduction of taxes that heavily burden lower income groups. The exemption from tax of intermediate commodities purchased by business would mitigate the tax cascading. The regressivity problem might be handled either through a basic deduction under the personal income tax or through the exemption of basic goods--unprepared foods and medicines--from the consumption tax. Considerable study is needed to work out this aspect of the tax design.
- A plan for phasing out the export tax needs to be developed.

Industrial and Trade Policy. The coordination of tax reform with industrial policy and the foreign trade regime is especially important in a small open economy such as Grenada. For example, a reduction in taxes on imports might exacerbate the balance of payments problem; the negotiation of tax treaties or trade programs may alter the GOG's views about the "best" tax practices; and general reforms of the income tax may be an even more effective industrial policy than a tax incentive package.

A careful analysis and plan for coordination is necessary because policymaking in these areas has been somewhat fragmented.

At this point it is difficult to establish the full scope of work for this study. We can, however, suggest some of the priority areas. A first has to do with the present fiscal incentive package, which has been formulated with very little coordination and input from the Ministry of Finance. An in-depth study is necessary to integrate alternative proposals for tax reform with the new Investment Code and other aspects of industrial policy. Indeed, changes in the investment code would be necessary if new company tax provisions were to make certain incentive provisions irrelevant, e.g., a change in the depreciation methods allowed under the company tax. Similar issues may arise with respect to indirect taxes, especially the preferential tax treatment of imported raw materials and capital goods.

Two other aspects of the fiscal reform that must be integrated with industrial incentive policies are: (a) the taxation of repatriated profits and other non-resident incomes through the (new) withholding tax; and, (b) the establishment of double taxation treaties with foreign governments. With respect to (a), it may be, for example, desirable not to exclude tax holiday profits from the (new) withholding tax if the profits are repatriated. In terms of (b), it would be of no value to sacrifice domestic tax revenue through the granting of incentives, if because of the lack of a bilateral treaty with the country of residence of

the foreign investor, the sacrificed revenue ends up in that country's treasury.

Finally, there is the question of how an altered tax structure will effect the balance of payments. The primary areas of concern, other than those mentioned above, have to do with phasing out the export tax, removing certain tax preferences for imported goods, tightening import valuation procedures, and reducing certain tax rates on imported goods. A careful study of these impacts is essential.

Tax Incidence. With such a comprehensive reform program as this, it will be essential to determine how the distribution of the tax burden will change. In particular, one would want to consider the impact of these reforms on low income families and to consider how alternative versions of the reform package will affect these families. This analysis will enable the GOG to determine how much equity can be gained by various types of tax adjustments, e.g., lower tax rates on foodstuffs vs. an increased level of income tax exemption.

A tax incidence study--an analysis of who will pay Grenadian taxes--must be carried out. This will be made very difficult because of the absence of data: there are neither national accounts nor a consumer expenditure survey. This leaves open only one option--the use of income tax return data, and the establishing of national tax burdens for representative, but hypothetical taxpayers. For low income families, it will be necessary to do a longitudinal family budget survey to determine how changes in the indirect tax structure (in tax rates on various commodities) would reduce their purchasing power, and how (which)

exemptions and preferential rates can soften the regressivity of the system.

Especially in light of the proposals under consideration here--flat rate, broad-based taxes which favor investors--it will be important to find ways to protect the poor from onerous increases in the burden.

Taxing the Tourist Sector. One hope for development of the Grenada economy is tourism. It will be important to develop a strategy for taxing the tourist sector that walks a fine line between generating adequate government revenues while not letting tax rates get so high that the island becomes uncompetitive. At present, the tax system can reach tourists through hotel occupancy and meals, airport departure, and excise taxes on items such as beer. The system might go much further in the areas of taxes on restaurant meals, taxi fares, the sales activity of tourist stops, and the use of utilities.

In any case, a careful analysis of the taxation of this sector is necessary. The analysis needs to specify ways in which tourist activities can be taxed, but needs to do this in a context of understanding the practice in competing countries. The use of company income taxes, personal income taxes, and consumption taxes need to be harmonized in looking for an optimal way to tax tourists.

Comparative Tax Practices. The Grenada economy is small, open, and must maintain a competitive tax climate. Comprehensive tax reform in Grenada will be constrained by the practice in other East Caribbean States. A basic background paper to this study is an analysis of the comparative level and structure of taxes in these countries.

Tax Administration and Training

There are four areas where tax administration and training assistance are essential: income taxation, property taxation, customs administration and the implementation of a general consumption duty. These technical assistance needs are only summarized here but are spelled out in some detail in Fiscal Memorandum Nos. 13, 12, 11, 10, respectively. We emphasize the importance of having this administration and training assistance march along with the structural reform. Much of the training and administration needed is basic, and can begin immediately (e.g., training in basic accounting and property valuation). Other needs are more closely tied to structural reforms and would not begin until year 2 of the project (e.g., training sales tax auditors to administer a general consumption tax).

In the following paragraphs, we outline the scope of work for technical assistance to improve the tax administration and to provide training in the four areas mentioned above. We also believe that technical assistance is necessary in the area of budgeting procedures and control, but we have not included this component in this paper.

Income Tax. Because of poor administration, the personal and company tax bases in Grenada are unnecessarily narrow. This is a major reason why the nominal rates are so high. For example, IRD officials estimate that an assessment program that would capture the self-employed would have increased 1984 personal income tax revenues by EC$3 million to EC$5 million. This additional revenue would have enabled a significant reduction in the marginal rates.

The first step to improved administration is to reduce the complexity of the income tax system by broadening the base, simplifying the rate structure and permitting fewer deductions. This could eliminate about 12,000 PAYE taxpayers from the enforcement program, leaving 2,500 self-employed and 300 company taxpayers to be considered for the Audit program. A group of 12 to 15 well-trained auditors could do this work.

The proposed technical assistance would provide this training, rewrite the assessment manuals, redesign the forms and generally advise on the operation of the department. The following ten points more or less define the scope of work for this technical assistance.

- Of the thirty-nine members of staff, only three have had any appropriate training. The training required will take approximately nine months.
- The present Manual would have to be reviewed and updated.
- A management information system would have to be designed, including preparation of feeder reports for the system.
- Assist in establishing a sound taxpayer assistance and education program.
- Assist in redesigning the tax forms and instructions.
- Assist in centralizing the collection activities.
- Assist in the preparation of a Collection Procedures Manual.
- Assist in developing norms for a modified assessment program.
- Assist in the preparation of job descriptions.
- Assist in complete reorganization of the assessment and collection functions, as soon as the self-assessment system becomes operative and provisional assessments can be discontinued.

To carry out this work, training and implementation, would require an experienced resident advisor for a period of 18 to 24 months.

Property Valuation. As noted above, there is virtually no property tax roll in Grenada. As a result, relatively little is collected (EC$700,000) and the real size of the legal tax base is declining. Some structural changes in the property tax, such as a flat rate structure and the exemption of low valued properties, could make the tax easier to administer. However, there remain important problems in the administration of the tax that need to be corrected. These include (a) carrying out a fiscal cadaster which locates and identifies every parcel on the island, (b) putting an efficient record-keeping system in place, (c) valuation of parcels to be taxed, and (d) establishing and implementing a collections procedure.

A first, necessary step in this reform is for the GOG to provide the following:

- Amendment of the Property Tax Management Law to eliminate sections prescribing certain forms and procedures, and to authorize establishment of the proposed system.
- A commitment to complete the "photogrammetric" topographical maps in suitable scales for property inventory and valuation purposes (1:2500 and 1:1250).
- The selection and hiring of the proposed PVD staff.

One full-time expatriate technical advisor (2 years) and one on-call expatriate advisor will be needed to help with development of training materials, work procedures and instructions and with the installation of the system. The latter includes the completion of an inventory of

identified parcels of land in a cadaster and of an accompanying revaluation of land and buildings.

The short-term technical advisor would be a person with broad experience in property tax administration, reassessments, systems design and installation, tax administration improvement, and design of the special assessment program. This advisor would serve short periods of time on special assignments, as needed, for a total estimated time of two months in a two-year period.

The long-term advisor would serve for 24 months and would be a person with extensive experience in performance and in supervision of field work, including the appraisal of land and buildings, and records management. He would (a) participate in the designing and conducting of the training program, (b) assist the valuations officer with the guidance and supervision of the installation of the new system, and (c) assist in the early completion of the cadaster and revaluation. This advisor would also be involved in the design and application of the tax collection enforcement procedures envisaged as a part of the improved recording and reporting of information (as a result of computerization), particularly of overdue taxes.

Implementation of a General Consumption Duty. If, as both this report and the IMF recommend, the existing indirect tax structure is merged into a general consumption duty, it will be necessary to have a technical assistance advisor during the implementation stage. The advisor will train the inspectors in sales tax audit and will provide all necessary

assistance in phasing in the tax. He should be in country for about 9 months, overlapping the period of implementation.

The importance of having such an advisor should be emphasized. Even after the tax is designed and the inspectors trained, there remain a host of problems to be resolved. For example, a record-keeping system needs to be designed and the possibilities for computerization explored; forms must be designed and printed; a taxpayer (businessman) education program must be carried out; the inspectors must be given continued on-the-job training in the early stages; and the "hard cases" must be dealt with individually. Experience in other countries has taught the lesson that implementation of such a major reform is very difficult and must go slow.

Customs Administration. Technical assistance in the Customs area, as noted in Fiscal Memorandum No. 11, will focus on three general areas:

- Modernize and render effective the conventional control of the Customs and Excise Department.
- Prepare the Department to adapt to the impact of future fiscal policy changes and new responsibilities.
- Provide a training plan which will equip middle and lower grade staff to administer an improved control system and equip more senior staff to organize and implement new procedures and controls.

The problems of Customs Administration in Grenada, which ultimately show up in a narrowing of the tax base, are undervaluation of imports and inadequate control of the domestic use of "concessionary" materials. The sources of these problems are many:

- The staff is poorly trained and there are neither instruction manuals nor adequate copies of the law.
- The law and regulations are out-dated and in need of revision.
- Routine operating procedures are deficient.

Technical assistance in the customs valuation area requires a long term advisor(s) who can assist the customs and excise department in the following scope of work:

- Create a four man specialist investigation unit to control fraud in contraband, valuation, domestic production traces and diversion of concessionary duty-free goods.
- Create a four man "industrial unit" to control excise and domestic consumption duties, use of concessionary material and verification of certificates of origin.
- Train all middle and lower grade personnel in conventional procedures, higher grade in specialist innovations and customs brokers.
- Set up and operate a customs valuation system
- Redraft the Customs Law and Regulations to encompass new activities and prepare instruction manuals.
- Commence preparatory work on the adjustment of the national tariff nomenclature to conform to the forthcoming Harmonized Commodity Description and Coding System - CCC Brussels.
- Permit the inclusion of a customs representative on the decision-making body for granting duty-free concessions.
- Prepare a special procedure for the import and export of goods connected with assembly operations.
- Make improvements where necessary in routine customs procedures, but specifically in the fields of tallying imports, refunds of duty, post-audit of documents, administrative penalties, and hydrocarbon oil control.

Three levels of technical assistance have been planned according to cost. Level I, 2 man years, recommended here, is designed to cover assistance in all fields where deficiencies have been identified. A six week preliminary study is recommended to prepare the ground for an advisory team. These scopes of work are further elaborated in Fiscal Memorandum No. 11.

The project could be carried out at lower levels of activity. Level II, 18 man months, covers the same fields but economizes on training by reduction of course lengths and subjects and use of local instructors. The Customs Ordinance would not be redrafted: merely the Regulations pertaining to new procedures and manuals. Level III, 12 man months economizes further on course lengths and subjects and omits brokers. There would be no legal, regulatory or manual drafting. In all levels the establishment of a valuation branch has been maintained as the essential element including the related training. The potential payoffs of "doing it right," however, would seem to argue for Level I.

Expenditure Planning and Control

What the GOG is able to do about effective tax reform in the long run depends on their ability to reduce effective tax rates, which depends in turn on their willingness to control expenditures. While no amount of technical assistance can increase this willingness, there are two areas where the ability to control expenditure increases can be strengthened: budgetary control and the institutionalization of a fiscal planning model.

Budgetary Control. The budget is the main instrument in the hands of a government to achieve its fiscal goals. Good budgeting procedures

require: (a) clear definition of government objectives and priorities, and the dissemination of this information to all governmental agencies, (b) the gathering of information from all agencies so as to identify needs, to control the size of each agency's budget, and to allocate funds, weighting requests against one another, (c) control and audit, to make sure agencies do not overspend and that they have allocated funds according to the budget.

The present budgeting procedures in Grenada are weak in relation to (a) and (b). As detailed in Fiscal Memorandum No. 2, the present system does not allow the gathering of the basic information needed, for example, to cut or increase expenditures in an efficient manner. With respect to (c) above, the MOF has in place a very effective mechanism to control non-budgeted spending, but auditing practices, as recommended in the IMF report, need to be reinstated.

The Government of Grenada should again review the recommendations of the 1979 IMF Report on financial management, and should consider seeking additional technical assistance for implementation in this area. The IMF might be a good source of technical assistance in this area.

Fiscal Planning Model. Another view as to how one controls expenditure growth is by understanding more perfectly how each expenditure decision impacts on the longer term growth of the Government of Grenada budget. A fiscal planning model has been installed in the Ministry of Finance to accomplish this objective (The model is described in Fiscal Memorandum No. 14). In its present version, the model is simplistic and needs to be expanded. Though the model allows basic projection of employment, wages,

and the other objects in the budget for each functional category, e.g., health, construction, etc, it could be improved in a second phase of this project.

- Using more complicated formulas, much more flexibility could be introduced to the expenditure forecasting part of the model. In particular, separate growth rates could be used to forecast employment and other objects in different functions, and growth rates could be allowed to differ across years.

- At present, capital expenditure planning is done on a year by year basis. This obviously does not allow a smooth capital expenditure pattern and makes forecasts of debt service for new capital commitments virtually impossible. The unplanned element in capital expenditure may leave unexpectedly large deficits or a scramble to introduce new taxes to close the deficit. Capital expenditure planning would be given careful study, and a realistic capital planning approach would be implemented.

- Due to a lack of detailed historical data on revenues, the revenue forecasting techniques used in the present model are less than could be done with better data. A second phase of the model would introduce improved revenue forecasting methods.

IV. Implementation Plan

One possibility for carrying out this project is through the Syracuse University Cooperative Agreement with USAID. This, obviously, is the possibility we would prefer. If this arrangement were used, the implementation plan would have four components: general project management; coordination with other donors; long-term, resident advisors, chiefly in the tax administration area; and short term technical assistance, chiefly in the tax structure area. The relationship established should be one in which the contractor reports directly to the

GOG on substantive matters, and USAID plays the role of an interested third-party and a monitor of contractor finances.

General Project Management

The Project Manager would be the Metropolitan Studies Program of the Maxwell School of Syracuse University. The manager would design the project, coordinate all short and long-term TA, review and approve all work, and maintain regular liaison with the Director-General Finance in the GOG. A Fiscal Advisor to the GOG would serve as Resident Director of the Tax Mission office in Grenada. We have used such an arrangement in Jamaica and it has worked very well.

Coordination with Other Donors and Other Projects

This project cannot be carried out in isolation, for any number of reasons. The most important is that Grenada is an open economy, heavily dependent on foreign trade. Moreover, Grenada is closely tied to other OECS countries through a common external tariff and currency union. Many of Grenada's tax policy problems cannot be solved unilaterally.

Second, there is a need to coordinate TA and policy advice from various donors to make sure that it is not at cross-purposes. Most notable here is the need to coordinate technical assistance and advice in the tax and budgetary policy area, from USAID, The IMF, and The World Bank. Third, resources are scarce and a coordinated tax policy effort can reduce the financial burden and speed the project implementation.

A first step in this tax policy program is for the GOG to call a meeting of all donors involved, agree to a more or less common approach, a timetable and a cost-sharing program. The consortium, represented by a

panel of experts drawn from the donors should meet semi-annually, with COG officials, to review progress and implementation plans.

Short-Term Technical Assistance

A number of studies of the Grenada tax structure must be carried out, as described above. The procedure is more or less as follows: two field visits, of about three weeks each, to gather data and discuss results. One to two months of home office work to prepare the report. Another two months of elapsed time is necessary for GOG and home office review. The tax incidence analysis will take a much longer time period to complete because of the survey research required. A Staff Paper with findings and preliminary recommendations from each analysis is the final product of this phase. The amount of time necessary for each study will vary, depending on the complexity of the topic. A first version of the set of studies required includes the following:

TABLE 1

Study Area	Man Months[a]	Trips
Personal Income Tax	3 (1.5)	2
Company Income Tax	3 (1.5)	2
Property Taxation	3 (1.5)	2
Indirect Taxes:		
Customs and Excise	2 (1.0)	2
Consumption Duty	3 (1.5)	2
Trade and Industrial Policy	3 (1.5)	2
Tax Incidence	6 (3)	5
Tourism Taxation	3 (1.5)	3
Statistics Improvements	1 (2)	1
Comparative Taxation	2 (1)	1
Fiscal Planning Model	2 (1)	4

[a]Number in parenthesis indicates man-months in the field.

Long-Term Technical Assistance

The Syracuse Project would open a Grenada office, from which the long-term advisors would work, and where the short-term field work would be carried out. We would anticipate a total effort of between 87 and 102 man months of long-term techical assistance.

The Tax Project office would be headed by the Resident Director, Fiscal Advisor. He/she would be an economist, would serve in residence for two years and would have the following duties:

- Coordinate all project activities in country.
- Advise the Ministry of Finance on Fiscal Matters.
- Discuss each staff paper and proposal with the Director General and staff and assist in preparing an implementation plan.
- Work with the Ministry in developing the fiscal planning model; and in continuously revising fiscal projections.
- Supplement the analysis of all short-term studies.

The duties of the other resident advisors--income tax administration, customs administration, property valuation, and consumption duty implementation--are described above and in the Fiscal Memoranda. The Long-Term technical assistance man-year requirements, at various levels of effort, are described in Table 2.

There is also need for an advisor in the area of budgetary planning and control. It is not included in this proposal, in hopes that funding could be obtained elsewhere (perhaps IMF).

TABLE 2

LONG-TERM TECHNICAL ASSISTANCE REQUIREMENTS
UNDER VARYING LEVELS OF EFFORT
(in man months)

Duty	High Level Package	Middle Level Package	Low Level Package
Fiscal Advisor	24	24	24
Income Tax Administration Advisor	18	12	12
Income Tax Collections Advisor	3	--	--
Customs Advisor	24	18	12
Property Valuation	24	24	--
Indirect Tax Implementation	9	9	9
TOTAL	102	87	57

V. Timetable

The timetable for Project analysis and implementation is 24 months. The structural studies described in the section above will take place during months 1-9. By month 12, a "White Paper" on comprehensive tax reform will have been presented to, and discussed with, the GOG. Of the short term TA studies, only the tax incidence analysis would continue past month 12.

The long-term TA will begin in month 1, with basic training and procedural assistance. Much of this work is very basic and need not wait for the GOG to initiate structural reforms in the tax system. Other administrative work and training--for examples, initiating a special assessment program under the property tax or training sales tax

auditors--cannot begin until the GOG has moved on the reform of the system.

A number of benchmarks in the training area might be established:

- By the end of month 12, 12-15 income tax inspectors will have received basic training. These persons will continue with on-the-job training, and specialized coursework during months 12-24.

- The Property Tax roll will have been established by month 12, and about 15-20 field assessors will have been trained. A full valuation will have been completed at the end of month 24, and an improved collection system will be in place.

- Training in 'basic skills' for Customs Officers, Class II and III will be completed by month 6.

ENDNOTES

1. A recent IMF report projects that the future recurrent costs implied by this public investment activity could be staggering. Unless some control measures are put in place, one might expect current and total expenditure shares of GDP (in 1990) of up to 30 and 45 percent, respectively. With controls in place, this growth can be slowed considerably, but the expenditure share of GNP will still remain high.

2. The data used to make this computation are from Vito Tanzi, "Quantitative Characteristics of the Tax Systems in Developing Countries," in Modern Tax Theory in Developing Countries edited by D. Newbery and N. Stern (forthcoming).

FISCAL MEMORANDUM NO. 1

TAX REFORM IN GRENADA

ROY BAHL

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GRENADA TAX PROJECT
Fiscal Memorandum Number 1

TO: Sam Skogstad, USAID
FROM: Roy Bahl
SUBJECT: Tax Reform in Grenada
DATE: May 30, 1984

1. I understood my assignment to be a review of the Grenada tax system, examination of current IMF and GOG activity in this area, advice on the kinds of tax reform that might be most conducive to a private sector led development strategy, and suggestion of an action plan for USAID to assist in revision of the tax code. These areas are all covered in this memo.

2. My six working days in Grenada have been full and useful, but of course it is a very short time and I have done too little by way of hard analysis. I met with the following people:

Ministry of Finance (General Policy)

Mr. L. Wilson
Mr. A. Kirtin
Mr. V. Calendar

Inland Revenue Department

Mr. B. Harford
Mr. Lowe
Mr. Hosten
Mr. Louis

Customs and Excise Department

Mr. P. Bubb
Mr. Stewart

Budgeting

Mr. Angus Smith

Exchange and Control Department

Mr. G. Phillips

OAS

Mr. Noberto Ambros
Mr. Thomas Riegert

I received very good and hospital cooperation in every case. The only exception was that the data gathered by the IMF mission were not made available to me, and only one table in a recent report on income tax reform was shown to me. In the latter case, Mr. Victor Calendar felt it would be premature to let us see these data. In the case of the data, I was told that the mission had taken it back to Washington and copies were not left.

3. This report does not contain specific estimates or hard analysis, but mostly my impressions based on a quick look. I do think, however, that the data are available to get answers on many of the big questions (e.g., what portion of the taxable capacity of Grenada is exempt by code or concession, which imports account for the larger share of indirect tax revenues, what revenue loss would various income tax rate cuts imply, etc.). I would be very surprised if the Fund team did not take steps to get at these questions by pulling samples of income tax files and customs declarations.

4. Time was short, and so I could not do as thorough an analysis as I would have liked. In particular, I have not had time to do much with

inheritance taxes, property transfer taxes, the tax treatment of foreigners, motor vehicle taxes, and export taxes. I assumed that fiscal incentives were part of someone else's assignment, but I would have liked to do more in that area.

5. This report contains a discussion of the current and prospective GOG budgetary condition; a discussion of tax reform analysis currently underway; a brief on the problems and issues concerning the present structure of taxes; a view of the need for overall tax reform; and a proposal for an action plan.

Budgetary Position

6. The FY 1984 budget suggests a current account deficit of about $8 million, or 9 percent of total recurrent expenditures (see Table 1). This estimate assigns all debt repayment to the capital budget and, hence, understates the current deficit. The 1984 deficit is a result of a slow growth in tax revenues (almost no growth over 1983), a discretionary reduction in tax revenues due to a reduction in the stamp duty rate, and a large increase in recurrent expenditures. The IMF estimated a 25 percent increase in personal emoluments in this total. The 1984 deficit would appear to be financed largely (about two-thirds) with general assistance from the U.S. Government.

7. What are the prospects for the next 3-5 years? The GOG has no long-term budget plan, nor have The Estimates for 1985 yet been prepared. Based on discussions with Mr. Victor Calendar and Mr. Angus

TABLE 1

BUDGETARY POSITION
(in millions)

	1984	1983	1982
Current Revenues	81	81.0	74.2
Recurrent Expenditures	89[a]	64.0[a]	67.5
Current Surplus (Deficit)	(8)	17.0	6.7
Capital Expenditures	131	116.1	101.1
Overall Deficit:	(139)	(99)	(94.3)

Financing:

USA general assistance	32
USA project assistance	52
Other	55

[a]Including debt repayment and military spending.

SOURCE: Data for 1984, 1983 provided by Mr. Angus Smith, Ministry of Finance. Data for 1982 taken from IMF consultation report.

Smith, however, Calendar chairs a working group on taxation which has just reported to the GOG. While the report could not be made available to us, he indicated that it recommended cuts in individual and business income taxes, and in the export duty. The short-term revenue losses which would result from these actions would be made up by a combination of economic growth and administration reforms which would occur between now and FY 1986. He indicated that these factors would generate an increase of $3-$5 million in revenues. Apparently, they have made some multi-year revenue projections because he was willing to state the percentage increases in real GNP which were assumed:

1984 2.5 percent

1985 4.0 percent

1986 5.0 percent

8. It is difficult to make even a preliminary assessment of the Calendar analysis without looking at the detailed report. One might, however, begin to investigate the three following questions. First, what are the recurrent expenditure increases planned for this three year period? If it is to increase faster than GNP during this period, quite substantial current account deficits could be in the offing. The difficulties of reducing public employment in a surplus labor economy suggest such an outcome. Second, exactly what are the tax administration improvements planned by the GOG, when are they expected to come on line, and how will they yield increased revenue? Remember, there is a substantial lag between the arrival of the technical

assistance, the training of local officers, and the flow of increased revenues. Moreover, all administrative improvements do not yield more revenues by themselves--some simply improve the efficiency with which an office operates and set the stage for longer term reform. Third, without structural tax reform, the projected GNP growth may not generate tax revenue growth at levels anticipated because the buoyancy of the Grenada tax system has been very low.[1]

9. One prognosis is for a substantial current account deficit over the next three years. This condition could be further exacerbated by deficits of the public enterprises if they are not divested. The last Fund Consultation Report (page 17) estimated a transfer of $14.5 million to the 11 non-financial public enterprises in 1982. This was equivalent to 9 percent of the total central government expenditures in that year. Even more important are the increased recurrent costs associated with operation and maintenance of capital facilities. The IMF suggests that these may reach 7 percent of GDP by 1987. Based on all of this, I would guess that, even with significant fiscal reform, a current account deficit from government operations is certain to occur over the next three years. To hold the magnitude of these deficits in check, USAID needs to assist GOG in the following areas.

-- divestiture of selected public enterprises

-- short-run technical assistance in tax administration and training

-- committing the GOG to comprehensive tax reform and advising on compatible short-run tax reforms

-- assisting the GOG in developing a fiscal planning capability.

This kind of assistance is probably not going to lead to current surpluses in 1985 and 1986, but it can begin to move the GOG budgetary position toward long-run balance and it can reduce the near term deficits below what they otherwise might have been.

Progress on Tax Reform

10. There is considerable current interest and activity in the area of tax reform. Victor Calendar (on secondment from IMF) heads a GOG working committee, and the IMF had a fiscal mission in Grenada in April. In addition, there has been some effort directed toward the comparative tax treatment of investment (the Charles Irish report). Neither the GOG nor IMF reports are presently available for study: the IMF report because it is not finished; the GOG report because it is an internal government document and could not be released.

11. Mr. Calendar reported that the GOG working group had taken as its primary objective "enhancing the responsiveness of the present tax structure to economic growth." They also are concerned about reducing the regressivity of the current system and improving its administration. It is important to emphasize that such a primary objective focuses on revenue raising and not on the provision of incentives for increased private investment and production. Surprisingly, the few hints he was willing to give about the tax

structure recommendations in the report suggest policy reforms that would reduce tax burdens and revenue responsiveness: e.g.,

-- reduce personal income tax rates and widen the brackets

-- reduce corporate tax rates

-- reduce the export duty and import tax shares of GNP.

It was not clear from the discussion where the increased revenues and increased GNP responsiveness (buoyancy) would come from. Administrative improvements were mentioned, but no specifics were given other than reference to an IMF offer of technical assistance in the income tax area. This report will require careful study by USAID, both in terms of its long- and short-run implications.

12. The IMF fiscal mission visited Grenada from April 9 to April 26, 1984, and is scheduled to complete its report by the end of July. The team was led by Ved Ghandi, a very capable and experienced tax policy analyst, and took as its objective a review of the fiscal system (taxes and expenditures) "...with a view of making it an instrument of economic growth (providing incentives for private initiative and enterprise) while enhancing the elasticity of the tax system and reducing its regressivity." The IMF objectives, then, are more directed toward the effects of taxation on the economy than are the objectives of the COG study which, according to Calendar, are relatively more concerned with how to capture more of the benefits of economic growth for government purposes.

13. Since the final IMF report is not available, we cannot know what reforms it will propose. The team did submit, however, its

"Preliminary Findings and Recommendations," which lays out the direction of their thinking. On the question of tax reform changes, they indicate the following directions for change:

-- lowering income tax rates

-- broadening the income tax bases through improved administration and taxing interest income

-- converting personal allowances from income tax deductions to income tax credits

-- removing discretionary exemptions from import taxes

-- increasing the taxation on services and utilities

-- converting duties on cigarettes and beer from a specific to an ad valorem basis

-- improving property tax administration.

In the "medium term," they suggest the imposition of a broad-based consumption duty, levied equally on imported goods and domestic output.

14. The IMF team also had a mandate to examine expenditure planning and control. Their preliminary conclusions and recommendations include:

-- regroup the present 18 ministries to only 7 or 8;

-- levy user charges on secondary education and health services;

-- slow down the rate of capital project implementation to reduce the recurrent cost burden;

-- reinstate proper budgetary measures.

In general, the Fund urged speed in "an honest appraisal of current expenditures" instead of waiting until tax reforms have been implemented which, they noted, could (and probably would) take a few years.

15. USAID should do a careful review of the IMF study when it is completed. While that study will surely be competently done--and there is certain to be much in it with which I will agree--it is not clear that its policy advice will be exactly the same as that which the mission would want to offer. The differences will have to be clearly flagged. It would be good to remember that, in this report, the Fund will be laying a plan for short-run deficit elimination, to which they may eventually try to hold the GOG. The mission needs to be very sure before it buys into this plan.

Problems and Issues Concerning the Present Structure

16. The present tax system in Grenada violates most of the maxims of good tax practice. First, it is complicated and therefore not easily understood by taxpayers. Second, it is unfair in that it discriminates among sectors of activity (e.g., heavier taxation of imported goods vs. domestically produced goods, of exports vs. domestic consumption, and of agriculture vs. services), among PAYE earners vs. the self-employed, and it may be regressive. Third, it is not automatically and proportionately responsive to income growth. The faster growing components of the tax base--government and

services--are not reached because of poor administration or because of exemption through code or concession. Finally, the tax system may provide important disincentives to income earning and employment generation with its high rates of income and export taxation. These problems have emerged because the tax system has grown up in an uncoordinated, piecemeal fashion, with almost annual adjustments in the tax rate to raise more revenues, and in tax concessions to provide relief. There is no history of a concern for reforming the "tax system."

17. The result of this history is a very complicated tax structure. While the high rates imposed have attracted much attention, the inequities among various classes of taxpayers may have produced even greater problems and disincentives to economic activity. The last thing one wants to do now is to continue in the direction of piecemeal revenue adjustments which are not tied to a long-term tax reform plan.

18. The distribution of recurrent revenues by type is described in Table 2.

Personal Income Tax

19. The personal income tax is levied on all sources of income except that earned from interest on savings deposits. There are no separate capital gains taxes. A fairly common set of personal allowances are permitted, including personal and dependent exemptions, alimony and housekeeping deductions, as well as an allowance for education expenditures abroad. To give an idea of the nature of the allowances: a family of five would face no income tax on the first

TABLE 2

COMPOSITION OF REVENUES IN 1984 BUDGET
(in millions of EC$)

	Amount	Percent of Total
Customs and Excise	26.2	32.2
Import Duty[a]	11.0	13.5
Export Duty[a]	3.7	4.6
Consumption Duty[a]	7.0	8.6
International Airport Levy[a]	4.1	5.0
Other	0.4	---
Taxes	43.7	53.8
Company Income Tax	7.5	9.2
Individual Income Tax	11.0	13.5
Withholding Tax	1.0	1.2
Stamp Duty[a]	15.5	19.1
Motor Vehicle Tax	1.5	1.8
Hotel Occupancy Tax	0.5	0.1
Foreign Exchange Tax[a]	5.0	6.1
Other	1.7	2.1
Licenses	1.5	1.8
Airport Dues	0.6	0.7
Earnings of Government Departments	4.7	5.8
Post Office	2.9	3.6
Rent and Interest	1.0	1.2
Other	0.7	0.8
Total	81.3	100.0

[a]Taxes which are levied principally on foreign trade.

SOURCE: 1984 Budget.

$3750 earned. Two important tax expenditures under the personal income tax are a deduction of up to $7,400 for mortgage interest and up to $1,400 for life insurance premiums paid. By law, then, the base of the tax is quite comprehensive.

20. The rate structure is progressive, reaching to 65 percent for annual incomes above $30,000. At approximately the average per capita income in Grenada, a family of five would have an income of $4050 and would pay $710 in personal income tax; $347 if it qualified for the full mortgage interest deduction. The amounts are equivalent to 17.5 and 8.6 percent of income, respectively. The broad base and graduated rates provided for by the law would appear to suggest an equitable distribution of tax burdens. This probably does not turn out to be the case, as described below.

