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THE TAX MISSION TO VENEZUELA, 1958-59

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1. Genesis of the Tax Reform

By 1957 Venezuela had experienced more than one hundred years of dictatorships. It became an independent state in 1830, and in the years that followed, control was held mainly by caudillos from the landowning class. Later, this developed into the "total and absolute tyranny" (Columbia University Encyclopedia, p. 2875) of Juan Vicente Gomez, who ruled from 1908 to his death in 1935. In 1948 a repressive military dictatorship siezed power, and by 1952 Col. Marcos Perez Jimenez had become dictator. He made "wide use of police state techniques," and in January, 1958, "A popular revolt, supported by liberal units of the armed forces, broke out." Perez Jimenez fled, and a presidential junta was formed.

In late 1957 and early 1958, Thomas Enrique Carrillo-Batalla, exiled by the dictator after imprisonment, was living in New York City, taking graduate work in economics at Columbia University, including a course in public finance. I was not acquainted with his background until, shortly after January 23, 1958, Carrillo approached me to ascertain if I would consider forming a tax mission to Venezuela. He and his Venezuelan friends, now among those who were in control, had been contemplating for some time the changes in Venezuela's economic and governmental measures that would be desirable once the dictator, if ever, was overthrown, and high on this list, in Carrillo's view, was a reform of the tax system, both structurally and in administration. This view was shared by many of his compatriots who had participated in the Revolution and who looked forward to creating large amounts of human capital by increases in educational expenditures (one-half the children of school age were not in school) and outlays on public health. Moreover, with almost two-thirds of total tax revenue coming from oil, the system had to be strengthened structurally to be ready to raise substantially more revenue from non-oil sources when the former began to dwindle. In addition, the national government was running a deficit equal to nearly one-third of its expenditures. Finally, the tax system, apart from that segment dependent on oil, consisted largely of indirect taxes, and was accordingly but slightly progressive, if at all.

II. Initiation of the Project

Upon the invitation of the Venezuelan Minister of Finance, Dr. Arturo Sosa, Professor Stanley S. Surrey and I visited Venezuela for a week early in May, 1958, to ascertain whether the terms I would propose for the mission would be acceptable, and whether the prospects for a useful study were sufficiently bright. On both counts the answer was yes. The mission would come to Venezuela early in the summer and submit its report before the end of August. Choice of the mission members was the director's responsibility. The report would be printed in both English and Spanish, and made available in book form. A Fiscal Reform Commission, composed of Venezuelan tax and finance experts, with Dr. Carrillo as chairman, would help the mission obtain information, and would comment on its preliminary proposals, while submitting suggestions of its own. The Government agreed to pay the director a certain lump sum, out of which he would pay the other members of the mission and other expenses, returning any unspent balance, after deducting his own specified compensation, to the Government; the Government did not undertake to pay any more, if the actual expenses outran the budget (a sizeable item for contingencies guarded against this danger, and in fact an appreciable amount was returned to the Government). In this respect the plans for the mission contrasted with those for Japan in 1949-50, where all finances were handled directly by SCAP and the director did not have to make up a budget.

Dr. Carrillo urged, and I readily agreed with, two features for the mission's composition and scope: first, that the members of the mission be not all from the United States, and second, that the report present some background material on the Venezuelan economy, notably distribution of income, rate of investment, sources of its finance, and optimum uses of capital. Later it was decided to add sections on estimates of cost for certain goals of education and public health, and on an analysis of the Government's accounting system with a view to changes that would facilitate gathering data for the national income accounts. In these respects the mission's work extended well beyond the tax field proper.

Again I was fortunate in obtaining an affirmative answer from those approached to be members of the mission. The fact that only one of them (Stanley Surrey) had also been a member of the Japan tax mission a decade earlier simply reflected my appraisal that the Venezuelan problem was substantially different from that of 1949-50 in Japan, and called for a different pattern of specialized skills within the tax-finance field. The members of the mission, aside from the director, were:

John F. Due, Professor of Economics, University of Illinois
Lyle C. Fitch, First Deputy Administrator, City of New York
Sir Donald MacDougall, Official Fellow, Nuffield College, Oxford University
Oliver S. Oldman, Assistant Professor of Law, Harvard Law School
Stanley S. Surrey, Professor of Law, Harvard Law School

In addition, Consuelo Maldonado, Director of the Office of Accounting Systems of the Treasury Department of the Commonwealth of Puerto Rico, devoted a month in the summer of 1959 to revising and expanding the missions's chapter on government accounting.

Contributions were made to various factual and analytical sections of the mission's report by Dr. Jean Due, Research Associate, and Anthony H. Pascal, Research Assistant.

It was feasible, in contrast to the Japan of 1949, to have wives accompany mission members, and all did so, at least for most of the summer. Nevertheless, social life was restricted by the need to work intensively and for long hours, with conversation around the breakfast, lunch and dinner tables largely devoted to the mission's problems and activities (at the Hotel Tamanaco, in Caracas).

The mission's report was submitted August 22, 1958, then mimeographed, translated into Spanish, and circulated within the Government. Additional information thus obtained led to some revision and expansion of the report in June, 1959, in the course of a three-weeks visit to Caracas by Shoup and Surrey. The revised report was published later in 1959 by The Johns Hopkins Press in one volume (pp. xii + 491). A Spanish-language edition was printed by the Government of Venezuela.

The Venezuelan Fiscal Reform Commission noted above proved quite helpful, meeting every week with the mission, and assisting in obtaining information, planning trips throughout Venezuela, and discussing technical and policy issues, and in revising the first draft of the report.

III. The Tax Mission Report

1. Publication

As noted above, the final draft of the mission report was published in the United States, with funds covered by the mission budget, and was sold by the Johns Hopkins Press at $8.75 the copy (roughly $32 in 1987 dollars). Complimentary copies were distributed among public finance scholars and libraries.

The Spanish-language edition of the report,[1] published separately (contrast the procedure in Japan) in two volumes by the Ministry of Finance, was apparently not available to the public with a sale price, and was not widely distributed in Venezuela by the Government (noted in the report prepared for this present research project by Dra. Carmen

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[1] Informe sobre el Sistema Fiscal de Venezuela: Mision Shoup. Republica de Venezuela, Ministerio de Hacienda, Comision de Estudios Financieros y Administrativos. 1960.Vol.I: x + 490 pp. Vol. II: 317 pp.

Adela Lopez de La Roche - see <u>References</u>). On the other hand, Professor Oliver Oldman concluded (1968) that publication of the report in Spanish "was crucial to the Report's having substantial impact. The Report has been and is probably still being used in Venezuelan universities... The role of the Report in stimulating interest in tax structure reform and in identifying problem areas ought not to be underestimated. Moreover, the impact of the Report in other countries ought not to go unnoticed. The Report received wide distribution in Latin America and no doubt had a bearing on the Conferences on Tax Administration (Buenos Aires 1961) and Tax Policy (Santiago 1962), as well as on the formulation of the tax planks of the Alliance for Progress. Reforms which have already taken place in such countries as Mexico and El Salvador and are in progress in such countries as Brazil and Chile parallel many of the Report's suggestions with respect to income taxation. Finally, the Report continues to serve as a model in the preparation of fiscal surveys for other countries."[2]

2. Contents, in General

For the most part the tax mission report, running to almost 500 pages (English text), was a straightforward description and analysis of the tax system, tax by tax. In four respects, however, its contents departed form what might be expected in a conventional report on a tax system. The non-tax material accounted for about one-fourth of the report.

The first two chapters, following the opening summary of the entire report, consisted of a pioneering estimate of the distribution of income by income class in Venezuela (MacDougall) and a discussion of the problem of capital accumulation, and economic development in general, in Venezuela (also MacDougall). Sections of the latter chapter covered taxation of the higher income groups, budget surpluses and deficits, and considerations affecting the future level of taxation, as related to the general issue of development, as well as sections on capital requirements, actual rate of investment in Venezuela, sources of finance for investment, importance of the oil industry and of other foreign capital and know-how, and protection. The large amount of time and effort devoted to non-tax background material was necessary because of the neglect of these fields under the dictatorships.

Secondly, much original factual research and even development of the relevant theory was accomplished in the chapter on costs and benefits of attaining certain goals under education and public health (Fitch). Again, the dictatorships had neglected both these areas, especially

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[2] Foreword to Enrique F. Gittes, "Income Tax Reform: The Venezuelan Experience," <u>Harvard Journal of Legislation</u> 125 (1968), pp. 125-127.

education (always dangerous for a dictator). Much of the effort of the revolutionary group was destined to be channeled into these fields, and some quantitative guidelines were needed.

