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Jack Newman, Acting Director FTAS

December 21, 1970

Conrado E. Longoria, Sr. Tax Advisor

Monthly Narrative Report, November, 1970

Liaison

The work on the target section of the PROP continues. We have prepared the target section using the format suggested by the Program Officer which in turn is the format used by the Dominican Republic mission. In projecting, in quantitative terms, the affect the tax administration program will have on revenue production we have used as a base the GOH's own revenue projections. For its projections, the GOH has taken into account the long range affect last year's hurricane, the war and common market problems will have on the Honduran economy. Consequently the GOH estimates, that income tax collections for 1970 will be six million lempiras less than in 1969 or a 15% decrease; also, that income tax collections will not reach the 1969 level until 1972. Following is a comparison of the two projections:

	<u>INCOME TAX PROJECTIONS</u>				
	<u>1969</u>	<u>1970</u>	<u>1971</u>	<u>1972</u>	<u>1973</u>
GOH	42.883.4	36.466.7	39.106.6	42.611.4	44.649.7
PROP	42.883.4	42.000.0	45.000.0	44.500.0	46.700.0

The Above comparison shows that our estimates anticipate that improvements in tax administration will partially offset the 15% decrease in income tax expected by the GOH for 1970. Also, that income tax collections will bounce back to the 1969 level by 1971. Attached is a copy of the table of projections prepared for the PROP. Your comments and observations will be appreciated.

SIECA/ICAP/OAS

I accompanied the Director General, Efraín Suazo, to the first Seminar of the Central American Isthmus on Internal Taxation held in San Jose, Costa Rica from November 30 to December 4, 1970. Also representing Honduras was J. Virgilio Caceres P. from the Superior Council on Economic Planning.

As an observer I found the discussions on tax and fiscal harmonization as part of the process of economic integration quite interesting. It gave me some idea of the problems facing the Central American common market. Much of the work presented by the experts on economic integration was over my head and judging from the lack of participation in the discussions that followed each paper, the material was also too deep for most of the Directors General. As a result, most of the dialogue was carried on among the experts of the international organizations represented.

The delegates participated more actively on discussions involving tax administration. Later when the atmosphere was more relaxed they even ventured to ask questions relative to the affect tax harmonization would have on the economies of the common market countries. The notes taken during the seminar may provide a better idea of what transpired during the first four days. The last day was used to discussed the conclusions reached. A copy of the notes for the first four days is attached.

ADP

The new master file project is progressing well but still behind schedule. The chief of the Processing Department prepared a draft of the returns processing procedure covering the receiving and preliminary review operations, the latter is an audit function. The procedure was well organized and will require very minor editing.

Three programmers were hired on a temporary basis upon the recommendation of the ADP advisor. The temporary programmers were needed to prepare the programs for the new master file system in order that the project remain reasonably on schedule. Eight of the programs for the master file system have been completed, however, the quality of the programs will not be known until they are assembled and tested.

As a result of extensive planning and coordinating on the part of the ADP advisor an RPG programmer class was formed. An instructor experienced in RPG Programming was contracted to give the course. The introductory part of the course was given by the ADP advisor with the assistance of a representative from the IBM Co. The course began on November 30 and will terminate on December

24. Classes are held in the morning from 7:00 AM to 10:00 AM every work day except Saturday. All ten participants are employees of the Ministry of Hacienda.

A schedule and machine time sharing plan was prepared by the ADP advisor which was submitted to the Director General and to Cristobal Colón, Systems Analyst on contract with AID. The primary objective in preparing the plan was to motivate those concerned to begin services planning on the joint operation. The proposal was acceptable to both the director and the systems analyst and perhaps it will serve as a catalyst to get the necessary planning underway.

#### Collection

Because of the scope of work involved the collection advisor, Mr. Henry Torres was unable to complete the TDA project even though Coburn and I participated extensively in the project. Most of the procedure has been written although it still requires considerable editing and thereafter translated to Spanish. All forms necessary for the project were designed and the principal ones will be printed by the middle of January. The procedure for the first part of the project which involves the reorganization of the outstanding accounts, was prepared and translated to Spanish. After the ADP Department performs its periodic balancing operation the general file will be sorted into three classifications; Notice Status, Delinquent Accounts and Inactive Accounts. Attached is a copy of Mr. Torres' closing report which provides more of the details.