21. By law, the tax is self-assessed; in practice it is not. Of potentially 15,000 taxpayers (IRD estimate), only about 2500 file a return. Of these 2500 returns, most are incomplete and have to be redone by IRD staff, based on data supplied on the form. The remaining assessments (about 5000) are made in the office (there are no self-declarations) and notices of taxes due are mailed out.[2] The latter are assessed on a basis of PAYE submissions, information received from growers cooperatives, what is known about past level of business sales, etc. Given that only ten (10) officers are available to carry out this assessment, and that there is bound to be a paucity of information about the self-employed, it is not likely that the coverage of the tax is very broad. Particularly the

self-employed--those in the service sector and those in agriculture--are likely to be undertaxed because they are so difficult to assess. So, while the statutory marginal and average rates look very high, the actual effective rates may be quite a lot lower in many sectors of the economy. Overall, personal income taxes accounted for only 3.9 percent of GDP in 1982.

22. There is much room for improvement in the administration of the personal income tax. The aim of these improvements would be to even out the tax burden, as between PAYE and the 'hard-to-tax' sectors, and to increase compliance generally. Both actions could broaden the tax base and enable either a revenue increase or a substantial rate reduction. Improved administration could also lead to a cleaning up of arrears and a one-time revenue increase. Among the income tax administration problems: (a) there is neither an office nor a field audit of returns; (b) there is not a modified assessment plan--a manual which enables a rough estimate of the income of the hard-to-tax sectors--nor are there field assessments/examinations of books of account of small firms; (c) there are almost no statistics to enable a monitoring of income tax performance; (d) the tax form is too complicated, therefore compliance is made difficult; and (e) sanctions against non-filers and those who under report are minimal (the penalty rate is 1.5 percent per month on the unpaid balance) and not enforced.

23. Two administrative actions would seem called for to broaden the base of the income tax and to increase compliance.

-- Tax administration assistance, presumably in the areas of income tax collections and assessments, has been offered by the IMF. (This was reported to us by Mr. Calendar and Mr. Wilson.) This will help measurably, and could yield some short-run revenue gains if accompanied by a vigorous enforcement program.

-- The GOG needs to seek assistance in training its staff in basic accounting and auditing, and needs to expand and fill the number of positions in the department. The present staff of 10 for assessment and audit of individual and company income tax (only three qualified to do field audits) is too small.

24. Are the individual income tax rates too high? On the one hand, the top marginal rates (up to 65 percent) clearly could discourage initiative, and the high nominal rates could provide a disincentive to work effort and lay a substantial burden for those who cannot evade (PAYE). However, the high rates discourage compliance and will stiffen resistance to a more vigorously and efficiently enforced income tax. There is a good case for lowering the tax rate.

25. On the other hand, there may be substantial evasion by higher income taxpayers which lowers the effective rate (i.e., the high nominal rates apply only if income is properly assessed). As is shown in Table 3, only 1.36 percent of all taxpayers report incomes in the 65 percent marginal rate bracket and only 6.39 percent fall in the brackets above 50 percent. When only 'chargeable' (taxable) income is considered, the comparable percents are 1.00 and 5.59, respectively. Interestingly, however, the 65 percent rate bracket accounts for nearly 15 percent of income tax revenues, and the 50-percent-and-over bracket accounts for 37 percent.

TABLE 3

DISTRIBUTION OF TAXPAYERS BY INCOME CLASS: 1983[a]

Income Category EC Dollars	Proportion of Taxpayers Based on Assessable Income (in percent)	Proportion of Taxpayers Based on Chargeable Income (in percent)	Proportion of Total Income Tax Revenue (in percent)
$ 0 - $ 1,000	1.86	10.78	---
1,001 - 3,000	10.18	23.61	6.68
3,001 - 5,000	22.56	24.74	7.81
5,001 - 7,500	28.05	16.52	14.67
7,501 - 10,000	14.41	8.95	13.04
10,001 - 12,500	8.42	4.82	11.69
12,501 - 15,000	5.25	3.00	8.78
15,001 - 20,000	4.78	2.79	11.80
20,001 - 25,000	2.17	1.24	6.75
25,001 - 29,999	0.96	0.56	4.46
30,000 and over	1.36	1.00	14.32

[a]These data are based on a sample of 7,296 taxpayers who paid total taxes of EC$7.07 million.

SOURCE: Provided by Ministry of Finance.

Company Tax

26. The company tax is levied at a flat rate of 55 percent of net income. A number of firms are exempt from the tax by virtue of incentives granted, but it was not possible to get an estimate of the revenue loss due to incentives granted. One must conclude that the rate of company tax is high enough to discourage private investment.

27. Apart from the level of the rate, there are other structural problems with the company tax that may have an unfavorable impact on the investment climate. Depreciation is allowed on an original vs. a replacement cost basis; hence, inflation imposes a kind of 'tax' on top of the government's tax. Similarly, inventories are valued on a cost basis, FIFO, which means that companies will understate their actual raw material costs (i.e., inflation will impose another hidden tax). Finally, dividends are taxed both as part of company income and as personal income received.

28. The Grenada company tax should be easy to administer. Only about 150 firms are liable for payment. On the other hand, the books of account are not adequately kept, especially by smaller firms, and only three staff are qualified to do audit work for individual and company income tax. Reform of the company tax is called for in a number of areas:

-- the nominal rates are too high and likely to discourage private initiative--they should be reduced;

-- inventory and depreciation allowances need to be adjusted for price level increases;

-- double taxation of dividends needs to be eliminated through some form of integration with the individual income tax;

-- the incentive package needs to be reviewed with an eye toward a more uniform treatment of firms;

-- the assessment and audit capability of the Inland Revenue Department needs to be improved through technical assistance and training.

Depending on how far rates are reduced, these reforms will almost certainly lead to revenue losses in the short-run.

Import and Consumption Duties

29. Taxes on foreign trade account for nearly two-thirds of total revenues, and include a complicated collection of rates and bases which are difficult to administer and whose impact is not easily assessed. The system has been built up over time to raise revenues, apparently with little concern for other objectives. (This history of discretionary changes is described in Appendix B.) Some feel for the degree of complication can be had from the rough summary in Table 4. To complicate matters even further, each of these taxes has a separate set of exemptions, either by code or by concession.

30. This structure of indirect taxes has led to a number of important problems: (a) the total effective tax rate on import value is high, around 27 percent on average and 52 percent for consumer goods according to an IMF estimate; (b) an inefficient and costly administration; (c) an unequal treatment of imported and domestically produced goods; and (d) many inequities which have grown out of concessional exemptions from duty.

TABLE 4

IMPORT AND CONSUMPTION DUTIES

Levy	Base	Rate
Import Duty	C.I.F. Value of Imports	Many, as provided in the external tariff, ranging from 0 to 35 percent
Stamp Duty	C.I.F. plus Import Duty	15 percent
International Airport Tax	C.I.F.	5 percent
Package Tax	Volume of Packages Landed	50 cents/5 cubic feet
Consumption Duty	C.I.F. plus Duty	8 ad valorem rate classes, plus some specific rates
Excise Tax	Domestic Beer Production	15 cents per gallon
Petroleum Increased Profit Margin Tax		
Foreign Exchange Tax	Foreign Exchange Purchases	5 percent

31. The reform program called for includes, as a first step, the amalgamation of these various duties and taxes (other than the common external tariff) into a general consumption tax. This would make the tax more easily administrable, would not discriminate against imported vs. domestically produced goods, and would set the stage for indirect taxation of growing domestic manufacturing and tourist-related activity. The duty would be collected at the import and manufacturing levels, and should have as few rates as possible.

32. The base for indirect taxation can be broadened in two ways. The first is by elimination of concessional exemptions. The exempt status of raw material and capital goods imported for re-export should be retained, but the case for exempt status for other imports and of parastatals should be re-examined. I was not able to get an estimate of the value of duty-exempt goods, but one gets the idea that it is substantial. The duty base can also be broadened by administrative reforms. While the clearance of goods from the dock is quite rapid, even given the complex tax system, virtually no valuation of imports is done. The stated value on the invoice is generally accepted. The Controller of Customs reports, however, that he suspects under-invoicing to be a growing problem--underinvoicing by Indian and Syrian merchants and of goods received from the free trade zone in Miami and Panama were cited as major culprits. Only one man in the C&E department is trained in valuation techniques. The GOG needs to augment this staff and USAID might consider providing technical

assistance in this area. A prospectus on training needs for the department is outlined in Appendix C.

33. Can the effective tax rate be lowered? Under present circumstances, only if a revenue loss is acceptable. With a general sales tax, better valuation and a tightening of exemptions, the rates could be lowered, but I was unable to get hold of data to suggest the magnitude of the changes that might be possible. Such data do exist, however.

Property Tax

34. The base of the property tax was changed from annual rental value (British system) to the capital value of land plus improvements (American system) in 1981. The tax rates, levied on assessed full market value, are as follows:

Agricultural Property	0.1 percent
Commercial/Industrial Property	0.8 percent
Government/Religious Property	0
Residential Property:	
under $15,000	0
$ 15,000 - $ 40,000	0.1 percent
$ 40,000 - 100,000	0.25 percent
$100,000 - 200,000	0.4 percent
over $200,000	0.5 percent

A new valuation roll was begun in 1981, but only about 70 percent of the Island was completed. For those 70 percent, the IR department reports that maps, sketches of improvements and ownership information exists, but I did not see the records. Presently, the tax is presumably collected on capital value where it has been assessed, and on rental value for the remainder. Collection efficiency is reported

to be 'not healthy' (though records were not available), the level of compliance is low and the yield is anemic.

35. The property tax is one area where there is scope for substantial revenue increase. It is about the only form of wealth taxation in the system, it can be a reasonably progressive levy, and its administration can be manageable if the structure of the tax is kept simple. USAID should move immediately to provide technical assistance in this area. The technical assistance might take the following form: (a) advice on property tax structure; (b) valuation assistance in completing the tax roll; (c) training for maintenance of this valuation roll; and (d) technical assistance in the area of record-keeping. Whether assistance is needed in the area of deeds and title registration will have to be determined by a reconnaissance.

36. One might also consider the possibilities of special assessments in Grenada. With over $200 million in capital improvements coming on line in the future, and with a possible growth in tourism, land values will grow quite dramatically. Even an efficient property tax--with reassessment every fifth year--will not recapture an adequate portion of this land value increment for government. A special assessment, some form of betterment levy, or a special provision for property tax reassessment can be a good answer.

Reforming the Tax System

37. To this point, the discussion has focused on changes in individual components of the tax system, as though they could be viewed in isolation from one another. A better approach is to consider reform of the entire fiscal system (e.g., how income elastic or equitable is each tax is surely a less important issue than the elasticity and equity of the total tax system). Indeed, it is the piecemeal approach to revenue raising that has gotten Grenada's tax system to the set of problems it now faces. In this section, I attempt to lay out, in a very preliminary fashion, a tax reform program which would conform with a private sector-led development strategy.

38. One must begin with a ranking of objectives: what are the most important goals with the new tax code? There are important tradeoffs to be made between revenue raising, elasticity, equity, interference with private sector initiatives, and administrative ease. My view of the best approach for Grenada, and the relationship among the objectives, is summarized below:

-- The tax system should be as simple and uncomplicated as possible, to facilitate administration and to minimize the effects of the tax system on private sector choices. Broad based, flat rates, and few exemptions are the rules to follow.

-- The yield and elasticity of the revenue system depend on the tax rates chosen, and ultimately on the rate of growth in public expenditures which is desired. To low an elasticity does not provide the revenue growth necessary to cover costs and leads to piecemeal revenue raising adjustments, as has been the case in the past. Too high an elasticity leads to automatic tax burden increases and may encourage more rapid recurrent expenditure increases.

-- The tax bases and rates should be as neutral as possible with respect to business decisions. Violations of the neutrality maxim are allowable to correct some market distortions which exists (e.g., not taxing intermediate inputs in order to preserve the competitive position of exports).

-- The use of taxation to protect domestic industry should be avoided, in part because it encourages inefficiency on the part of domestic industry. Rather than give specific domestic firms a tax incentive, it is better to keep the tax base broad and offer a lower average tax rate to all domestic firms. This conclusion, however, needs to be reviewed in light of the tax structure of competing islands.

-- Equity measures should be carefully evaluated against their costs. Administrative ease probably calls for the tax exemption of low income workers, low valued houses, and some necessities. Such exemptions serve an important equity objective, i.e., lowering the tax burden on the very poor. On the other hand, an attempt to fine-tune the progressivity of the tax system with graduated rates is likely to impede administrative ease, encourage evasion by the higher income and possibly not achieve the desired objective. The view here is that equity could best be served by exempting the very poor, staying with broad-based flat rate taxes, and following distributional objectives primarily on the expenditure side.

39. There are constraints to be faced in formulating comprehensive tax reform in Grenada. First, revenue needs will be substantial in the next few years--probably so substantial that tax reduction will not be possible. Many past commitments are irrevocable. Second, the unemployment rate is high and the tax system should not be changed so as to discriminate against labor. Third, even a growing Grenada economy is likely to be led by the 'hard-to-tax' sectors: Tourism, trade and agriculture. In this context, the following reform package might be considered.

40. First, move the individual income tax in the direction of a flat rate levy. On the administrative side, broaden the base of the tax by technical assistance to improve the system of provisional (modified) assessment, develop the use of third party information, and tighten enforcement. The GOG needs to commit to a more vigorous enforcement and to expand the Inland Revenue staff in the areas of assessments and collections. The IMF has offered assistance in the income tax administration area and perhaps IMF or USAID would initiate a training program. How far the rates could be cut and how much the base could be expanded (and how fast) require analysis of data to which I could not get access. In all probability, however, the move toward a flat rate tax at any reasonable rate level would lead to a revenue loss. Given the time and cooperation, the data could be assembled and the estimates could be made. One would expect that the IMF had access to such data, and that they will make an estimate.

41. Second, reduce the corporate tax rate, build in an inflation adjustment for depreciation and inventories, and eliminate the double taxation of dividends. The revenue loss implied by these actions could be substantial in the short-run, depending on the size of the rate reduction.

42. Third, amalgamate the indirect tax system into a common external tariff and a general consumption duty. The consumption duty rates should be few in number, and should treat domestically produced and imported goods the same. The base of import duties could be expanded by improved valuation and by expanded staff in the C&E department.

Technical assistance in the customs valuation area might be provided by USAID. Given revenue constraints, it probably will not be possible to reduce the effective rates in the near future.

43. The three major reforms mentioned above will lay the groundwork for a stronger tax system in Grenada, but they imply short-run revenue losses. Some of the losses will be made up by a tighter administration and economic growth, but a short-run revenue cost is certain. Four actions could offset some of these losses. The first is divestment of selected public enterprises. This will both offload some budgetary costs and expand the private sector tax base--to the extent these firms can operate profitably in the private sector.

44. Second, there are too many incentives and exemptions in the present system, and these lead ultimately to higher tax rates on other companies and goods, and on individuals. Where possible, the exemptions should be eliminated--traded in for lower average rates for everyone--and a lid should be placed on the granting of new incentives and exemptions. Incentives for export promotion are a notable exception, but even here the GOG should be zealous about granting tax advantages.

45. Third, the service sector is undertaxed and, as (if) tourism grows, will be a major revenue producer. Taxes on restaurant meals, consumer telephone and power bills would be good places to start. Ultimately, the ability to capture substantial revenues from the service sector depends on the improved ability of the income tax administration to deal with this hard-to-tax area.

46. Finally, the time is right to strengthen the national property tax, and to increase its revenue yield. USAID could provide technical assistance to complete the roll and advise on the tax structure. We do not have the data to estimate total yield at various rates but, given time, such estimates could be made. This property tax should also allow for special assessments, or more frequent reassessments in areas where land value increments are substantial. The huge public investment program being undertaken by the GOG, and the prospects for increased tourism, will surely generate marked increases in land values. The property tax can be used to capture some of these increases for the public sector.

47. Finally, there is the issue of export taxes. They surely cause a disincentive to production by farmers, but they yield $3.7 million. Moreover, many farmers successfully avoid the individual income tax, and the export tax is one way to capture their taxable surplus. Our view is that the export tax should be abolished, as the GOG moves to tighten the assessment capability of IRD staff and as a property tax is put in place.

An Action Plan for USAID

48. There are many levels at which USAID could work to help the GOG generate a comprehensive tax reform. One approach which may fit mutual needs is outlined here, and the kinds of commitments USAID and GOG would make are suggested.

49. The role of the IMF cannot be ignored and, at least in the early stages, a joint USAID/IMF/GOG working committee on tax reform should be set up. The committee should work toward advising the GOG on the proper long-term tax reform package. As a first step in this process, USAID needs to undertake a careful and thorough review of the IMF report when it is submitted in August.

50. USAID and GOG might commit to the following fiscal reform actions:

a. Put in place a simple projection model to monitor the long-run budgetary implications of various public actions (e.g., tax incentives, the operation of new capital facilities, divestment, etc.) The model would be updated annually and used by both GOG and the Donors. USAID would develop the model, and GOG would employ an expert to keep it current.

b. GOG would commit to a program of long-term, comprehensive tax reform and would begin a dialogue with USAID and IMF on the components of this package.

c. GOG would commit to a significant strengthening of the property tax, including a staffing commitment, at the earliest possible date. USAID would provide TA for advice on the structure and completion of the valuation roll, and setting up the administration.

d. GOG would commit to adding staff to Inland Revenue, and to tightening income tax enforcement. IMF would provide TA in administration, and USAID would provide training assistance.

e. GOG would commit to adding staff in Customs, and to moving toward a general consumption duty. USAID would provide customs valuation assistance and training.

51. The next steps for USAID are to undertake a review of the IMF report, to formulate its own tax policy position, and to send reconnaissance

missions to Grenada to prepare terms of reference in the areas of property tax reform and training, customs valuation and training, and income tax training. USAID needs to appoint a fiscal advisor to work with the mission and with GOG as the tax reform proceeds.

52. The work might be coordinated in one of two ways. It could be done directly by USAID/Grenada, who would contract directly for the various components of the work. Alternatively, it could be coordinated by a contractor, who would subcontract as needed. If the latter route is chosen, my group might be a good choice since we are providing quite similar services (including training) in Jamaica.

NOTES

1. "Buoyancy" refers to the responsiveness of tax revenues to GNP growth. The "income elasticity" is the percent increase in revenues which results from every one percent in income.

2. A copy of the forms and notice of assessment is included in Appendix A.

APPENDIX A

Income Tax Forms

CONFIDENTIAL

198

Form No. 1A

GRENADA

Inland Revenue Department

INDIVIDUAL INCOME TAX RETURN

For the Year of Assessment 198

(Form Prescribed Under Section 70 Income Tax Law 1980)

PLEASE READ INSTRUCTIONS CAREFULLY BEFORE COMPLETING THIS FORM

It is a serious offence to make a false return

1	Name	7	Your File No
2	Address for Service of notices	8	Your Spouse's File No Employment or Business Address
3	Name, Address on last return (if different from above)	9	Occupation, Business, Profession
4	Tick appropriate box: Male ☐ Female ☐ Resident ☐ Non-Resident ☐	10	Check Status: Single ☐ Married ☐ Separated ☐ Widowed ☐ Divorced ☐ Date of Marriage / Whether Registered: Yes ☐ No ☐ / Are you Living Together: Yes ☐ No ☐ / Whether Wholly maintained by Taxpayer: Yes ☐ No ☐
5	Is this your first Income Tax Return? yes ☐ No ☐		
6	Telephone No. Office ..... Home	11	Spouse's Full Name (or female, name prior to marriage)

	TAX COMPUTATION TO BE COMPLETED BY TAXPAYER				Official Use Only
12	Wages, Salary or Pension from Gov't Office or Employment		$	12	
13	Wages, Salary or Pension from other Office or Employment			13	
14	Total other Income, Loss - enter loss in brackets ( )			14	
15	Total Net Income Sum of Lines 12, 13 and 14			15	
16	"Assessed Loss" Relief			16	
17				17	
18	TOTAL ASSESSABLE INCOME Line 15 minus Line 16 and or 17		$	18	
CONCESSIONAL DEDUCTIONS	19 Personal Allowance $1,500	$		19	
	20 Spouse Allowance 600			20	
	21 Maintenance Alimony Amount paid			21	
	22 Child Allowance			22	
	23 Education expenses 700 each			23	
	24 Housekeeper 120			24	
	25 Dependent Relative 120			25	
	26 Life Insurance			26	
	27 Approved Pension Fund			27	
	28 Mortgage Interest – Owner Occupied property			28	
	29 Payments under Deeds or Covenant			29	
	30			30	
	31 Total Concessional Deductions Lines 19-30			31	
32	Chargeable Income Line 18 minus Line 31			32	
33	Tax on Chargeable Income See Tax Rates Page 4			33	
34	PAYE per P24 attached			34	
35	Tax Instalments Paid			35	
36	Double Income Tax Relief			36	
37	Withholding Tax [illegible]			37	
38	Total of Tax Payments and Reliefs		$	38	
39	TAX PAYABLE		$	39	
40				40	
41	NET TAX PAYABLE (Refundable)		$	41	

GENERAL DECLARATION - I ..... declare that in all statements contained herein and in any statement of accounts sent herewith I have given a true Return and particulars of the whole income from every source whatsoever required to be returned under the provisions of the Income Tax Law No. 20/1980.

....

Signature of Person preparing Return, if other than Taxpayer *Date* *Signature of Taxpayer, Agent, Trustee etc.*

Please submit the completed return on or before the 31st day of March 198 to the Comptroller, Inland Revenue Depart-

Form No. 1B

CONFIDENTIAL

100

GRENADA

Inland Revenue Department St. George's

ANNUAL RETURN OF INCOME FOR COMPANIES, PARTNERSHIPS, JOINT VENTURES, TRUSTS, ESTATES OF DECEASED

(Form prescribed under Section 70, Income Tax Law 1980)

YEAR OF ASSESSMENT 198

PLEASE READ INSTRUCTIONS CAREFULLY BEFORE COMPLETING THIS FORM

It is a serious offence to make a false return

	Name of Company, Partnership etc.	5	Telephone Number / File Number
1	Mailing Address	6	Address of Registered Office
2	Nature of Business or Principal Activity	7	Date and Place of Registration or Incorporation
3	Accounting Period — From		To
4	State if (Tick as appropriate) Resident ☐ Non-Resident ☐ Company ☐ Branch of Non-Resident Company ☐	8	Partnership ☐ Joint Venture ☐ Trust ☐ Estate of Deceased Person ☐

GENERAL DECLARATION

I.....declare that this is a true and correct Return of the whole of the income or profits of

.....

(Name of Company, Partnership, Joint Venture, etc.)

from every source whatsoever chargeable under the Income Tax Law 1980, and that the Schedules and Statements included in the Return are true and correct, and I further declare that I am authorised to sign this Return.

Given under my hand this.....day of..... 19

..... *Signature* ..... *Office*

SCHEDULE A

STATEMENT OF TAX DUE AND PAID

				Official Use Only
9	Chargeable Income	$		
10	Assessed Loss Relief			
11	Chargeable Income (Adjusted)			
12	Tax Payable		$	
13	Total Advance Tax Payment			
14	Reliefs : (a) Dividend Credit			
15	(b) Credit for Foreign Tax Paid			
16	(c) Any other Reliefs (Attach Schedule)			
17	Total Payments and Reliefs (Line 13 to 16)			
18	Balance of Tax Payable			
19	Tax Refund Due		$	

NOTES (1) This Return is required to be submitted to the Comptroller of Inland Revenue, St. George's, Grenada, not later March 31, 198 . The Return is required to be signed by the Principal Officer of a company, or by the precedent partner or a duly authorised agent and to contain a calculation of the chargeable income and an address for service of notices.

(2) A copy of Audited Accounts must be submitted with the certificates required under Section 77.

SCHEDULE 1

CHILD ALLOWANCE (*See* Instruction No. 22)

CLAIM LIMITED TO $650 PER CHILD FOR FIRST TWO CHILDREN AND $350 FOR ANY OTHER CHILD, INCLUDING AN INVALID CHILD OVER THE AGE OF 16.

Full Name of Child	Date of Birth			Educational Institution Attended or Nature of Invalidity	Income of Child	Amount Claimed
	D	M	Y			
					$	$
TOTAL CARRIED TO LINE 22, PAGE 1						

SCHEDULE 2

DEDUCTION FOR CHILD EDUCATION EXPENSES OVERSEAS

(Claim limited to $700 for each Child) *See* Instruction No. 23

Full Name of Child	Date of Birth			Name and Address of Educational Institution	Income of Child	Amount Claimed
	D	M	Y			
					$	$
TOTAL CARRIED TO LINE 23, PAGE 1						

SCHEDULE 3

ALIMONY AND MAINTENANCE : (*See* Instruction No. 21)

Limited to lower of actual amount paid or $1000.

Name and full address of Spouse Divorced or Separated	Deed of Separation Court Order or Decree			Amount actually Paid	Amount claimed Enter below and on Line 21 Page 1
	Date	Registered Number	Country of Origin		
				$	$

SCHEDULE 4

HOUSEKEEPER ALLOWANCE : *See* Instruction No. 24

(Claim limited to one (1) person and $120.) Allowable only to Widow or Widower.

Full Name of Housekeeper	Whether residing with Claimant?	Whether Married, Single, Widowed, Separated or Divorced	Age	Amount Claimed Carry to Line 24 Page 1
				$

SCHEDULE 5

DEPENDENT RELATIVE ALLOWANCE : (*See* Instruction No. 25)

Claim not to exceed $120 per relative up to two relatives.

Name of Dependent Relative	Relationship to Claimant	Nature of Incapacity	Income of Relative	Contribution by Other Persons	Your Contribution	AGE	Amount Claimed
			$	$	$		$
TOTAL CARRIED TO LINE 25, PAGE 1							

SCHEDULE 6

LIFE INSURANCE RELIEF (*See* Instruction No. 26)

Claim limited to lesser of 1/6 of assessable income or $14[illegible], and in the case of a policy providing for lump sum benefits, 7% of the Capital Sum.

Insurance Company	Life Assured	Date Contracted	Maturity Date	Capital Sum Assured	Premium Paid	Premium Claimed
				$	$	$
TOTAL CARRIED TO LINE 26, PAGE 1						

SCHEDULE 7

APPROVED PENSION FUND CONTRIBUTION :

Claim not to exceed 10% of assessable income.

Approved Fund to which Contribution is made		Amount of your Contribution	Amount Claimed
		$	$

SCHEDULE D

PARTICULARS OF GAINS OR PROFIT

	Sources of Gains or Profits	Gains or Profits (show Losses in Brackets)
	BUSINESS :—	$
1	(a) Agriculture, Farming, Working of Estates	
2	(b) Profession or Vocation	
3	(c) Trade or Business	
	RENTALS AND ROYALTIES :—	
4	(a) Rentals	
5	(b) Royalties	
	INTEREST AND DISCOUNTS :—	
6	(a) Interest	
7	(b) Discounts	
	PREMIUMS, COMMISSIONS, FEES, LICENCE CHARGES :—	
8	(a) Premiums	
9	(b) Commission	
10	(c) Fees	
11	(d) Licence Charges	
	ANNUITIES :	
12	(a) Alimony and Maintenance	
13	(b) Deeds of Covenants	
14	(c) Other Annuities	
15		
	DIVIDENDS :—	
16	(a) From Resident Companies	
17	(b) From Non-Resident Companies	
	OTHER TAXABLE SOURCES (List Source)	
18		
	ENTER TOTAL ON PAGE 1 LINE 14	

TAX EXEMPT INCOME

_____ $

_____ $

_____ $

TOTAL $

ATTACH STATEMENT TO SUPPORT GAINS OR PROFITS OR LOSSES FROM EACH SOURCE. COPY OF AUDITED ACCOUNT MUST BE SUBMITTED WITH CERTIFICATES REQUIRED BY SECTION 77.

TAX RATES

Where the Chargeable Income Exceeds $7,336.

	$	c.	Income $	Tax $
For every dollar of the first	1,000	Nil	1,000	Nil
For every dollar of the next	2,000	15c.	3,000	400
For every dollar of the next	2,000	20c.	5,000	800
For every dollar of the next	2,500	25c.	7,500	1,425
For every dollar of the next	2,500	30c.	10,000	2,175
For every dollar of the next	2,500	35c.	12,500	3,050
For every dollar of the next	2,500	40c.	15,000	4,050
For every dollar of the next	5,000	50c.	20,000	6,550
For every dollar of the next	5,000	55c.	25,000	9,300
For every dollar of the next	5,000	60c.	30,000	12,300
On the excess over	30,000	65c.		

Where the Chargeable Income does not Exceed $7,336.

Exceeds $	Does not Exceed $	
0	1,000	NO TAX
1,000	2,000	5% of excess over $1,000
2,000	3,000	$50 + 10% of excess over 2,000
3,000	5,000	$150 + 15% " " 3,000
5,000	7,336	450 + 40% " " 5,000

Are you paying rent? .....

Name and address of Landlord .....

Form No. 1A

SCHEDULE 8

DEED OF COVENANT PAYMENTS :

Limited to 10% of assessable income.

Covenantee	Deed No.	Date of Deed	Period of Deed (years)	Amount of your Contribution	Amount Claimed
				$	$
TOTAL CARRIED TO LINE 29, PAGE 1					

MORTGAGE INTEREST OWNER-OCCUPIED PROPERTY :

SCHEDULE 9

Limited to lower of Actual Amount paid or $7,200.

Lender	Address	Interest Paid	Amount Claimed
		$	$
TOTAL CARRIED TO LINE 28, PAGE 1			

SCHEDULE A

CLAIM FOR CREDIT FOR ADVANCE TAX PAYMENTS :

To be supported by Receipted Advance Tax Instalment Remittance Forms

Instalment Due	Date Paid	Receipt No.		Amount Paid
November 30				$
February 28				
May 31				
Other Payments				
TOTAL CARRIED TO LINE 35, PAGE 1				

INCOME FROM DIVIDENDS AND CLAIMS FOR DIVIDEND CREDIT

SCHEDULE B

Company	Address	Dividends from Non-Resident Companies	Dividends from Resident Companies
		$	$
AMOUNT CLAIMED CARRIED TO LINE 37, PAGE 1			

SCHEDULE C

APPORTIONMENT OF NET INCOME OF PARTNERSHIP, ETC.

Net Income		$
Deduct :		
Salaries to Partners	$	
Interest on Capital of Partners, Joint Owners	$	$
Apportionable Income		$

Names of Partners, Joint Owners or Beneficiaries (1)	Share of Apportionable Income (2)	Salaries of Partners or Joint Owners (3)	Interest on Capital of Partners or Joint Owners (4)	Total Columns 2 to 4 (5)	Apportionment of Dividend Credit (6)	Share of Tax Exempt Income (7)
	$	$	$	$	$	$

Form. No. 1D

GRENADA

INLAND REVENUE DEPARTMENT

NOTICE OF ASSESSMENT

Year of Assessment 198

Income Year 198

File No.

Asst. No.

Please note that you have been assessed according to the details shown hereunder:

SOURCE		$
Agriculture, Farming, etc.		
Profession or Vocation		
Trade or Business		
Rents		
Interest and Dividend		
Salaries etc. - Government		
Salaries etc. - Other		
	TOTAL	$
ALLOWANCES		
Capital	$	
Interest		
Losses		
Personal		
Spouse		
Children		
Education case		
Insurance		
		$
CHARGEABLE INCOME		
TAX ON CHARGEABLE INCOME		$
NET TAX PAYABLE (REFUNDABLE)		
TAX DUE IS PAYABLE BY 31st AUGUST 196		

WHEN TAX IS DUE AND PAYABLE

(a) by 31st August in the year of Assessment;

(b) within 30 days of the date of service of notice of assessment, whichever is the later. (Sec, 99)

INTEREST ON UNPAID TAX

" Any tax ..... not paid by the due date shall bear interest at the rate of one and one half percent per month or part thereof for the period during which it remains unpaid." Sec. 100 (1)

OBJECTIONS AND APPEALS

" Any person who is aggrieved by an assessment or a determination by the Comptroller made on him may, by notice in writing to the Comptroller within THIRTY DAYS after the date of service of the notice of assessment or determination... (Sec. 91)

PLEASE BRING OR SEND THIS NOTICE WHEN MAKING PAYMENT OR CLAIMING REFUND

FILE AND ASST. NO. .....

INCOME TAX ASSESSMENT 19.....

	FIRST ASST.		REVISED ASST.	
INCOME HEAD:—	$	$	$	$
A				
B				
C1				
C2				
D				
E1				
E2				
F				
G				
DEDUCTIONS:—				
A				
B				
C				
D				
E				
F				
G				
H				
I				
CHARGEABLE INCOME		$		$
TAX PAYABLE:—				
on $				
on $ @ %				
		$		$

NET TAX PAYABLE	$	$
ASST. ENTERED	.....	.....
CARD NOTED	.....	.....
N/A ISSUED	.....	.....

SCHEDULE F

COMPUTATION OF BALANCING ALLOWANCES AND CHARGES

Description of Asset	Cost (2) $	Date of Purchase or (Disposal) (3) $	W.D.V. at Date of Disposal (4) $	Total Allowances Granted (5) $	Proceeds of Sale or Trade-in Value (6) $	Balancing Charge —Profit (7) $	Balancing Allowance (Loss) (8) $

SCHEDULE G

CLAIM FOR CREDIT FOR ADVANCE TAX PAYMENTS

To be supported by Receipted Advance Tax Instalment Remittance Forms

Instalment Due	Date Paid	Receipt No.		Amount Paid
November 30				$
February 28				
May 31				
Other Payments				

SCHEDULE H

INCOME FROM DIVIDENDS AND CLAIMS FOR DIVIDEND CREDIT

Company	Address	Dividends from Non-Resident Companies $	Dividends from Resident Companies $

CLAIM FOR DIVIDEND CREDIT $

SCHEDULE

RECONCILIATION OF CHARGEABLE INCOME WITH PROFIT AND LOSS ACCOUNT

Profit/Loss per Profit and Loss Account $.....