Thirdly, the concept of "tax" was extended to cover the Government's profits from a certain kind of exchange control: the petroleum companies operating in Venezuela were required to satisfy their needs for bolivars by purchasing them from the central bank at a rate slightly above three to the dollar, and the central bank resold those dollars to the commercial banks and the public at a substantially higher rate.

Fourth, although the mission report described the special tax measures that aimed at a 50-50 sharing of oil profits between the companies and the Government, no recommendation was made on whether to change that ratio: "this matter of national policy involves so many important issues other than taxation that it lies outside the scope of the commission's technical recommendations" (p.2).

Much of the chapter on Venezuelan National Government accounts and accounting reports encompassed more than a traditional tax study would include, since it also presented detailed descriptions of the accounting and reporting systems in offices dealing with expenditures. The point to be made was the practice of completely separating the functions of tax administration and tax collection, on the revenue side, and, ultimately, the degree of usefulness of the accounts in the task of compiling national income accounts, and in assisting in the formulation of fiscal policy.

The remaining chapter not devoted to a particular source or sources of revenue was that on the tax system as a possible agent in stabilizing the economy in booms and depressions through appropriate changes in tax rates.

A detailed examination of the income tax, personal and corporate, occupied about one-third of the report. Of this segment, about two-fifths was given over to administration of the tax, testifying to the importance the mission attached to this aspect of tax policy and practice. Indirect taxation, although of far greater current revenue importance, was allotted only about one-eighth of the total pages; the technical issues were less complex, and the mission's aim was to show how the direct-tax part of the system might carry a larger share of the total load. A substantial chapter on state and municipal finance (40 pages) reflected the status of these units as spenders of tax moneys raised almost entirely at the national level, and as potential revenue raisers should it be decided to decentralize the tax system somewhat.

Four appendicies dealt with (a) details of the differential exchange rate system noted above, (b) estimates of total taxes, direct and indirect, borne by each of twelve hypothetical Venezuelan families with varying amounts and sources of income and varying family status, under certain standard assumptions of shifting and incidence; (c) a description and appraisal of the income tax revision of December, 1958, and (d) a brief comment on the existing law of public credit ("both too restrictive and too loose").

The volume contained almost no references to articles or books in the public finance field (except the chapter on a possible general sales tax). A thirteen-page index concluded the report.

3. Recommendations: Substantive and Structural

The chief structural and substantive changes in the Venezuelan tax system recommended by the Commission report (administrative changes are covered in Section 4 below) concerned the income tax, the customs duties, the 0.5 percent turnover tax (to be repealed), the gasoline tax (to be increased), and a strengthening of the municipal real estate tax in urban areas. Suggestions were also offered for revision of the grants-in-aid system. Costs were computed for a program of enhanced education and the increase in income tax rates that would cover this cost were specified.

1. The nine schedular income taxes, and the overall complementary income tax to be replaced a single, unified tax. Under the existing law, income was classified into nine schedules (rents from real property, interest and royalties, business profits....) and each schedule had its own rules for deductions and its own flat rate. The complementary tax was applied at a progressive rate scale to the sum of the amounts entered under the schedular computations. The schedular rates, percent, were:1 (salaries and wages, 2 (agricultural profits and profits from non-commercial professions), 2 1/2 (oil and mining profits, business profits, rents from real property), 3 (interest and royalties, and gains from sales of real property) and 10 (lottery prizes). An inordinate amount of time and effort was taken up in deciding under which schedule a given item of income and, especially, expense, should be placed. The basis of the mild progression, type of income, was deemed inferior to size of total income. Instead, the complementary income tax was to be the only personal income tax; its rate scale, ranging from 1.5 percent to 26 percent, would be strengthened to take account of repeal of the schedular taxes. Personal exemptions under the unified tax would take account of family status, which they did not under the schedular taxes.

2. The corporation income tax to be henceforth a distinct, separate tax, not a virtual duplication of the personal income tax. At that time, corporations were subject to just the same set of schedular taxes and the complementary tax, at the same rates, as individuals. Dividends were not included in the taxable income of the shareholder.

"The present system would be understandable perhaps in an economic society in which corporations were family-owned and family-managed." (p. 112) But when individuals started to receive income from various sources, the progressive feature was weakened by the flat schedular rates, and, moreover, the progressive rate of the complementary tax led to the splitting of a family corporation into two or more corporations. The advent of the modern widely held corporation also negated the rationale of the identical-rates treatment of the corporation and the individual. Moreover, if tax policy required an increase in the rates applicable to individuals, that same rate change would probably not be deemed appropriate for corporations. Accordingly, a separate rate scale was recommended for the corporate tax: 10 percent of the first 50,000 bolivars (Bs.) of profits, or perhaps the first 100,000 Bs., 20 percent on the next block of profits up to, say, Bs. 10,000,000, and a top rate (not specified) on profits above that. The existing reductions in tax rates for the top three brackets (complementary tax) for reinvested earnings should be repealed.

3. Double taxation of dividends, or something close to it, would occur under the new regime, unless measures were spelled out to prevent it, and the Commission report went into great detail in arriving at a suggestion of the best way to avert or mitigate such extra taxation (pp. 114-125). The deduction-to-corporation technique and that of credit to shareholder (with grossing-up) were closely compared, and seen to be virtually the same in the more important results; administratively, the credit method was thought to be somewhat simpler. In either case, the aim, for reasons given, was to reduce the double taxation, but not to eliminate fully the effect of the corporate tax.

4. At some later date, a world-wide principle of taxing income to be adopted, to replace the existing territorial (or "source") principle. Credit would be given for foreign income taxes paid. This issue was not urgent, because in 1958 Venezuelan individuals and corporations were apparently receiving little income from abroad. A change to the world-wide principle would discourage the use of Venezuela by "base companies", established there to control foreign operating subsidiaries or branches and to receive income from such foreign sources. Also, continuation of the territorial principle might give an undesirable incentive to Venezuelans to invest abroad. Meanwhile, the actual application of that principle in Venezuela was too strict, in disallowing some expenses, just because they were made abroad, that were properly allocable to income earned in Venezuela. Non-residents, of course, would in any case be taxed only on their income arising within the country. The report goes into some detail regarding certain troublesome conceptual and accounting problems on this score.

5. Exclusion of certain amounts or types of interest from

taxable income, and certain rents, should be "re-examined," and, the report implied, probably repealed.

6. Capital gains should continue to be taxed, but with the benefit of an averaging formula. Gains accrued at death should be reached, perhaps indirectly through a special regime under the death or gift tax.

7. Certain recommendations were made concerning the existing limit on deduction of corporate salaries, loss carry-overs, worthless-stock losses, and deductions for certain personal expenses (pp. 169-171). Some liberalization of the accounting rules permitted taxpayers was suggested, and certain changes in the statute of limitations (pp. 172-174).

8. As to property passing at death or by lifetime gift, the report made no firm recommendation for change from the existing succession tax, levied on the donee, to an estate tax, levied on the donor. The pros and cons were spelled out, and at least some doubt was expressed on the advisability of making the amount of tax depend on the relationship of the recipient to the donor.

9. Venezuela, the report recommends, should move away from the existing pattern of raising some 70 percent of non-oil national tax revenues from indirect taxes, instead, strengthening the income tax, repealing the general sales tax, reducing many of the customs duties, and raising the admittedly moderate taxes on liquor, tobacco, and motor fuel only because, as to the first two, additional general revenue might well be needed to finance education and health and balance the budget, and, as to motor fuel and the like, benefit taxation did call for some increase. The case for decreasing the overall share of indirect taxation was particularly strong for Venezuela, given that it had an important source of tax revenue in its natural resources, and that the income tax, apart from the oil sector, was "little more than a token levy" (p. 5).

10. As to the particular excises, there were "no obvious features of liquor taxation which appear to warrant drastic revision" (p. 257). The cigarette tax, instead of being at a uniform specific rate, might well be graduated in two to four brackets according to the retail selling price. The tax on gasoline, collected at the refineries, should be raised from .01 Bs. a litre (.01 Bs for super grade) to .05 Bs. and .09 Bs. respectively.

11. The customs duties not levied for protection, i.e., imposed on articles not produced in Venezuela, should be removed, except for luxuries (see No. 12 below). Many of these items were producers goods and the tariff burden on the consumer goods was haphazard. Especially

appropriate for such exemption were various food items, paper, industrial machinery, and chemicals. (No estimate was given of the revenue loss.)

12. On a specified list of articles regarded as luxuries, the import duties should be kept, but transferred from a specific basis (so much per pound, usually) to a percentage-of-value (ad valorem) basis. If the article were also produced in Venezuela, a similar rate would be imposed: the same, if no protection was sought. The rates suggested by the report, as examples, were low (10 to 30 percent) compared with usual luxury-tax rates. No revenue estimate was given.