Since the implementation phase of the TDA system was also to be used as a period of on-the-job training and since there still remains much to be done in preparing the final procedures we asked AID to finance a short term collection advisor for another 60 days. What we have in mind is to bring Torres back, if he is available, for two months to complete the job. Should Torres not be available then perhaps FTAS could look for an alternate. Henry Torres mentioned at least one bi-lingual person from the L.A. District who he would recommend and who has a background similar to his. That person expressed an interest for a short term assignment. The ideal situation, of course, would

be for Torres to return so that lost time could be kept to a minimum.

Public Relations and Taxpayer Education

We have assisted in the preparation of a tax calendar to be distributed primarily to businesses. The tax program provides some funds for printing costs. Originally our plan had been to use the funds (\$2,000) to print a pictorial pamphlet for distribution to the general public, but because of political overtones -- Honduran planes straffing Salvadorean supply trucks -- AID decided against financing the printing of the pamphlet.

Conrado E. Longoria

Enclosure.

Conrado E. Longoria, Sr. Tax Advisor

December 14, 1970

Henry Torres, Collection Advisor

TDY Assignment Report - September 12 to December 10, 1970

### Background

My assignment to Tegucigalpa, Honduras, was primarily intended to accomplish two objectives. The first objective was to train personnel responsible for the collection of delinquent accounts; the second, was to accelerate the collection of delinquent accounts. Accomplishment of these two objectives was predicated on the assumption that previous tax team studies and recommendations in this area would provide a good starting point, that the GOM had partially implemented the recommendations; and, that the Honduran Government had a workable taxpayer delinquent accounts system.

After a two-week study of the existing collection system, together with numerous discussions with both the tax team leader and the Section Chief of the Delinquent Account Section, it became apparent that the objectives had to be revised to accomplish the following:

1. Develop and implement a billing and collection system for current accounts and for delinquent accounts of taxpayers; viz,
  - (a) Notice Accounts
  - (b) Taxpayer Delinquent Accounts
  - (c) Inactive Accounts
2. Prepare the necessary procedures, processing techniques, and forms for an office collection system of taxpayer delinquent accounts.
  - (a) Office Processing of TDA's.
  - (b) Procedures on Transferring accounts to an inactive category.
  - (c) Designing and printing the necessary forms for an office collection operation.
  - (d) Prepare the necessary recommendations for the additional office equipment required for an efficient office collection operation.

3. Prepare a manual for reference and training purposes incorporating the procedures described in 1. and 2. above.

### Findings

The current system of collection in effect revolves around one gigantic general file of all outstanding accounts. This system does not provide for any identification of the various accounts as to age or status in the collection process. Consequently, the file contains 1970 billings as well as billings going back for a period of fifteen years or more, and the file does not provide for identification of the various accounts as to whether they are current, delinquent or inactive accounts.

The Departamento de Computación Electrónica (PAD) initiates collection action by preparing a notice or bill in duplicate of the tax owed by the taxpayer. One notice is mailed to the taxpayer, while the other is filed with the taxpayer's individual tax return. Approximately 21,000 notices are mailed annually to as many taxpayers.

PAD also prepares a collective invoice in quintuplicate, which contains all taxpayer's accounts serviced by a designated bank. The five copies of the collective invoices are used by the respective banks and the tax agency to control and process the tax payments. As part of the billing process PAD prepares IBM cards in quadruplicate. These cards contain all the information relative to the billings and to adjustments thereto. The cards are used by both the banks and tax agency to control and process the respective remittances; but in addition, one of the four IBM cards is used to establish the general file of outstanding accounts mentioned previously. The file called "Fichero de Tarjetas de Cuentas Pendientes de Cobro." is updated periodically using the payment information received from the bank through the Accounting Section. The updating is accomplished by pulling the IBM cards from the general file, and by preparing new IBM cards on those accounts with partial remittances.

The collection of delinquent accounts, under the present system, begins with the receipt by the Sección de Apremios (Collection Section) of a print-out of all outstanding accounts. The printout or register, referred to as

"Cuentas Pendientes de Cobro," is prepared each month. The Section Chief reviews the printout; crosses out accounts being worked on by the section, accounts that have been collected, and accounts previously determined to be uncollectible. From the remaining accounts, those that offer the greatest potential for collection are selected for collection action. The selection is done using the following criterion:

1. Large outstanding accounts
2. Accounts of taxpayers with known employer.

Large outstanding accounts are assigned to investigators for field contact and investigation. Accounts of taxpayers who are employed are given to the office secretary for preparation of notices of levy.