Add / Deduct Expenses not allowable

(1) $

(2)

(3)

(4)

$

Deduct/Add Allowable expenses not charged and Exempt Income not included in accounts

(1) $

(2)

(3)

(4) $

Adjustable Profit / Loss $

THIS RECONCILIATION IS REQUIRED UNDER SECTION 77(1) FROM EVERY PERSON WHO CARRIES ON A BUSINESS.

SCHEDULE J

COST OF SALES

1. Stock at beginning of Year	$
2. Purchases of Goods for Sale or Manufacture	
3. Direct Salaries and Wages	
4. Other Direct Costs per Accounts	
5. Sum of Lines 1 to 4	
6. Stock at end of Year	
7. Cost of Sales or Operation (Line 5 less Line 6)	$

SCHEDULE K

TAX EXEMPT INCOME (List type of Income)

1.	$
2.	
3.	
4.	

SCHEDULE L

GROSS PAYMENTS AND WITHHOLDING TAX PAID

Item	Total Payment $	Payment to Residents $	Payment to Non-Residents $	Withholding Tax Deducted and paid to Comptroller $
1. Interest				
2. Discounts				
3. Rentals				
4. Lease Premiums				
5. Royalties				
6. Licences				
7. Fees				
8. Commissions				
9. Management Charges				
10. Annuities				
11. Income of Trusts				
12. Independent Personal Services				
13. Sub-Total (Lines 1 to 12)				
14. Dividends				
15. TOTAL PAYMENTS AND DIVIDENDS				

SCHEDULE M

CLAIM FOR CAPITAL ALLOWANCE

Description of Asset	Written Down Value B/Forward	Additions or (Disposals) During Year	Date of Addition or Disposal	Industrial Incentive Allowance		Annual Allowance		Written Down Value C/Forward
				Rate	Allowance	Rate	Allowance	
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
	$	$		%	$	%	$	$
TOTALS								

Show Disposals in Column (3) in brackets

APPENDIX B

History of Discretionary Changes in Indirect Taxes

STAMP DUTY - CCAP 283

STAMP DUTY - LEGAL AUTHORITY AND AMENDMENTS

		CAP 283	
5%		Act. 39/1975	1975
7½%		Act. 11/1978	11.2.1978
10%		People's Law No. 6/1981	February 1981
12½%		People's Law No. 18/1982	1.1.82
17½%		People's Law No. 43/1982	1/10/82
20%	of C.I.F. + Duty	People's Law No. 1/1983	1/1/83
15%	of C.I.F. + Duty	Ordinance 1/1984	23/1/84

CONSUMPTION DUTIES

Consumption Duty	Principal Act	43/1968	
	Amendments to Act	9/1972	Schedule
		41/1973	Schedule
Consumption Duty on Rum		3/1974	
$100 per case Beer		22/1974	Amended 5/1982 People's Law
		38/1975	
	People's Law	17/1981	
	S.R.O.	11/1981	Schedule
	People's Law No.	3/1981	
		27/1981	
Consumption Duty on Beer 1600 per Gallon		5/1982	
Schedule S.R.&O.		2/1982	9th March, 1982
C.I.F. + Duty	People's Law	2/1983	1/1/83
Time of Physical Examination of Goods		11/1983	1/1/83
Class. 22-09-39 $25 per Gallon		12/1983	11/2/83

REVENUE TRADE TITLE	LEGAL AUTHORITY	DATE OF REVISION
(1) Import Duty	Ordinance 35/1960	JUNE 1981 S.R.&O. 10/1981
(2) Consumption Duty	Act 43/1968	People's Law No. 11/12-1983
(3) Excise Duty on Beer	Ordinance 27/1961	12th February, 1981
(4) Export Duty	CAP. 114	S.R.&O. 10/1966
(5) Add. Export Duty	CAP. 114	S.R.&O. 10/1966
(6) Stamp Duty	CAP. 283	Ordinance 1/1984
(7) Package Tax	Act. 50/1968	50¢ per 5 cu/ft. 9/3/1982
(8) Cess on Cocoa	CAP. 59	
(9) Customs Fines	Ord. 35/1960	
(10) License to Brew Beer	Ord. 27/1961	
(11) Proceeds of Sale	Ord. 35/1960	
(12) Excise on Rum	CAP. (111)	

APPENDIX C

Training Needs for Customs and Excise

In replying the above number and date of this letter should be quoted.

AND EXCISE,
ST. GEORGE'S,
GRENADA, W.I.
27th April, 1994.

From: Comptroller of Customs

To: Permanent Secretary (Planning)

Subject: Training Needs Customs and Excise Department.

In keeping with our recent conversation Benjamin/Bubb on the above subject, I submit hereunder details requested:-

---

Upper Level Management and Public Sector Administration

Name of Officer	Grade	Academic Qualification	Private Training relative to job	Available Source of Training
(1) P. Bubb	Ag. Compt.	Senior Cambridge Advance level Econ. & Public Affairs	Management Degree Course (M.P.A. Tax Administration University of Senior Cambridge U.S.A. distinction, Customs and Excise procedure Regional Training School Trinidad. (Drug Interdiction Course. Washington(D.C.) Kyoto Convention facilitation of Trade Orlando U.S.A.	Institute for Tax Administration U.S.A. Royal Institute for Public Administration. U.K.
(2) Courtney Renwick	Deputy/ Compt./ Harbour-Master.	Senior Cambridge	1965 Regional Training School for Customs officers Trinidad. 1971 B.I.N. Course U.W.I. St. Augustines Trinidad. 1973 U.N.D.P. Fellowship in Customs Administration Egypt. Belgium -C.C.C. Ireland. 1976 Generalised System of preference Guyana 1982: (1) Wooden Vessel Surveyor. (2) Register tennage measurement. (3) Elementary machinery survey. (4) Sales verification survey attended at St. Lucia - 6/9/92-	Do.

COMPTROLLER OF CUSTOMS GRENADA

Upper Level Management and Public Sector Administration

Name of Officer	Grade	Academic Qualification	Previous training relative to job	Available source of training
(3) Eric Stewart	Asst. Compt.	Senior Cambridge	1971- 6 months of training at Customs Regional Training School (Trinidad) Gained Distinction 1978- Drugs Interdiction course in U.S.A. (Washington) 1981 - Training in B.T.N. classification in Barbados.	Institute for Tax Administration U.S.A. Royal Institute for Public Administration U.K

Basic Customs Course
Customs and Excise Procedure

Name of Officer	Grade	Academic Qualification	Previous Training relative to job	Available source of training
*Michael Neol	Class II (Clerical)	G. C. E. O level	Nil	Regional Training School for Customs & Excise Officers Trinidad.
*Everaude Antoine	Class II	Do	"	
*Joan Pivott	Class II	Do	"	Crown Agents with U.K. Department of Customs & Excise.
*Brian Joseph	Class II	Do	"	&
*Joslyn Bruno	Class I	Do	"	
*Keneth Rennie	Class II	Do	"	Federal Law enforcement Training School Glynco, Georgia U.S.A.
*Isiah Louison	Class II	Do	"	
*Dennis Paterson	Class II	Do	"	Do

* Priority

OF CUSTO

Supervisory

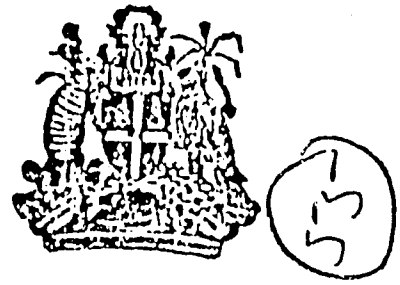
Middle Management Level

Name	Grade	Academic Qualification	Previous Training relative to job	Available source of Training
*V. Cyrus	Ag. Supervisor	Senior Cambridge	Basic course Customs & Excise Procedures Regional Training Trinidad	Crown Agents with U.K. Department of Customs & Excise
*Reyfold St. Louis	Ag. Supervisor	Do	Do	&
* L. Flavigny	Do	Do	Do	Federal Law enforcement Training School Glenco, Georgia.
*George Francis	S.C.O.	Do	Do	
		Customs Inspectors & Examiners Course		
*Evolyn Cenac	S.C.O.	G.C.E.	Training in Basic Customs & Excise Procedures Regional Training School Trinidad.	Crown Agents
*Linus Thomas	S.C.O.	G.C.E.	Do	&
Claudius Lewis	S.C.O.	" "	Do	Federal Law Enforcement Training School Glenco, Georgia.
Ronald Bell	S.C.O.	" "	Do	
Samuel Sandiford	S.C.O.		Do	
*Franklyn Roberts	S.C.O.	Senior Cambridge	Do	

* Priority

CONTROLLER OF CUSTOMS

Ref. No.....
In replying the above number and date of this letter should be quoted.



PORT, HARBOUR, CUSTOMS
AND EXCISE,
ST. GEORGE'S,
GRENADA, W.I.
5th April, 1984.

From: Comptroller of Customs

To: Permanent Secretary (Planning)

Subject: Training Needs Customs and Excise Department - Ministry of Finance.

I refer to tele-conversation on the above subject on Friday 30th March, 1984 between your office and myself and also to circular letter 1/84 of even reference emanating from your office. I crave your indulgence, to refer to my memo of 10/2/84 which among other things attempted to draw your attention to some of our needs as well as certain drawbacks and constraints encountered relative to efforts made in having these needs satisfied.

In keeping with your request, I would like to emphasise that our No.(1) priority lies in the area of Courses in Basic Customs procedures since the majority of our officers are relatively young, untrained and with no more that five years experience in Customs and Excise practice and procedure. Priority No.(2) Training at upper and middle management level in the specific area of Customs Administration, tax management and fiscal policy making. (3) [illegible] at all levels to enhance and keep current training had as well as to widen horizons and help officers to mature at a early age.

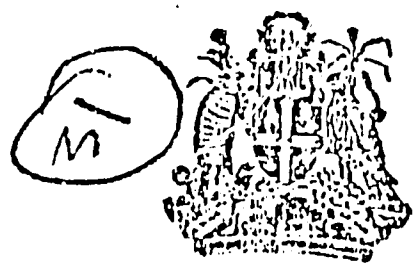
The importance as well as urgency of our needs cannot be over-emphasised given the new trends and developments in regional and international trade as well as agreements and economic grouping and organisations and the movement towards facilitation of both persons and goods. In this context too, one cannot overlook our own immediate needs and effort towards resurrecting the free enterprise system. The impact that the Caribbean Basin Investment Plan can have at O.E.C.S. and Caricom levels taking in to consideration that the Customs Department is the Authorised body for certifying and verifying documents pertinent to the movement of goods within [illegible] terms of these agreements.

Yours faithfully,

.....
Comptroller of Customs

GRENADA

Ref. No. ...40/01
In replying the above number date of this letter should be quoted.



PORT, HARBOUR, CUSTOMS
AND EXCISE,
ST. GEORGE'S,
GRENADA, W.I.

10th February, 1984.

From: Comptroller of Customs

To: Permanent Secretary,
Ministry of Planning,
St. George's.

I refer to a copy of a telex originating from T. Joseph Carioco - giving approval for Messrs. Carlyle Felix and Everaud Antoine to attend the Basic Customs Course in Trinidad from January 3rd to April 29th,1984. Attached please find copy of a memo to Ministry of Foreign Affairs on the matter and the reply thereto which speaks for itself.

You would appreciate that the kind of training that we are seeking particularly at the basic level is available only in a few institutions in the region and this is granted subject to the exigencies and convenience of those institutions. You would appreciate too, that this cannot be accepted as ideal in terms of our goals and aspirations. Given that one of our main functions in the Customs and Excise Division of the Ministry of Finance is the protection of Revenue and along with that role we are called upon to perform a host of protective Agency Duties on behalf of the Armed Forces, Police, Agriculture, Health etc., I submit that like opportunity for training as made available for the Police Force should be afford us. I further submit that for the purpose of the Revenue, we are the Police and in fact we have to work hand in hand in the interdiction of narcotics and the prevention of smuggling. The fact is in many a case, Customs assume the major role since according to the prescriptions of the laws of Grenada related to imports the Customs is the institution that is empowered to demand declarations, carry out examinations, make assessment as to duties, collect duties and fines, effect seizures and forfeitures and mitigate penalties. I outline all this to enhance our need for training and to emphasise an equal urgency and importance as is now meted out to the Police Force.

In keeping with your Circular letter 1/84 on the subject of "Training Needs" I exhort you in your contacts with your United States Counterparts to bring home to them our case since there is a full time Training School at Glenco U.S.A. It is not asking too much since at the Regional level the availability of places is so problematic as well as the resources for setting up a Regional Training School with-in the O.E.C.S. seem so limited and the idea forfetched.

Yours faithfully,

.....
Comptroller of Customs

FISCAL MEMORANDUM NO. 2

BUDGET PROCEDURE IN GRENADA

JORGE MARTINEZ

SYRACUSE UNIVERSITY
LOCAL REVENUE ADMINISTRATION PROJECT
THE MAXWELL SCHOOL | METROPOLITAN STUDIES PROGRAM
409 MAXWELL HALL | SYRACUSE, NEW YORK 13210 USA | 315/423-3114, TELEX 937430

GRENADA TAX PROJECT
Fiscal Memorandum Number 2

TO: Mr. Laurie Wilson
FROM: Jorge Martinez
SUBJECT: Budget Procedure in Grenada
DATE: August 13, 1984

1. In recent years the Grenadian government sector has played an increasing role in the economy of the country and it is likely that the high relative size of the public sector (about one-fourth of GNP) has contributed to the present stagnation of GDP. We would take the position that there is a need to control the growth of the public expenditures and to reduce tax rates in order to set the Grenadian economy on a new economic growth path--one led by a private, export-oriented sector.

2. To provide public goods and services, the Government extracts, through taxation, scarce economic resources from the private sector of the economy. This activity is generally justified because the social return to the nation from the use of those resources in the public sector is larger than if they were left in the private sector. One is left, therefore, with the nebulous conclusion that the government sector must be large enough to accommodate social needs but not so large as to require tax rates that discourage private incentives to produce. Establishing the "right" share of GDP to be allocated to the public sector is, however, very hard to do. Without good information on how government spends its money, and what it "buys" for its

citizens, ore cannot make good judgements about whether, and how, the GOG budget may be contracted. Information is required if the Government is to achieve any of the following objectives:

-- to identify how much of the annual budget is uncontrollable, and how much discretion the government has in controlling expenditure growth

-- to find a better basis for allocating public funds among various ministries and agencies

-- to efficiently plan for and distribute expenditure cuts among agencies in the event of revenue shortfalls

-- to identify public activities that might better be carried out in the private sector

-- to plan for any future expenditure adjustments that might be called for by changing costs or workloads (for example, a projected smaller number of school-aged children, or an increased cost of aspnalt).

3. At present, the necessary information to support analyses such as outlined above are not available. Indeed, the lack of adequate budget preparation and control has been an important contributing factor to the growth of the GOG budget. The current procedure involves mainly the gathering and adding-up of requests and expenditure projections of the different ministries and independent agencies for the next fiscal year. The information is collected under the broad categories of "Personnel Direct," "Personnel Indirect," "Supplies," "Overheads," and "Other." Though some paring down of the budget requests is surely done, there is not a systematic evaluation.

4. The purpose of this memorandum is to suggest some principles to underlie changes in the present system of budget preparation. The main objective of these changes is to generate that information from each ministry which would allow the Ministry of Finance to make sound decisions on (i) the overall size of the budget; (ii) the weighting of the different expenditure items against one another, and (iii) to generally make sure that the budget is in line with the overall policy objectives of the Government.

5. If the general principles laid out here are acceptable, the next step is to design the specific format of the report required from each spending unit. We would envision that at the same time the Ministry of Finance (MOF) sends up the forms for expenditure requests and projections for the next fiscal year, it should demand information of the following type described in the paragraphs below.

6. Each spending unit should produce a memorandum describing the objectives of each program in which it is involved. In the same memorandum each ministry should (attempt to) allocate their expenditure over the last year (in personnel direct, personnel indirect, supplies, overhead and other) to the programs and activities identified. The budget for that agency could then be examined in terms of how much was being spent for each activity. In other words, in addition to a breakout by object of expenditures (e.g., personnel services, overhead, etc.), each agency would be able to disaggregate spending by program (e.g., primary education instruction, education administration, etc.). Clearly, the identification of programs/

activities will be more difficult for some ministries than for others: the overhead units such as the office of the Chairman will be especially difficult. Assistance from the Ministry of Finance will be needed in the beginning to assist other ministries in the identification of programs and objectives.

7. Each ministry should identify in the same document which, if any, of the last year programs will be discontinued or reduced in size, and whether any new programs are being proposed. The philosophy here is to begin by estimating "how much will it cost next year to continue to do what we are now doing?" The analysis should then move to proposals to increase (reduce) expenditures because of service level expansion (reduction) or because of the institution of new programs. The objectives to be achieved by any proposed new programs should be clearly elaborated. The Ministry should also indicate the permanent or temporary nature of any new program(s) or program expansions. If they are temporary, a statement of the fiscal year in which they will be phased out should be included.

8. Each ministry should be required to estimate how it would reduce its proposed budget by 10, and by 20 percent, if such a reduction were required. The estimates should be made in detail (which positions would be eliminated, etc.) An accompanying memo should describe the potential effects of such cuts on program levels.

9. Some indicators of physical inputs used and workload measures should accompany the budget request. These would give the budget office an idea of where cuts might be possible, and what service level costs

might be involved. Examples of the information required are as follows:

-- number and description of filled vs. vacant positions

-- estimated number of FTE temporary employees, and a job description for each

-- workload measures such as numbers of students enrolled, hospital patients served, etc.

10. In its review of each ministry's requests, the Ministry of Finance should separate requested expenditures between "controllables" and "noncontrollables." In the latter case the expenditures are inescapable, for example, because of previous contractual agreements (e.g., agreed upon salary raises, security imperatives such as police training, debt repayment). For most departments, however, there is an element of expenditures that is discretionary and another element that cannot be avoided. Placing each budget item in each spending agency in one of these two categories will be arbitrary. This is inevitable. The exercise will, however, facilitate decision making since controllable expenditures can be identified as possibilities for reduction and their benefits scrutinized. The information obtained can also be invaluable when expenditure cuts are called forth due to unforeseen developments, e.g., revenue shortfalls or donor pressures for current budget balance.

11. Debt service (interest and repayment of principal) is especially important item in the uncontrollable part of the budget. The Ministry

of Finance should have a five to ten year projection of the annual costs of servicing the debt. Short-term debt should also be identified and included in the projections. In addition, the Ministry should alter the projections of total debt service costs each year, in order to show the current revenue coverage of these fixed commitments. Augus Smith, we understand, is already at work on such projections.

12. One of the requirements of good budgeting is comprehensiveness. All expenditure (and revenue) items should be included in the budget. However, as pointed out by the IMF Executive Summary on Fiscal Reform (August 1984), the 1984 budget does not cover government loans and advances. Even though these items may be completely accounted for in the long-run in some independent ways, it is still essential that they be explicitly included in the Annual Budget.

13. Capital budgeting procedures need to be overhauled. At present, it would appear that each ministry has the responsibility of identifying project needs and formulating requests. The Ministry of Planning is responsible for finding external funding for the projects. What is less clear is the assignment of responsibility to evaluate capital requests and to establish priorities. These ambiguities should be cleared up, and a more formal capital budgeting process should be instituted. The following are necessary elements of that process.

   -- a five year capital budget, which establishes priorities and includes a financing plan, should be put in place and reviewed annually.

-- Every capital budget request should be accompanied by a cost-benefit evaluation of the project. The fact that projects are being externally funded does not negate the need for independent GOG evaluation. In most cases estimates of costs are not hard to produce, but estimation of benefits is usually more difficult and more controversial. But even when quantification of full benefits is not possible, a description of benefits will be more helpful than no information at all. Capital resources are, of course, also scarce and they should be used only for those projects with the highest net social return. The Ministry of Finance and Planning will have responsibility for these analyses.

-- Each capital project request should be accompanied by an estimate of the annual recurrent expenditures implied for the next three to five years. Information on projected revenue from fees and user charges (if any) generated from the operation of the project should also be included. These recurrent costs should then be assigned to the annual budget request of the relevant agency.

This latter information should actually be collected by the Ministry of Finance for all capital projects approved and on the way in 1984. Some estimates are contained in the feasibility studies produced by the donor countries (e.g., the Point Salines Airport). The concern shown by the IMF in this regard are is well founded.

14. Steps should be taken to comply with present legal provisions concerning the auditing of the Government accounts. The auditing by an independent agency of each of the ministry's accounts is necessary to insure that funds have been spent according to the budget and that the accounts truthfully represent the ministry's activities.

15. The next step in reform of the budget process is to develop a budget justification request for each spending agency. The Syracuse project will be willing to assist by reviewing these documents when they are prepared in draft form.

cc: Augus Smith
Roy Bahl

JM/eg

FISCAL MEMORANDUM NO. 3

GRENADA TAX PROJECT WORKPLAN

ROY BAHL

SYRACUSE UNIVERSITY
LOCAL REVENUE ADMINISTRATION PROJECT
THE MAXWELL SCHOOL | METROPOLITAN STUDIES PROGRAM
409 MAXWELL HALL | SYRACUSE, NEW YORK 13210 USA | 315/423-3114, TELEX 937430

GRENADA TAX PROJECT
Fiscal Memorandum Number 3

TO: USAID, Grenada; Ms. P. Buckles
FROM: Roy Bahl RB
SUBJECT: Grenada Tax Project Workplan
DATE: August 13, 1984

1. Jorge Martinez and I met with Mr. L. Wilson on August 9 and discussed the objectives of the present phase of the Grenada Tax Structure Project, a workplan and timetable, and a set of deliverables. We have reached agreement and Mr. Wilson understood that we would meet with you to seek whatever clearance is necessary to proceed. This memo is a follow-up to our meeting of Friday, August 10th.

2. To briefly summarize our (Bahl, Martinez and Wilson) discussion of fiscal objectives and strategies, the following three elements are essential to a sound reform program. First, the share of government in Grenadian GNP is too large, and must be reduced. This can be done through some combination of attrition, devestment, more efficient budgeting, and expenditure retrenchment. Expenditure reduction and tax reduction go hand-in-hand; however, a retrenchment program will be especially difficult given the present employment situation, the need to service new capital investment, and the budget deficit. These constraints lead to the second general principle: that the fiscal reform plan must be multiyear. Tax reductions will have to be phased in with improvements in tax administration, structural reforms in the

tax system and expenditure control. The Fiscal Planning Model will provide a way to chart and monitor this phasing-in. Third, reform of the tax system should be guided by the goal of stimulating a private sector led development effort, by attracting foreign and domestic investment and by encouraging risk taking.

3. Given these general goals, the terms of reference in the cable of June 1984 (Fiscal management TA for Grenada), and our initial review of the fiscal situation, we have developed a workplan in the following areas: advice on short-run expenditure evaluation and control; the development of a fiscal planning model; review and evaluation of the IMF, Government Working Party and other reports on the fiscal system; Preparation of a preliminary assessment of the current tax system; and the design of a longer term technical assistance program for comprehensive tax reform.

Expenditure Control

4. The GOG Budget Office is in process of reviewing the expenditure request of each ministry. Mr. Martinez is assisting in this effort by helping in the preparation of budget justification (BJ) requests. The BJ statements include estimates of workloads to back up personnel requests, explanations of all new programs requested, etc. The form of these requests will vary by Ministry. In addition, meetings with the finance officers of each of the 39 budget "votes" will begin next

week to gather information on actual numbers employed, vacancies, and more detail on temporary employment. In general, our role here is advisory and focused on helping establish procedures to gather necessary information for program evaluation. We will not participate in the actual ministry-by-ministry actions.

Fiscal Planning Model

5. We will develop a fiscal planning model to generate five year projections of Government Revenues and Expenditures, under alternative assumptions about national economic growth and discretionary government policy. Mr. Michael Wasylenko will be in charge of this effort, and will arrive in Grenada on August 14th. The GOG has assigned Mr. Angus Smith and Ms. Angela Holas as counterparts. We have reached agreement with the GOG on the type of microcomputer equipment necessary.

Tax Structure Evaluation

6. Mr. Martinez is preparing papers on the direction for structural reform of income and property taxes, which assess the present structure against theoretical norms and against the objectives of GOG policy. In this connection, he will review the findings of previous reviews and analyses of these taxes. His report will include recommendations for whatever additional TA is necessary to bring about comprehensive reform of the taxes.

7. A consultant will be named to carry out a similar tax structure evaluation for indirect taxes. We hope to bring the consultant to

Grenada within the next three weeks. He would need one-week in-country to complete his report.

Tax Administration

8. In order to assess needs for long-term TA in tax administration, we propose to bring three experts, each for one week, in income tax, customs valuation, and property tax valuation. Their reports would deal with needs in the areas of administration and training. In our final report, we would review these recommendations (with Mr. Wilson) and define alternative programs of long-term TA.

Reports

9. We will issue our reports to Mr. L. Wilson in the form of fiscal memoranda (FM). Copies to USAID will be at his pleasure. We will also prepare a final report for GOG and USAID which could form the basis of a Project Paper.

10. The FM will be issued as completed, and after each consultant's visit. The final report can be delivered within two weeks after the fiscal advisor completes his assignment in Grenada. A preliminary, summary version will be submitted before the fiscal advisor leaves the country. The Fiscal Planning model can be operational in September, if the computer can be obtained. All of the above assume no unforeseen circumstances.

cc: Mr. L. Wilson
Mr. Jorge Martinez
Mr. Robert Firestine

RB/eg

FISCAL MEMORANDUM NO. 4

DISCUSSION WITH MR. LAURISTON WILSON ON
SEPTEMBER 9, 1984 IN GRENADA

ROY BAHL

SYRACUSE UNIVERSITY
LOCAL REVENUE ADMINISTRATION PROJECT
THE MAXWELL SCHOOL | METROPOLITAN STUDIES PROGRAM

409 MAXWELL HALL | SYRACUSE, NEW YORK 13210 USA | 315/423-3114, TELEX 937430

GRENADA TAX PROJECT
Fiscal Memorandum Number 4

TO: Distribution Below

FROM: Roy Bahl RB

SUBJECT: Discussion with Mr. Lauriston Wilson on 8/9/84 in Grenada

DATE: August 20, 1984

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1. The purpose of the meeting was to discuss a strategy for tax reform in Grenada, to solicit the views of Mr. Wilson, and to discuss the agreements and disagreements that we have with the reports by the IMF and the Government Working Party. On the former, it should be noted that the IMF report is not yet ready, and we have seen only an Executive Summary.

Objectives of Tax Reform

2. We pointed out that there seemed to be a disagreement between the general objectives laid out in the Government Working Party Report (The Callender Report) and the IMF's. The former indicated that revenue raising was a paramount concern, that equity was very important, and that work and investment incentives seemed to be running a distant third. The Fund, on the other hand, seemed to take the position that the Government of Grenada had the stimulation of private sector-led export development as its main objective. Mr. Wilson noted that while the Government's Economic Memorandum (drafted with the assistance of the Caribbean Development Bank) reflected more the view of a planned economy, the GOG was indeed committed to private sector-led development. I take this to mean that the tax reform package on which we are working should emphasize the stimulation of private incentives to a great degree.

A Fiscal Planning Model

3. I explained to Mr. Wilson what a fiscal planning model does and does not do; namely, that it will allow us to project expenditures for five years under a variety of assumptions about performance of the Grenadian economy and about government policy measures such as employment increases, compensation increases, etc. The uses of the fiscal model will be to analyze "gaps" between projected revenues and projected expenditures; to examine the impact of alternative discretionary measures on both the tax and expenditure sides (e.g., issuance of new debt, change in a tax rate, etc.); it can also be used as a control device, i.e., to show what sorts of measures are necessary to control the growth in public expenditures.

4. The most important contribution of the fiscal planning model is that it will get the focus on long run rather than short run planning. In fact, my view is that the growth in the Grenadian public sector will have to be slowed largely by attrition and by economic growth (an increase in the denominator of the expenditure-GNP ratio). We really need to get a feel for how long this process could take.

5. As far as the mechanics of doing the fiscal planning model, I explained that Mike Wasylenko will be in Grenada next week. I also explained his considerable experience with this kind of work: that he has done a similar exercise in Thailand as well as participated in one in Kenya. We also discussed the computer equipment that would be needed, and the steps necessary to get it properly equipped and into the country.

The Objectives of Tax Reform in Grenada

6. A first objective is a reduction in the size of government. The present level of about 27 percent of GNP and projected levels (IMF) of more than 40 percent of GNP are not conducive to private sector development. As noted above, some of the reduction can take place through attrition and through GNP growth. This, however, will take quite a while and will probably not be adequate. Other measures that might have to be taken are (a) improvements in the budget process to increase its efficiency; (b) a freeze on new hirings and on salary levels; (c) a divestment of currently held public enterprises; and (d) an increased use of user charges (particularly in the public utility area). The biggest problem in this set of proposals had to do with a salary freeze--Mr. Wilson noted that a proposed increment of as much as 30 percent was already on the table for discussion. He did think, however, that an employment freeze might be possible. In later discussions with AID, we were told that they would not like to be on record as supporting a public employment freeze.

Personal Income Taxation

7. A first need of tax reform in this area is to cut the rates, which are already far too high. We would also propose to consider fewer brackets, a flatter rate structure, and a broadening of the base. All of this would seem to be in agreement with the IMF, but in outright disagreement with the Government Working Party. The latter proposed to increase the number of rate brackets, and would not have cut the rates very far at all.

8. Our interest would be in the direction of simplifying the income tax. Here we would think in terms of elimination of "unnecessary" deductions and credits, in favor of lower rates on lower income families. This is in partial agreement with the IMF, but would seem to be in disagreement with the Government Working Party which was more or less silent on the issue of changing the status of deductions, etc.

9. We would move to increase the tax net by bringing "income-in-kind" into the tax base. We also would propose to expand the base by improved administration and training. Here we are thinking of a modified assessment program, improved audit procedures, and substantial improvements in assessment. One could speculate that these improvements would capture a substantial amount of the self-employed who presently evade the tax. These thoughts are in general agreement with the IMF Report.

10. We would propose the continued taxation of dividends, and the taxation of interest (presently not taxed). The IMF would agree, but the Government Working Party would exempt both dividends and interest. Mr. Wilson expressed some concern about our initial view, but accepted the idea that a minimum exemption could be placed on taxes payable on interest; for example, the first $X could be tax free. He said that seemed appropriate and that he was ready to push ahead with that recommendation.

11. Penalties and enforcement need to be stiffened. In particular, we might look for ways to use other transactions as methods of enforcement, e.g., exit permits requiring tax clearance, etc. The IMF would agree on this. Mr. Wilson also agreed and noted that he had produced a paper on this subject for the Committee.

12. We argued that, with a good income tax, the estate duty could be completely eliminated. He agreed with this, as did the Government Working Party and the IMF Report.

13. We would propose phasing-in the new personal income tax structure over a three-year period. The phasing-in would occur as the base was broadened and the administration improved. In this way, the effective tax rates could fall on many classes of taxpayers without substantial short term revenue losses.

14. On virtually all of these points, we reached agreement with Mr. Wilson and he urged us to push ahead with our preliminary work. We agreed that Jorge Martinez would draft the first summary paper on this subject, and he could lay out the first design for the longer term study to be undertaken.

Company Income Tax

15. The company tax needs to be reformed in a way that would make Grenada more attractive to foreign investors and to encourage greater risk-taking. This objective suggests rate reduction and a liberalization of terms under which profits may be repatriated. Increased risk-taking may be encouraged by extending the loss offset. A question that arose was whether one would allow a carry forward of losses incurred during the holiday period.

16. There is a need to integrate personal and corporate income taxation in order to eliminate the double taxation of dividends.

17. The question of tax incentives, double tax treaties, repatriation of profit(s) are interrelated and need to be considered simultaneously. A full review is necessary.

18. There are also administrative needs in the area of company taxation which more or less parallel those for the personal income tax.

19. A final set of questions was raised by Mr. Wilson including: (a) the possibility of using company taxes to encourage the company vs. partnership form; (b) the need to deal with the depreciation issue; and (c) his hesitancy about the IMF proposals concerning imputation. We agreed to examine these issues. In general, we were in agreement with the IMF on areas of integration, encouraging risk-taking, and rate reduction.

Indirect Taxes

20. Our view of the indirect tax system is that it is unduly complicated and fragmented. One possibility for a long run goal is to merge the present system into (a) CARICOM external tariff, (b) a general consumption duty which would include services and have as flat a rate a possible, and (c) perhaps an excise on a few of the traditional goods. In this approach, we would probably disagree with the IMF Report, though it is unclear exactly what they have proposed from the Executive Summary. Such a tax reform would have to be phased-in with appropriate broadening of the base, and with administrative help.