13. The so-called consular fees, levied at ad valorem rates progressive with the size (value) of a shipment, should be imposed at a single rate, with exemptions, possibly, of a few basic goods consumed in large amounts by lower-income groups.

14. The general sales tax, a turnover tax of one half of one percent on all sales, with no allowance for tax paid at earlier stages of production or distribution ("cascade tax") should be repealed. The many well known faults of this type of tax were cited, including its burden on the poor, its artificial inducement to vertical intergration of business firms, and the difficult administrative tasks it posed. This tax had been yielding some Bs. 120 million a year. Total national tax revenue was running at slightly under Bs. 4,000 million. The revenue loss would therefore be on the order of only 3 percent - owing to the very low rate. If Venezuela desired to retain some form of general sales tax (an action not recommended by the Commission), it should probably adopt a wholesalers sales tax. A retail sales tax, or a value-added tax carried all the way through the retail stage, would be preferable in principle, but not in practice, in view of the administrative problems to be encountered with the very large number of small shops and stands at the retail level. (The report spelled out in some detail how such a wholesalers tax should be constructed and administered).

15. On the question of whether the Venezuelan states and municipalities should be given substantially more taxing power, or exercise more of the power they already had, the Commission did not take a stand one way or the other (p. 350). The states had virtually no taxing power of consequence, and the municipalities, only the business license tax ("patente"), the urban real estate tax, and the automobile license tax. For the fiscal year ending June 30, 1959, the national government was estimated to collect Bs. 3,809 million in what the Commission considered tax revenues; the state governments, only a few millions; the Federal District (this includes Caracas), between Bs. 50 and 100 million; and the rest of the municipalities (strictly, distritos), less than Bs. 100 million (p. 3).

16. "The only taxes now imposed by the states are very minor ones on raffles and sales of lottery tickets of other states, and the anomalous unconstitutional tax on imports imposed by the State of Zulia," (p. 317), yet the Commission concluded that "Even assuming that constitutional barriers were removed, there are few feasible tax sources which the states can effectively administer," and that therefore the states' taxing role would have to remain minor. One possible new state tax would be a "supplement income tax assessed on residents of the state, or a percentage of taxable income as defined for national income tax purposes, reported by residents of the state. This tax, imposed by the states, would be collected by the national government and turned over to them. This is to be distinguished from a state-collected tax based on what the taxpayer shows on his national income tax return, or expressed as a percentage of the national tax. Another possible state tax, one "which would take some time to develop," was "a tax on agricultural land holdings; these now pay no tax at all" (pp. 326-327).

17. As to municipal taxes, the Commission was not happy with the patentes on industry and commerce, which took two main forms: a per millage of gross sales or gross revenues, the rate depending on the type of business, and a system of flat-sum taxes, the amount depending on the "class" of the particular firm. But if the tax were retained, it should be removed from manufacturing and wholesaling firms, eliminating the flat-sum feature, and restricting the rate structure to two basic rates. The tax law should be revised and codified, through a national "model" tax law.

18. The urban real estate tax, in contrast, was regarded favorably: it was "the only state or municipal tax source capable of yielding substantial increased revenues" (p. 336). It should continue to be based on rents rather than on capital values (the Federal District tax rate on rents was 6.5 percent), including imputed rent. Future increases in rates should probably be laid more heavily on land than on improvements (pp. 339-340). In any event, "the tax on urban real estate should be left to the municipalities. Taxes on agricultural land should be reserved to the states, or possibly to the national government, in connection with a general land reform program" (p. 340). If land were to be taxed more heavily than improvements (as to future increases in tax), it would be necessary to move from a rental basis to a capital-value basis. "It is suggested that [the increase in] the rate on land be twice that on buildings." (p. 340). Special assessments should be imposed to recover the cost of public improvements that enhance the value of land.

19. The rates of the municipal tax on automobiles, which varied among municipalities, and induced many car owners to register falsely in low-rate municipalities, should be made uniform thoughout the country. The base of the tax for passenger cars should be changed from weight to

value. The national government should collect the tax for the municipalities.

20. The national government should make general-purpose grants direct to the municipalities, according to need and financial capacity, so that the richer localities would meet their needs from their own resources. Specific-program grants might also be instituted. The report offered some suggestions as to the particular structures of possible grants.

21. In any case, "the national government must continue to raise the bulk of the nation's public revenues". (p. 348). The potential increases in local tax revenues would be chiefly from better administration and expanded use of the real estate tax, partly offset by repeal or improvement of the patentes. The report presented a number of reasons for granting more spending powers to the local units, along with several reasons to the contrary, but did not make a firm recommendation on this point, noting only that a great percentage increase in local spending could be made by accepting only a small percentage decrease in national spending. More cooperation among the three levels of government was badly needed, in view of overlapping responsibilities for supplying education, water supply, sanitation, health and medical facilities, rural roads, and measures to increase farm productivity; the report offered some concrete suggestions to this end. Finally, the pressing needs of the Federal District could readily be met by increasing the rate and enforcement of its real estate tax.

22. Only about one-half of the number of children in the age-group 6-12 years were attending elementary school and kindergarden in Venezuela in 1957-58. The drop-out rate was high: the number of those completing sixth grade in the 1956-57 school year was only 18 percent of the number who had entered first grade in 1950-51. Many schools were offering no more than two or three grades. Data gathered and analyzed by Lyle C. Fitch on comparative earning power by level of education, and on the cost of supplying education (including earnings forgone) indicated that in Venezuela at that time the incremental rate of return on an additional dollar spent on education in the primary schools would be between 82 percent and 130 percent per annum - far higher than could be obtained by almost any business investment. For additional secondary school education the annual rate of return was estimated at only 17 percent, rising somewhat to 23 percent for university education. The difference was due in large part to the earnings-forgone cost for the older students. The cost of the expanded education program proposed could be met, in the first year, by a moderate increase in the corporation income tax rate along with an increase in the unified personal income tax rates that resulted in bracket rates ranging from 6 percent to somewhat above 14 percent for total revenue from this tax.

23. Public health expenditures were seen to be another sector where additional expenditure could be easily justified, but the data did not permit the kind of cost-benefit computations made for education.

24. Each of the tax measures recommended by the Commission was examined, in Chapter XIII ("The Tax System and Economic Stability"), to ascertain whether it increased (+) or decreased (-) the sensitivity of the national tax system to fluctuations in business. Such sensitivity was deemed desirable, if the fluctuation occurred in the non-oil sector, since an increase in tax revenue would automatically tend to check a boom and a decrease in tax revenue, to dampen a business depression (changes in oil-sector tax revenue would have modest or no effects, given the degree of foreign ownership of the oil companies). Non-oil tax revenue was so small, however, relative to national income, that the automatic effect would be slight. The plus or minus ranking of the proposed tax changes is reproduced here from Table XIII-1, p. 362. All of these changes were recommended for reasons other than sensitivity.

Recommended Tax Measures Classed by Effect on Sensitivity of Non-Oil Segment of Venezuelan Tax System
(Table XIII-1, P. 362, Commission Report)

Income Tax	Increases in Sensitivity	Decreases in Sensitivity
1. A more progressive rate	+ (?)	
2. Lower personal exemptions	+ (?)	
3. Carry-backs of business loss	+	
4. Taxation of dividends		-
5. Higher rates but less progression in corporation income tax		-
6. Current payment of tax on estimated income of current year; and extension of withholding	+	
7. Averaging of capital gains over several years, and carry-forward of unabsorbed capital losses		-
Customs Duties		
1. Higher tax rates on certain luxuries	+	
2. Lower tax rates on certain necessaries	+	
3. Extension of ad valorem basis in place of per kilo basis	+	
Gasoline Tax		
1. Higher rates	+	
Real Estate Tax		
1. Improved administration and increased rates		- (?)

(Question mark indicates considerable doubt which category the item belongs to.)

4. Recommendations on Tax Administration

(a) Income Taxation

The report's recommendations on tax administration were especially lengthy and detailed with respect to the income tax. Some idea of the degree of detail can be gained by scanning Appendix A, which shows the topics and sub-topics covered in the recommendations chapter for income tax administration, following a chapter describing the existing procedures. Only the major recommendations are listed here.

1. The declaration form to be redesigned, to encourage and in some cases require that the taxpayer himself compute his net taxable income and the tax due (both of these tasks were being performed by the tax administration, on the basis of declarations of income submitted by the taxpayer, and information at source.)

2. Major taxpayers to pay the tax at the time of submitting the forms, instead of awaiting a bill computed and sent by the tax office.

3. A list of potential taxpayers to be drawn up, and kept current.

4. Collection of delinquent accounts to be improved by (a) visits by a specially trained group of tax officials to delinquent taxpayers to determine capacity to pay and use of installment payments, (b) garnisheeing wage or other payments made to delinquent taxpayers and attaching liens against their properties; (c) gradually ending the existing system of turning over large overdue accounts to private lawyers on a commissions basis.