21. The base of the indirect tax system needs to be broadened in order to bring down the inordinately high tax rate. We probably would not favor a very broad tax at the import level that would not exempt any imports of raw materials. A credit for taxes paid on raw materials could be allowed for domestic producers. This value added element might not be too difficult to administer, but we will need to get an expert into Grenada to assess this for us. I promised to contact Professor John Due. The base could also be broadened by bringing all services within the legal tax base--restaurant meals being a first step in this direction. In addition, there is the question of the inordinately heavy amount of government exemptions presently allowed. The IMF would abolish all; I'm sure we would abolish many of them. This question needs analysis.

22. The export tax is a particularly obnoxious component of the tax structure in that it discourages both production and incentive in the economy. Our first leaning would be toward abolition of the export tax but, as that is phased-in, we must work out a substitute for it. We have not yet given this enough thought.

23. Finally, there is need for technical assistance to expand the base of indirect taxation and to make the system more fair. In particular, there is the question of a need for improved valuation of imports. Apparently, some technical assistance of this type was provided in the past, but it has not been fully put into effect. The IMF called for similar technical assistance.

Property Taxation

24. The property tax in Grenada is very anemic, and there is much room to expand its role in the tax system. Properly administered and structured, the property tax can be a good component of the tax system and can be a good substitute for income taxation. In Grenada, the government is pretty much starting from scratch. This has the advantage of allowing us to structure a "new" property tax, without being saddled with history. But, on the other hand, it means that there is a high start-up cost associated with putting the tax in place.

25. A first item on our agenda is to get some idea of the quality of the current tax roll and to make some estimate of the cost of completing the roll and making it usable. With respect to these administrative needs, we have in mind identification of parcels, valuation, record keeping, and collection. In general, our view would be that the right kind of property tax for Grenada is one which does not cover all small parcels--the administration involved is more costly than the amount of revenue collected.

26. Two other important items on the structure of property taxation need attention. The first is whether there should be a property transfer tax and, if so, how it should be administered. On the one hand, it is the closest thing to a capital gains tax in the Grenadian system. It also has the advantage of providing the basic valuation data used as inputs for the property tax. On the other hand, it is badly administered at the present time. One thing that must be examined in our present work is what it would take to create a more efficient operation of the property transfer tax. The second structural issue which we must consider is the possibility of betterment levies. With so much capital construction going on in Grenada, it is clear that land values will increase dramatically. We need to develop a system of special assessments to capture some of this betterment for purposes of government.

Phasing-in of Tax Reform

27. The tax reform will have to be phased-in over a period of time to avoid inordinately high budget deficits in the very short run. (Even in the absence of any new government action, the budget deficit in the next few years promises to be very large.) At first look, one would think of a four-year, phased-in program (FY 1985 - FY 1988). The following is a list of those potential revenue reforms and those expenditure measures which will be resource using in the short run, and the fiscal years in which this revenue drain might be felt:

Income tax rate cuts (1985, 1986, 1987)

Recurrent cost of new capital investments (1985 onward)

Increased current expenditures (e.g., wage increases in 1985)

New debt service costs (1985 onward)

Increased tax administration expenditures (1985 onward)

28. The following are those potential reform measures--revenue and expenditure side--which could add to resources available. These measures, and the fiscal years of initial impact, include:

Improved valuation of imports (1986)

Broaden indirect tax base to include services (1986)

Improved income tax administration by training, modified assessment program, improved procedures, tougher enforcement (1986)

Reestablished property tax, add betterment levy (1987)

Divestment of public enterprise activities (1985)

Employment and wage rate freeze (1985)

Increased rate of economic growth and increased revenue from tourism (1985)

Our Work Plan

29. The responsibility of Jorge Martinez will be to serve as our Resident Advisor in Grenada, to manage the activities of the project in Grenada, and to provide the kinds of technical advice as outlined in the Terms of Reference. In addition, he will prepare a paper on income taxation, a paper on property taxation, and will participate in preparation of the Final Report.

30. The responsibility for the fiscal planning model will be primarily in the hands of Mike Wasylenko who, we anticipate, will arrive in Grenada during the week of August 14th. How long he stays, and how quickly the model can be made operational in Grenada, depends on when the microcomputer can be shipped to Grenada.

31. An Income Tax Administration Advisor is needed for one week to write a Terms of Reference for a longer term analysis. This work will involve a scrutiny of the current situation and past progress. I propose to contact George Whitehouse in our Kingston office to arrange for him to go to Grenada for about a week, hopefully around the first week in September.

32. There is need for technical assistance in the area of customs valuation and training. Identification of the kind of technical assistance requires the opinion of an expert. I propose to contact Ken Stacey and ask him to go to Grenada before the first week in September.

33. The set of taxes that constitutes consumption duty, stamp duty, etc., is inordinately complicated. There probably is need for a harmonization and coordination of these taxes, and probably for their amalgamation into one or two more general levies. We need the services of an expert to examine this possibility and to outline future technical assistance necessary to implement such a change. I propose to contact Professor John Due to see if we can not get him to Grenada before mid-September.

34. The property tax cannot move forward until the property tax roll is completed. I will soon contact a firm that specializes in preparing such rolls, ask them to send someone to Grenada for one week, and give them the mandate of assessing the current situation and estimating the cost of preparing a new roll. My first contact will be with CLT Systems.

Possible Long Term Technical Assistance

35. Until we complete the reconnaissance exercise, we cannot say firmly what the long term technical assistance needs will be. One can, however, already anticipate what some of the needs will be.

36. Grenada needs a comprehensive tax reform that includes both structural change and administrative change, as well as training. It would be incorrect to rush into such changes without carefully thinking through what is needed. Moreover, in the name of not duplicating efforts, the comprehensive reform should coordinate the assistance of USAID, the IMF, perhaps the British, and perhaps the United Nations. A first service that USAID might provide is this coordination. The fiscal planning model could be an important tool in centering the attention of all the external parties on the long term fiscal future of the country.

37. The components of a long term technical assistance will be defined at the end of this project. Our preliminary view is that the long term needs include at least the following. First, there needs to be a study of the indirect tax system and a design of some sort of reform in the direction of a general levy. Following this design phase, there needs to be an implementation program to train local personnel and to actually put the new tax in place. Second, it is likely that an Income Tax Advisor

will be needed to assist in improving audit and assessment procedures, as well as to train inspectors in accounting and audit procedures. Third, technical assistance in the area of customs valuation will be required. Fourth, the property tax is in need of a careful structural study to design the "right" kind of property tax for Grenada, and then to provide the administrative back-up necessary to complete the roll and to implement the new property tax system. Fifth, there needs to be some further work on structural studies in several areas. Among these, and we will have more to say in a Final Report, are: (a) the proper level and type of tax incentives to be offered by the Government of Grenada; (b) the proper structure of the company tax and its integration with the personal tax; and (c) the impact of reforms in the tax system on the distribution of income, with special reference to low income families.

38. I would propose that an efficient way to proceed would be to wait until our work is completed by the end of September (and by then hopefully the IMF work will be completed) and call a meeting of technical experts, either in Grenada or in Washington. From this meeting, we could plan a strategy for long term reform.

Reports

39. From now until the end of September, we would propose to issue our reports in the following format. First, there would be fiscal memoranda, brief reports that describe the results of each activity. These reports will be "numbered" memoranda and will be issued as the occasion calls for it. Second, there will be longer consultants reports. based on field visits. Third, there will be a Final Report, first in draft form at the end of September, and in final form after Syracuse home office review.

RB/pb

cc: Mr. L. Wilson
USAID Grenada
USAID Barbados (Don Harrison)
USAID Washington (Bob Firestine)
Jorge Martinez
Sam Skogstad

FISCAL MEMORANDUM NO. 5

THE PERSONAL INCOME TAX IN GRENADA: AN EVALUATION OF PRESENT STRUCTURE AND PROPOSED REFORMS, PRELIMINARY RECOMMENDATIONS, AND SCOPE OF NEEDED FUTURE WORK

JORGE MARTINEZ

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SYRACUSE UNIVERSITY
LOCAL REVENUE ADMINISTRATION PROJECT
THE MAXWELL SCHOOL | METROPOLITAN STUDIES PROGRAM

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GRENADA TAX PROJECT

Fiscal Memorandum No. 5

TO: Mr. Lauriston Wilson, Jnr.
FROM: Jorge Martinez
DATE: August 30, 1984 (Revised, September 26, 1984)
RE: The Personal Income Tax in Grenada: An Evaluation of Present Structure and Proposed Reforms, Preliminary Recommendations, and Scope of Needed Future Work*

I. The Present Income Tax Structure

1. The personal income tax has played only a modest role in Grenadian public finances. In the period 1980-83 the annual revenue collected from the tax was only around 15 percent of total tax revenue and a little over 3 percent of gross domestic product. At the present time there exists no indication of any trend that will alter this weak performance. This lack of buoyancy can (partly) be blamed on certain structural and administrative peculiarities of the Grenadian personal income tax, which are reviewed below.

The Tax Base

2. The tax is levied on all sources of income, but it gives preferential treatment to income from capital, in two ways.[1] First, interest income from deposits in any bank in Grenada and from most government securities is tax exempt. Secondly, capital gains from the sale of assets are not included in the definition of assessable income and therefore escape the tax.

3. Imputed income from owner occupied housing is by law excluded from the tax base. Farmers and some retailers are, however, imputed income

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from "in-house" consumption.[2] All in-kind incomes (e.g., housing, automobiles or grocery vouchers) are also by law fully taxable, although the law lacks detail in this respect. In-kind benefits seem to have grown in importance over the last few years.

4. Under the present legislation pension benefits are fully taxable. In August 1984, the Interim Council "contemplated" changes in the law that would exempt from the tax the first EC$7,200 received in pension benefits as well as 50 percent of any amount above the initial EC$7,200.

5. The income tax law does not contain any provision for income averaging or any other treatment of irregular (uneven) income. Because of the steep rate structure of the income tax, two individuals with identical incomes over a period of two or more years may end up paying considerably different taxes.

6. The law does not contain any provision to correct for automatic increases in tax burdens induced by inflation. Because of the progressivity of the rate structure, as nominal incomes rise to keep up with price increases, taxpayers find themselves sliding into higher and higher tax rate brackets. Taxpayers' real tax burdens increase even though their real incomes may have remained constant or even decreased.

Using the Retail Price Index, for example, a taxpayer's income of EC$5,500 in 1980 would have to be EC$7,843 in 1984 in order to have the same purchasing power in both years.[3] Using the GDP deflator, the 1984 income would have to be EC$7,309. Because of inflation, the tax burden in this example would have increased from EC$925 in 1980 to EC$1,528 in 1984 (EC$1,377 when the GDP deflator is used). This represents an increase in

tax liability of 65.18 percent (48.86 percent using the GDP deflator) which is well beyond the rate of increase in prices and nominal incomes. Real incomes stay the same but real tax burdens increase.

Since 1980 there have not been discretionary changes in the tax law that could have (partially) offset the increases in tax burdens induced by inflation.[4]

7. The personal allowances and some of the deductions allowed to arrive at taxable income are quite standard. But the law, for example, also allows deductions of up to EC$700 per child, for overseas educational expenses, and of up to EC$1,440, for life insurance premiums. The most conspicuous deductions of up to EC$7,200, is granted for owner-occupied mortgage interest payments.

At the moment we are in the process of reading 1983 data from all individual tax returns into the computer. In the near future we will be able to estimate the revenue losses implied by the present system of deductions.

The Rate Structure

8. The present nominal or statutory rate structure is highly progressive, reaching a rate of 65 percent for taxable incomes of or above EC$30,000. From data made available by the IRD for taxpayers with over EC$25,000 of taxable income, the effective average rate[5] also appears to be highly progressive. Once the data from all 1983 tax returns is read into the computer, we will be able to establish the effective degree of progressivity for the whole income scale.

Income Tax Administration

9. The tax by law is self-assessed, but the IRD estimates that of 15,000 potential taxpayers, only 2,500 file a return. Eventually, between 7,000 and 8,000 pay the tax after the IRD mails out a Notice of (Income) Assessment to those that have not filed. The present tax form is perhaps too complicated, which encourages lack of compliance and overburdens the IRD resources because many returns have to be redone.

10. By law, employers must withhold part of their employees' salaries along the lines of a PAYE system, and all but the very small companies appear to do so. At the end of the year, the very small companies are assessed and charged for the income tax owed by their employees.

11. There appears to be considerable tax evasion, on the other hand, by the self-employed, including professionals, taxi drivers, and small shop owners. The resources of the IRD do not seem adequate to undertake the assessments and field audits necessary to control tax evasion in these traditionally hard to tax sectors.

12. The problem, however, does not seem to be only a lack of resources. There exists a 1979 assessment manual (or modified assessment plan) written with the technical assistance of the IMF, which could be used for field audits of the "hard to tax". The manual, however, has not been used since 1981. Instead, the self-employed have been assessed only a small fraction of their true incomes and the assessment has not changed much over the last few years. Only very recently has the IRD attempted some field-auditing.

13. Income tax evasion in the agricultural sector, another traditionally hard to tax sector, is relatively small due to the peculiarities of the Grenadian marketing channels. Practically all sales of the four major crops (nutmeg, cocoa, bananas, and "minor spices") have to be made through the (four) producer associations, which effectively operate as export monopolies. The IRD, then, uses the records from the associations to tax farmers. Only small farmers who grow cash crops escape the income tax net completely.

14. The income tax law establishes civil penalties for failing to file a return (up to 10 percent of the tax due), and for filing a fraudulent return (up to three times the amount of the tax avoided). Criminal proceedings are also envisioned in the law with penalties of up to two years in prison. Civil penalties for filing a fraudulent return, however, are hardly ever imposed, and criminal penalties have never been imposed, at least in recent years.

II. Normative Criteria for a "Good" Personal Income Tax

15. A traditional way to evaluate any tax structure is to examine how well it conforms to the normative principles of a "good tax". Some conflict between these criteria is, however, unavoidable and it is always necessary to evaluate the tradeoffs and seek some sort of balance among the advantages and disadvantages.

This type of exercise is valuable because it allows us to detect the most flagrant shortcomings of the tax structure, and it points to the

direction for reform. A list of the desirable criteria for the personal income tax in Grenada should include the following:

i. The tax should not be an impediment but rather contribute, to the main policy objective of the GOG: increasing the rate of economic growth led by an export oriented private sector. Among other things, this implies that the tax not create strong disincentives to work effort, investment and savings.

ii. The tax should be flexible or elastic, producing changes in revenue that are proportionate to changes in public expenditure requirements. In this way the tax becomes not only a reliable source of revenue but also an automatic stabilizer or macroeconomic activity. For the tax structure to play this role, income generated in most sectors of the economy, especially the fast growing ones, must be included in the tax base.

iii. The distribution of tax burdens should be fair, both horizontally and vertically. The tax is horizontally fair if those with the same income and under the same basic circumstances pay the same tax (independently of the source of their income). The tax is vertically fair if it taxes different income groups according to their ability to pay and reduces inequities in the distribution of income. Vertical equity is of course a much more subjective concept, and therefore more difficult to define, than horizontal equity.

iv. The tax should interfere in the least possible way with private decision making. That is, the tax should not induce changes in consumer and producer behavior, because those changes decrease individual well being without compensation somewhere else in the economy. To minimize these "excess burdens" the tax should not discriminate between sources or uses of income.

v. Finally, the administration of the tax should be economical and non-arbitrary. Tax forms should also be clear and simple to keep taxpayer compliance costs to a minimum.

III. An Evaluation of the Present Personal Income Tax Structure and of the Proposed Reforms

16. In this section we evaluate the tax base, rate structure, and administration in the light of the normative criteria listed in the previous section. We also review specific tax reforms recommended in two

recent fiscal documents, the Working Party Report, chaired by V. Callender, of June 1984 (hereafter the WP report) and Grenada: Agenda for Fiscal Reform, IMF - Fiscal Affairs Department, of August 1984 (hereafter the IMF report). We should emphasize that this evaluation is very tentative, because the treatment of certain perferences, etc. depends on the general income tax structure chosen. For example, one's view on exemptions and deductions may be quite different under a consumption-based tax than under a comprehensive income tax.

Issues Related to the Tax Base

17. The exemption of interest income is horizontally unfair because it discriminates against other forms of capital income (e.g., dividends) and against labor income. The exemption is also vertically unfair because it benefits those with a larger share of interest income in their total income--the higher income.

The exemption also creates excess burdens, and reduces incentives to equity investment--therefore retarding economic growth. Finally, it erodes the tax base, which reduces the revenue elasticity of the tax.

Three types of arguments may be used in favor of the exemption. First, it may be argued that the exemption is necessary to encourage small savers to open savings accounts at local banks. To achieve this desirable goal, however, it might be sufficient to exempt the first EC$200 or EC$300 of interest income. It can also be argued that the exemption is a compensation for the controlled low interest rates that are payed domestically. However, there are many other sources of income that are controlled in the Grenadian economy and they are not exempted from the

tax. This argument will also be irrelevant once interest rate policies are liberalized. Finally, it could be argued that by increasing the net return to savings, national saving and investment would increase. This is a more serious argument, but the empirical evidence on this issue in other countries is inconclusive and, at any rate, there is not reason to give special treatment only to interest income.

From the points just made it is clear that we agree with the IMF recommendation of eliminating the exempt status of interest income. The IMF report, however, advises not to do so until controls on interest rates are removed, inflation is controlled, and savers are insured a positive rate of return. The removal of the exemption must be coordinated not only with the total reform of the tax but also with other structural reforms in the economy. The last two conditions listed by the IMF are, however, impossible to insure and accepting them could delay the removal of the exemption forever. The removal of interest rate controls is likely to be sufficient most of the time to produce positive rates of return to savers. It should also be noted that the problems caused by inflation are not unique to interest income and are best dealt with in a comprehensive way.

The WP recommendations on this issue is quite different. It advises extending the exemption to include interest income <u>and</u> dividend income. We believe this recommendation is unjustified. While the double taxation of dividends is a very important issue, it is best dealt with in the reform of the company tax in which this tax is integrated with the personal income tax. Extending the exemption to dividends leaves

unanswered most of the criticisms addressed above with respect to the exemption of interest income.

18. The non-inclusion of capital gains in the definition of taxable income is subject to the basic criticisms (unfair, distortionary, etc.) addressed to the exclusion of interest income. In favor of the present policy, one could use the argument of administrative difficulties. But this argument carries little weight when only realized capital gains are taxed. The IMF and WP reports do not address this issue.

19. In principle all accrued income, including imputed income and in-kind benefits, should be taxed. The exclusion of imputed income from owner-occupied housing, although it may be justified on administrative grounds, is unfair and distortionary. Renters, who tend to be low income, are not allowed any housing expense deduction, and the greater rate of return to homeownership reduces investment in other, more productive sectors of the economy.

Once the cadastral roll for the property tax is completed and computerized, it may not be too costly to make imputations for owner-occupied housing income. The present law, after all, imputes income to employees from the housing provided by their companies.

Imputation may still be too cumbersome and it may be better to follow the IMF recommendation of not changing the exemption of imputed income from owner-occupied housing. We also agree with the IMF report, when it recommends strengthening the tax law provisions for the taxation of in-kind benefits. Specifically, the report recommends specifying the minimum imputed income for each benefit that will be taxable. Some other

options, however, should be considered. If the law specifies only the minimum amounts, there is a risk that only minimum amounts will be imputed.

20. The "contemplated" changes in legislation designed to partially exempt pension benefits are fundamentally inequitable. This is because contributions to qualified retirement plans are tax deductible.[6] Besides being unfair, the proposed exemption would further reduce the buoyancy of the tax and create (perhaps undesirable) incentives to early retirement.

It is difficult to come up with reasonable arguments that would support this exemption. For example, the low income of some pensioneers is not a relevant point, because low income taxpayers are, independently of their sources of income, exempted or taxed at lower rates. If a higher minimum exempt income is desirable, then it should be raised for everyone, not only pensioneers.

The WP report does recommend the elimination of taxes on pensions, but absolutely no effort is made there to justify this measure.

21. The lack of income averaging provision in the present income tax may have given rise to serious horizontal inequities. The policy probably has also discouraged work effort and investment in more risky activities. Neither of the two reports deals with this issue.

22. The lack of inflation adjustment has caused large increases in tax burdens in recent years, creating taxpayers' discontent and reluctance to comply with the tax. This type of tax increase is inherently arbitrary, not intended in the law, and very likely damaging to both

horizontal and vertical equity (e.g., the self-employed versus subject to PAYE).

While the WP report does not address this problem, the IMF advises "...to keep the taxable income brackets under constant review and adjust them in case the rate of inflation accelerates." This recommendation approaches policy from a discretionary point of view and it may be a little too vague. Questions such as, "at what rate of inflation or inflation change does an acceleration take place?" or "how frequently shoud brackets be adjusted?" have still to be answered. Consideration should also be given to some kind of automatic adjustment, for example the indexation of the income tax brackets.

As a final point, the problem of inflation adjustment has to be simultaneously considered with the reform of the income tax rate structure. The lack of inflation adjustment becomes less severe a problem, the less progressive the rate structure is. In the extreme case of a single flat tax rate, the problem completely disappears.[7]

23. The IMF report concludes that at the present time tax deductions are too numerous and too generous. We agree with most of that statement. Together, deductions and personal allowance considerably reduce the revenue elasticity of the tax.

The home mortgage interest payment deduction is the most conspicuous in its generosity. As in the case of the exemption of homeowner imputed income, this deduction discriminates against renters, eroding horizontal and vertical equity. It also creates distortions in the capital accumulation process by increasing the attractiveness of housing vis a vis other assets.

The deduction for life insurance premiums is much less generous, but still questionable at least on equity grounds. The most important issue concerning the treatment of contributions to pension funds, is the need to avoid double taxation. This would occur if both contributions and benefits are taxed. Of course the simultaneous deduction of the former and exemption of the latter are equally unjustifiable. The argument used in the IMF report against the life insurance policy and pension contribution deductions, that they encourage compulsory saving, is, on the other hand, not entirely compelling. Purchasing a private life insurance policy can hardly be seen as compulsory saving. Some other deductions, such as the overseas education deduction, may also be inequitable.

Limiting most of these deductions along the lines proposed by the IMF report appears reasonable. One exception concerns the limitation of the number of children eligible for child allowance. We do not find this recommendation justifiable.

An alternative, not considered in the IMF report, to the reduced but still independently itemized deductions, is a general "standard" deduction to be used with a much simpler tax form. Some thought should be given to this option.

Finally, the IMF report recommends converting all personal allowances into credits. While deductions, in principle, should be used for adjustments to gross income (to account for the cost of earning income), credits should be used for items or circumstances requiring special relief. The other important difference between deductions and credits is that while in the case of the former benefits increase with the marginal

income tax rate (bracket) of the taxpayer, in the case of the latter all taxpayers receive the same dollar benefits. Based on these two sets of notions, some of the IMF recommendations for conversion seems desirable, and we would take issue with some others. The WP report did not deal with any of these questions.

Issues Concerning the Tax Rate Structure

24. There is a general agreement tht the present rate structure is too steep.[8] The high marginal rates have produced disincentives to work effort,[9] savings, investment, and risk taking behavior. The high rates have also very likely encouraged resistance and lack of compliance.[10]

On the surface, it appears that the steep progressivity of the rate structure has at least served the goal of an equitable distribution of the tax. The evidence available so far points at a quite progressive distribution of burdens.[11]

Because of the unknown but potentially large degree of tax evasion by the self-employed, the actual distribution of tax burdens may be less progressive than shown by the income tax returns. Those subject to withholding may at times pay more than self-employed taxpayers with higher incomes.

25. Both the IMF and WP reports recommend reforms of the rate structure. Specifically, the IMF report suggests the removal of the 60 and 65 percent rates, and putting a cap of 35 percent on the maximum average effective rate. This report also recommends a lowering of all rates when "the revenue situation permits". The WP report essentially leaves the highest marginal rate of 65 percent the same, introduces more

intermediate rates and widens the income brackets, effectively slowing down the progressivity of the present tax burdens.

The common characteristic of both sets of recommendations is the timidity of the proposed changes. This in part may emanate from an overwhelming concern about revenue losses. Such small changes, however, will likely have very little impact on the present disincentive effect, on work effort, investment, and risk taking behavior. That is, these reforms do not support strongly enough the policy goal of fast economic growth led by the private sector.

26. The main problem with a bolder reform of the tax structure, besides the revenue losses, is the potential sacrifice of a progressive distribution of tax burdens.

Acutally, no one can state with certainty what is the proper degree of tax burden progressivity. For many, a flat proportional tax is equally defendable. The level of progressivity, on the other hand, is not only a function of the rate structure, but also of the minimum level of income that is not taxed, i.e, the level of exemptions, deductions, or tax credits. For example, a flat proportional income tax can be made quite progressive through exemptions and deductions.

In the matter of the implied revenue losses, it is likely that a comprehensive reform of the personal income tax (including the elimination or reduction of some existing deductions, and administrative reform) will allow, on a zero revenue loss basis, a greater rate reduction. Actually, the IMF report estimates that through better assessments and improved tax

collections, revenues could increase in EC$1 million. The corresponding estimate in the WP report is between EC$3 million and EC$5 million.

There is a need to consider the issue of rate structure reform in an integrated way with the rest of the reforms being proposed. When the data from the personal income tax returns, already collected, are read into the computer and analyzed, it will become possible to consider the revenue and burden progressivity implications of various blueprints (base and tax structure) of the new income tax.

Issues Concerning Tax Administration

27. There is complete agreement on the need to improve the administration of the personal income tax. The present tax evasion by the self-employed, besides reducing revenue elasticity compromises the horizontal and vertical equity of the tax.

Even though the IRD does a good job, given the resources available, there is an obvious need for training in basic accounting, and in desk and field auditing methods.

We agree in this area with many of the assessment and recommendations contained in the IMF report (See Fiscal Memorandum No. 13). Outside technical assistance will be needed.

IV. Some Recommendations and Scope of Future Work Needed for a structural Reform of the Personal Income Tax.

28. In this final section we list some very preliminary recommendations which follow from the analysis in Section III. We also indicate what extra work will be needed to undertake a structural reform of the personal income tax.

The GOG needs to carefully study the options of a personal consumption tax vs. a comprehensive income tax.

29. The new income tax should not exempt interest income. At most, only the first EC$200 or EC$300 should be tax exempt.

30. Consider the taxation of realized capital gains.

31. The new income tax should provide in much more detail, for the taxation of in-kind benefits. This requires further study.

32. Some consideration should be given to the imputation of income from owner-occupied housing. Otherwise renters should receive an equivalent advantage.

33. Do not implement the exemption for pension benefits, "contemplated" by the Interim Council in August 1984.

34. Give consideration to some kind of provision for income averaging unless the new tax rate structure is relatively flat.

35. Give consideration to the indexation of the tax rate brackets to avoid the arbitrary increases in tax burdens produced by generalized inflation.

36. Eliminate or drastically reduce the mortgage interest deduction. As a second best, grant equivalent benefits to renters.

37. Reduce life insurance, qualified pension fund and overseas deductions. The treatment of pension contributions must be coordinated with the treatment of pension benefits.

38. Study the introduction of a general "standard" deduction as an alternative to the itemized deductions.

39. Study the revenue and incidence impact of converting all personal allowances into credits.

40. Study the revenue and incidence impact of different tax rate structures, including, but not limited to, those mentioned in the WP and IMF reports. The possibility of a flatter rate structure should be given serious consideration.

41. Undertake, along the lines of the recommendations contained in G.W. Whitehouse's Fiscal Memorandum No. 13 and the IMF report, a training program in basic accounting and auditing techniques. Upgrade and implement the modified assessment manual to reduce tax avoidance and fraud by the self-employed. Upgrade the position of tax collectors. Revise civil and criminal penalties.

43. The tax form should be simplified. An alternative reduced tax form (without any itemized deductions) should also be considered.

44. Study the integration of the personal and company income taxes to avoid double taxation of dividends. The IMF recommendation on this issue should be considered along with other possibilities.

45. Develop a timetable to phase in the new tax, paying special attention to the implied revenue losses, and in coordination with other aspects of the tax reform. Because tax administration improvements and their impact on revenues will likely take place over a period of two to three years, the new tax shoud be phased in over a similar time span.

ENDNOTES

* I have greatly benefited from conversations with Mr. Basil Harford.

1. Non-resident incomes are subject to a withholding tax (with rates of 20 and 25 percent) and exempt from the personal income tax. Little revenue is collected from individuals with this tax.

2. According to the Inland Revenue Department (IRD) a grocer with a family of four can be imputed up to EC$4,000 of income.

3. The Retail Price Index estimate for 1984 is 142.6 (100 for 1980), according to the Ministry of Finance (MOF) Statistical Office and IMF estimates.

4. Because capital gains are not presently taxed, no inflationary increases in tax burdens have occurred in this area.

5. Tax paid divided by total assessable income.

6. Some pension plans are non-contributory.

7. If capital gains were taxed, they would have to be adjusted for inflation even in the case of a single flat rate.

8. See Table 15 of the IMF report for a comparison with the rate structure of neighboring countries.

9. Some evidence of this is provided by the reported reluctance and refusal of some employees to work extra-time.

10. Some evidence is provided by the increasing role of in-kind compensations.

11. See Tables 20 and 21 of the IMF report for the tax paid by a hypothetical taxpayer at different levels of income. See also tables 22 and 23 of the same report for the actual distribution of tax burdens for taxable income above EC$25,000.

FISCAL MEMORANDUM NO. 6

THE COMPANY TAX IN GRENADA: AN EVALUATION OF PRESENT STRUCTURE AND PROPOSED REFORMS, SOME RECOMMENDATIONS AND SCOPE OF NEEDED FUTURE WORK

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GRENADA TAX PROJECT

Fiscal Memorandum No. 6

TO: Mr. Lauriston Wilson, Jnr.
FROM: Jorge Martinez
DATE: September 7, 1984 (revised September 26, 1984)
RE: The Company Tax in Grenada: An Evaluation of Present Structure and Proposed Reforms, some Recommendations and Scope of Needed Future Work

I. The Present Company Tax Structure

1. The Company Tax has played a decreasing role in Government Revenue over recent years. From 15.8 percent of total tax revenue and 3.7 percent of GDP in 1980, company tax revenue had dropped to 11.4 percent of total revenues and 2.7 percent of GDP in 1983.

The number of firms covered by the tax has been decreasing over the last few years and it is now around 140. Of this number, less than 30 percent have "gross sales" over EC$1 million. The bulk of the tax revenue is levied, as it is typical of other countries, on a smaller number of large companies, around fifteen.

We have collected in collaboration with the Inland Revenue Department (IRD), data from all company tax returns due on 1982 income (Year of assessment 1983). Once those data are read into the computer and analyzed, we will have a clearer picture of the structure of the present company tax base.

There are multiple causes for the poor performance of the tax, including the weak general performance of the economy, and the poor

investment climate in recent years. But the structure of the company tax itself, we believe, is partly responsible for this poor record. Witness for example, the repeated increases in the statutory tax rate to the present discouraging levels.

Tax Base

2. The Company tax is levied on world-wide income, including gains from the sale of business assets, of all resident companies. Intercompany dividends are excluded.[1] Because of their non-for-profit status, the four growers associations are exempted from the tax and so is the National Importing Board. Non-resident companies are taxed only on business income originated in Grenada.[2]

3. The expenses incurred during production, including interest, are deductible. There are special provisions for insurance companies, which are allowed to build (deduct as a business expense) reserves for outstanding risks. Banks, however, are not allowed to build special reserves for "bad-loans."

4. To prevent certain abuses, the law empowers the Comptroller of Inland Revenue to disallow some deductions. For example, foreign affiliates have an incentive to expatriate profits through deductible items (interest, royalties, etc.) Similarly, closely held companies have incentives to distribute profits through deductible items such as wages or interest. The disallowed deductions are taxed profits.

5. Real assets can be depreciated only at original or purchase cost and on a straight line basis. The rates range from 2.5 percent for buildings to 33 1/3 percent for aircraft equipment. Faster depreciation

rates can be granted in special cases, such as intense use of plant and equipment because of multiple shifts. The incentive depreciation allowance of 10 percent is granted on top of the normal allowance for the purchase of plant and equipment by qualified industrial businesses. There is no provision for depletion allowances.

6. Inventory accounting of stock-held in trade is done on a first-in first-out basis.

7. The law does not provide for any kind of inflation adjustment of the tax base. During inflationary periods, the replacement cost of capital will generally exceed original prices, hence, depreciating on a historical cost basis artificially inflates profits. Taxes therefore, are larger than they "should be." Similarly, with increasing costs of production during an inflationary period, valuing inventories on a first-in-first-out basis makes profits to look larger than they actually are. Taxes are again increased with no counterpart increase in real profits.

Offsetting forces may be at work, on the other hand, if inflation has not been anticipated or for other reasons (e.g., usury laws), it has not been incorporated in the nominal interest rates companies are charged on their borrowings. In this case, the real value of the companies' liabilities goes own, increasing real profits without increasing taxes.

8. By law, losses cannot be carried forward beyond a period of three years, and in any particular year the losses to be deducted cannot exceed one-half of the company's net income.[3]

9. In addition to the incentives for business investment in the income tax law, the GOG is at present drafting an Investment Code which provides far more generous incentives. For example, new businesses with a domestic value added content of at least 50 percent would be granted a tax holiday (which includes complete exemption from the company tax) of 15 years. See also, Appendix 1 of the IMF Report for other legislation presently in force providing incentives for business investment.

10. There is no special provision in the law concerning the double taxation of dividends. All profits, distributed and retained, are taxed at the same rate, and dividends are then taxed again as individual income.

11. Although the law contains provisions to avoid the double taxation of repatriated profits by non-residents, through the signing of international treaties, it is unclear which treaties are presently in force.

The Rate Structure

12. At present the company tax rate is 55 percent. The rate applicable to expansion of existing operations (since January 1982) is 45 percent. For new industries and hotels (since January 1982) the rate is 40 percent. Controlled companies (domestic companies with no more than five share holders) pay an excess tax at a rate of 15 percent on those profits that the Comptroller of Inland Revenue considers to be "insufficiently distributed."

Tax Administration

13. The IRD does not have a master roll of all the companies in the country, from the small number of companies presently filing, the tax

should not be very hard to administer. The IRD is, however, presently understaffed in terms of qualified personnel. Only three people, which includes the Comptroller, do field auditing for the enforcement of the company and personal income taxes. Actually, no field auditing of companies, including the fifteen or so large ones, has been performed in recent years.

The poor accounting practices of the small companies have not, of course, helped matters. Some companies have not filed returns in the last few years, and quite a few others only submit their account statements, leaving the IRD to complete the return.

Record keeping practices in the IRD are generally poor, especially in the area of investment incentives. Firms under a tax holiday do not have to file a return or keep any other kind of contact with the IRD. The Ministry of Industrial Development does not provide the IRD either with any information on the companies that have been granted favorable tax treatment. There is therefore, no knowledge of the revenue losses implied by the present tax incentive policies.

II. Normative Principles for a "Good"

Company Tax

14. The principles or criteria for a good company tax are quite similar to those of the personal income tax or any other tax.[4] But because of the lack of generality of the company tax (it taxes only capital income and then only capital income generated in the incorporated

company sector), some principles gain special importance while some others are to a large extent sacrificed from the outset.

15. Most investment in the private sector is likely to be undertaken by companies. The impact of the tax on company incentives to invest and to take risks is therefore of paramount importance in connection with the GOG objective of obtaining fast economic growth led by an export-oriented private sector. This is the reason why policies on particular issues such as the carry-forward of losses or repatriation of profits gain special significance.

16. Because in principle the tax falls on only one type of capital income, it therefore discriminates in favor of other types of capital income, as well as labor income. This violates the principle of horizontal equity. However, because shareholders are likely to belong to the upper ranges of the income distribution, the tax presently, probably contributes to a more equal distribution of income and wealth in the country.[5]

Within the company sector itself, the principle of horizontal equity can be sacrificed, for example, by the concession of fiscal incentives to only new companies. These inequities should always be weighed against the benefits of a faster pace of investment and economic growth.

17. Because the tax falls only on business income from (incorporated) companies, it interferes with and distorts the process of investment in the private sector. In short, it gives an incentive to stay out of the company sector. Special provisions, selective incentives, etc., can further distort the investment process by affecting the relative prices of

different types of capital (e.g., short versus long lived) and of capital and other factors of production including labor.

18. As is the case for any tax, the law and tax forms should be simple so as to keep administration and compliance costs to a minimum. Still one must accept that the company tax has to be intrinsically complex because of the diversity of the economic base covered.

III. An Evaluation of the Company Tax Structure and of the Proposed Reforms

19. In this section we evaluate the present tax structure against the list of desirable criteria for a "good" company tax. We also evaluate the reforms recommended in the Working party (WP) report and the IMF fiscal report concerning the company tax.

Issues Related to the Tax Base

20. In the absence of inflation the present rates for depreciation allowances, on a straight line basis, seem to be adequate though a bit conservative.

The IMF report takes the view that the present rules may be encouraging too much capital intensity which is especially undesirable when the unemployment rate is as high as in Grenada. Without making a final judgement now, the apprehension shown in the IMF report may not be entirely justified, if onw takes into account other aspects such as risk, which has made investment opportunities in Grenada less than attractive. Witness the paucity of investment in the last few years. It is also

common in other countries to allow more liberal depreciation policies than those available in Grenada.[6]

Existing legislation and legislation being drafted (the Investment Code) on the other hand, appears to discriminate excessively against already established businesses.

21. The present depreciation allowance policy, would not be adequate if inflation were to be significant. In an inflationary period, the present inventory accounting policy, on a first-in first-out basis would not be adequate either. To avoid the increase in tax burdens and therefore the discouragement of investment, capital assets should be depreciated at replacement cost, or some other type of inflation adjustment should be allowed. Inventories should in turn, be valued on a last-in first-out basis, which automatically excludes the artificial gains introduced by inflation. Both of these recommendations are made in the IMF report. The WP Report does not mention this issue.

The proglem with the above policy changes is, besides the potential large cost in revenue losses, the considerably higher demands placed on administration. The recommendations should therefore be carefully reassessed after technical assistance for training of IRD personnel is decided upon.

22. There is agreement that the present policy of allowing carry-forward of losses for a maximum period of three years, and limiting any year loss-offset to 50 percent of net income, is unduly restricted. The policy is more restrictive than the one practiced in most countries.

Interestingly enough, under the Caricom Harmonization of Fiscal Incentives Agreement the loss-offset period is of five years.

We agree with the IMF recommendations of liberalizing the carry-forward of losses period to at least five years and imposing no limit on the loss-offset allowed in any year. The present draft of the new Investment Code actually offers a carry-forward period of five years. Horizontal equity would require that existing companies are granted the same advantage.

A carry-forward period of over three years will be difficult to administer, especially given the poor accounting practices of some Grenadian businesses. But a better trained income tax administration will be better able to enforce the law and it may provide an "incentive" for local firms to keep better accounting records. It will be to their own benefit to be able to document that losses actually existed.

23. This is not the right place for an in-depth evaluation of the investment incentives presently being considered. The importance of the issue demands a separate and comprehensive study. What seems evident at the moment is that there will be a need to coordinate or integrate the reformed company income tax and the new Investment Code. if the reformed company tax contains more liberal deductions and lower tax rates, the scale of the fiscal incentives could be brought down. There also is a need to have a less discriminatory treatment toward existing firms.

24. While under the present tax law, interest costs are fully deductible, no deduction is allowed for the opportunity cost of equity capital. Instead, income from equity capital, including opportunity

costs, is taxed by the company tax, and the portion that is distributed as dividends is taxed again under the personal income tax. This process creates a distortion against equity capital, and at the same time invites tax arbitraging through debt financing. The funds that otherwise would have been used in equity financing can be lent out, with interest payments free of tax, and the principal used as collateral to obtain an equal sum in loans.

The fact that distributed profits are taxed twice also invites the retention of profits. If capital gains are not subject to the individual income tax, as is the case in Grenada, profit retention tends to become a true bargain. If the market for company shares in Grenada were larger and more active, there would be little reason to distribute profits in the form of dividends. The present law actually anticipates that possibility and penalizes, with a 15 percent surtax, insufficient distributions by "controlled" companies. But even in this case, if company shareholders are in a personal income tax bracket above 15 percent, they can profit by receiving all their company income via retention (capital gains).

[illegible] taxing capital gains as recommended in Memorandum No. 5, there is obviously a need to integrate the company and personal income taxes to avoid the double taxation of dividends.

This need for integration is expressed in both the WP report and the IMF Report. This latter in particular recommends a return to full or partial imputation of dividends, in force until 1982, whereby shareholders were granted a tax credit for the company tax they had paid on dividends. This is one of the procedures available for the integration of personal

and company income taxes and it is known as the "dividends--received credit" or withholding method.

True integration of both taxes would mean that the company tax is only used to insure that the profits accruing to any shareholder are taxed at his personal tax rates.[7]

If capital gains (the way in which non-distributed profits accrue to shareholders) were not taxed as is presently the case in Grenada, then using a partial integration system (for individuals only) is the appropriate way to proceed. The "dividends-received credit" method recommended in the IMF report is a partial integration method. Another one is known as the "dividends-paid" method.[8]

When capital gains are taxed under the individual tax, a fuller integration is desirable. Full integration, however, almost implies the elimination of the company tax. Under full integration you can either impute company profits to shareholders and tax them as personal income,[9] or you tax all capital gains (realized and not) under the personal tax.[10]

It is clear from this brief analysis that full integration is hardly a practical proposition, given the administrative difficulties involved.

To follow the IMF recommendation may then be the most desirable way to proceed. The revenue costs of this alternative or any other, however, needs to be established. We think we will be able to do that once the company return data are analyzed.

Issues Concerning the Tax Rate

26. There is agreement that the present rate of 55 percent is extremely high and that this feature of the tax may have played a very important role in discouraging investment in the recent past.

Both the WP report and the IMF report recommend, not surprisingly, cuts in the rate: the former cuts the rate to 50 percent and the latter to no more than 45 percent. None of the two reports analyzes the revenue losses implied by their recommendations. With the company data collected, we again hope to be able to establish the revenue implications of 50 and 45 percent rates. In our opinion even a lower rate of 40 percent should be considered, because of the potential impact on investment and risk-taking.

IV. Some Recommendations and Scope of Future Work Needed for a Structural Reform of the Company Tax

27. Estimate the revenue losses implied by the present system of exemptions and any new proposals in this area.

28. Undertake a re-examination of the institutions presently enjoying a tax exempt status.

29. Retain the exemption of intercorporate dividends.

30. Give some consideration to special deduction to particular economic sectors (e.g., a bad-debt reserve for commercial banks).

31. Study the possibility of giving firms a choice of depreciation methods, including accelerated depreciation. The IMF concerns over distortions are perhaps a little overplayed.

32. In conjunction with. training policy, study the possibility of allowing firms to depreciate assets at replacement cost and to value inventories on a last-in first-out basis. Consider other possible ways of adjusting the tax base for inflation.

33. If capital gains were to remain largely untaxed, consider the expansion to all companies of the surtax penalizing excess retained earnings in closely held companies.

34. Liberalize the loss-offset period and do not impose any annual limits to the deduction.

35. Current policy design of tax incentives does not seem to have enoukgh input from the MOF. There is a need to integrate the new investment code and the reformed company tax.

36. One area of this integration that deserves special attention is the severity of discrimination against already established firms.

37. The issues of tax incentives to foreign investors, double taxation treaties, and repatriation of profits need to be simultaneously reconsidered. There is, for example, little value to granting generous tax incentives if the tax revenue sacrifice eventually ends up in another government treasury. Other questions such as whether repatriated tax holiday profits should be exempt from the withholding tax require further study.

The GOG should, in the framework of the regional associations, forcefully seek the establishment of international tax treaties. An inventory of treaties presently in force should be undertaken.

Study the most efficient and equitable way to integrate the personal and company income taxes. Establish, at the same time, the revenue loss, and if possible the administration costs, of the preferred integration methods.

40. Study the revenue implications in an integrated fashion (i.e., taking into account other proposed reforms of the company tax) of cutting the present rate to 50, 45, and 40 percent.

41. Study the desirability of giving preferential treatment (e.g., lower rates) to small companies.

42. Study the possibility of enlarging the company base by taxing the economic activity of non-resident companies in Grenada. For example, even though (by law) non-resident shipping and airline companies are supposed to be taxed on 2 percent of gross receipts originating in Grenada, at present they are not. It has also been suggested that for example foreign credit card companies could be taxed on fees originating in Grenada.

43. Concerning administration of the tax, there is a need to improve the assessment and audit capabilities of the IRD. For detailed recommendation on field auditing, etc., see Mr. Whitehouse's Fiscal Memorandum No. 13.

44. The IRD should maintain and update a company master roll to keep track of compliance.

45. All companies, including those under tax holidays, should file a tax return (even when nothing is due) and financial statements with the IRD annually. This is especially important if under the new investment code tax-holiday companies will enjoy a loss carry-forward period of five

years. There will be an obvious incentive to create artificial losses toward the end of the tax holiday period. The Ministry of Industrial Development should provide the IRD with a list of companies that have been granted tax incentives, as well as with a detailed description of each firm's incentives.

46. There will be, of course, a need to revise the company tax form. Private sector input on the format would be desirable. The IRD should also offer help, at least initially, on how to properly fill out the return.

47. The phasing-in of the new company tax needs to be coordinated with the training program in the IRD and with the rest of the fiscal

ENDNOTES

1. There exist special provisions for some companies. Life Insurance companies' assessable income is computed as equal to 10 percent of their gross investment income.

2. Companies, by law, must withhold tax on dividend, interest, and other payments made by them to non-residents. Most of the withholding tax revenue accrues through this source.

3. See section 40 of the 1980 Income Tax Law. Subsection 3 is somewhat confusing and could be interpreted as imposing no time limit for most losses.

4. See Section II of Fiscal Memorandum Number 5.

5. The company tax burden may be shifted forward to consumers in the form of higher prices, or backward to other forms of capital or even to labor in the form of lower rates of return and lower wages. The final incidence of the tax is a controversial issue and the final answer depends among other things of the company sector economic structure (e.g., degree of monopoly power, etc.). If the tax is shifted forward to consumers it becomes virtually inequitable.

6. This is typically done by granting businesses the opportunity to use accelerated depreciation (e.g., the double declining balance method or the sum-of-years-digits method). These policies tend to be, however, more distortionary than the straight line method. Granting first eyar additional allowances as is presently done in Grenada is more desirable.

7. That is, from a strict integrationist viewpoint, the company tax should not exist if companies were not allowed to retain profits.

8. In this case, dividends are excluded from the company tax base, i.e., the company tax applies only to retained earnings.

9. This is known for obvious reasons, as the partnership method.

10. This is known, again for obvious reasons, as the partnership method.

FISCAL MEMORANDUM NO. 7

THE PROPERTY TAX IN GRENADA: AN EVALUATION OF PRESENT STRUCTURE AND PROPOSED REFORMS, SOME RECOMMENDATIONS, AND SCOPE OF NEEDED FUTURE WORK

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GRENADA TAX PROJECT

Fiscal Memorandum No. 7

TO: Mr. Lauriston Wilson Jnr.
FROM: Jorge Martinez
DATE: Setember 14, 1984 (Revised, September 25, 1984)
RE: The Property Tax in Grenada: An Evaluation of Present Structure and Proposed Reforms; Some Recommendations, and Scope of Needed Future Work.*

I. The Present Property Tax Structure

1. The tax was reformed in 1981, moving away from the British tradition of assessments based on the rental income of properties, to the method of assessing the tax on the market value of the property. As remarked in the Working Party report, this was a step in the right direction since the new tax encourages fuller use of land and structures.

The reform, however, has not been completed. The property tax has yet to fill its potential in the Grenadian tax structure. Revenue from the property tax remained stagnant between 1978 and 1981 at EC$0.8 million, and decreased slightly after the reform. The property tax share in total revenues fell from 2 percent in 1978 to 0.9 percent in 1983. This performance can and should be reversed by both completing and amending the reform begun in 1981.

The Tax Base

2. The tax is levied on the market value of all land and structures, with no differentiation made between market value and assessed value. No other type of property (other than real estate) is covered by the tax.[1]

Government property is tax exempt as is property used for educational, religious, and some other purposes. Residential properties with market value of under EC$15,000 are also exempt. Exempt status can also be granted by ministerial discretion.

3. There is little available information on the composition or structure of the property tax base. We do not know, for example, what proportion of the tax base is exempt, or what proportion is residential or commercial.[2]

Some information on agricultural land is contained in the 1981 Grenada Agricultural Census. In that year, there were approximately 8,200 farms with an average size of 4.2 acres. Of the total, 68 percent of the farms were 2 acres and less and only 5 percent, 10 acres or over.[3] Present prices can be as high as EC$4,000 per half acre.

The Rate Structure

4. The rate structure differentiates between agricultural property, taxed at 0.1 percent, industrial and commercial property, taxed at 0.8 percent, and residential property. This latter, above the maximum exempt value of less than EC$15,000, pays according to a progressive structure. For residential properties with market values between EC$15,000 and EC$40,000 the rate is 0.1 percent for those between EC$40,000 and EC$100,000, 0.25 percent; for properties between EC$100,000 and EC$200,000, 0.4 percent, and for those above EC$200,000 the rate is 0.5 percent.

Property Tax Administration

5. At the time of the reform of the tax a Property Valuation Division was created within Inland Revenue. The new Division was supposed to complete a market valuation list (close to a cadastre) for all properties in the country. A Valuation officer worked on this from 1981 to 1983. In the present the position of valuation officer is vacant.[4]

It is not possible to state with confidence, at the present time what proportion of all properties were valued between 1981 and 1983, because no one knows the total number of parcels to be valued. Figures between 50,000 and 100,000 have been used in the past. Similarly, the cadastre has been reported as 50 and even 70 percent completed, but the actual percentage may be much smaller, as discussed below.

Taxpayers whose property has not been valued still pay their property tax on the old rental assessment basis. Actually, the entire collection of the tax is still based on the taxpayer list from the old tax with a ledger for each of the six parishes. The only change the reform has brought is that for some of the entries (owner names) in the ledgers, the rental assessment has been replaced with a market value assessment.

To keep the property tax roll updated, the registry, by law, is supposed to send to the IRD monthly information on all transactions, including the names of buyers and sellers and prices. The Registry, however, has never complied with this obligation, and taxpayer rolls are quite outdated allowing new property owners to evade the tax.[5]

The Property Valuation List ("Cadastre")

6. The property valuation information collected between 1981 and 1983 is contained in "books", two for each parish, separating parcels with and without buildings. Each parish book contains information by town, villages, estates, etc. which are set in alphabetical order. Within towns, information is classified by streets, and the final entries are of owners (not parcels) set again in alphabetical order. Besides the name of the owner, each entry contains some imprecise information on location of the parcel, present use (residential, commercial or agricultural), assessed value and tax. Properly speaking, therefore, the present valuation list can not be called a fiscal cadastre. In a useful cadastre, each parcel is plotted on a mpa, given an identification number, and described in various ways.

The likely reason why the present valuation list was not done properly is the lack of maps which are essential to the cadastral exercise. The only maps that were available for reference were photogrammetric plots of St. George's and the rest of the south-west area of the island. However, only buildings, not parcels, were identified.[6] The work one between 1981 and 1983 covered the whole island so it is not possible to identify what areas contain the largest number of unassessed parcels.

For each property assessed, when the owner could be found, a valuation questionnaire (data sheet) was filled out, specifying a number of structure and lot characteristics.[7] On the back of the questionnaire, the assessor also wrote the outside dimensions of the building(s). These

data were not given explicit weights, adn they do not appear to have been used in any formula or statistical technique to arrive at market value.

7. The usefulness of the valuation list is limited not only because of the lack of direct information on parcels but also because of difficulty of establishing the accuracy or quality of the valuations.

The number of valuations that were contested furing the 1981-83 period are believed to have been around 15 percent. This may be taken as indicative of lack of excessive disagreement by owners, at least on the over-valuation side, with the assessors' estimates. Some of the valuations made in 1981, on the other hand, may not be outdated, especially in areas such as St. George's, Grand Anse, etc., where land prices have increased significantly during 1984.

The proper way to evaluate the quality of the present valuation list would be to field assess a random sample of properties and compare the results to those in the unfinished "cadastre."[8] Field assessment will not be made easy by the thinness of well identified markets and the paucity of transactions.

In lieu of field assessments, we used recent market sales data obtained from the Registry, in a preliminary attempt to evaluate the quality of the unfinished "cadastre." Of the 225 initial sales extracted from the Registry, only 20 could be matched with entries in the existing valuation list or "cadastre." This low number of matches is a reflection first of the way the present valuation list is kept. If the property is transferred or sold, the new owner's name may never be entered in the list. If the list was kept by parcel numbers instead, the entry would

always remain active regardless of changes in ownership or title. The second reason for the low number of matches between the Registry information may be that the valuation list is indeed much more incomplete than what had been previously, anticipated.

For the twenty parcels that were matched, the differences between market values as collected in the Registry and the assessed values in the "cadastre" were quite large. The absolute value of the error ranged up to 300 percent of market value, for low value parcels.[9] For more expensive properties, the relative errors were more moderate, but still high, typically around 30 percent--as high as 207 percent and as low as 5 percent.[10]

One final point should be raised in consideration to the "veracity" of the market price information extracted from the Registry. Because real estate transactions are subject to a stamp duty, there is an incentive to underdeclare the value of the asset. This phenomenon is less likely to occur, however, when transactions involve banks through mortgage financing. For some of the transactions involving bank financing, the error was still large.

Penalties

8. At present the prenalty for non-payment is 5 percent of the tax due, with no interest charge. When taxes become due over a year, the comptroller of Inland Revenue can issue warrants for the sale of property. This provision, it seems, has not been used. The IMF Report states that in the case of an objection, there is no provision requiring the tax to be paid in advance of the appeals. However, Section 7 of the Taxes

Management (Amendment) Law of 1982 seems to establish the obligation to pay regardless of appeals, as well as the right to be refunded if the appeal is won by the taxpayer.

II. An Evaluation of the Property Tax Structure And Proposed Reforms

Issues Related to the Tax Base

Exemptions

9. There are no good theoretical reasons to exempt all forms of wealth other than real estate from the property tax base. There are, however, good administrative reasons to exclude certain forms of property (jewelry, intangibles, etc.) Other forms of property (e.g., automobiles and boats) still could be easily taxed.

The treatment under the property tax of small value real estate is anothe important issue. The exemption of low value residential property, as in Grenada, is desirable from a vertical equity viewpoint only if it applies to owner-occupied property and the owner is under a certain income level. The fact that no agricultural property is exempt in Grenada goes against horizonatal fairness.

The issue of low value agricultural property exemption is also important from an administrative viewpoint. Levying a property tax on all agricultural properties, regardless of size and value, will require including them in the fiscal cadastre. The cost of inclusion in the cadastre of 20,000 or so properties may be quite high. If we add annual recurrent tax collection costs, it may be worthwhile to sacrifice the EC$140,000 that the exemption may cost.[11]

Unfortunately, the exemption of small value agricultural parcels may create some problems.[12] In particular, it gives an incentive to sub-divide existing properties to (perhaps) less efficient sizes. Through artificial subdivision (i.e., by just nominally transferring ownership titles) one could also evade the tax. Basing the exemption on total personal property, holdings will just be a partial solution.

Site-Value and Improvements

10. Under the present law, both land (with its improvements) and structures are valued and taxed together. This approach tends to discourage improvements of all kinds because the tax burden increases proportionately with the value of the improvements.

As an alternative, it is grequently suggested that the site-value and improvements (structures) should be assessed separately.[13] This would allow the heavier taxing of site-value, thus encouraging the most productive use of the land, and taxing the value of improvements at a much lower rate so to minimize disincentives to improvement expenditure.

Betterment Levy and Special Assessments

11. The property tax can be justified not only on the grounds of the higher ability to pay of wealthier individuals, but also in terms of the benefits individuals receive from government services which may eventually raise the market value of their property holdings.

In the event of property value increases due to particular government services, even a good fiscal cadastre, updated every five years, may not be adequate to capture the variety of market value changes. In Grenada,

this is a relevant issue because of the massive infrastructure programs that are currently being implemented.

Two approaches are possible if it is deemed desirable to tax property value increases caused by particular government services. One approach is to undertake special reassessments of properties in the area(s) directly impacted by the new government services. These property base increases can be taxed at the standard rate. A second way to do it is to levy a "betterment tax" (which can be a once-and-for-all payment) on those properties directly benefiting from the new or increased services. This second approach is more justifiable when benefits can be measured quite directly (e.g., frontage of a sidewalk, paved access road, street lights, sewerage, etc.

Neither of the two reports, IMF or WP, dealt with property tax base questions.

Issues Related to the Tax Rate

12. In Grenada, it is quite common to use different tax rates for different uses of real estate property (residential, commercial, etc.) The present rates, however, may be too low.[14] For example, the agricultural rate of 0.1 percent may not justify in many cases the valuation and tax administration costs.[15]

The progressive rate structure on residential property in Grenada makes the tax harder to administer. There are other potentially undesirable effects of the progressive property tax rate structure. First, the progressive structure may not be vertically equitable since the tax applies to individual properties, rather than to the complete property

holdings of individuals. For this same reason, the progressive tax structure is very likely horizontally unfair. An individual owning a single property will pay more in property taxes than somebody else with the same real estate wealth divided into two or more properties. Finally, a progressive rate structure gives an incentive to the fragmentation of property. For reasons already discussed above, the fragmentation may not always be desirable.

Issues Concerning Tax Administration

13. The poor performance of the property tax is not surprising, given the present state of affairs in the Property Valuation Division. The WP Report and the IMF Report strongly agree on the need to fill the present vacancies in the division and on the need to complete the property valuation list.

From the evidence gathered so far, the present valuation list seems to be too incomplete and inaccurate to be of much value in the future. We think it is necessary to start a fiscal cadastre from ground zero. Technical assistance will be needed to do the cadastre and to train Grenadian valuation officers (See Olsen's Fiscal Memorandum No. 12). A good fiscal cadastre is vital to avoid inequities and to control taxpayer resistance to the tax. The cadastral exercise has potential value for other government institutions such as the Ministry of Agriculture and the Registry. The latter would benefit from a legal cadastre.

III. Some Recommendations and Scope of Future Needed Work for a Reform of the Property Tax

14. As in previous memoranda, in this section we list some recommendations which follow from the analysis in Section II. When it would be premature to give any firm recommendation, we indicate what extra work is needed to undertake a reform of the property tax.

15. Re-examine the desirability of maintaining the tax exempt status of all properties that have been granted that privelege by statute and by discretionary order.

16. Examine the possibility of taxing other types of property (wealth). Motor vehicles ownership is a good candidate. This may require reforming the present motor vehicle tax and license.

17. Study the proper exemption treatment of small value properties. The issues of vertical and horizontal equity, administration (including cadastral costs) and incentives to fragmentation have to be considered simultaneously.

18. The exemption of small value properties for residential use should only be granted if the owner-resident is below a certain income level. The treatment of small value properties that are rented requires further study. The answer here will depend on whether the property tax is shifted forward to tenants.

19. Examine the desirability (revenue, costs, efficiency, etc.) of taxing site-value and improvements at different rates.

20. Consider the use of special reassessments or of a betterment levy in those areas and cases where new government services and spending will increase property values.

21. Property tax rates are presently low and they should be raised.

22. Consider the substitution of the progressive rate structure for residential properties with a flat rate. Some minimum exempt property value[16] (e.g., what is known in the U.S. as a homestead exemption) would help to produce effectively progressive rates. Rate differentiation among the various uses of property (commercial, residential, etc.) may still be desirable.

23. Undertake the development of a new fiscal cadastre. The present valuation list is poorly organized, quite incomplete, and many of the assessments inaccurate or outdated. Technical assistance is needed in this area.

24. Before starting the cadastral exercise consider the usefulness of the cadastre (and variations thereof) in other areas of governmental activity. To this end consult among others with the ministries of Agriculture and Housing, and the Registry.

25. Make provisions for the periodical updating of the cadastre every three or five years. Up-to-date valuation information is essential for the horizontal and vertical equity of the tax as well as its buoyancy.

26. If it is found desirable to tax site-value and improvements at different rates, the cadastre will have to keep information on those two entries separately.

27. Information on the property tax mortgage deduction could be used to update the cadastre.

28. To the same end, renovation or improvement building permits could be required to be filed with the Valuation Division of the IRD.

29. To keep the Cadastre updated it will be necessary to train from two to four valuation officers.

30. Consider the possibility of computerizing the cadastral information. In the future more sophisticated valuation techniques (e.g., regression analysis) could be used. Easy and fast access to property information may also be important for auditing personal income tax returns.

31. It will also be much easier to keep the cadastre updated if the Registry complies with the law and sends monthly information on real state transactions to the IRD.

32. Fines for failure to pay should be increased and interest charged on the balance due.

33. The more effective way to ensure compliance would be to tie rightful ownership or title to the demonstration that property taxes have been actually paid.

34. Because the property tax reform and administration improvements have a great revenue potential, they should figure at the head of the list of the fiscal reform implementation plan.

ENDNOTES

* I wish to thank Mr. David Seales of the Valuation Division (IRD) for his assistance.

1. There is also a "Transfer Tax" on real estate transactions involving aliens as either buyers or sellers, and an Estate Duty. These taxes are discussed in Fiscal Memorandum Nos. 8 and 9.

2. No aggregate information exists either from the unfinished property valuation list or cadastre, which we discuss below.

3. State farms and farming cooperatives were much larger. Most of the former were over 100 acres and they represented 10 percent of all farmed land. Most co-ops were over 20 acres but represented only 1 percent of all farmed land.

4. The position of Assistant Valuation Officer apparently has never been filled.

5. Information is kept by owner's names rather than parcels.

6. The maps for the Northwest were produced by the Lands and Survey Division of the Ministry of Agriculture. There are not maps for other parts of the island.

7. See Appendix A.

8. It should be noted that property assessment is by no means an exact science and that regardless of the sophistication of the procedure employed, errors should be expected. But we do expect those errors to be small and random.

9. Parcels valued for example between EC$6 and EC$10,000.

10. See Appendix B for these data.

11. This figure is computed as the product of 20,000 parcels, an average small parcel value of EC$7000, and the 0.1 percent tax rate.

12. Small owners may sometimes be in favor of a small property levy as the means of re-certifying their ownership title on the property.

13. Site-value theoretically is the highest bid one could receive for the land (for any use) if the land were to be put for sale.

14. The IMF calls them the only reasonable rates in the whole Grenadian tax structure.

15. There is some concern that higher tax rates will be met with taxpayer resistance and lack of compliance. The property tax has been traditionally an unpopular tax everywhere. One possible reason may be its visibility (it is paid in one single installment). Horizontal inequities are also quite visible and probably play an important role in the unpopularity of the tax.

16. This minimum exempt which would apply to all properties should be distinguished from the total exempt of low value properties also discussed in the memorandum.

FISCAL MEMORANDUM NO. 8

THE TRANSFER TAX IN GRENADA. AN EVALUATION OF ITS STRUCTURE AND PROPOSED REFORMS

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GRENADA TAX PROJECT

Fiscal Memorandum No. 8

TO: Mr. Lauriston Wilson, Jnr.
FROM: Jorge Martinez
DATE: September 25, 1984
RE: The Transfer Tax in Grenada. An Evaluation of its Structure and Proposed Reforms

1. The tax is levied on the value of any transfer of land to or from a non-Grenadian citizen or company under alien control.

2. The present tax rates are high.[1] Aliens, either as buyers or sellers, pay 15 percent of the value of the parcel. When a Grenadian sells land to an alien, the Grenadian citizen pays also 5 percent of the transaction value.

3. The tax is administered by the Office of the Prime Minister (the office of the Chairman at the moment) and revenue collections have been negligible. Some tax evasion, especially for transactions between aliens, is likely occurring.

4. The main justification of the tax has obviously not been raising revenue, but discouraging land ownership by foreigners. Aliens' purchases of land could have, the reasoning goes, undesirable economic (e.g., higher prices for Grenadian nationals) and political consequences. However, taxing the sales by aliens to Grenadian nationals, as is presently done, runs counter to these policy objectives.

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[1] The rates are the highest among the countries in the region that tax similar transactions. See Table 18 of the IMF report.

5. The transfer tax would also be viewed as the closest thing in the Grenadian tax structure to a tax on capital gains, although a very crude and discriminatory one.

6. It appears that the high rates of the tax together with the overall economic and political climate in the recent past may have been all too successful in discouraging foreign interests.

7. We agree with the IMF recommendations that the tax rate should be reduced. This is especially desirable if capital gains under the new personal income tax (and withholding tax for aliens) become taxable.

8. If political apprehensions could be overcome, the transfer tax could actually be eliminated without any serious consequences. If the tax is kept, its administration should be transferred to the IRD from the Office of the Prime Minister.

FISCAL MEMORANDUM NO. 9

THE ESTATE DUTY IN GRENADA, AN EVALUATION OF ITS STRUCTURE AND PROPOSED REFORMS

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GRENADA TAX PROJECT

Fiscal Memorandum No. 9

TO: Mr. Lauriston Wilson, Jnr.
FROM: Jorge Martinez
DATE: September 25, 1984
RE: The Estate Duty in Grenada. An Evaluation of its Structure and Proposed Reforms

I. Structure and Administration

1. The tax is levied on the entire value of estates transferred at death. All gifts *inter vivos* made within five years of death are also added to the estate. The value of assets is estimated at market prices at the time of death and those estimates have to be approved by the comptroller of the IRD.

2. Real estate property outside the island is exempt and so are public pensions, some small charitable contributions donated for public purposes, funeral expenses, etc. An exemption of up to EC$100,000 is also granted for real estate property in Grenada, provided it was occupied by the deceased at the time of death and that it is passed on to a close relative.

3. The estate duty rates were last raised in 1979. The first EC$10,000 of estate value is exempt; on the next EC$10,000 the rate is 15 percent; on the next EC$130,000 it is 30 percent, and finally for values of over EC$150,000 the rate becomes 45 percent. All these rates are cut down by one-third when property is passed on to either parents, spouse or

children. The rates are raised by one-third when the recipient does not belong to a quite extensive list of distant relatives.

4. The tax is administered by the IRD and around 200 estate returns are processed each year. The total yield of the tax has fluctuated between EC$200,000 and EC$300,000. It is left to the estate's executor or administrator to file a return and some evasion does take place. Part of the real estate property that escaped estate duty is, however, uncovered at the time of sale or other transfer of title.