5. A system to be built up for gathering information from payors of various types (other than those withholding tax) as to payments made to individuals and business firms.

6. The field audit function to be expanded and systematized, a function "now largely performed in an inadequate, haphazard fashion" (p. 212), and the office auditing to be improved also. Some tax agents should be especially trained to handle cases involving fraudulent reporting.

7. Strengthen and streamline the system of certificates of solvency. This certificate, attesting that the individual was not delinquent on income tax, was being required of anyone entering into a contract with a governmental agency, obtaining a license to operate a business, getting permission to go abroad, and the like. "It seems that this type of sanction is quite acceptable to Venezuelan social political philosphy, while direct sanctions, such as jail sentences for tax violations, are not acceptable" (p. 217). The solvency system "should as nearly as

possible require certificates of only those persons who are obligated to declare their income and to pay tax" (p. 217) Therefore the requirement should be cast in terms of various groups of persons that are likely to consist largely of taxpayers. "Businessmen of almost all kinds constitute a likely group. So too do purchasers of homes above a certain price. Buyers of expensive cars....Members of the legal, medical, engineering, and accounting professions..." Then comes the problem of finding an annual, or more frequent occasion for showing the certificate. Then, "how often should a certificate be issued and for how long should it be valid"....Our tentative thinking...is that the tax receipt itself should serve as the basic certificate of solvency" (p. 218). The report offered several additional suggestions on use of the solvency certificate in the five pages it devoted to this important administrative subject.

8. The withholding of income tax on wages and salaries to "be made into a more effective collection device" than the existing 1 percent withheld tax under one of the schedules (p. 220). This could be readily done under a unified income tax. Tax refunds would occasionally be necessary, and the report suggested details for such a procedure.

9. To put other taxpayers on a par with those withheld from, a pay-as-you-go system should be introduced: payment, in quarterly installments, of the estimated tax on the current year's income.

10. The taxpayer to be allowed to appeal within the tax administration against any claim for additional tax asserted against him, instead of having to go directly to court. The Tax Court was working well, but it should have all of its decisions published regularly.

11. "The present system of penalties, based on a range of 10% to 100% and 200% of the amount of tax involved,...involves too much administrative discretion" (p. 228). The report therefore suggested a series of penalties largely automatic in their gradation, for failure to file a declaration on time, late payment of tax amounts admitted to be due, and increase in tax owing to failure to report items of income or to disallowed deductions.

12. The work of the Technical Division, a section of the Income Tax Administration, to be recast. "This division should essentially be a group of skilled technical experts, legal and accounting, charged with the tasks of interpreting the statute and regulations and dealing with the complex technical problems arising at the administrative level," and with supplying information to the public (pp. 230-231).

13. A reorganization of the tax work within the Ministry of Finance to be carried out as suggested in a chart on p. 234 of the report.

14. The checking function of the Controller of the Nation to be retained, but with far less duplication of procedures - or perhaps the work of the Controller in this area to be ended entirely.

15. More specialized training to be given to the tax personnel, including some training in courses abroad.

16. Much more statistical information, obtained from the income tax returns, to be assembled and published.

17. The pool of funds from a part of delinquent taxes collected, and the like, disbursed to certain personnel, to be discontinued, and a direct increase of salaries substituted.

18. More information to be made available to the public on the structure of the tax system, methods of administration, and the public's tax responsibilities. Special tax courses to be available in law schools and business schools. "...it would be helpful to form an organization interested in the subject of taxation, such as a Venezuelan Tax Association," to "hold meetings devoted to discussions of tax subjects and publish a periodical containing articles on tax policy and technical tax issues". (p. 241).

(b) Other Taxes

Administrative and compliance problems of taxes other than the income tax took up relatively little of the report, only some seventeen pages scattered throughout several chapters. This reflected the Commission's emphasis on the income tax as the chief source of additional revenue for future years if the budget deficit were to be eliminated and if large additional funds were to be made available for education and public health. It also reflected, to a moderate degree, the weighting of expertise among the Commission's members toward the income tax, in terms of the professional backgrounds of those members. This weighting was deliberate, however, in the choice of the Commission membership.

The chief administrative recommendations with respect to these other taxes were as follows:

1. Administration of the inheritance and gift taxes to be transferred from the Indirect Tax Administration to the Income Tax Administration.

2. Bearer shares promote evasion of the inheritance and gift taxes, as of the income tax, and if the devices to deal with this, suggested for the income tax, proved effective, there could be repealed the inheritance tax on a corporation that issues bearer shares to a stockholder whose capital contribution to the corpoation exceeds 50 percent of the property

he owns at that time; otherwise, this provision should be retained and strengthened.

3. As to liquor taxation, the report implied that, owing to rigid control measures, this tax was being well enforced; however, "some illicit production and sale occurs, the magnitude of which is difficult to estimate, but it is probably not a large proportion of total consumption." (p. 256).

4. In administration of the customs duties and consular fees, ten specific recommendations were offered, including (i) elimination of the system of granting a portion of fines assessed to customs inspectors and other personnel, contingent on an increase in base pay, (ii) certain increases in number of inspectors and physical facilities, (iii) simplification of consular invoices (if the fee is retained), (iv) codification of customs regulations, and (v) sharp curtailment in assessment of fines when no intent to defraud is evidenced.

5. Better administration by local tax officials, needed throughout Venezuela, should be promoted by the national government by (i) drafting model tax laws for the local taxes, (ii) devising model forms and procedures for administering those taxes, (iii) conducting training sessions for tax administrators in the several states, (iv) creating a permanent central unit charged with improving local tax administration, (v) exploring the idea of making grants conditional on greater local effort to raise tax revenue.

IV. Degree of Implementation of Tax Commission's Recommendations

1. The Pace of Tax Reform, 1958-1987

As background for assessing the extent to which the Commission's recommendations were adopted, we first take a general view of tax reform in Venezuela in the nearly thirty years that have elapsed since the Report was written.

The very year 1958 saw adoption of one of the most immportant recommendations, that is, repeal of the turnover tax ("cinco por mil"). Thereafter, tax reform languished, except for a 1961 law that adopted a separate income tax rate schedule for corporations. In late 1966, however, the core of the Commission's reform for the income tax was adopted, by substituting, for the schedular taxes and the complementary tax, a unified income tax. Oil and mining companies continued to be taxed under a special regime. In 1973 customs duties were changed to accord with the Andean Pact. In 1983 the Commission on Fiscal Study and Reform, chaired by Dr. Carrillo, submitted its report, which has been debated in Congress but has not yet led to extensive change in the tax system (this report covered a wide range of government fiscal activities besides taxation: government expenditure, public debt, budget, and administration, accounting and control, areas that are not covered in the present research project). In 1986 a fairly comprehensive stamp tax was enacted, which some have seen as a type of general sales tax. A few other changes were made in the 1958-1987 period that will be noted in the appropriate sections below.

This summary does not include reforms in tax administration, to be treated separately below.

2. Extent of Adoption of Report's Tax Recommendations: Substantive and Structural Matters

The following paragraphs will take up the nineteen substantive and structural tax recommendations listed in Section II above, to ascertain the extent to which they became incorporated into Venezuelan tax law.[1]

(1) Schedular Taxes

Replacement of the schedular income taxes and the complementary tax by a unified income tax on individuals and a separate income tax on corporations, effected by 1966, has been maintained to the present. Individuals, including partners and sole proprietors, pay a progressive-rate tax on total income, including their shares of partnership profits (PW, 70), computed under "Tariff 1." Corporations and similar entities pay tax under a separate progressive-rate "Tariff 2." Petroleum and iron mining companies were nationalized in 1976 and 1975 respectively; when in private hands they had been subject to a third type of income tax regime.[2] This transformation of the income tax structure was the single most important income tax recommendation in the Commission's report.

Family status, not taken into account in the schedular taxes, is allowed for by personal tax credits: a basic credit, plus a smaller credit for a dependent wife not filing separately and for each other dependent that is an ascendant or descendant.

(2) Corporation Tax

[1] The sources used are chiefly those listed in the References below as follows: Carrillo, Gittes, International Bureau of Fiscal Documentation, Lopez de La Roche, Price Waterhouse.

[2] However, there continues to exist a separate income tax rate applicable to mining and hydrocarbon activities of 60 percent (PW, 70, 124), and 67.7 percent (PW, 131), respectively.