5. Penalties for non-filing are quite severe. Unless an extension has been granted by the Comptroller of Inland Revenue, failure to file--within 6 months of a death in Grenada, or within 12 months for a death anywhere else--raises the tax payable by 50 percent. Late filing estates are also charged a 10 percent annual interest rate on the amount payable. According to the IRD, the application of penalties is not an uncommon occurrence.

II. Evaluation and Reforms

6. The IMF report does not contain a detailed discussion of the estate duty. Nevertheless, the report considers that the rate structure, especially the top marginal rate of 45 percent, is extremely high, and that all rates could be cut without much revenue loss. The WP recommendation is more radical. It advises to completely eliminate the estate duty, but it does not contain any discussion of the tax.

7. There is wide recognition in the field of public finance that the estate duty could never become an important revenue producer. The tax is

quite generally seen and accepted as a useful instrument for redistributing income and wealth in the society.

8. Without getting into much doctrinnaire detail, one of the main positions taken against the tax has been to consider it unjust because it taxes accumulated income which had been previously taxed during the lifetime of the deceased. An opposing view holds that the estate is a necessary vehicle to correct for the lightly taxed or exempt income (e.g., capital gains) that accrued to the estate during the lifetime of the deceased.

9. One cannot make a recommendation about estate duty without knowing the reform proposed for income taxation. The two must be considered together. Under the right circumstances, one could agree with the proposal to drop the estate duty. Under other circumstances, one could recommend keeping the estate duty in the future Grenadian tax structure. The tax can play an important role as a potential equalizer of the distribution of private wealth. We also agree with the IMF report that the present rates should be reduced. In addition, the new tax would contain a more liberal treatment for those estates being transferred to spouse and children, i.e., besides the lower rates that would apply, certain percentage of the estate could be exempt when it is transferred to close relatives.

FISCAL MEMORANDUM NO. 10

THE INDIRECT TAX STRUCTURE AND EXPORT DUTIES

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GRENADA TAX PROJECT

Fiscal Memorandum No.10

TO: Mr. Lauriston Wilson, Jnr.
FROM: John Due
DATE: September 26, 1984
RE: The Indirect Tax Structure and Export Duties

The purpose of this paper is to provide a preliminary survey of the indirect tax structure of Grenada, suggest major defects and avenues of reform, indicate additional work that needs to be done and evaluate the proposals of the IMF study: Grenada: Agenda for Fiscal Reform (August 1984), and the Report of the Working Party. This paper is based upon extensive discussions with Mr. Patrick Bubb, the Comptroller of Customs; Mr. Basil Harford, Commissioner of Inland Revenues, review of the IMF report noted above, the World Bank Economic Memorandum on Grenada (August 1982), the report on Customs Administration by Mr. Kenneth Stacey, various customs tariff and related volumes and discussion with Mr. Jorge Martinez, resident representative of the Syracuse project. In view of Mr. Stacey's report, this paper does not deal, except incidentally, with Customs administration.

I. Survey and Evaluation of the Indirect Tax Structure and Proposals for Reform

The General Picture of the Revenue Importance of Indirect Taxes

Since detailed tables of revenues are available in the IMF report and elsewhere, only a brief summary will be given here.

1. Indirect taxes yielded, in 1983, 64 percent of all tax revenues, comparable to other small Caribbean countries.

2. Import duties of all forms, constituted 61 percent of all tax revenues or 93 percent of indirect taxes, an extremely high figure by comparison with other countries.

3. The taxes on foreign trade are highly complex, with six major levies and three specialized ones. Bases differ; a number of rates are specific, though most are ad valorem, and some taxes use both.

4. The combined rates of the taxes on imports are very high, equalling 26 percent of the value of imports despite exemptions, or 53 percent of the value of imports subject to duty. Basic foods carry combined rates of over 29 percent, and other foods from 37 to 86 percent. Nonfood consumer goods carry rates ranging from 48 percent to 96 percent, with some up to 1400 percent of the import values. While materials and capital goods are taxed less heavily, there is considerable tax burden ranging from 10 to 54 percent.[1]

5. Taxation of services and domestic transactions are very limited.

6. While relatively few commodities are exempt, exemptions to government, statutory bodies, and businesses favored under tax incentive legislation are substantial. In 1983, 57 percent of all imports entered free of duty.

7. The level of protection is very high.

8. Taxation of exports constituted 6 percent of total tax revenue in 1983. Revenues were derived primarily from nutmeg, mace, and cocoa. This figure is not included in the figure of indirect taxes above.

9. Tax revenues from import transactions are affected by import licensing, which was general for several years up to 1983, and is now limited to specific categories of goods.

The Various Taxes Applying to Imports

The complex picture of the taxes on imports defies simple summarization.

The Import Duties. The Customs tariff is that of the Eastern Caribbean Common Market (ECCM) from which Grenada cannot deviate unilaterally. This provides a common external tariff, and (with exceptions) duty does not apply to imports from ECCM countries. The ECCM tariff differs somewhat from the standard CARICOM tariff, with lesser breakdown of categories and higher rates on some goods.

The ECCM countries were authorized to apply duties on imports from other CARICOM countries from 1973 to 1983 because they were less developed. They are still continuing to do so; under present proposals rates will revert to 1973 levels in January 1985, but no final decision has been reached. These apply only to a limited range of high-revenue commodities.[2]

The ECCM tariff is not high by standards of developing countries; there are few rates above 30 percent and many at 5, 10, and 15 percent.

Much importing is done by the Grenada Marketing and National Importing Board, a government agency. Established to gain control over imports, it began with essential goods, then added others. But it became apparent that it was not getting the best deals. Its scope is now declining and phase-out is likely. It is still buying currently, however. The Board pays customs duty and sells primarily to the wholesale distributors, who also run retail businesses as well as selling to retailers.

A substantial amount of importing is done by retailers, through the Agency of Wholesale Firms. They began to do so when wholesaler-importers would not finance the transactions. There are no licensed brokers.

Many retailers now are Syrians and Asians, who have come from Trinidad, where they are linked with family firms in that country.

The Stamp Duty. This has become the major revenue element of the taxes on imports. Now imposed at a flat 15 percent ad valorem rate, it applies to the CIF price plus customs duty (as of 1983). Exempt are goods exempt from the ECCM tariff and government purchases, and a few others exempted under discretionary powers. Duty applies to imports from CARICOM, including ECCM.

This is not collected by stamps, but at customs clearance. Unable to raise import duties, Grenada imposed this tax as a device to raise more money at importation.

Consumption Duty. This levy has been introduced in several Caribbean countries--e.g. Barbados, Guyana, and Jamaica--to offset the loss of revenue when transactions between CARICOM countries were made duty free.

The tax is imposed on most consumption goods, at rates from 10 percent to 45 percent (on some 502 tariff items) plus 89 specific rates. The rates vary by commodity. The base is CIF value plus import duty. Consumption duty applies to imports from CARICOM, including ECCM.

By law and CARICOM requirements, the duty applies to both imported and domestically produced goods. But in fact, with exceptions noted below, it does not apply domestically for several reasons. Domestic production is small and collection is not cost effective. Customs lacks the staff to do an adequate job. These are struggling industries, which the government wants to encourage.

Domestic manufactures are taxed in only three categories.

1. Rum. It should be noted that there is no custom duty on rum from CARICOM countries, though it could be imposed. Much rum is imported from CARICOM.

2. Beer

3. Cigarettes

There was application also to sugar, but this was eliminated because of the decline of the sugar industry.

Administration of these levies will be summarized below. Beer is subject to a low excise duty, and is the only excise now imposed.

"International Airport" Tax. In 1982, an additional tax, then of 2 percent, now of 5 percent, was levied to aid in the financing of the new airport, designed to lure tourists to the island. The tax is due to expire in 1985, when the airport is complete.

Initially, there were no exemptions, even imports from ECCM countries are taxed. Even now, there are only minor exemptions.

Package Tax. This is a low yield specific rate tax (first imposed 1968) on physical measurement of all imports without exemptions. The rate is 50 cents per 5 cubic feet, with a minimum tax of EC$1

This is purely a revenue measure, but the yield is very low.

Special-sector Indirect Taxes on Commodities.

1. The motor vehicle tax was originally called a "purchase tax", but the name changed for legal reasons. For dealers, this tax is applied at a 40 percent rate to the CIF value plus duty plus standard markup. The dealer pays when he sells the car, and a receipt of payment must be

provided before the car can be registered. On importation by a non-dealer, the base is the CIF value plus duty.[3]

The tax is administered by Inland Revenue.

2. The purchase tax on radios and TV sets. These are collected from dealers by Inland Revenue; on imports by individuals, tax must be paid before the goods can be cleared through customs. The tax is 20 percent of the selling price.

3. Tax on petroleum profit margins occurs when the import price falls but the domestic selling price (a controlled figure) does not. The amount is calculated by the energy unit of the Ministry of Planning and collected by Customs on the basis of monthly returns from the two importers--Shell and Texaco.

Foreign Exchange Tax. This is a 5 percent tax on foreign exchange purchases, collected by the banks and paid to the Ministry of Finance. This amounts to an additional tax on imports. Exchange to pay for certain basic foodstuffs and drugs is exempt.

Some Administrative Aspects of the Indirect Taxes

As noted above, this paper does not attempt to explore administrative aspects in detail. Four points, however, warrant mention.

The smuggling problem. This is serious and has become worse. There are several aspects:

- Beer, coming in primarily from St. Martin in small boats which make the trip primarily for cigarettes but bring beer also.
- Cigarettes, a major item.
- Whiskey, refrigerators, etc.

These come in small boats, much of them initially to the Grenadian island of Carriacou.

- Undervaluation on expensive items at the airport. Goods are bought cheaply in Panama, Miami, or New York. Fake invoices are obtained, and thus too little duty is paid. Particular trouble is encountered with imports by retailers from Trinidad (where wholesalers are controlled by the same family).

The boat smuggling is very difficult to control. The undervaluation requires trained valuation officers.

Personnel. The urgent need for training has been stressed in the Stacey Report (Fiscal Memorandum No. 11).

There is also a problem of loss of personnel due to inadequate salaries.

The training school in Trinidad has been satisfactory, but now is oriented more to the needs of Trinidad. Customs has always had problems in getting funds to send people, and in getting openings.

Collection of Consumption Duty is Limited to Three Products, as Noted Below.

1. Rum, this is made from local sugar to the extent of availability; some must be imported. All local rum is consumed locally; it is 140 proof, preferred in the rural areas. While import duty could be imposed on rum imported from CARICOM countries, this is not done. Originally some rum was imported for blending; more and more, the imported rum serves as the base and local rum is added for blending.

   There are two pot stills; the control seal is made where the rum comes out of the pot. The other still is a continuous one, with the usual seals, and checked by the inspector on the tank.

   Customs officers are not stationed in the distilleries, but are called when needed to unlock the facilities to permit shipment. The persons doing the work are specialized.

2. Beer, there is one brewery. Control techniques are similar, but check is made on release of sugar, and the officer checks more frequently.

3. Cigarettes, there is one local factory, using imported tobacco. Documentary control is used; nothing more is needed.

Inland revenue collection of the motor vehicle tax, purchase tax on radios and on TV sets, hotel and entertainment taxes.

1. The tax on motor vehicles, essentially a retail tax, is collected without difficulty because cars cannot be registered until tax is paid.

2. Tax on radios and TV sets is collected from the dealers, with monthly return and payment. There are about 20 dealers. A register is kept of these in Inland Revenues, and when returns are not filed an inspector checks. Some check is made on records. Inland Revenue believes that there is substantial escape from tax, as well as smuggling.

3. Hotels and guest houses report and pay on a monthly basis. If payment is not received, a phone call is made, and ultimately an inspector visits and checks the records. Little problem is encountered with the hotels, of which there are 12. The smaller guest houses (10) give more trouble. A register is kept by Inland Revenue.

4. Entertainment tax, mainly cinemas. Inland Revenue has relied mainly on the film booking agents for reported charges. Problems are encountered with small mobile units.

Inland Revenue does not have separate inspectors for these taxes, which are handled by income tax personnel.

Evaluation of the Indirect Taxes

Merits.

The indirect taxes produce substantial revenues.

2. High level administrators are obviously competent and interested in improvements in the duty structure and operation. The competence of the Comptroller of Customs is particularly impressive.

Objectionable Feature.

High reliance on taxes related to foreign trade. This is almost inevitable, given the nature of the economy, but some shift away is necessary and in time, possible. The existing combined burden on imported goods, including those used in the lower income groups is very heavy.

2. Complexity. The most serious objection is the use of several levies applying to imports: import duty, stamp tax, consumption duty, international airport duty, package tax (and foreign exchange levy). The coverage is not identical; some use specific rates, some ad valorem, some both. No document shows all levies by commodity class. Thus correct application of the tax is very difficult if not impossible.

3. Discretionary exemptions. The government has freed many imports by type of purchaser--government, semi-government agencies, tax holiday business. Some of these have merit, but in total they have seriously reduced yield.

4. Levying of some nominal taxes: the excise on beer (in addition to the consumption tax); the package tax (a source of great administrative nuisance).

5. Limited taxation of domestic transactions and services, including failure to conform with ECCM rules on consumption duty. This limitation results primarily from the nature of the economy, and there are currently only limited potentials.

6. Collection of the purchase tax on radios and TV sets from the retail dealers with inadequate controls.

7. Application of tax on meals only to hotels, not other restaurants.

8. Apparent provision of excessive protection.

9. Provision of protection by levies other than the import duties.

Administrative Inadequacies.

1. Lack of adequate training of personnel, at middle and lower levels.

2. Lack of a valuation program for Customs because of lack of trained personnel.

3. Low salaries for Customs personnel.

4. Substantial smuggling, very difficult to control.

5. Administration of motor vehicle tax, purchase tax or radios and TV sets, hotels and entertainment taxes by Inland Revenue instead of Customs. Such division of responsibility is undesirable. The tax on radios and TV sets is admittedly poorly enforced.

Direction of Proposed Reform

Constraints. Reforms must be considered in terms of major constraints: adherence to ECCM and CARICOM requirements; the nature of the economy; the availability of trained personnel; the need to protect revenue.

Some of the changes proposed will not be of much immediate consequence, but will head the indirect tax structure in the directions important as development continues.

Structural Reform.

1. Simplification. The most urgent change is simplification of the indirect tax structure, eliminating the stamp tax, the international airport tax, the package tax, the motor vehicle (purchase) tax, the purchase tax on radios and TV sets, the tax on petroleum profit margins, and the one excise (beer).

2. The import duties would, of necessity, remain unchanged, except for review of the duties applied temporarily to certain imports from CARICOM. The import duties alone would provide protection.

3. The primary revenue indirect tax would be a greatly revised consumption duty which would become in a sense a general sales tax on importation and domestic manufacture. This tax would be levied uniformly on imports and sales by domestic manufactures. Initially, perhaps 95 percent of the revenue would be collected at importation, but the domestic segment would increase with economic development.

While time does not permit provision of details of the proposed tax, a few key elements can be noted:

a. Commodity exemptions would be limited to fresh fruit, vegetables, fresh meat, and poultry; a few processed food items widely used by lower income groups; basic medicines.

b. To prevent cascading of tax, manufacturers would be able to buy or import materials and semi-finished goods in effect tax free. Preferably they should pay tax on these transactions but receive credit for the tax against tax due on their sales.

c. Exports would be free of tax, and exporters would receive refund of tax paid on raw material, etc.

d. The rate would be chosen in terms of revenue needs; the IMF report suggests a figure of 26 percent if a flat rate is used. This is high by comparison with rates on similar taxes in other developing countries, but may be necessary to protect revenue.

e. A single rate would simplify operation but, in terms of equity and discouraging imports of luxury goods, two basic rates might be used: 25 and 50 percent, for example. All rates would be ad valorem. Special rates would apply to beer, liquor, cigarettes, motor fuel and motor vehicles.

f. Manufacturers using only craft methods, with no mechanical power, would be exempt.

4. Excise taxes would not be used. There is no need for separate taxes on traditional excise goods; these can be reached by special consumption duty rates; as in Barbados. Separate excises simply increases complication. There is only one minor excise now, and it would be unwise to add more; this one should be repealed.

5. The consumption duty at a lower (10 percent) rate or a separate service tax, would apply to (a) hotels, (b) restaurants, excluding very small ones, (c) all telephone service, (d) entertainment, (e) possibly electric power. It is not operationally feasible to apply tax to a wide range of services.

6. The foreign exchange tax should be reconsidered. This is essentially another import levy, justifiable, if at all, only because of an overvalued exchange rate the country cannot alter.

7. It must be stressed that the primary immediate gain from the basic change proposed above is to lessen complexity and simplify operation of the taxes. There will be little increase in yield from taxes on domestic transactions for some years, as there is little domestic manufacturing. But the tax structure will be readjusted so as to reach domestic manufacturing as it develops.

Administrative Reforms.

1. Transfer all indirect tax administration to Customs and Excise; moving those now administered by Inland Revenue.

2. Establishment in Customs of a separate unit to specialize in domestic application of the Consumption Duty, and the taxes on services. This unit would be small initially but would grow in importance as domestic manufacturing increases.

The persons in this unit should have training in basic accounting, and ultimately in auditing. Given the small number of persons that would be involved, one person should be sent for training in a country using a sales tax at the manufacturing and import level. Canada would be a good choice.

The training and approach for control of taxes on domestic activity are quite different from those necessary for customs operation.

3. Provision of training for Customs Officers and Valuation Officers along the lines proposed in the Stacey report, FM No. 11. I have little

to add to his thorough report and take exception on only one issue. He suggests customs advice for training from the U.K. As alternative I would like to suggest Ireland and Canada. Both of these countries have similar backgrounds as the U.K. but are much smaller.

4. Salaries of customs personnel should be increased to allow retention of adequate personnel.

Appendix to Part I. Domestic Manufacturing

Domestic manufacturing is of limited importance, yielding no more than 4 percent of GNP. The major sectors are listed below.

1. Rum, three distilleries, as noted above.

2. Beer, one brewery, as noted above.

3. Cigarettes, one plant.

4. Garments, there were four. Two imported semi-finished goods and finished them. But a change in CARICOM rules in 1983 made it impossible for them to continue to import tax free and they have virtually closed down, with substantial goods in the pipeline. Two others, making sportswear, shirts, and pants, continue to operate, importing thin cloth tax free.

5. Soap, the factory is owned by a large wholesale firm. The factory was importing coconut oil from Dominica; it is now importing oil from the U.S., merely using local oil to blend, and thus endangering its tax and duty status.

6. Jams and jellies, now closed down. The firm produced from local fruit, but had to sell only locally because of lack of adequate health standards. Management (government) was poor, as was marketing.

7. Flour.

8. Perfume. Little more is done than blending and bottling.

There are of course soft drink bottling and food processing for local use. Most manufacturing is locally owned, independent of the wholesale firms.

II. The Export Duties

The export duties have been used for many years; the rates of many have not been changed since 1909.

A. The significant ones:

1. Cocoa: EC$.12 per cwt plus 20 percent of the amount by which price exceeds EC$.28 per pound.

2. Nutmeg, EC$.12 per CWT plus 20 percent of the amount by which the price exceeds EC$.14 per pound.

3. Mace, EC$.24 per CWT plus 20 percent on the excess over EC$.44 per pound.

4. Bananas, EC$.15 per 100 pounds.

B. Others, not operative as there are no exports.

1. Coconuts, EC$.24 per CWT.

2. Copra, EC$.06 per CWT plus 20 percent excess over EC$.05 per pound.

3. Cotton, EC$.24 per CWT; cottonseed, EC$.06 per CWT.

4. Limes, EC$.04 per 28 lb box, EC$.24 per 168 lb barrel; lime juice, raw, EC$.05 per 100 gallons; concentrate, EC$.24 per 100 gallons; lime oil, distilled, EC$.12 per pound; oil of nutmeg, EC$.02 per pound.

5. Animals, per head, donkeys, EC$2.50; cattle EC$2.50; goats EC$.50; horses EC$5.00; pigs EC$.75; poultry EC$.06; others EC$.50.

C. The significant export items except bananas, are marketed through producers associations, which buy from the producers and food

markets. The association notifies customs of exports, and pays the tax for clearance. All export sales are taxed, including those to CARICOM countries.

D. In the production of these crops:

1. Nutmeg is grown on "estates"--formerly British owned, now in part locally owned and in part government owned. There are also smaller producers who sell through the larger ones for processing; the average acreage is 3. After harvesting, the shell is removed, the nutmeg dried, crushed, and sprayed, before shipping. The mace is removed and crushed.

2. Cocoa is also produced on "estates," the pod is crushed, the cocoa fermented and dried. Small producers sell to the estates after crushing. This is a very labor intensive activity. The average acreage is 10.

3. Bananas are also largely grown on "estates" of 10 to 15 acres. Dealers pick up the banana from buying stations where the farmers take them, and haul them to the pier for loading.

E. The export duties are relatively heavy. The IMF report indicates that the export duty on Cocoa is equal to 20 percent of the growers price, on nutmeg, 32 percent; on bananas, negligible (p. 137). The report also concludes that there is little in the way of profits for the farmer after tax and in many instances costs are not covered.

F. Objections to the export duties:

1. The use of both a nominal specific cost and an ad valorem rate is an unnecessary complication.

2. The threshold figures have not been adjusted in terms of changing prices.

3. The taxes are severely burdening farmers who are, on the whole, barely covering costs. Thus export production is discouraged.

G. Proposed reform--the export duties should be eliminated because of the serious potential adverse effects on agriculture. If they are retained temporarily, the threshold figures should be raised to catch only windfall profits and the rates possibly made progressive. The specific cost levies should be repealed immediately together with the obsolete levies on crops and animals not reported.[5]

APPENDIX TO PART II

Major Export Commodities
Grenada 1978-82

	Quantity	Value EC$ (millions)	Quantity	Value EC$ (millions)
Nutmeg[a]	2.1	10.8	2.0	8.2
Bananas[b]	13.7	9.1	9.3	8.9
Mace[a]	.26	1.7	.33	2.5
Cocoa[a]	2.4	19.6	2.1	12.5
Clothing	---	1.0	---	6.7
Frest Fruit[a]	.4	.4	2.6	4.5

The principal buyers are (1982): Nutmeg, U.K., West Germany, USA, USSR; Bananas U.K.; Mace, West Germany, U.K.; Cocoa, U.K., Netherlands; Clothing, Trinidad; Fresh Fruit, Trinidad.

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[a]Million Kg

[b]Thousand tons

SOURCE: Grenada, Annual Digest of Trade Statistics, 1982.

III. Terms of Reference for a Longer Term Study

1. More thorough study of the Grenada economy, with reference to the nature of manufacturing, the nature of wholesale distribution, the

relationship among importers, wholesalers, manufacturers and retailers. Attention would be given to the nature of record and accounting systems.

2. Consultation with major segments of the business community including the Chamber of Commerce, manufacturers, wholesalers, banks, etc. to obtain their views about the present indirect taxes and avenues of reform.

3. Analysis of potential revenues from the proposed consumption duty, and comparison with IMF figures.

4. Development of a detailed statement of the proposed consumption duty; subsequent preparation of the Act, Regulations, and Instructions, for application at importation and to domestic firms. Attention is particularly needed to questions of rates and exemption.

5. Attempt to assess the distribution of burden of the present and proposed indirect tax system by income groups.

6. Development of a pattern of operation and administration of the proposed consumption tax.

7. Develop details of a training plan for personnel for domestic application of the consumption duty, and of implementation of the Stacey proposals.

8. Study of the interrelationship of the tax incentive program and the indirect tax structure.

9. Study of the implication of price controls and import licensing for the proposed tax charges.

10. On export duties study of the actual relationship of the duties to farm costs and profits beyond the IMF work, to get a clearer picture of adverse effects of the duties.

IV. Evaluation of the IMF Report: "Grenada Agenda for Fiscal Reform, August 10, 1984"

In general the Report is a relatively grand one, and I am in agreement with most major proposals. There is no need to restate them in detail.

1. "Import duties should form the basis for protection." This proposal obviously has merit; use of other levies for protective purposes obscures the amount of protection and in some instances violates the CARICOM principles.

2. "Exemption for government and quasi-governmental bodies should be abolished." The proposal has merit, especially for government commercial enterprises. There is no great merit so far as government itself is concerned. Taxing government imports clouds the picture of the contributions of the taxes to government revenues.

3. "The foreign exchange levy should be abolished when not needed for balance of payments reasons." This proposal is warranted--but the country does face a foreign exchange problem that it alone cannot solve.

4. "Replacement of the stamp duty, international airport duty, package tax, motor vehicle tax and purchase tax by a broad based consumption tax on imports and domestic manufacture."

This proposal is almost the same as that proposed in this report and is clearly desirable. The proposal favors a flat rate or only a few rates; the suggested 15, 25, 45, 55 percent figures are too close together and are excessive in number.

5 and 6. "Excises should be expanded to cover liquor, wine, cigarettes, tobacco, and petroleum products, at ad valorem rates, on both imported and domestic goods."

There is no need for excises on these goods, they can be taxed under the consumption duty at higher rates. Separate excises simply complicate the tax structure and its operation unnecessarily.

7. "Taxation of services should be expanded to cover all restaurants, all telephone services, and electric power above a certain minimum."

This has merit. Although taxing industrial use of electric power is questionable, unless a tax credit is allowed the industrial firms.

8. "The valuation branch should be made operational." This I fully agree with.

9. "Improvement of training." In general, I agree, but the Stacey report considers them in much more detail.

10, 11, 12, 13. "Penalties and internal operation; license refunds, new regulations and manual." I agree completely.

On export duties: "Revision of thresholds; producing progressive rates; ultimate removal of the duties." I would argue that they should be eliminated immediately. If not, certainly the thresholds should be raised.

My only objection to the IMF report beyond those noted is: the recommendations appear too much like a clone of those for other countries, despite differences between the economy of Grenada and others. Application of tax to domestic manufacture is desirable--but not doing so will not make much difference currently--and the report fails to note this. Violation of CARICOM rules is more apparent than real.

I take exception to the statement on page 84, "Export duties are always justified whenever exporters earn excess profits or in lieu of

income tax, if no income tax is applied to producer." Export duties are very crude methods of reaching farm income and windfall gains.

The report in places ignores the difference between relation with ECCM countries and other CARICOM countries.

V. Evaluation of Report on Working Party on Review of Taxation, June 1984

1. The Report (p. 17) reminds one of the very high ratio of taxes to GDP in Grenada and most Caribbean countries.

2. The basic limitation of the report is that it does not face up to the serious complexity of the present indirect taxes and proposed changes are mere bandaids.

3. With regard to specific proposals: (ii, p. 13)

   a. "Extend the hotel tax to restaurants." This has merit, as noted above.

   b. "Income tax on airline tickets to 10 percent." The problem is that persons may merely buy tickets to nearby islands and then acquire the remainder of the ticket.

   c. "Increase airport departure tax from EC$5 to EC$10." This increase brings the charge more in line with those of other Caribbean countries.

   d. "Replacement of the stamp transfer duty on documents by a one percent retail sales tax. The latter part of this proposal is highly objectionable; enforcement would be very difficult, given the nature of much retailing in Grenada. The yield would not justify the effort, and a higher rate would aggrevate the enforcement problem.

4. Proposed change in import taxes (iii, p.14).

   a.b. "Removal of the import duty on cigarettes, and the stamp duty on beer, malt and stout." This is

proposed to lessen smuggling, and is of doubtful desirability.

c. "Lower rates on watches, perfume, jewelry, to lessen smuggling." This is also of doubtful desirability.

d. Waving "international airport" tax on machinery for expansion and materials for manufacture and re-export.
This proposal, in itself, would add one more patch-up exemption. It can better be solved by the changes proposed in the main report above.

5. Proposals in iv, p. 14.

a. "Eliminate 2 percent tax on freight of exports." This is clearly desirable.

b. "Waive foreign exchange tax on machinery and raw materials." This tax should be eliminated; meanwhile it should not be patched. The objective is to conserve foreign exchange.

c. "Reduce export taxes." This is clearly warranted.

Thus while some of the proposed changes are warranted, the report is disappointing in not facing up to the major weaknesses of the indirect taxes.

ENDNOTES

1. Figures in this paragraph are from IMF Report, Grenada: Agenda for Fiscal Reform, August 1984.

2. They do not apply on imports by one ECCM country from another ECCM country.

3. Any person importing more than two cars a year is treated as a dealer.

4. See Fiscal Memorandum No. 11.

5. Some fruit and animals are exported to Trinidad but in small boats difficult to control.

FISCAL MEMORANDUM NO. 11

IMPROVEMENT OF CUSTOMS AND EXCISE ADMINISTRATION--GRENADA, W.I.

KENNETH STACEY

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LOCAL REVENUE ADMINISTRATION PROJECT
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GRENADA TAX PROJECT

Fiscal Memorandum No.11

TO: Mr. Laurie Wilson
FROM: Kenneth Stacey
DATE: September 28, 1984
RE: Improvement of Customs and Excise Administration-Grenada, W.I.

I. Issues and Findings

This study forms part of the wider Grenada Tax Project undertaken at the request of the Government of Grenada. The course of the study has been influenced by two important reports; the Government Working Party Review of Taxation June 1984 and the IMF Agenda for Fiscal Reform-Grenada August 1984. The latter played by far the major role as it dealt in detail with administrative matters of Customs and Excise whilst the former was more related to policy. The Study Approach at II below will indicate the degree of acceptance of the findings of both reports and the area of research into matters not previously dealt with which the consultant considers germane to this reform project.

Twin Aspects of Reform

The areas recommended for reform fall into two categories: those where existing conventional Customs and Excise procedures are deficient and those where quite new measures will be necessary as a result of likely fiscal policy changes recommended to the Government and external issues such as the U.S. Caribbean Basin Initiative.

It will become important when planning the composition and timing of technical assistance to be aware with some certainty of what policy changes the Government will accept and legislate although in fact the bulk of the recommended project could be implemented with subsidiary regulatory

changes under existing laws. Important examples of administrative change flowing from policy reform are the proposals to widen the base of consumption duty to compensate for other indirect tax modifications and also the reform of exemptions for various classes of incentive.

New Issues

Four important issues have not been dealt with in the material made available to the consultant:

1. The administrative effects of the U.S. Caribbean Basin Initiative.

2. The new Brussels tariff nomenclature which combines tariff and statistical classifications into one coding.

3. The replacement of the Brussels system by the GATT system of valuation and the special protocols available to developing countries.

4. The special administrative arrangements for assembly industries which are believed to be under consideration in an investment promotion program.

Before a technical assistance project is implemented it will be necessary to take the following action:

1. Consult with U.S. Customs to discover the extent to which they wish to cause to be investigated suspicious claims to origin, the format of their certificates of origin and the rights of participation of U.S. Customs officials in foreign enquiries.

2. Consult with ECCM and CARICOM regarding their intentions for conversion of their Common Internal tariff to the Harmonized System and the timing for its introduction.

3. The policy of CARICOM and ECCM must be established to discover whether they intend to harmonize valuation procedures under GATT or to proceed as at present under the protocol which allows them to postpone change until 1989. (Also important for the establishment of a national valuation system.)

4. Very simple procedures can be established for the importation of inputs for assemply operations and it would be beneficial for prospective investors to know that these can be arranged.

Training

A staff training program is vital both for conventional procedures and new controls. The local customs staff is only 101 of which 48 are guards but in spite of the small numbers involved, the Customs and Excise operations are prejudiced by the lack of training of junior and middle level personnel. There are no problems involved in remedying this deficiency. Training for new procedures including valuation will involve the drawing out of experienced staff for specialist training with the consequent input of new recruits. The Customs budget will have to be prepared with this eventuality in mind but cannot be done effectively until staff requirements are estimated by the technical advisor proposed to perform the preliminary study discussed later. Training is dealt with more fully under III Detailed Work Plan.

Previous Technical Assistance

The only technical assistance in the Customs field in recent years was provided by the IMF for about 3.5 months in 1979 in valuation. This resulted in new legislation introducing the Brussels system of valuation. As a follow-up three officials were trained in valuation in Cyprus. (The advisor was from that country.) No implementation followed from the new law as all trainees were promoted to new positions leaving no qualified personnel to set up a department.

A British Valuation Advisor, Mr. Don McPhail, has done a lot of advising work recently on the subject for Dominica and some of his reports have filtered through to Grenada via the ECCM Secretariat. No action has

been taken on them but it would be useful for a local advisor to obtain a full set.

Coordination of Technical Assistance

On 30 May 84 the Director of the Syracuse Advisory Project sent a report to Mr. Samuel Skogstad at USAID entitled Fiscal Memorandum No. 1. In paragraph 49 the Director proposed an action plan for USAID in which he stated "The role of the IMF cannot be ignored and, at least in the early stages, a joint USAID/IMF/GOG working committee on tax reform should be set up." The consultant strongly supports this proposal to avoid duplication of effort. Although the Project Design submitted in this report contemplates a single donor source, the consultant believes that a joint effort might be feasible although the question of division of responsibilities and control in the Customs and Excise field would be difficult to establish.

Objective

The Consultant's terms of reference in general call for the design, at three levels of cost, of a technical assistance project which will satisfy the needs of the Customs and Excise Department as revealed by deficiencies identified in existing controls and new administrative methods arising from proposed policy changes. This can be summarized as follows:

1. Modernize and render effective the conventional control of the Customs and Excise Department.

2. Prepare the Department to adapt to the impact of future fiscal policy changes and new responsibilities.

3. Provide a training plan which will equip middle and lower grade staff to administer an improved control system and equip more senior staff to organize and implement new procedures and controls.

It is unlikely that the proposed advisory assistance will have an important impact on revenue generation during its first year of operation; in fact staff increases may produce a net deficit.

The IMF Agenda for Fiscal Reform Part I.3 (page 13) states: "...tax reform in Grenada for purposes of revitalizing the private sector is going to be 'costly' in revenue terms." Viewing administrative reform against this background it can be said that all the measures proposed will have a beneficial financial effect in varying degrees and time-spans becoming visible after a year's operation of the project.

Summary of Recommendations

1. Create a four-man specialist investigation unit to control fraud in contraband, valuation, domestic production traces and diversion of concessionary duty-free goods.

2. Create a four-man "industrial unit" to control excise and domestic consumption duties, use of concessionary material and verification of certificates of origin.

3. Train all middle and lower grade personnel in conventional procedures, higher grade in specialist innovations and Customs brokers.

4. Set up and operate a Customs Valuation system.

5. Re-draft the Customs Law and Regulations to encompass new activities and prepare instruction manuals.

6. Commence preparatory work on the adjustment of the national tariff nomenclature to conform to the forthcoming Harmonized Commodity Description and Coding System - CCC Brussels.

7. Permit the inclusion of a Customs representative on the decision-making body for granting duty-free concessions.

8. Prepare a special procedure for the import and export of goods connected with assembly operations.

9. Make improvements where necessary in routine Customs procedures but specifically in the fields of tallying imports, refunds of duty, post-audit of documents, administrative penalties, and hydrocarbon oil control.

10. In the field of tariff policy take all steps possible to reduce the number of separate duties, employ a single base for computation and convert specific to ad valorem duties.

11. If export duties cannot be wholly abolished for revenue reasons the impact should be lessened by elimination of the specific duty element and reduction of the ad valorem rates.

Although these recommendations directly concern tariff policy they have a significant impact on Customs clearance procedure.

II. Study Approach

At the outset of the study the consultant familiarized himself with the local situation by reading the material listed in Appendix B, in particular the IMF and Government Working Party reports--both of which were a great value in offering a comprehensive overview of the Customs and Excise operation and in enabling measures to be worked out to conform with the relevant policy proposals.

The study was complemented by discussion with the Comptroller of Customs and the Director-General of Finance and by physical inspections of some procedures. Throughout the course of the study frequent consultations were held with Mr. Jorge Martinez the resident representative of the contractor, Syracuse University, The USAID project manager was also informed of developments.

The project study derived greatest assistance from the part of the IMF report dealing in detail with Customs and Excise administration. It was clearly the result of searching enquiry and the consultant's own enquiries conducted over a shorter period led him to similar conclusions. It will be noted that the present study covers certain aspects not emphasized in the IMF report such as the development of the Caribbean Basin Initiative origin procedures, assembly operations, licensing and training of brokers, control of concessionary duty-free goods and the nomenclature Harmonized Systems. Extended enquiries were possible because of the wide groundwork already covered in the IMF report.

It may be assumed that the consultant agrees with all the relevant IMF conclusions to administrative reform but alternative solutions are offered in the case of contraband control, refunds of duty and hydrocarbon oil control.

III. Detailed Work Plan

The following items are numbered to conform to the sequence of the Summary of Recommendations.

1. Investigation Unit

Background. There is no separate investigation unit in the Customs Service. Smuggling is countered by part of a 48-man guard force but its effectiveness is confined to direct encounters with smugglers, ship's rummaging and thefts from ships. There is no system for the collation of information, detection and investigation of suppliers, routes, distribution, etc.

Fraud in other fields has rarely been encountered but when it becomes apparent, e.g., undervaluation of invoices, cases would be investigated on an ad hoc basis by a senior officer.

Findings

Although smuggling is not a grave problem, it is sufficiently common to cause complaint from the Chamber of Commerce. The sources appear to be principally the island of Carriacou and the duty-free zones of Panama and Miami, i.e., by sea route. Even a sophisticated coastal patrol system would have difficulty in protecting effectively the Grenada coastline.

Commercial contraband is almost always centralized for sale in urban centers so that in Grenada the logical point to concentrate control would be in St. George's. This is most effectively done by challenging retail outlets or sales points revealed by informers, seizing the goods of foreign origin when not adequately supported by proof of legitimate purchase and prosecution of the offender by direct fine or the courts. Present law supports this action.

Fraud is very likely to have taken place in the field of undervaluation of invoices but there has been no mechanism to combat this. The present recommendations envisage the establishment of a Valuation Department and also units to inhibit the illegal diversion of concessionary goods and to control domestic production under an expanded application of the excise and consumption taxes. The routine checks which these new controls will develop are certain to throw up suspicion of evasion and a unit specializing in investigation of suspected fraud should be in existence to take over from this point.

Recommendations. Create a four-man investigation unit of not less than Class I personnel in service to enquire into Customs and Excise fraud with emphasis on contraband, valuation, excise and consumption duties on domestic manufacture and misuse of duty-free material imported under concession. They would receive specialist training under the technical assistance project and function under the direct orders of the Comptroller.

2. Industrial Unit

Background. The term "industrial unit" is intended to describe functions which include the control of concessionary duty-free material, excise and consumption duties on domestic production and verification of certificates of origin under the Caribbean Basin Initiative, the CARICOM/ECCM scheme and the Generalized System of Preferences.

It is difficult to quantify exactly the various classes of exemption which would call for post-importation control. The IMF shows two categories, "Approved Enterprises (Investment Incentives)" and "Other discretionary exemptions" which together represent an import value of EC$58.9 million or 37.2 percent of total imports. Fifty-three enterprises are listed as receiving concessions. There is no system for post-importation control of any of these concessionary goods.

Only three domestic producers are subject to Customs and Excise control--beer (excise and consumption duty) and rum and cigarettes (consumption duty only). The IMF report recommends (Part III. 3.f. page 43) that the coverage of consumption tax should be extended to all

consumer goods which would imply a commensurate increase of taxable domestic producers.

Artifacts of Origin are currently required to be signed by Customs for exports to many developed countries under the Generalized System of Preferences and to Common Market countries under the CARICOM/ECCM scheme when duty-free or reduced duty entry is claimed by the local exporter. With the advent of the Caribbean Basin Initiative, further Certificates will be required for duty-free entry into the U.S. Currently, it is rare for any check to be made on a Certificate of Origin's correctness although international agreements expect this to be done.

Findings. The amount of duty exempted for incentive reasons to enterprises such as manufacturers, hotels, tourist activities, agriculture, etc. is sufficient to warrant a systematic control to avoid misuse of raw material, machinery, equipment, etc., all of which is subject to a clear condition of prohibition of resale in the home market in its imported form. Although ECCM tariff stipulates the general areas of concession to harmonize the incentives, there is still considerable scope for national freedom of action in incentive policy. Although the IMF recommends (Part III. 1.C, page 35) "a review of all exemptions with a view to assessing whether they are justified in the economic interest of the country", they also recommend a full drawback of all taxes on imported raw material used to produce exports (Part V.1.b, page 91). With the imminent influence of the Caribbean Basin Initiative it is reasonable to presume an upward trend in manufactured exports or assembled goods with a consequent broadening of the field of exemptions.

There is no defect in the present control of taxable domestic products inasmuch as only three are liable to a tax. If the forecasted increase of taxable producers mentioned in the Background above is realized, there will be a commensurate expansion of Customs and Excise responsibility.

The verification of certificates of origin prior to their certification by Customs is understandably not regarded as a very productive exercise. Their falsification does little harm to the country of exportation as it is intended principally to deceive the Customs of the importing country. It is the practice for donor countries to reserve the right to request investigation into suspicious claims or even into a routine percentage of claims received. One gets the impression that such checks under existing preference arrangements are very rare but it would be misleading to assume that the U.S. Customs would accept the CBI certificates with similar abandon. It would be prudent, therefore, to construct a mechanism for exercising any necessary checks.

Recommendations. Create a four-man Industrial Unit of not less than Class I personnel to exercise a systematic control over concessionary duty-free material, verify the excise and consumption tax payments of domestic manufacturers and when necessary, verify the correctness of certificates of origin, particularly for manufactured goods. The personnel would receive specialist training under the technical assistance project and operate under the direction of Supervisor B.

3. Training

Background. The present training scheme relies entirely on overseas courses and is offered only to senior staff including Class I officers.

Numerically this has accounted for 18 trained officers leaving a balance of about ther same number of senior staff untrained. There is also the whole of the Class II and III range of staff untrained and an estimated 20 guards whom the Comptroller feels would respond to basic training to equip them for promotion to Class III. Thus a body of some 55 officials is in need of training in basic procedures and some specialization. The 18 senior staff who have already received training aborad would also be available for specialist training. There are probably 12/15 Customs brokers available for any special courses which might be arranged. Apart from space there are virtually no facilities for local training and more of the senior staff has received training in instructional skills. There are insufficient copies of the law and regulations and no manuals of procedural instruction.

Findings. There is an urgent need for training in basic skills for officers of Class II and II levels and selected guards. The new measures proposed such as control of consumption tax, investigation, control of concessionary material, certificates of origin, valuation, etc., will call for quite long-term specialist training. The frequent errors in Customs documentation are in large part due to ignorance on the part of Customs brokers who at present need no particular qualifications to perform their function. Although senior staff are technically highly qualified, they have not, nor can be expected to have, any experience of course presentation.

The general result is that staff cannot easily be moved around as their knowledge is confined to a restricted field, promotion candidates

are hard to find and morale suffers through lack of prospects. Foreign training is too infrequent and is not tailored to the particular needs of the Service.

Recommendations. A training scheme should be established with the help of technical assistance instructors with a four-point objective:

1. To train suitable middle and lower level candidates in conventional Customs & Excise procedures.

2. To train senior personnel in specialized Customs & Excise procedures, specifically those which form part of the overall plan of fiscal reform.

3. To train selected senior officers in instructional skills.

4. To prepare and conduct a Customs brokers course of limited scope sufficient to equip them to perform their function efficiently.

4. Customs Valuation

Background. As a result of IMF advice and assistance the Customs Ordinance 1960 was amended by a new law in 1979 legislating the Brussels system of valuation. The branch did not become operational and an advisor from Cyprus arrived in 1981 to assist in implementation. The assistance was complemented by overseas training for these officials but ensuing and continuing staff problems have prevented any active steps to installing a valuation system.

In Grenada the determination of value is of great importance due to the extensive range of ad valorem duties and the likelihood that even the remaining specific ones may shortly be converted to ad valorem. This tendency also extends to the excise and consumption duty field.

Although the GATT system of valuation was published in 1979 as a substitute for the Brussels system, many developing countries (including Grenada and the whole of CARRICOM/ECCM) are still using the Brussels system and under a special protocol may continue to do so until 1989 without infringing the GATT rules. There is not yet any indication from ECCM of their intentions for the future in this regard.

Findings. As a first step it is important for the Government to decide which system they wish to establish and it would be prudent to consult with ECCM before making this decision. Much of the initial work, such as the establishment of a data bank of values information, is common to both systems but nevertheless training would be jeopardized unless a firm choice were made at a fairly early stage.

Invoice values are currently checked but seldom challenged as there is no norm against which declared values can be compared. There is no post-audit of documents which would permit a value to be investigated. There is no ad hoc or systematic method of establishing whether an importer has commercial relations with his supplier which could lead to the declaration of an illegal value.

Recommendations. A decision should be made by the authorities on which valuation system to employ and an amendment to the legislation made if that of GATT is selected. With the help of technical assistance a valuation branch should be established and the staff given specialist training. Complementary measures should be taken to collect information regarding values and trading relationships and some attention given to values in a post-audit system of documents review (see IV.1.c. below).

Customs Law and Regulations

Background. Customs and Excise operations are governed by the Customs Ordinance 1960 and Regulations 1961 and a Tariff Law harmonized with the ECCM model. The Ordinance and Regulations are founded on fifty year old British legislation and the ECCM tariff law follows the Brussels nomenclature rules and the methods of classification (the Interpretative Rules). There is a serious shortage of copies of all three publications. There are no manuals of instruction written for the guidance of operational staff.

In the import tax structure of Grenada there are nine separate duties all or some of which could be charged on a particular merchandise. The ECCM tariff carries only the common external import duty whilst the remainder are scattered throughout the various legal instruments enacting the particular tax.

Findings. The time is long overdue (50 years) for an overhaul of the Ordinance and regulations, but even so it is possible for the service to function efficiently by means of superimposed ad hoc legislation. The most practical need is the issue of manuals of instruction available to all grades of staff which convert the law and regulations into simple language directing their day-to-day duties. It would be unwise to spend time preparing manuals based on out-dated laws, therefore, if any attempt at modernization is made it should preferably cover the whole field of law-regulation-manual reform.

There can be no criticism of the Customs Tariff Law per se but the large number of subsidary duties whose rates have to be sought and or a variety of enactments present an administrative nightmare for the examining officer. If they cannot be combined into one or two rates they should all be published together in one document.

Recommendations. The Customs Ordinance and Regulations should be redrafted and modernized to accord with proposed reforms and new procedures. Manuals of instruction should be written to cover important procedures, particularly those of most recent introduction. Administrative difficulties should be resolved by unifying the separate duties or at least publishing the separate rates in one document according to the Brussels nomenclature.

6. Harmonized Commodity Description and Coding System (HS)

Background. The Customs Cooperation Council (CCC) in Brussels have for some years been working on a structure of the tariff nomenclature which provides a complete harmonization of the tariff chapter headings and the statistical coding of merchandise. The Harmonozed System was approved on 14 January 83.

Previously the tariff nomenclature and the Standard International Trade Classification (SITC) were two independent classification systems and a conversion table was necessary to produce Foreign Commerce statistics from tariff nomenclature terminology. This is clearly a major advance--an example is as follows.

Heading No.	H.S. Code	Description
13.01	---	Lac; natural gums, raisins, gum-raisins and balsams
	1301.10	Lac
	1301.20	Gum arabic
	1301.90	Other

The new H.S. means that changes will have to be made in some tariff headings and sub-headings. In the local context it will involve changes in the structure of the Common External Tariff which would presumably be undertaken by the ECCM Secretariat but also changes in minor sub-headings which are left to national discretion. There would naturally be ramifications into many Customs activities, particularly those involving information storage such as valuation.

The timing of the H.S. implementation is very possible for developing countries so that there is no immediate need for concern.

Findings. No national action has yet been taken to prepare for change and the regional position is not known. Before moving into various areas of reform such as classifying valuation information, attaching tariff nomenclature codings to new ranges of duties such as the consumption tax on domestic production, etc., it would be wise to act in concert with the ECCM Secretariat to coordinate timing. Certain preparatory steps could also be taken to codify national sub-divisions and to train all personnel in the implications of the forthcoming change. Such training would also be important to Customs brokers and to staff of the national statistical office who presumably belong to a separate Ministry.

Recommendations. With the help of the technical assistance project, courses of training on a broad basis should be given to prepare for the forthcoming new nomenclature. Close coordination with the ECCM Secretariat should be maintained to ensure that current procedures and new reforms should be aligned in time to the new format. Work should commence on identifying national sub-headings and allotting the new code in readiness for absorption in the new nomenclature.

7. Granting of Exemption from Duty

Background. The Grenada Investment Incentives Law 1984 is the latest legislation which grants exemptions from duty on imported raw material, machinery and equipment to authorized enterprises. No enquiries have been made into the detail of the procedure for granting exemptions but it is known that no representative from Customs and Excise is on the committee.

Findings. It is important that the authorizing body, the Investment Review Committee, have a Customs and Excise representative on their establishment so that administrative matters and control can be discussed.

Recommendations. The composition of the Investment Review Committee should be amended to include a representative of the Customs and Excise Department.

8. Assembly Operations

Background. The assembly operations referred to in this proposal are those in which the components remain the property of the foreign exporter, are assembled in Grenada with no or minimal local value added except labor costs and whose product is returned to the proprietor of the components.

From an inspection of the list of concessionaries in the IMF report pages 87-90, it does not appear that there are any such operators currently existing. Discussions with government officials and USAID reveal that potential investors are beginning to be attracted to this type of enterprise, through the incentive plans and the consultants experience in Central America and the Caribbean has shown that this activity is the earliest to start and the quickest to grow where foreign investors are concerned.

Findings. In countries where an industrial exemption scheme is already in existence it is the initial practice to submit the materials for assembly to the full treatment accorded to raw materials for manufacture and domestic sale or general export. There is however, a much simpler solution given the special characteristics of the goods remaining the property of the foreign exporter and the imported inputs being identifiable at export.

Instead of submitting the operation to the whole procedure of government authorization, establishment of quotas and post-importation control, the components are treated as a routine temporary import procedure under existing Customs law and covered by simple bond until the export of the product. The facility would be available to anyone doing assembly work with no formality other than the presentation of a temporary import entry on arrival of the components and production of the assembled articles to Customs at export. It is possible that for other reasons, such as employment policy, the Government might wish to authorize an assembler's operation and its location.

A principle underlying this concession is that the components should still be identifiable in their assembled state, e.g., a shirt would be acceptable but a confection made from imported sugar, cocoa, etc., would not. It appears that the wording of Sec. 37 of the Customs Ordinance 1960 would permit their operation although of course such temporary use would not have been contemplated when the Act was framed.

Recommendations. A Customs regulation should be prepared to advise staff of the proposal to employ Sec. 37 of the Ordinance for this function and establishing any special procedures necessary. The Ministry of Finance through the necessary channels should make prospective investors aware of these facilities.

IV. Miscellaneous

1. Customs Procedures

Time has not permitted an in-depth inspection of all Customs activities but four areas have come to light which merit further study to improve efficiency.

a. Import tallying. At present it appears that tallies of landed cargo made by the Port Authority are consulted when amendments have to be made to the ship's manifest and that the Customs security guards present do not conduct a formal tally. It is recommended that Customs tallies should be made independently and referred to jointly with the Port Authority when required.

b. Refunds of duty. The IMF report at Part III.4.d.6 on page 50 refers to the large number of duty refunds which could be reduced by

procedural reform. They are of two categories: those paid on fuel used by fishing boats and those for deficiencies found on examination of goods after the payment of duty. The former is dealt with below under hydrocarbon oils.

In the second category the remedy proposed by the IMF does not appeal to the Comptroller for a number of technical reasons. An alternative remedy might be to devise some method of advising the broker of damaged packages likely to have been pilfered and noted at the time of the tally. The broker could then request joint inspection of the goods with the Customs so that an entry could be prepared on the basis of the goods found. This is known as Bill of Sight procedure but does not seem to appear in the 1961 Regulations. It is recommended that this proposed solution be studied.

c. Post-audit of documents. The consultant agrees with the important recommendation made in the IMF report Part III.4.i page 56 that the manifest should be included in the post-audit of documents. After the establishment of a Valuation Branch, the post-audit should also include an element of values checking.

d. Administrative penalties. There are no administrative penalties for errors in declaration as also referred to by the IMF report Part III.4.d(4) page 50. The Comptroller estimates that 10 percent of the time of staff dealing with Customs entries is spent helping brokers who do not understand their job. In Recommendation 3 of this report the training plan includes special courses for brokers but it is also very necessary that the Comptroller should be empowered to impose times for entry

errors. It is recommended that the brokers training scheme should be supplemented by a scale of administrative fines imposable by the Comptroller. They could be written into the redrafting of the 1960 Ordinance.

e. Hydrocarbon oil control. The existing revenue control of hydrocarbon oil does not inhibit duty evasion through theft committed by oil company employees. It is recommended that measures be devised, with the help of the technical assistance project, to eliminate loss through theft by the checking of road tanker deliveries and to reformulate the operation of the duty-free fuel concession to fishing boats mentioned at b above.

2. Administration of Import Duties

The present proliferation of nine possible import duties imposes a grave administrative burden on the examining officer with consequent delays by queries to brokers and importers and time-consumg examinations such as measurements for the package tax. In addition the various rates of tax are not published in the tariff but have to be sought for throughout the range of separate enactments. Although the unification or elimination of these duties is largely a matter of tax policy, the impact on administrative efficiency is so damaging that this alone might serve as a notice to justify tax reform. At the same time there are strong policy arguments for converting specific duties to ad valorem, a measure which would greatly reduce the time for examination of goods and simplify entry checking.

3. Export Duties

The consultants terms of reference call for an appraisal of export duties. There are no problems in the administrative field except that most duties are dual specific and ad valorem, causing delays in examination.

On the question of policy it seems to be generally accepted that the farming producers are suffering unfairly under the export tax burden. To remedy this and to ease the administrative strictures it is recommended that the specific duty be eliminated and that an ad valorem duty be levied on values over a price threshold which could be established in relation to world commodity prices. For further equity the duty rate could be raised progressively on a scale commensurate with commodity price levels.

V. Technical Assistance Proposals

1. Rationale

In response to the terms of reference three levels of technical assistance have been planned according to cost. Level I, 2 man years, is designed to cover assistance in all fields where deficiencies have been identified and new procedures envisaged including training of adequate personnel in all fields.

Level II, 18 man months, covers the same fields but economizes on training by reduction of course lengths and subjects and use of local instructers. The Customs Ordinance would not be redrafted: merely the Regulations pertaining to new procedures and manuals.

Level III, 12 man months economizes further on course lengths and subjects and omits brokers. There would be no legal, regulatory or manual drafting.

In all levels the establishment of a valuation branch has been maintained as the essential element including the related training.

Although logistic support was not mentioned in the terms of reference, a list of equipment and supplies has been provided below together with a commentary on priorities.

2. Preliminary Study

A six-week preliminary study is recommended to prepare the ground for an advisory team. It would be necessary whatever level of advisory service were decided although the period could be reduced to four weeks if level III were chosen. The optimum timing would be as soon as possible after USAID funding levels had been decided and after the Governments' agreement on the nature and extent of the relevant reforms. An important component of the project agreement would be the budgeting of extra Customs and Excise staff required under the reforms, numerical details of which would be provided in this preliminary study. The duties of this consultant would be as follows:

a. Prepare staff assessments for new and reformed procedures.

b. Prepare work plans for all advisors.

c. Draft working instructions for fundamentally new procedures and for the more important reforms.

d. Study the latest developments on the Caribbean Basin Initiative insofar as it relates to procedural requirements to be imposed by U.S. Customs. Cooperate with the ECCM Secretariat in this respect.

e. Ascertain the intentions of the ECCM Secretariat in regard to the Harmonized System Brussels nomenclature, harmonized caluation-GATT or Brussels and any other project matter which might be the subject of uniform treatment, e.g., exemption and assembly procedures.

3. Levels of Technical Assistance

The following tables show in each of three levels the duties of each advisor and a brief indication of the accomplishments expected. The short terms allotted per advisor are considered preferable in order to get quicker results and some team supervision but if the qualifications were right the total time schedule could be extended for fewer advisors.

4. Control Visits

It is recommended that the progress of the team be monitored by visits of a week's duration by the Contractor's project design staff on a quarterly or six-month basis according to the level of assistance selected.

5. Qualifications and Recruitment of Advisors

As issues other than Customs are involved in the Fiscal Reform Project it seems advisable to recruit a team through a U.S. contractor experienced in Fiscal Reform and Customs and Excise in the Caribbean area. There is a distinct difference between Customs operations in the Latin American and the ex-British Caribbean countries. Apart from different legal systems and many procedures there is the fact that both Customs and Excise are combined in services based on British law. This is particularly important in the case of Grenada where fundamental excise reforms are contemplated.

The same argument tends to the desirability of U.K. advisors. In this respect it is also likely that U.S. Customs Advisors working under a PASA agreement might have strictures about reporting to an institution other than the U.S. Bureau of Customs. Apsrt from these comments it would be quite feasible technically to operate a U.S., U.K. or joint team. It would be unadvisable to employ other nationalities because of traditional and linguistic problems.

The Chief of Team and General Advisor should have at least ten years service in Customs and Excise preferably with some experience of operating in developing countries. The valuation ultimately with the Brussels system of valuation and an extensive knowledge ofthe GATT system. Advisory service in Customs valuation in a developing country would alsobe an advantage. It would be an added advantage in the case of all three advisors if they had had some experience in training and course planning.

VI. Cost and Logistical Support

Unfortunately time has not permitted a study of the costs of the proposals presented here but an approximate figure for advisory services canbe calculated from some statistics supplied by the USAID Mission. The result is as follows:

1.	Preliminary Study	6 weeks	US$ 8,000
2.	Level I T.A.	24 man months	US$229,000
3.	Level II T.A.	18 man months	US$171,750
4.	Level III T.A.	12 man months	US$114,500

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Some logistical support would be essential for the efficient implementation of the project. The following list is offered in order of priority with essential items starred and a reason given for their need.

*1 Vehicle	Use of Investigation Unit
*1 Vehicle	Use of Industrial Control Unit
*1 Typewriter 26"	For Valuation Branch
*Classroom material	Blackboards, desks, chairs, stationary

*Audio Visual Aids for classroom
6 Calculating machines for entry checking and valuation
12 Desks and chairs for staff of Investigation, Industrial Control and Valuation Units
6 Filing cabinets for the three specialist units
1 Photocopier for general office use
1 Typewriter for general office (36" carriage)
1 Accounting machine for cashier
12 Desk fans

US$1,000 for starting a Customs library of Customs Cooperation Council Publications, values pamphlets and literature, etc.

VII. Conclusion

Recommendations have been made in this report for improvements in current procedures and for innovative controls, but in so doing it fails to give an appreciation of the current effectiveness of the Grenada Customs and Excise Service. It should be known that this service is operating at a high level of efficiency within its existing code. The conditions under which it operates are the worst that the consultant has seen in his experience which includes some of the most undeveloped West African countries. It is a tribute to the Comptroller, Mr. Patrick Bubb that he has been able to fulfill his role as the principal revenue collector in these circumstances.

I wish to thank him for the assistance he has given me in reviewing the Customs and Excise activities. I wish to thank also Mr. Jorge Martinez, the resident representative of the Syracuse University project for his valuable advice on the broad economic front and for arranging my liaison with local authorities and USAID.

APPENDIX A

MATERIAL FOR INCLUSION IN THE TRAINING COURSES

The following is intended as a guide to the general subject matter to be taught. The selection will, of cours, have to be adjusted in accordance with the level of advisory service decided upon.

Conventional Training

Ships' reports, rummage, tallying, arrival procedure
Functions of the ships manifest
Division of responsibilities between Customs & Port Authority
Security of cargo before dispatch
Functions of different types of Customs entry including transhipment and warehousing
Entry checking procedure
Examination of merchandise
Classification of goods
Treatment of deficiencies & excesses
Bonds
Warehousing procedure
Contraband, powers of officers, penalties
Cashiers functions
Organization of Customs and Excise
Relation of Customs to Government Departments

Specialist Training

Control of Excise and domestic consumption tax
Administration and control of industrial exemptions and others
Certificates of origin under the various existing schemes
Valuation--all aspects of the Brussels and GATT systems
Investigative methods for Customs & Excise fraud
The Caribbean Basic Initiative

APPENDIX B

Officials and Publications Consulted

1. Officials

Mr. Bell	Senior Customs Officer
Mr. Patrick Bubb	Comptroller of Customs and Excise
Ms. Pattie Buckles	USAID Project Manager
Mr. Don Harrison	Economist, USAID Barbados
Mr. Alan Kirtin	Ministry of Finance
Mr. Jorge Martinez	Resident Representative, Syracuse University
Mr. Lauriston Wilson	Director General of Finance

2. Publications

IMF Report - Grenada: Agenda for Fiscal Reform August 1984
Grenada Government Working Party on Review of Taxation June 1984
Customs Ordinance 1960
Customs Regulations 1961
ECCM Customs Tariff
Grenada - Peoples Laws 1980-83
Brussels Explanatory Notes on Customs Valuation
GATT Agreement of Origin Booklet
Customs (Caribbean Community) (Origin of Goods) Regs. 1980
Harmonized Commodity Description & Coding System CCC Brussels 1983
Project Correspondence - Syracuse University, USAID, Government of Grenada

FISCAL MEMORANDUM NO. 12

PROPERTY TAX ADMINISTRATION

IRVING OLSON

SYRACUSE UNIVERSITY
LOCAL REVENUE ADMINISTRATION PROJECT
THE MAXWELL SCHOOL | METROPOLITAN STUDIES PROGRAM
409 MAXWELL HALL | SYRACUSE, NEW YORK 13210 USA | 315/423-3116, TELEX 937430

GRENADA TAX PROJECT

Fiscal Memorandum No. 12

TO: Mr. Lauriston Wilson, Jnr.
FROM: Irving Olson
DATE: September 26, 1984
RE: Property Tax Administration

I. Property Tax Administration in Grenada Now

The existing system of property tax records (in Inland Revenue) and of real property ownership records (in the Land Registry) is not conducive to efficient and productive property taxation.

There is continuing property tax administration of a sort--valuations are being raised and taxes are collected. However, nothing is being done to include unvalued and untaxed properties on the roll--a great unknown, unmeasured and not measurable under present conditions. The simplest, "easiest to compile" kind of statistics are lacking. A count of land parcels, of assessment entries, total property taxes collectible, total tax delinquency for the previous year, etc., has not been done. There is no way to estimate missed property tax revenue without basic statistics.

Assume however, that an estimate of 25,000 land parcels is correct and the reported property tax revenue in 1983 (EC$700,000) is accurate; that is an average tax per land parcel of only EC$28 (US$10.61).

No valuation work is being done currently by the three person staff in the Property Valuation Division. The expected arrival in 1984 of a valuation officer and assistant has not yet happened. Nevertheless, the

staff deals sympathetically with tax complaints and has introduced many of the new valuations in the existing property tax roll--a big, cumbersome volume with columns for several tax years.

A good deal of field work was done in the 1981-83 revaluation project, but, surprisingly, no information identifying each property and its location is to be found in the valuation data sheets. Thus, a key element needed to substitute of new valuations for existing assessments in the ongoing tax roll is missing. Still, some of the new valuations have been introduced in the tax roll. These are generally for properties that have been owned by the same person for many years' and properties valued in the higher ranges.

The IMF recommendations for property taxation are appropriate and uncontroversial, though in my opinion, these might have been more specific and far-reaching:

- A staff of twenty or more for the PVD would not be excessive, because all taxable properties must be identified, coded, mapped, and appraised.
- Changes in certain laws can make property tax collection more self-enforcing.
- Requiring payment of current and back taxes before transfers can legally be made effective and recorded is one such change.
- Giving first priority to and making the unpaid tax a lien on the subject property, as well as higher interest rates and penalties, would encourage more timely tax payment.

II. Present Status of Property Tax Records

Although the property tax was "overhauled" in 1981 by changes in law, establishment of a Property Valuation Division (PVD) in Inland Revenue, and a major effort "to update the cadaster" and "revalue all property quickly," no significant improvement in the system or its performance is evident.

First, a "cadaster" or "register of lands" is to be found in neither the PVD of Inland Revenue nor the Supreme Court Land Registry. The only lists are of owners names and land values in the former and document indexes arranged by names only in the latter.[1]

Second, the 1981-82 revaluation, 60 percent completed, failed to identify the properties valued. The alleged owner's name and address is the only consistent clue to the location of the property, but in many cases the address is no more than a P.O. Box number. None of the kind of information relevant to ownership determination had been picked up during field contacts with owners.

In Mr. Seales study of land conveyances during a six month period October 1983 to April 1984, he gleaned close to 250 land transfers from the index in Land Registry, but could match only 10 percent of the 250 with entries in the new valuations list.[2] The information linking data from the two sources is not available.

The lists of assessments prepared since 1981 is for practical purposes, useless, in my opinion, to any new effort that might be undertaken solely to prepare an up-to-date property assessment role.

III. General Statement on Problems in Present Property Tax Administration

Faults in the present property tax are basic and a block to effective administration. The absence of a land cadaster or tract index and the resulting "in persona" vs. "in rem" approach is the major deficiency. Any resources spent to improve administration and records without basic changes in law and approach, will have no lasting or substantial benefit.

There is no land cadaster, or master list of registered lands. Land conveyance instruments are registered and copied in books, but the indexing for finding the recordings is by names of parties to the transfers.[3] Valuation and tax rolls identify owners by names and addresses, but do not identify the land. The listed owners may be former owners, claimants, non-existent persons, or real owners found in the rolls in more than one entry for the same land. There is no workable control against omissions and duplications.

The lack of a land parcel identification code or location system makes it virtually impossible to match (collate) new data from 1981-82 to valuations with existing assessment entries. The inherent uncertainty and inaccuracy of the roll thwarts any serious attempt at enforcing payment of delinquent taxes. Thus, there is substantial delinquency of long duration.[4]

IV. Establishment of a Workable Property Tax System in Grenada

A workable and efficient property tax system can be established and maintained by an expanded PVD staff, provided this staff is carefully selected and trained.