The graduated rate schedule applicable to "corporations (S.A.s) and limited liability companies (S.R.L.s); participants with corporate attributes in limited, civil, temporary and de facto parnerships; and foreign corporations with operations in Venezuela, not engaged in the exploitation of hydrocarbons, mining and related activities" (PW, 123) ranged, in 1984, from 18 percent on the first Bs. 300,000 to 50 percent on taxable income over Bs. 20 million. In 1986 it was simplified to 15 percent (first Bs. 500,000), 35 percent (next Bs. 4,500,000) and 50 percent (all above).

The rules for determining taxable income for a corporation are the same for all types of business income, and of course no distinction is made in the tax rate schedule, in contrast to the regime in force in 1958, where different types of corporate income were taxed at different rates under the schedular taxes.

(3) Dividends

Double taxation of dividends, under the new regime of a corporate tax and an individual tax, was mitigated in the 1966 law by allowing a tax credit of 40 percent of the dividend, in the individual's return, but without a "gross-up" (Gittes, 150). At present, however, no such credit is allowed, hence dividends are currently taxed twice, once by the corporate tax and again by the individual tax. For a two-year period starting December 29, 1982, an individual shareholder could deduct 50 percent of dividends received from corporations registered on the Stock Exchange (PW, 88, 104). Dividends received by a corporation are not subject to the corporate tax. The Commission's recommendation on dividends has therefore in general not been adopted.

(4) World-Wide and Territorial Principles, Income Tax

Nearly thirty years later, Venezuela gave tentative acceptance to the Report's recommendation that its income tax be extended to income derived from abroad by Venezuelan residents, with some allowance for foreign taxes on such income. The 1986 tax law provided, apparently, for limited taxation of foreign-source income, but without immediate implementation. To be sure, the Report had said there was no urgency here, but thirty years seems ample time to allow, so that the recommendation's acceptance has been only partial at best.

(5) Partial Exclusion of Interest and Rents

The Report's implied suggestion that the partial exclusion from taxable income of certain amounts and/or types of interest and rents should be ended has on the whole not been accepted. Individuals are exempt as to interest on time deposits made for periods of at least ninety days in national finance or banking institutions and, within established limits, on savings accounts (PW, 105). Moving from the recipient to the payor, we find that deduction is allowed to the individual taxpayer for "Interest on loans to purchase or enlarge the principal residence...or for rental of the principal residence" (PW, 105), with a ceiling (for this and three other types of deduction, apparently, together) of 30 percent of total income if not over Bs. 200,000, plus 1.5 percent on the portion of income from Bs. 200,000 to Bs. 500,000.

(6) Capital Gains and Losses

Capital gains are included as ordinary income to both corporations and individuals, and capital losses are deductible under specified circumstances (PW, 75, 104). Thus the Commission's recommendation has been accepted, aside from the absence of an averaging provision and, apparently, taxation of gains accrued at death.

(7-A). Limits on Corporate Salaries

The Report, while agreeing that some limits had to be put on deduction of corporate salaries, at least those salaries that went to officers who were also stockholders, pointed out several unsatisfactory features of the existing limitations (pp. 169-170). These features have been, on the whole, removed in the present law (PW, 78-79).

(7-B). Loss Carry-Overs

The recommendation that business losses should be carried forward two years or possibly three under a unified income tax has been accepted, but, contrary to the Report, no loss carry-back is allowed (PW, 82).

(7-C). Worthless-Stock Losses

(Information is not at hand, as this is written, as to whether, as recommended by the Commission, worthless-stock losses are deductible.)

(7-D). Deduction of Personal Expenses

More, not less (as recommended in the Report), deduction is allowed for personal expenses than in 1958 (PW, 105; Report, 170-171).

(7-E). Accounting Rules

Installment-method accounting and deferred-payment accounting were not allowed in 1958; both were recommended by the Report. The former method is now allowed and, apparently, the latter also under the completed-contract and percentage-of-completion methods (PW, 74).

(7-F). Statute of Limitations

The point in time at which the obligation for payment of tax on a given year's income and the right of the Government to impose fines both lapse has been shifted somewhat from that in 1958, but apparently not closely in line with the Report's suggestions on this score [PW, 115-116].

(8) Death and Gift Taxes

The succession type of tax has been retained for transfers at death by living gifts, and, with it, the variation in tax rates according to or the relationship of the donee to the donor (the Report doubted the usefulness of this relationship variation). The Report's recommendation for cumulation of transfers from any one donor to any one donee, over time, has been partly accepted. Such cumulation, used to determine the tax applicable under the progressive rate scale, now is required for a five-year period (PW, 107). The Report was favorably disposed toward higher rates, at least at the upper part of the rate scale, for this tax, and, over the years, the rates have indeed been raised, so that they are about double what they were in 1958, in the upper ranges at least (PW, 129; Report, 244).

(9) Pattern of Taxation in Non-Oil Sector

The structure of that part of the national tax system applied to the non-oil sector has developed in line with the Report's recommendation in 1958. The non-oil income tax, instead of being "little more than a token levy," (see p. 8 above) is now "the linchpin of the non-oil tax and fiscal system" (Carrillo, p. 61), though, indeed, "its proceeds come largely from the tax on business income and the tax on income from games and betting" (Carrillo, p. 63) -- the individual income tax is still modest, by international standards. No general sales tax has been levied to replace the turnover tax repealed in 1958, though the stamp tax passed in 1986 may prove an important revenue source. Customs revenues have declined from their 1958 degree of importance, though apparently more from restriction of trade due to protectionism rather than, as the Report recommended, through lowering of duties. The excise taxes have not increased, relatively, enough to alter the general picture that shows a shift of the structure to direct taxation.

Social security payroll taxes were unimportant in 1958, and were not studied in detail in the Report (p. 10), but by the 1980's they had developed to the point where the two major payroll taxes, the one, contributing to the Venzuelan Social Security Institution (IVSS) and the other, to the National Institute of Educational Cooperation (INCE), supplied, in 1980, more than twice the revenue produced by the personal income tax. The rate of the former (in 1933) was 11 to 13 percent on the employer, and 4 percent on the employee, a total of 15 to 17 percent, while the education institute tax was only 1 and 0.5 percent on employer and employee (Carrillo, pp. 89-90). The proceeds are paid, rot into the national treasury, but directly into the respective agencies.

If these payroll taxes are considered direct, the change in the direct-indirect tax pattern from 1958 has been even greater than indicated above.

(10) Excise Taxes

As this is written, information is not at hand on the two recommended changes noted on p. 8 above: graduation of the cigarette tax according to retail price, and increase in the gasoline tax. Since nationalization of the hydrocarbons industry in the 1970s, the latter tax, as such, no longer exists.

(11) Customs Duties

The recommendation that customs duties not levied for protection be removed, except for luxuries, has been followed to some extent (Lopez, p. 37), but in relative importance has been overshadowed by the growth in protectionist duties. (The Commission Report did not take a stand for or against protection.)

(12) Duties on Luxuries

Information is not at hand on the degree, if any, to which specific duties have been restated as ad valorem duties, on luxury imports. The chief influence on these and other duties has been the Cartegena agreement adapting the duty structure to the Andean Pact, under a decree effective from January 1, 1973 (Lopez, p. 37).

(13) Consular Fees

Apparently the recommendation on consular fees has not been followed (p. 9 above).

(14) General Sales Tax

The Commission's recommendation to repeal the low-rate turnover tax was adopted immediately, in late 1958. The 1986 stamp tax, on the other hand, seems like a step back toward the turnover tax.

(15) Degree of Taxing Power for States and Municipalities

Evidently the states and municipalities have not been granted significant increases in their taxing powers. The Commission made no firm recommendation on this issue, aside from concluding that the states' powers would have to remain minor aside from, possibly, a supplement income tax; this latter has not been adopted.

(16) Restructuring and Restricting of Municipal Patentes

The industrial and commercial license tax levied by municipalities has apparently not been reformed substantially, if at all, along the lines recommended by the Commission.

(17) Real Estate Tax

The only major change recommended in the urban real estate tax, rate increases to be laid, probably, more heavily on land than on structures, seems not to have been adopted. Agricultural land is still not taxed.

(18) Municipal Tax on Automobiles

Information is not at hand on the present status of this automobile tax, but apparently the recommendations for rate uniformity, a value base, and national collection have not been adopted.

3. Summary of Results Shown in Section 2

The degree to which tax reform in Venezuela, 1958-1987, on substantive and structural matters has coincided with (and, possibly, been caused by) the Commission's recommendations cannot be estimated by counting all of them as of equal importance. Views on the weighting to be attached to each of the proposals will of course differ. The present writer, for example, considers the most important recommendation, by far, to be that of replacing the schedular taxes and the complementary tax on incomes, levied on individuals and corporations alike, by a unified personal income tax and a separate corporation income tax. Without this change Venezuela could scarcely hope to raise non-oil tax revenue to the level required by prospective increases in expenditures (especially on education and health) without imposing a heavy general sales tax that would partly negate the purposes of the improvements in education and health.