Some features of the proposed system and its establishment are:

a. Property tax revenue would need to be increased to justify such an investment in staff. The first increases could be realized soon after establishment of the revamped PVD.

b. A PVD staff of 22 or more will be needed to establish and maintain the system.

c. An annual tax list, tax billing, tax delinquency and collection statistics, tax delinquency notices, etc., will be computerized.

d. In the course of establishing the system a complete and up-to-date land cadaster will be developed.

e. Temporary code numbers will be assigned to all assessments. Permanent parcel ID numbers reflecting geographical location will be assigned upon completion of field work in a district.

Important prerequisites of the program must be met before work such as training, revaluation, and substantial technical assistance contracts are made. The following are listed in order of priority.

a. Amendment of the Property Tax Management Law to eliminate sections prescribing certain forms and procedures and to authorize establishment of the proposed system. A firm commitment by the Government to do this may be sufficient cause to proceed.

b. A commitment to complete the "photogrammetric" topographical mapping of the island and to produce topographical maps in suitable scales for property inventory and valuation purposes (1:2500 and 1:1250).

c. The selection and hiring of the proposed PVD staff.

The staff recruited is to be organized as follows:

1. A Director and Assistant Valuations Officer.

2. Two persons assigned to work on Land Registry records at the Land Registry office. They will report all conveyances and will furnish accurate copies of surveyor's maps found in such instruments. They will also look up the

recorded owners of land parcels in coincidence with field work to help identify, inventory and appraise land parcels.

3. Twelve interviewer-appraiser field persons--a team of two for each parish--who are residents of the parish. They will systematically identify, sketch map, and make a preliminary appraisal of each parcel and obtain critical and important ownership information for verification in the Land Registry.

4. A team supervisor to instruct, work with, and stimulate each team and to inspect their work and collect completed parcel identification and valuation reports.

5. A person to serve as custodian of ownership maps, and to be in charge of parcel coding and maintenance of the cadaster and ownership maps.

6. Clerical staff, including persons capable of maintaining property records and providing the input for computer processing (4 persons).

In all, a staff of twenty-two persons.

The valuations completed by the teams should be taxed in the current year if completed before March 31st. Otherwise, the new valuation will be held over to the next year.

In the case of omitted property discovered and valued, taxes for the current year should be collected (Section 34).

If the valuations completed by the teams are a large multiple of previous valuations, and if this increase is not due to omission, a uniform percentage of the increase for each such property might be held back and added in the year when the revaluation is completed for the country.

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The teams will make the appraisals or valuations according to guidelines and by use of their judgement of comparative worth. Valuations must be consistent and may be conservative.

The more valuable and extensive properties can be identified and revalued first, to obtain early increases in tax revenues. The new valuations of such properties can be substituted for those in the ongoing tax roll more easily. The higher taxes from these properties will justify the extra effort. When the more numerous properties of lower values are valued, a uniform percentage of the increase may be held back until the year revaluation is complete.

As parcels are being identified, mapped, and valued, a temporary parcel number is assigned by the team. This number is written in pencil on the map and on the property form. As each parish, plot map, and 25 hectare field map will have a permanent code number, these locational code numbers will be written on the property form ahead of the temporary parcel number (see Exhibit 1).

The existing tax roll can be coded to some extent and made a part of the same new tax roll, old assessments being replaced by the new valuations when made and matched.

The tax list or tax roll can be prepared by computer annually, even as the revaluation continues. By this process, useful statistics can be produced for guidance and reporting.

V. Training Programs for PVD Staff Organized and Proposed

General training in property tax administration should be given to the entire staff. This will require some advance preparation of material.

Special training will be given to each of the following, the twelve field team members and their supervisors (the valuation officer and assistant), the map custodian, and the registry researchers. Areas of training would be:

a. interpretation of topographical maps,

b. the parcel identification system, permanent and temporary,

c. methods of contacting owners, advance notice, etc.,

d. interviewing the owner and recording the ownership information obtained,

e. sketching parcel boundaries on the topographical map and on the back of the property card. Assignment of temporary parcel number,

f. appraisal of land and buildings, separately.

For the map custodian and the researchers to be posted in the Land Registry, training will cover responsibilities and work procedures.

VI. Technical Assistance Proposal

One full time expatriate technical advisor and one on-call expatriate advisor will be needed to help with development of training materials, work procedures and instructions and with the installation of the system including the completion of an inventory of identified parcels

EXHIBIT 1

THE PARCEL IDENTIFICATION NUMBER CAN BE
A SEVEN DIGIT NUMBER

	Parish Number	Plot Map Number	25 Hectares Subdivision	Parcel Number
Length of Code	0	00	0	000
Capacity in Code	10	100	10	1000
Number Needed	6*	31**	8	1000***

*There are six parishes plus two islands.
**31 average, 99 maximum.
***If all lots out of 25 Hectares were 10 x 25 meters, there would be 1,000 lots in the 25 hectares tract.

of land in a cadaster and of an accompanying revaluation of land and buildings.

The short-term technical advisor would be a person with broad experience in property tax administration, reassessments, systems design and installation, and tax administration improvement. This advisor would serve short periods of time on special assignments as needed for a total estimated time of two months in a two-year period.

The long-term advisor would serve for 24 months and would be a person with extensive experience in performance and in supervision of field work in particular, including the appraisal of land and buildings and in records management. He would participate in the design and conducting of the training program, assist the valuations officer with the guidance and supervision of the installation of the new system and of an early completion of the cadaster and revaluation. This advisor would also be involved in the design and application of the tax collection enforcement procedures envisaged as a part of the improved recording and reporting of information (as a result of computerization), particularly of overdue taxes.

Topographical "Photogrammetric" Plot Maps Available for 20 Percent of Grenada

While a survey of all land ownerships (all land parcels and lots) and the establishment of an accurate list of all parcels, identified by code numbers on the surveyor's maps and in the list, would be the ultimate and best basis for ownership registration and recording and for property

tax administration, its high cost and the long time required for completion rule out this approach as impractical.

The alternative is an adaptation of photogrammetic topographical prints or maps to the small scale (large size of detail) needed for ownership maps or tax maps. The photo negatives images are blown up to scales of 1:600 and 1:1200 (1 inch = 50 feet and 1 inch = 100 feet).

Grenada has been "photogrammetrically" mapped from 1970 flight photography and subsequent map production has been completed for 39 Plots (each 1 kilometer N-S by 2 km. (E-W) out of an estimated 185 or more such plot maps required to cover all of Grenada. Transparencies of the 39 "plot" maps are on file in the cartographic section of the Land Survey Office, Min/Agr., Botanical Gardens. The cartographic office there appears to be surprisingly well equipped with drafting and storage, reproduction and tracing machines and devices.

Further inquiry will be made about the plot transparencies and the printing process. The master wall map based on the photo survey shows metric quadangularation of the entire Island into a grid of square kilometer divisions (each 1 km. long and wide in other words). This master or key map is at the scale 1:25,000. The plot maps are on the scale of 1:2,500 with each map covering 2 sq. kms. These are too large for field use. (Without including the border and any overlap, the 2 sq. km. at 1:2,500 would take a space of 40 cm x 80 cm).

A compromise between convenience of size and size of scale would be maps 40 cm x 40 cm (about 16" x 16") and a scale of 1:1,250. At that size and scale each map would cover .25 square kilometers or 25 hectares. A

parcel 50' x 100' would appear on the map as a 1/2" x 1" area--adequate for sketching and inserting the parcel number.

At this size and scale 1,480 maps would cover the country, but fewer will be needed as the larger scale 1:2,500 would be suitable for the forest, range, and large farm areas.

If the parishes were divided for mapping at the scale of 1:1,250 the Plot Map Code can be two digits and the 25 hectares subdivision maps a one digit (only 8 maps out of each 2 sq. km. plot map).

ENDNOTES

1. The index is segmented by year of recording and within each annual segment by the initial of the surname of the conveyee, etc.

2. Mr. Seales was one of the field team that did the revaluation.

3. In the Supreme Court Land Registry.

4. Total taxes assessed in the property tax rolls for given years are unknown (have not been summed up) so the rate of delinquency is not readily determined.

FISCAL MEMORANDUM NO. 13

INCOME TAX ADMINISTRATION AND TRAINING NEEDS IN GRENADA

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GRENADA TAX PROJECT

Fiscal Memorandum No. 13

TO: Mr. Lauriston Wilson, Jnr.
FROM: George W. Whitehouse
DATE: September 28, 1984
RE: Income Tax Administration and Training Needs in Grenada

I understand my assignment to be a review of the Grenada income tax administration, identifying needs for improvement, procedures and training with the principal emphasis on the full range of income tax matters: assessment, audit, record-keeping and collection.

My three working days in Grenada were full and quite interesting and as usual always too short to do everything that one would like to accomplish. I met with the following people:

Ministry of Finance

Mr. L. Wilson

Inland Revenue Department

Mr. B. Harford

Mr. C. Lowe

Mr. M. Hosten

Mrs. J. Tomar

U.S.A.I.D. - Grenada

Ms. P. Buckles

U.S. Embassy - Grenada

Mr. S. Noble - Econ. Officer

I received excellent assistance and co-operation from Mr. Wilson and the staff of the Inland Revenue Department.

I. Review of Reports

Review of IMF and Government Working Party Reports

IMF Report. The above report was reviewed and I am in full agreement with it except for the following areas:

1. "...and training is being provided in lower level accounting and auditing".

The accounting training has not started to take place as indicated in the report.

2. "Inflation adjustments of inventories, through adaptation of 'Lifo' in lieu of 'Fifo' and depreciation allowances through some form of indexation of original costs, as soon as revenue situation permits. Given the administrative capacity, however, it may not be feasible in the near future, until these measures can be introduced, therefore, a more liberal depreciation allowance may be considered".

In addition to the limited administrative capacity, it appears that the taxpayers will have to become more sophisticated in their record keeping and reporting for tax purposes if these changes were introduced. Consideration should also be given to making the changes elective.

Government Working Party Report. The above report was reviewed and appears to identify some of the existing problems. The report does not go into specifics, however, it does pin-point several areas of major deficiencies, lack of training, the need to strengthen the Inland Revenue

Department and widening the net to include more of the self-employed taxpayers.

I would like to comment on the following paragraph:

> "Members felt that there was widespread tax evasion on the part of self-employed businessmen, taxi drivers, hoteliers, mechanical workshop operators and independent professionals. Widening the tax net through better assessments and improved collections could yield EC$3 to $5 million annually from this source".

Officials apparently fail to realize that by law they have a self-assessment income tax system and that it should function by taxpayers voluntarily complying with the laws enacted by the Government. A strong enforcement program will have to be put into place to correct the present assessment system.

Previous Technical Assistance

During the year 1979 under the IMF Technical Assistance Program, a three month training and assistance program was conducted for the Inland Revenue Department in Grenada.

The program included, in addition to a limited amount of training, the preparation of an Audit Manual - see Appendix A. The advisor, a former U.S. - I.R.S. employee designed an examination record control card, which was never put into use.

Several hours each morning were devoted to teaching auditing techniques to approximately seven of the senior members of the Inland Revenue Department. Since that time two have retired from the Department and one other has resigned leaving four of the top officials who were exposed to the training.

The Manual has not been used to train any additional staff members nor has it been put into use. The control card designed by the advisor was never implemented as recommended.

The three-month period apparently was too short to implement and carry out the Technical Assistance Program offered by the Fund.

Programs such as the above must be long-term to be successful.

II. Administration of Income and Company Taxes in Grenada.

Organizational Structure

The income tax operation of the Inland Revenue Department has thirty-nine positions - see Appendix B for organizational chart. At the present time there are six vacancies in the organization. One of the critical vacancies is the position of Inspector (Field Audit).

There are two main branches, Assistant Comptroller (Assessments) and Assistant Comptroller (Collections, Investigation, and Services). There is one Bailiff assigned to each of the five parishes outside St. George. This is not shown on the chart.

Assessment

As pointed out above, the self-assessment system is not working. There are approximately 2,500 individual and 150 company income tax returns filed each year. Many of these returns are incomplete and not properly prepared. In addition to the above, approximately 5,000 provisional assessment notices are prepared and mailed out during the period April 1 to August 31 of each year. These assessments are prepared

on information from prior year assessment or from available third party information.

It is estimated that another (approximately) 7,500 individual and 200 company returns should be filed. The Department's Master Taxpayer File has in excess of 20,000 taxpayers' names. This file is not reliable because it contains names of deceased taxpayers and those who have moved from the country and are no longer required to file tax returns.

Some of the principal causes for the above problems are as follows:

- Lack of training in accounting, law, etc.
- No taxpayer assistance and education program.
- Provisional assessments too low. The Department is interested in securing agreement rather than having taxpayers object to assessment. The current inventory of objection ranges from five to ten cases. The last case taken to the Appeal Board was in the year 1981.
- Penalties are not applied for non-filing. There is no record of any penalty being assessed in recent years.
- Forms are too complicated.
- Instructions are available at the Inland Revenue Department upon request only and need clarification.

The Inland Revenue Department is too small to have so much specialization in its assessment section. This condition also exists in the collection section, requiring an abundance of supervisory positions for a few technical employees. See Appendix B.

There is a lack of uniform interpretation of the Income Tax Law on the part of the employees and officials in the Inland Revenue Department. The Department does not have a legal officer, however, it has access to the Attorney General for opinions but this source is rarely used.

Assessment norms have been established for mini buses and small grocery stores dispensing alcoholic spirits. It does not appear that these norms are being used to the extent that they should be.

The provisional assessments are not reviewed. However, the mathematical computations are checked by the clerical staff or junior tax officers.

Audit

The only personnel qualified to conduct examination are the three top executives in the Inland Revenue Department. The position of Inspector (Field Audit) is currently vacant.

There has been a limited number of desk audits conducted. These audits have been confined to questioning one or two expense deductions claimed by the taxpayer. If the taxpayer does not respond to a request for verification or substantiation of deductions, there is little follow-up on the request.

A well balanced audit program cannot be started until the personnel in the Department have received training in accounting, income tax law and auditing techniques.

Collections

The personnel responsible for the collection of taxes are the Revenue Collectors and Bailiffs. There are two Revenue Collectors assigned to the Office located in St. George. They are responsible for the collection of the more difficult cases. The three Bailiffs assigned to the office in St. George collect the less difficult accounts. If the Revenue Collector

or Bailiff needs assistance they rely on the Inspector (first line Supervisor).

In each of the outlying five parishes, there is one Bailiff to collect the taxes from the taxpayers residing in their parish. The monies which they collect in the outlying parish are generally forwarded to the Accountant General through the treasury office in the parish.

The Bailiffs in the parish offices receive little, if any, supervision from the Headquarters and have had no training in the collection law and procedures.

The Bailiffs receive 5 percent of the monies which they collect. This fee must be paid by the delinquent taxpayer. It is known (rumored?) that some Bailiffs receive more remuneration per annum than the Comptroller.

Although the law permits the Department to levy for non-payment of taxes, there has been only one levy served in the past fifteen years. In the year 1976 property and goods were seized and sold for non-payment of taxes.

It is a common practice to assess interest on taxes in arrears against traders and planters but against no other taxpayers.

The Inland Revenue Department does apply refunds due taxpayers on current years taxes against taxes due from prior years. This task could be made easier if the Department is records were computerized.

Administration

- There is no Management Information System in place. There is no record of the number of tax returns filed, revenue collected, penalties assessed, and the amount of taxes in arrears.

- Management does not prepare an annual work plan. There are no goasl or objectives established for the various sections of the Department.

- The employees have no meaningful job descriptions. The present job descriptions are an outline of what the employee is doing and not what he is expected to do.

- There are no employee annual performance evaluations.

- The Department does not have any formal career development program in place. The GOG does follow a seniority list which is taken into consideration when promotions are made.

- There is no legal officer on the staff to assist in interpreting the laws.

Taxpayer Assistance and Education

- There is no formal program for assisting taxpayers.

- Many employers are over-withholding on employees, causing the taxpayer to file claims for refund. This is due to the lack of educating the employers on the proper use of the withholding tax system.

- If more time was devoted to assisting and educating the taxpayers, the Department would spend less time in perfecting incomplete and incorrect income tax returns.

- The most important result from a good taxpayer assistance and education program would be to increase voluntary compliance and improve the self-assessment tax system.

Training

The lack of training on the part of the majority of the employees within the Inland Revenue Department is causing many administrative problems. The three top executives within the Department are devoting the major portion of their time performing technical tasks.

The comptroller, the senior officer, is the only person performing any technical work on the 150 filed company returns. He is reviewing them for

possible provisional assessments and requesting additional information if returns are not complete.

Since the year 1976 a limited amount of training has been conducted. Appendix E lists academic qualifications and previous training completed by personnel of the Inland Revenue Department.

During the year 1979, the IMF sponsored a Technical Assistance Program offering a limited amount of training to seven senior members of the staff of the Inland Revenue Department. Three of these have since retired or resigned leaving four remaining.

During the year 1982, a course was started in the newly enacted Income Tax Law No. 20, year 1980. The instructor completed about fifty per cent of the material and the course was discontinued.

A tax law course was given during April to May 1984 to approximately twelve members of staff. The course was conducted three days a week from three to four p.m. See Appendix F for course content. A previous course was conducted during 1983 but not quite as intensive.

Junior members of the staff have not been provided any training to date. The above record of trianing supports the Department's conclusion that there has been a limited amount of training since the year 1976.

Tax Returns and Instructions

There are currently two types of individual taxpayers in Grenada: the self-employed and the PAYE. However, there is only one complex tax return available for both taxpayers, Form 1a. See Appendix D.

There should be a separate simple one page form with instructions for preparation on the reverse side for the PAYE taxpayers. This form woudl accomodate aobut 80 percent of the taxpayers.

The current Form 1a and instructions were printed in 1980 to cover the Income Tax Act No. 20 of 1980. At the time of printing, the instructions were mailed out to the taxpayers. Currently the instructions are not mailed but are available at the Inland Revenue Department upon request.

If there is to be a specific form for self-employed individuals then the information contained on separate Schedules E, G, and H should be made a part of the new form.

The Form 1a and instructions could be more explicit especially in the area of concessional deductions.

The company taxpayers must prepare Form 1(b). Currently there are no instructions for the preparation of this Form which has a number of obvious deficiencies, e.g.,

- No reconciliation of line 9 "chargeable income".
- Schedule J "cost of sales" is the only information relating to an income statement on the return.
- No Schedule for gross receipts.

Clearly time must be spent in the redesign of this Form.

The law does require that a copy of audited accounts be submitted with the return. However, for uniformity, an income statement and balance sheet should be made a part of the tax return.

Tax Administration in a Simplified System

The tax administration would be improved considerably if the income tax system was made less complicated by broadening the base, simplifying

the rate structure and permitting fewer deductions. This could eliminate approximately 12,000 PAYE taxpayers from the enforcement program, leaving 2,500 self-employed and 300 company taxpayers to be considered for the audit program.

A group of 12 to 15 well trained auditors could examine the above 2,500 self-employed and 300 company taxpayers. During the course of the examination of the above group, they could be trained to examine the employers PAYE withholding method to assure that the remaining 12,000 individual PAYE are complying with the law.

III. Technical Assistance Needs

Training Requirements

Staff	Basic Accounting	Advanced Accounting
Inspectors	5	5
Tax Officers	6	6
Cashier	1	1
Clerks	2	2
Revenue Collectors	2	
TOTAL	16	14

Staff	Income Tax Law Course
Inspector	5
Tax Officers	6
Clerks	7
Revenue Collectors	2
Bailiffs	8
TOTAL	28

Staff	Audit Technique Course
Inspectors	5
Tax Officers	6
Clerks	2
TOTAL	13

Staff	Report Writing Course
Inspectors	5
Tax Officers	6
Clerks	2
TOTAL	13

Staff	Investigation Techniques and Report Preparation
Inspectors	3
Revenue Collectors	2
Bailiffs	8
TOTAL	13

Staff	Public Relation Course
All members dealing with the public	35

Staff	Instructor Cadre Training
Top Management	2
Mid-Management	2
First line Supervisors	5
TOTAL	9

Because of the limited number of staff, the above indentified training needs will have to be conducted on site during the normal working day. This could be accomplished by scheduling classroom sessions several hours per day for two or three days each week. The tax advisor plays an important role in the design and presentation of these proposed courses. It is clear that the three employees selected for the Instructor Cadre must equally be closely involved.

Modified Assessment Scheme

After discussion with Officials of the Inland Revenue Department, the feeling conveyed was that any modified program would have to be limited for the following reasons:

- Political pressures by certain business groups.
- Limited numbers of taxpayers within some professions or business groups.

For example, it was pointed out that there were only three or four dentists in the country. A modified asessment plan could possibly be used for taxi drivers, auto repair shops, craft shops, beauticians, barbers, etc. Association membership lists, trade license, etc., could be used to decide on the types of business to be included.

Technical Assistance Requirements

The necessary involvement of one experienced Advisor to implement a program of improved tax administration that could be sustained would require at a minimum twelve months to a maximum of eighteen months. This is ont he condition that there are no changes in the present structure of the Income Tax law and there is no computerization of the Department.

The reasons for the above conclusion are:

- Of the thirty-nine members of staff only three have had any realistic training. The training required will take approximately nine months.
- The present Manual would have to be reviewed and updated.
- A management information system would have to be designed including preparation of feeder reports for the system.
- Assist in establishing a sound taxpayer assistance and education program.
- Assist in redesigning the tax forms and instructions.
- Assist in centralizing the collection activities.
- Assist in the preparation of a Collection Procedures Manual.

- Assist in developing norms for a modified assessment program.
- Assist in the preparation of job descriptions.
- Assist in complete reorganization of the assessment and collection functions as soon as the self-assessment system becomes operative and provisional assessments can be discontinued.

If there are any major changes to the tax structure then the length of time required for an Advisor would be extended from a minimum of twenty-four months to a maximum of thirty months.

If more resources were to be made available, a short-term collection advisor should be considered to assist in the improvement required in the collection activity.

The rock-bottom investment would be as above. A good example of what happens if you do half a job was the 1979 experience of the IMF Technical Assistance. The technical assistance should be for a period long enough to implement the recommendations, field test them and ensure that the changes are working.

Meeting with Mr. Lauriston Wilson, Director General (Finance) Ministry of Finance

The folloowing agenda was used as a basis for discussing my tentative findings:

A. Self-assessment System -

1. Needs strengthening.
2. Too much time being expended on provisional assessments.
   a. Possible solutions.
      1. Increase taxpayer assistance and education program.
      2. Simplification of returns and instructions.
      3. Application of penalty sections of law for non-compliance. See Appendix C.

4. Provisional Assessment Methods should be reviewed and strengthened by:
   a) training personnel,
   b) develop a MAP System for certain business categories.

5. Develop a strong field and desk audit program of a certain percentage of self-employed and company taxpayers. This would be done after:
   a) adequate training for tax officers has been completed, and
   b) all third party information, indirect methods for determining correct income and other audit techniques would be applied. In addition penalties should be recommended if warranted.

6. A plan should be developed to bring the remaining estimated 7,500 taxpayers into the tax net through:
   a) third party information
   b) trade license,
   c) possible canvass procedures.

7. Review and update Taxpayer Master File. (Possibly computerize).

B. Develop an annual fiscal year work plan.

1. Prepare management information reports to monitor the plan monthly.

C. Collection Activity.

1. Bring all collection management and supervision under the Inland Revenue Department (Centralization).

2. Maintain Bailiffs in the parishes as it is now for convenience of taxpayers residing outside of St. George.

3. Training is needed in the law, collection procedures and public relations.

D. General Administration

1. Planning - Short range and Long range

2. Training
   a) Top Management - Possible overseas participant training and local training.
   b) Mid Management - Possible overseas participant and observation training, and local training.
   c) First-line Managers - Local training.

3. Establish an Instructor Cadre for training technical employees.

E. Technical Assistance

1. Tax Administration Advisor to assist in:
   a) Assessment procedures
   b) Audit techniques
   c) Training courses
   d) Update the Audit Manual
   e) Develop Management forms and reports.

2. Possible short-term Collection advisor to assist in:
   a) preparation of procedural Manual
   b) develop management forms and reports
   c) develop an annual Collection Activity plan.

Enclosures
Appendices A-F

FISCAL MEMORANDUM NO. 14

FISCAL PLANNING MODEL

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GRENADA TAX PROJECT

Fiscal Memorandum No. 14

TO: Mr. Lauriston Wilson, Jnr.
FROM: Michael Wasylenko
DATE: September 26, 1984
RE: Fiscal Planning Model

I. Background

The fiscal planning model is used principally to forecast central government expenditures and revenues. On the expenditure side, objects of government operations, for example, employment, wage rates, allowances and supplies, are forecast for each vote or function. Forecasts are based on assumptions about employment changes due to changes in government service levels, and about wage increases due to real and inflationary increases in pay scales. The other objects of expenditures are forecast based on both inflation and, if the expenditure on the particular object changes with employment levels, the number of employees. Separate analyses are required to forecast debt service, capital expenditure, and other special functions, such as pension schemes.

Forecasts of revenues are generally based on historical increases in revenues. These historical increases should be calculated when the changes in revenue that are due to discretionary changes in the tax code are omitted from the revenue data series. The level of sophistication at which this analysis can be performed depends heavily on the amount of historical data on revenues and discretionary changes that are available.

The model has a variety of uses on both sides of the fiscal account. It can be used to simulate what effects changes in wage rates, employment levels and other objects have on recurrent government expenditures. At

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another level, one could analyze the longer-term implications that changes in capital expenditure have on debt service expenditure. On the revenue side, various changes in real economic growth and inflation can be traced through to their implications for government revenues. Perhaps most important is that the forecasted expenditures and revenues can be used to produce estimates of future government deficits. Such an early forecast of the deficit facilitates better fiscal planning for controlling government expenditure and for the phased introduction of appropriate revenue increases to reduce the budget deficit in the future.

The fiscal (expenditure) planning model has two immediate objectives and several longer-range objectives. In the near term, the current expenditure items in an adjusted version of the 1984 budget are put into an IBM personal computer. Adjustments are made to the employment figures reported in the 1984 budget so that the employment figures in the computer reflect the actual number of employees instead of the preliminary figures in the budget. This gives a more accurate picture of the actual expenditure level for 1984 and a better basis on which to forecast expenditure in subsequent years.

The longer range objectives include the introduction of more flexibility into the expenditure forecasting model and integrating this model with the revenue side of the budget. In addition, capital planning and expenditures can be introduced into this model, and the repayment of principal and interest on debt can also be added to the model in a more sophisticated manner.

II. Breakdown of Expenditure by Object

The budget is organized by votes or functions (health, construction, etc.) and within each function by object. The broad classifications of objects of expenditure are personnel direct expenditure; including employment, average wages and allowances; personnel indirect expenditure; supplies; overhead and bulk items including the category "other". The expenditure objects are further disaggregated to accomodate the calculation of certain budgetary items, such as the National Insurance Scheme, and to facilitate making reasonable expenditure forecasts without disaggregating the model to the point where it amounts to forecasting each item in the budget.

Personnel Direct Expenditure

This expenditure category is about 50 percent of current central government expenditure. For purposes of the model, personnel direct expenditure for each function is disaggregated to five employment categories, five corresponding wage categories and a category called allowances. The five employment categories are based on the wage scale for the employees in the category. The first employment group consists of the head or heads of the agency. Generally these persons are the highest paid. The second group are the employees in established positions that earn more than EC$15,000 per year. A third group are in established positions and earn between EC$10,000 and EC$15,000 per year, while a fourth group contains persons in established positions and who earn less than EC$10,000 per year. A fifth employment category are workers in

unestablished positions, and who generally earn the lowest wage of the employees in the functional category.

The average wage for employees in each category is calculated for each function. Allowances are usually a relatively small expenditure and include expenditures for housing allowances, leaves and some overtime payments. The heads of the ministries generally receive the allowances and leaves.

There are two reasons for disaggregating the employees into five categories. The wage and employment growth rates are likely to differ in each of the five categories. Employment increases (and declines) will generally occur more at the lower wage levels than at higher wage levels. It is important then to be able to simulate different employment growth rates in each of the employment categories. In addition, employment growth in low wage categories will influence expenditures less than employment growth among higher wage workers. This disaggregation of employees into five categories gives the model the flexibility to simulate a variety of employment growth rates in each of the five categories. In forecasting this important category of expenditures, employment and wages are forecast in each of the five categories. To obtain total direct personnel expenditures, each of the forecasted employment levels is multiplied by their respective forecasted wage level and the five products are summed. Total allowances are forecast and then added to the sum of the labor costs in the five categories.

This breakdown in employment and wage into EC$15,000 and above and below EC$15,000 also facilitates the calculation of the expenditures on the National Insurance Scheme. This will be discussed below.

Indirect Personnel

Indirect personnel expenditures includes funds for reimbursing professional entertainment, expenses, and travel within and outside of Grenada. These amounts are generally allocated to officials of the Grenadian government and are not generally a function of total employment or increases in total employment. Therefore, this item is forecast using the same technique as in allowances.

Supplies

Total supply expenditures are taken as a ratio to total employment n the functional category. Thus, total supply expenditures can grow for two reasons. The cost and quantity of supplies per employee may increase and the number of employees may also increase. To forecast total supply expenditures, supply expenditures per employee are forecast and this figure is multiplied by the forecasted number of employees.

Overhead

For purposes of the model, overhead is disaggregated into two categories: utilities, which is telephones and electricity, and other overhead. The purpose of this disaggregation is to allow the utilities to grow at a different (higher) rate than the other overhead items. Thus each of these two items in overhead are forecast and the results are then added to produce forecasted total overhead expenditures.

Bulk

A fifth expenditure object includes current contributions to organizations, and, in 1984, expenditures for past contributions that were not paid in previous years, or arrears in contributions. Also included in

bulk items is a category called "other". For forecasting purposes, because arrears are non-recurring expenditures, they are subtracted from total bulk expenditures and the difference is used as the basis to forecast bulk expenditures for 1985 and other years.

Pensions

The pension system was revised in March 1983. All employees are now covered under the new pension scheme or the National Insurance Scheme. The government contributes four percent of wages under EC$15,000 per year per employee. Each employee also contributes four percent of his/her wages up to the maximum of EC$15,000 of wages per year.

The former pension scheme had no employee contribution and is strictly a pay-as-you-go system. Persons employed by the Government prior to 1983 have earned certain pension rights by 1983 under the old scheme. The employees retain the rights they earned before March 1983, but are now covered under the new pension plan and do not continue to earn pension benefits under the old scheme. However, upon retirement these employees will receive two pension payments for the contributions under the new and the benefits earned under the old scheme.

The government payments for current retirees under the former scheme are forecast using the annual rate of growth in these payments between 1980 and 1983. This growth rate figure is about 12.3 percent per annem.

The contributions to the new pension scheme for employees earning under EC$15,000 per year expenditures, are forecast using the level of forecasted labor costs multiplied by four percent. The government contributions for employees earning above EC$15,000 per year is calculated

by multiplying four percent by EC$15,000 and that product by the forecasted number of employees earning above EC$15,000 per year.

Debt Repayment

The Ministry of Finance has calculated the schedule of repayment of principal and payment of interest for 1985 through 1989. These figures of course represent payments for debt that has already been incurred. The total debt service payment for future years also depends on the number of new debt commitments that government may take on in subsequent years. New debt commitments are obviously related to the method of financing new capital expenditures. Capital planning will have to be implemented before accurate measures of new debt commitments can be added to the model. Thus, the forecasts of debt service only include that due on existing debt.

Capital

Capital planning does not appear to be well implemented in Grenada. Thus, only rough estimates of capital expenditure for 1985 and beyond are put into the model as a separate item.

III. Improvements to the Model

Presently, different growth rates can be applied to various objects of expenditures to simulate or forecast expenditures in future years. Thus, the Ministry of Finance can examine the implications of an across-the-board wage increase on labor costs and on national insurance scheme payments. More importantly, Government can analyze the expenditure implications of different wage increases for various types of personnel (high vs. low paid) and for employment cutbacks or increases in various

types of personnel. These types of simulations can also be performed for the other objects of government expenditures.

Despite the advances that the model introduces to fiscal planning in Grenada, there are several improvements that could be made to the model in a Phase II of the project. Presently, the model is programmed so that the same growth rate in employment for persons earning between EC$10,000 and EC$15,000 for example, will apply to this category of workers in all 110 functions. The model allows flexibility in choosing a growth rate for any of the objects described above, but once the growth rate is chosen, that particular growth rate applies to that object in every function. In a second phase of the model, one could allow--more realistically--different growth rates in employment in different functional categories. Similar flexibility for expenditure changes could be added to the other objects of expenditure.

Moreover, once a growth rate is chosen for employment, for example, that same growth rate is used for that object, not only for every function, but also for that object for every year into the future in which a forecast is made. This is a problem if forecasts of expenditures for more than one year are desirable, because it is unlikely that employment grows at the same rate in every forecasted year. Both of these limitations greatly reduce the flexibility of the model and reduce the number of interesting questions which the model can address. Subsequent versions of the model should introduce more complicated formulas and programming flexibility into the model.

Debt service and capital expenditure are not estimated very well in the model. This is due primarily to a lack of data in the Ministry on future capital projects and how they will be financed. Additional work on fiscal planning should emphasize capital planning and some estimates of debt service for future years.

At present, the model makes some forecasts of central government revenue. Due principally to a lack of historical revenue data, these forecasts are somewhat less sophisticated than they could be. A second phase of this research would also revise the forecasting methods for revenues.