For illustrative purposes and to set out my own weightings, the following table is offered. The recommendations, represented by the numbers attached to the respective sub-sections in Section 2 immediately above, are classified as either Major or Minor, and are distributed in the table according as they were implemented (Yes), or were not (No) or were implemented only in part (Yes-No) or "Don't Know".

Yes	No	Yes-No	Don't Know
	Major		
1	3	4	
2	16	6	
9		8	
14		11	
	Minor		
7-A	5	7-B	7-C
7-E	7-D		10
	7-F		12
	13		18
	15		
	17		

4. Extent of Adoption of Report's Tax Recommendations. Administrative Matters

(A) The Record

As with Section 2 above, the present section will take up, paragraph by paragraph, the recommendations made by the Commission, to ascertain the extent to which administrative changes now in force, compared with the practices of 1958, coincide with those recommendations (eighteen, for the income tax; five, for the other taxes). Only the major recommendations are considered here; a close reading of the Report will show many more recommendations and suggestions, the fate of which could be ascertained only by a far more intensive study. The information in the present section has been obtained chiefly from the Final Report of the Commission on Fiscal Study and Reform: Reform of the Venezuelan Fiscal System (English Edition), 1983. This Report devotes 49 single-space typed pages to "Administrative Features": of the Venezuelan tax system. In the following paragraphs of this Section 4, numbers in parentheses, unless otherwise noted, refer to page numbers of this 1983 Report. The number at the beginning of each paragraph corresponds to the similar number in Section IV above.

(a) Income Taxation

(1) Self-Assessment

The recommendation that the income-tax payer himself compute his net taxable income and the tax due was adopted, apparently nearly twenty years after the 1958 Report, but was implemented only some years later, in 1980. This procedure is also decreed for the inheritance and gift tax. (112). "The introduction of selfassessment has caused severe administrative problems, mainly as a result of the shortcomings that were already present in the tax administration but also because of tactical errors in implementation." (114). Part of the trouble no doubt stems from an ignoring of the 1958 recommendation that the declaration form be redesigned to facilitate self-assessment. "The layout of the forms gives the taxpayer little help in avoiding mistakes, the accompanying instructions are rudimentary, inadequate for advising taxpayers even to a minimum extent..." The forms "lack...headings and properly numbered lines..." And they are not supplied free of charge. (114)

(2) Payment of Tax

The taxpayer may now deposit payment with any one of the 23 banks with about 1,400 branches all over the country. Apparently, payment is made at the time of filing the tax return. (113). It would appear that payment is best made by going directly to the bank instead of relying on the postal system, since, in another connection, the 1983 Report notes that "the Tax Information Register has revealed the drawbacks of any system based on the use of the mail for tax administration in Venezuela, since existing postal facilities are not the best." (113).

(3) List of Potential Taxpayers

The listing of potential taxpayers is still somewhat of a problem. On the other hand, "the use of identity card numbers as the basis for the Fiscal Information Register" has not caused major problems (113).

(4) Collection of Delinquent Accounts

Delinquent accounts seem still to pose a problem. The 1983 Report says that the problem is "critical", because "the collection system, which is undergoing a comprehensive reorganization up to the stage of standard collection, has proven to be wholly inadequate for bringing delinquent debtors to heel," and because "mismanagement of accounts, coupled with an inefficient legal mechanism, has led to a chaotic situation regarding the State's claims. If a taxpayer intends not to pay his taxes, there is a strong likelihood that he will succeed." (115). Nothing is said about garnisheeing wage or other payments made to delinquent taxpayers, and at least some delinquent taxes are assigned to private lawyers to collect.

(5) Information from Non-Withholding Payors

The 1983 Report makes no mention of information being supplied by payors other than those that must withhold tax.

(6) Field Audits

The appraisal of the audit procedure given in the 1983 Report seems no more optimistic than that found in the 1958 Report. In the six pages devoted to this subject, the following passages are typical: "There is no coherent selection system that is able to embrace general criteria and specific tactics with the aim of maximizing auditing coverage. The surveys that have been carried out suggest that the greater the degree of evasion, the lesser the likelihood of being audited... Standards or instructions concerning the way to make the selection [of taxpayers to be audited] are not known." (119). There exists "an unsatisfactory policy regarding the use of [auditing] personnel." The "reduced complement of specialized trained personnel" is due partly to the fact that "earnings are frozen at low levels," with a consequent "constant drain of personnel." (118). The task of the Internal Information Department is that of "obtaining information concerning the taxpayer, analyzing it, selecting any significant information regarding taxes and keeping it properly filed," a function that "can only be understood and performed within the framework of highly programmed, steady and integrated auditing operations. This is not the case at present." (117).

(7) Certificate of Solvency

The certificate of solvency, to which the 1958 Report attributed so much importance, is still in use. The Income Tax Law as of October, 1986, Article 102, requires that it be shown (a) by "Venezuelans to obtain approval for leaving the country when they are not residents of Venezuela and by foreigners whether or not residents of this country," (b) by those incorporating, dissolving, etc., companies, (c) for real estate transfers, (d) upon contracting with the Government, (e) when obtaining patents, trademarks and the like, and (f) to take up public office.

(8) Withholding of Tax from Wages and Salaries

The withholding of income tax from wages and salaries is of course automatically more significant now than it was under the old low flat rate of the schedular tax. The 1958 recommendation that withholding be adjusted to a degree of accuracy that would require occasional refunds seems not to have been heeded; the 1983 Report nowhere mentions a refund procedure or refund problem.

(9) <u>Pay-As-You-Go (Estimated Tax) System</u>

Payment of estimated income tax on current year's income by installments during the current year has been adopted in Venezuela. Aside from income on which tax is withheld, the current year's estimate may not be less than 80 percent of the preceding year's income. "This system entails the declaration of taxable gains at the lower levels of the progressive scale," and "The tax paid in advance will always tend to be lower than the tax for the previous year" (115). The 1983 Report recommends that the final payment of tax be accelerated, that the number of installments be reduced in some cases, that minimum amounts be fixed for each installment, and that the percentage of the previous tax <u>(sic)</u> used to fix the minimum advance payment be increased (142).

(10) <u>Taxpayer Appeal within the Tax Administration</u>

The taxpayer may now, evidently (in contrast to 1958), appeal within the tax administration instead of having to go directly to court, since the 1983 Report recommends that he also be allowed to do just what he had to do formerly: obtain "direct access to appeals litigation without passing through administrative appeal" (143).

(11) <u>Penalties</u>

No information is at hand as to whether the system of penalties has been made largely automatic in the gradation of amounts for the types of infraction noted in the 1958 Report. Interestingly enough, the 1983 Report does not consider penalties as a separate subject (but see p. 125).

(12) <u>Technical Division's Work: Recasting</u>

(13) <u>Reorganization of Work Within Finance Ministry</u>

To ascertain what changes have been made in the internal organizational structure of the tax administrative bodies would require a degree of technical description and analysis that is beyond the scope of the present study. The interested reader is referred to pp. 176-179 and 233-236 of the 1958 Report and p. 109-112 and 139-141 of the 1983 Report.

(14) <u>Checking Function of Controller of the Nation</u>

Information is not at hand on whether the 1958 Report's recommendation on this point was adopted.

(15) <u>Specialized Training</u>

Judging by the general tenor and some scattered remarks on the technical ability of the personnel, the 1983 Report implies that the 1958 recommendation for more specialized training of the tax personnel has not been fully heeded.

(16) Statistical Information

Although appreciably more statistical information appears to be compiled now than in 1958, partly due to the computer age, the range and depth of such compilations seems to be less than is justified, both for internal use and for economic analysis of the results of the tax system, and also for data aiding the making of estimates of foreign trade (through customs data), national income totals, and the like. See, e.g., in the 1983 Report, pp. 143 and 147.

(17) Compensating Tax Officials from Delinquent Tax Payments

Information is not at hand as to whether there still obtains the practice of pooling 10 percent of delinquent taxes, additional taxes, and fines for distribution to field agents, lawyers, other technical personnel and all chiefs of sections (p. 239, 1958 Report).

(18) Information Available to the Public

Apparently not as much progress as the 1958 Report recommended has been made in informing the public as to the structure of the tax system, methods of administration and compliance, and the public's tax responsibilities; the 1983 Report contains some uncomplimentary comments on this area. Strangely, even the private sector makes little or no effort here. "... there is no sustained work by professional associations, major consultants, and private publishing houses in the area of taxation" (123) (see also 143). There is no "Venezuelan Tax Association" (p. 241, 1958 Report).

(b) Other Taxes

(1) Administration Responsible for Inheritance and Gift Taxes

The recommendation that administration of the inheritance and gift taxes be transferred from the Indirect Tax Administration to the Income Tax Administration has perhaps been rendered irrelevant by the 1971 administrative reform that combined two agencies, the Administration of Internal Revenue Taxation and the Income Tax Administration into a Revenue Directorate (109). Details on the internal structure of this Directorate are not at hand.

(2) Bearer Shares and the Corporate Inheritance Tax

Information is not at hand as to whether that segment of the inheritance tax collected from certain corporations still exists.

(3) Liquor Taxation

The fact that the 1983 Report has no specific criticism of the administration of the liquor tax indicates that, as in 1958 (p. 256), there is no great concern over this sector of the tax system.

(4) Customs Administration

The 1983 Report devotes fourteen pages to customs administration: ten of description and four of recommendations. It would require a more intensive study of this sector than is feasible of the present report, to ascertain the degree to which the particular recommendations in the 1958 Report have been adopted. In general, the 1983 Report seems not to concentrate on the particular reforms that the 1958 Report advocated (1983 Report, 127-139, 145-148).

(5) Administration of Municipal Taxes

We may infer that little or no progress has been made in improving the administration of municipal taxes along the lines recommended by the 1958 Report, from the general tone of the 1983 Report on this sector (148-151): Many of the tax regulations "are antiquated, use obsolete systems." "Few municipalities use computers." "Municipal land Registers, if they exist at all, are out of date, and there are no vehicle registers." "Auditing is non-existing for some taxes....evasion is widespread even for taxes...with a high yield." As to collection, "primitive procedures survive."

(B) Appraisal

No "score sheet" of the kind given for substantive and structural recommendations will be attempted here for the administrative sector, but a general appraisal may be as follows:

Under the income tax, the adoption of self-assessment and of pay-as-you-go (estimated tax) can be regarded as major achievements that coincide with the 1958 Report's recommendations. Payment of tax has also been facilitated notably by use of the banking system. These are features of what may be termed external administration, or even compliance, as distinct from internal administration. Internal administrative matters (compensation and training of tax officials, structure of the tax administration) have probably been less influenced by the 1958 Report, partly because that Report placed more emphasis on external administration. (This may be what the 1983 Report has in mind in asserting that the 1958 Report "focused primarily on substantive rather than administrative aspects of the [tax] system" and exhibited "a lack of concern with the urgent needs for reforms in the administrative system" (p. 139, 1983 Report); but these comments seem not entirely consistent with the fact that the 1958 Report devoted sixty-five pages to income tax administration).

On other external-administrative matters the record of achievement is not encouraging: audit procedures (perhaps); statistical information for external use; information available to the public.

The degree to which internal-administration recommendations have been followed is less clear, but in general the record seems rather less encouraging.

V. An Appraisal of the Report

The tinge of apprehension that I felt upon learning that the Japan Tax Mission Report had been implemented almost at once with very few exceptions (were we really right, in everything?) had no counterpart with respect to Venezuela. The eight-year gap between Report and any implementation - with the important exceptions of repeal of the turnover tax and a separate corporate rate schedule - should have given plenty of time for thoughtful consideration. Indeed, it can be argued that so long a delay makes any causal connection implausible. A more subtle interpretation, made by Gittes, writing in 1968, is that some sort of tax reform would have occurred in 1966 whether or not the 1958 Report had been written, but that the decisions as to what the reform should consist of were influenced by the Report (171-172), although of course "It is virtually impossible to determine to what extent the changes in the new law are derived from the Report's recommendations"(172). We can safely omit the "virtually"? The 1983 Report of the Commission on Fiscal Study and Reform (Carrillo Commission) was somewhat more positive: "The history of Venezuela's tax system, written by a group of experts for the Commission on Fiscal Study and Reform, shows that the guidelines and point of reference for reforms implemented in the 1960s and early 1970s were based on the recommendations contained in the work of the 1958-60 [Fiscal Reform] Commission and those made by Professor Shoup and his colleagues" (p. 4).

One of the commentators on the 1958 Report correctly points out that any such document starts with two handicaps. First, the very fact that the recommendations are made by outsiders, foreign experts, tells against them in any socially sensitive field (Lopez, p. 23), because "potential domestic contributions, typically characterized by a deeper analysis of national realities, are ignored and at the same time local egos are bruised. Examination by insiders, whether tinted by partisan or ideological considerations or not, means a better grounded interpretation of existing internal tendencies." Second, citing Oldman and Surrey, pp. 289-290, Lopez adds that "political factors are always present in a subtle manner even in the technical matters handled by experts" (p. 25).

On the other hand, there were some advantages to be gained by getting assistance from outsiders. "A new and up-dated view of its topics changed the predominantly institutional approach so far used to deal with them. A joint economic, administrative and legal approach that appears from its text pioneered new studies. Founded on the Venezuelan reality, the 'case study' nature of the Report pointed out problems detected in the course of the research at different levels of the public powers, making fiscal matters less theoretical and more solidly grounded." (Lopez, p. 26).

The economic and political climate of the time of course affects the degree to which any tax reform will be undertaken. In 1958-1959 there was not the urgency for improving the tax system that was widely perceived in Japan in 1949-1950. The oil revenues formed a comfortable fiscal cushion; the deficit seemed to have no immediately alarming consequences; the need for more education and public health measures was not immediately apparent to everyone. At the other extreme, too, one of fiscal crisis, the pressures are not uniformly in favor of tax reform. At present, for example (May, 1987) the Minister of Finance is obviously preoccupied with discussions on how to restructure the public debt. But these discussions are likely to involve proposals for strengthening the revenue system, to assure servicing of the debt; 1987 does seem on balance to be exerting more pressure for tax reform than did the longer-term aims of 1958. Possibly, some of the proposals of the 1983 Report will be adopted with less delay than was the case for all but two chief recommendations in the 1958 Report.

VI. Hindsights

The major suggestion as to how the work of the Commission to Study the Fiscal Commission of Venezuela might have been differently structured to advantage is probably that of Gittes, who implies that a continuing effort beyond the Report stage was needed, "a continuing process of analysis and development of alternatives to the end of creating a new law." Indeed, Gittes implies that the Report itself was of secondary importance compared with the continuing technical help that he thought essential: "More often than not, it is in the working out of technical details that expert help is needed; today foreign technicians will not be the first persons in the host countries to suggest broad policy changes such as the elimination of schedular taxes or the taxation of dividends." (p. 172). There is an interesting parallel here with the thinking of the then Finance Minister of Japan, Ikeda, in 1949 (see p. 44, September, 1987 draft of my research paper on the tax mission to Japan). And the comments I make on that pattern of thought are almost equally applicable to Venezuela, except that in the schedular income tax system Venezuela was burdened with a basic structural handicap that had to be eliminated before any major use could be made of that tax.

The "continuing process" that Gittes envisaged implies that one or more mission members should stay in the host country for some time after the Report proper had been submitted, to be available on technical questions. The procedure adopted in the Venezuelan study was, however, thought to be one that largely eliminated this need. Administrative problems were discussed at length by Professors Oldman and Surrey with a group of tax officials on many days for rather long periods. None of the members of this mission could have stayed into the autumn and winter months, owing to other engagements, chiefly academic posts. The alternative seems to be to have a somewhat larger mission, not all the members being together in the host country at all times. This technique has been used successfully in recent years (e.g. in Malcom Gillis' mission in Indonesia).

VII. The Federal District Report

1. Origin and Scope of Report

In 1959 Dr. Francisco Carrillo Batalla, the Governor of the Federal District of Venezuela (and brother of Dr. T.E. Carrillo Batalla) requested me to form a commission to appraise the fiscal system of the district. I obtained the assistance of Professor C. Lowell Harriss and Professor William S. Vickrey, of Columbia University. We spent part of the summer of 1959 in Venezuela. A mimeographed draft of our report was circulated, in Spanish and in English, during the autumn and winter of 1959-1960, and a printed volume (English) was produced in Baltimore and distributed from New York City in 1960. The cost of printing and distribution was covered by sums set aside for that purpose in the funds made available by the District for the project. Our Commission to Study the Fiscal System of the Federal District of Venezuela was assisted in many ways by several Venezuelan scholars and officials, especially by an Advisory Committee appointed by the Governor; the Committee's chairman, Dr. Alfonso Espinosa, was Governor of the Central Bank.

The Federal District was analogous to the twenty States and the three Federal Territories that made up the entire geographic areas of Venezuela; it resembled the District of Columbia in the United States, except that it was much larger, relatively, in population: about 1,300,000 out of 6,600,000 in 1959. It contained (a) the rural and port economy of the Department of Vargas and (b) a large part of Metropolitan Caracas, which spilled over into the neighboring State of Miranda. These features of the District and Metropolitan Caracas remain much the same today, relatively.

The occasion for the fiscal study of the District was much the same as that for the study of the Venezuelan fiscal system: a current deficit, plus the prospect of much heavier expenditures in the years ahead for education and some purely local services, to make up for the neglect in the past.

In its printed form the Report was a book of x + 162 pages, of which 90 pages were devoted to an analysis of the District's existing tax system, and 15 pages to possible new taxes, and a revenue program for the District.

A chapter was devoted to a brief description of metropolitan revenue systems in certain other countries: District of Columbia, New York City, London, Paris, Buenos Aires, and Montevideo. Other chapters covered the District's quasi-taxes (e.g., the lottery), fees, prices, miscellaneous receipts, autonomous institutes, and fiscal coordination with the State of Miranda.

Attention was centered on the real estate tax, with nearly fifty pages of description, analysis, and recommendations. This was a tax of 6 1/2 percent of the annual rental received or that could be received. Significantly, no tax was levied on property not provided with paved streets, street lighting, and street cleaning; non-urban real estate thus paid no tax. This was a low-rate tax, compared with the United States, for its yield was only about 0.6 percent of the estimated national income in the District; the average throughout the United States for this tax was about 4.0 percent. The District tax rate, fixed by statute, had been stable for almost a decade.

The Report's recommendations on this tax consisted of a considerable number of measures designed to improve its effectiveness and uniformity, without notable structural change, but the District was urged to consider the desirability of imposing heavier taxes on pure land values than on improvements (p. 70). No early shift from the rental to the capital value basis was recommended. Several specific administrative improvements were suggested, to help the self-assessment feature of the tax work more effectively. Also, the base of the tax might be broadened, to include, for example, machinery and business equipment. Much of the text of this chapter cannot be readily summarized here: mapping, photographs, regulations, manual, recruitment and training, office and other facilities, property cards, supplementary sources of information, specialization and the use of outside specialists, mechanization in assessment, procedure for owner appeal.

The other major tax of the Federal District, the tax on commerce and industry (patentes) was judged to have major disadvantages, but no reasonable alternative was found. The recommendations included a simplifying of the schedule of twelve different rates on gross receipts, depending on the specific business, and, as to patente rates based on capital, replacement of the series of fixed amounts by a schedule that would be a single rate regardless of the size of invested capital. Moreover, "If the patentes are retained in anything approaching their preseent form, drastic steps need to be taken to improve administration" (p. 84). The recommendations referred to improving the roster of taxpayers, the scale of fines, the process of checking against understatement of gross receipts, the spotting of false data, and methods of payment.

The vehicular patente was discussed in connection with a possible motor fuel tax, a combination of the two being deemed advisable, with higher taxation in metropolitan districts (a country-wide uniform rate was being urged).

Some minor recommendations were also offered on the local amusement taxes and the tax on advertising. No summary will be attempted here of the sections devoted to the lottery, the share in racetrack betting, parking meter charges, garbage removal charges, fees for building permits, fees for verification of weights and measures, charges for copies of documents, etc., and public parks revenue, nor of the several types of prices charged by the District (see Chapters VII, VIII, and IX of the Report).

Among the possible new taxes the district might imposed, the Report recommended a tax on motor fuel to be levied in conjunction with the District of Sucre in the State of Miranda. In addition, the District might well impose an income tax of, say, 10 percent of the amount shown on the return for the national income tax. "Sometime into the future, the Federal District will probably want to have its own general income tax, administered by its own officials," but "At present, the District tax administration is not in a position to handle such a tax successfully, and the earliest practicable date will be many years off." (p. 146). The feasibility of administering a retail sales tax was deemed doubtful, and the same conclusion applied to a possible wholesalers' or manufacturers' District sales tax, or a general-scope value-added tax.

2. The Results

An attempt to ascertain the degree to which the recommendations of the District Report were adopted would require, to be comprehensive, a field study of a scope not possible in the present research project, so much did those recommendations concern a large number of rather small details in structure and administration. On a broader view, it appears that the Report has been kept in mind, at least as to the impracticability of certain new suggested taxes.

(Further information is expected to be available for a later draft of this paper.)

Appendix A

List of Headings and Sub-Headings in Chapter VI of Commission Report:
"Income Tax Administration: Recommendations"

Declarations and Payment
- Redesign of Declaration Forms
- Payment

Instructions and Tax Table
Processing of Declarations
Checks on Whether Declarations Are Filed
Liquidation, Billing and Payment
Collection of Delinquent Accounts
Investigation through Information
Investigation through Office Examination and Field Audit
- Selection of Declarations above Bs. 100,000
- Selection of Declarations under Bs. 100,000
- Random Selection
- Office Examination
- Field Audit
- Over-all Scheduling of Work
- Special Investigations

Certificates of Solvency--Expansion of the System
Withholding of Tax
Pay-as-you-go System
Appeals by Taxpayers
- Administrative Consideration
- Judicial Consideration

Refunds
Penalties
Technical Division
Field Offices
Organization
Controller of the Nation
Miscellaneous
- Training
- Filing System and Machine Operations
- Statistical Material
- Percentage of Increased-Tax Pool
- Information to Public
- Accountants and Lawyers

Appendix B: Outline of Chapter XIV of Commission Report, "Venezuelan National Government Accounts and Accounting Reports"

A. Functions of a Modern Accounting System

B. The Venezuelan Accounting and Reporting System

1. Description of the Accounting and Reporting System

(a) Receipts Accounting and Reporting
(1) Offices in Charge of the Administration of Revenues
(2) Receiving Offices
(3) Banco Central and Banco de Venezuela
(4) Office of the Treasurer
(5) Contraloria General de la Nacion
(6) Central Budget Office

(b) Expenditures Accounting and Reporting

(1) Ministries
(2) Tesoreria Nacional and Banco Central and Banco de Venezuela
(3) Sala de Centralizacion de la Contraloria
(4) Section 1 of the Sala de Control
(5) Section 2 of the Sala de Control
(6) Central Budget Office

(c) Property Accounting

(1) Ministries
(2) Sala de Centralizacion

(d) Materials Accounting

(1) Ministries
(2) Sala de Centralizacion

(e) Central Reporting for Revenues, Expenditures, Assets, Liabilities, Appropriations, and Balancing Accounts

(1) Revenues
(2) Expenditures
(3) Balance Sheet Items

2. The Venezuelan Budgetary System, Accounting and Reporting System, and Economic Planning

C. Necessary Changes in the Venezuelan Budgetary and Accounting and Reporting System to Meet Economic Planning Needs

1. The Central Government as an Operating, Proprietary, and Trust Unit

(a) Central Government Sector

(1) General Fund
(2) Earmarked Revenue Funds

(b) Government Enterprises Sector

(c) The Trust Unit

2. The Classification of Receipts and Disbursements for Economic Planning

(a) By Impact on the Asset Position of the Government

(1) Current Expenditures and Receipts
(2) Capital Expenditures and Receipts
(3) Financial Expenditures and Receipts

(b) By Economic Character

(c) By Precise Object of Expenditure and Detailed Revenue Source

(d) By Economic Sector to Which Directed or from Which Received

(e) By Region of the Country in Which Originated or to Which Directed

(f) By Function

3. The Receipts and Disbursement Effects on the Asset Position of the Government

4. Adjustments of the Present Budgetary and Accounting System to Meet Economic Planning Needs

(a) Budget Law

(1) Revenue Estimates
(2) Expenditures Estimates

(b) Accounting

(1) Receipts
(2) Disbursements

(c) Reporting

D. Reporting and Economic Planning

1. The Three-Government-Sector Reporting System

2. The Three-Account System

(a) Significance of Current-Account Balance
(b) Significance of the Balance of the Current and Capital Accounts
(c) Significance of the Financial-Account Balance

3. All Government Sectors Accounts

4. Central Government Expenditures by Function and Economic Character

E. Coordination between Budgetting, Accounting, and Economic Planning

F. The Venezuelan Fiscal Organization

G. The Autonomous Institutes

H. The Local Governments

I. Receipts and Disbursements Procedures, Financial Management, and Accounting Reporting

Appendix C

Outline of Chapter XVI of Commission Report, "Non-Tax Revenues"

A. Prices
   - Civil Aviation Fees and Prices
   - Toll Roads
     - Caracas-La Guaira Toll Road
     - Valencia-Tejerias Toll road
   - Postal Service
   - Salt
   - Telegraph and Radio Service

B. Rentals
   - National Property
   - National Public Lands

C. Fees
   - Cartage and Stevedoring
   - Overtime and Customs
   - Channel Dredging
   - Docks
   - Lighthouses
   - Piloting
   - Patents and Trademarks
   - Department of Health Fees
   - Warehousing at Customs

D. Summary

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