The "Sección de Apremios" is located in an office at street level which is very convenient for taxpayers. The staffing of the section consists of; one section chief, a secretary, and three investigators. Two of the investigators are stationed in Tegucigalpa, the third is stationed in San Pedro Sula. The Section Chief, Sr. Jose E. Martinez is young, energetic, resourceful, and has impressed me with his overall approach to collection and its problems. He is handicapped only in his lack of exposure to a truly effective collection system, and as a result some of my proposals were totally new to him.

The objective of the "Sección de Apremios" is to contact delinquent taxpayers and direct them to make their tax payments to their local depository agent (bank). They accomplish this objective through oral persuasion, pointing out the courses of action available to the government if the taxpayer fails to meet <sup>his</sup> ~~their~~ legal obligations. The collection authority of the Director General in the collection of taxes is very restricted, limited to levy action on salaries and on accounts receivables and then only with respect to income taxes. All other enforced collection process must be done through the Attorney General.

#### Recommendations

In view of the lack of personnel available to the "Sección de Apremios," and the overall funding problem, the thrust of my recommendation is designing

a taxpayer delinquent accounts system, geared to expeditiously close as many accounts as possible using established office procedures.

Part of my recommendation, copy which is attached and made part of this report, is the reorganization of the "Fichero de Tarjetas de Cuentas Pendientes de Cobro." This recommendation was a team effort involving both of my associates, here in Honduras. Mario<sup>N</sup>Coburn, ADP Advisor, whose services were invaluable in providing the necessary technical ADP knowledge needed for designing a workable system. Conrado E. Longoria whose expert suggestions and assistance were instrumental in producing clear and concise procedures and instructions.

The reorganization of the accounts receivable file, will consist of classifying the accounts and setting up three separate files: Notice accounts file, delinquent accounts file, and an inactive accounts file. The objective of this reorganization is to establish an accounting system which will reflect the status of an account, whether it be in current, delinquent or inactive status. In addition, the reorganization would permit the orderly progression of accounts depending on the collection status.

Incorporated in the above recommendation is the preparation of the taxpayer delinquent account notice, and the procedure for transmitting the notice to the "Sección de Apremios."

The second part of my recommendation, which in effect is a continuation of the first part, involves an operational system for processing and otherwise disposing of taxpayer delinquent accounts by the "Sección de Apremios." The procedures, instructions, and necessary forms, were developed as previously indicated to assist this section in closing as many accounts as possible by established office procedures. In developing the procedures, I worked very closely with Mr. Longoria, Tax Team Leader and Mr. Jose E. Martinez, Section Chief of the "Sección de Apremios." This approach I feel, enabled me to keep my feet firmly planted on the ground, and as a result we were able to develop a workable, realistic, collection system, uniquely suited to Honduras.

Problems

The major problem encountered, was that it took longer than anticipated to formulate the required taxpayer delinquent accounts system, with all its ramifications. Considering the time and money expended thus far on the project and to assure that implementation is properly carried out it would be highly desirable that a collection advisor be assigned, full time to guide the project through the critical implementation phase. Another problem that affected the time plan was the unavailability of funds to finance the printing of required forms. This appears to be a temporary problem, the matter was discussed at the closing conference with the Director General who indicated that funds would be available for the next fiscal period, beginning on January 1, 1971. Due to the delay in securing the necessary forms required to implement the taxpayer delinquent account system, a decision was made to postpone the reorganization of the master file until January 1971. It is desirable to conduct the reorganization of this file, immediately prior to the preparation of the TDA assembly, as part of the overall implementation of the new TDA system.

Summary

It is essential that a follow-up be maintained on the printing of the new collection forms, so that the target date set for late January 1971 for implementing the new TDA system can be met. Along with this, it would be desirable, if not indispensable, to have a collection advisor assigned to Tegucigalpa, Honduras in early January 1971 to supervise the actual implementation.

I would also recommend that continuous discussions be maintained with counterparts on all aspects of the new collection system, in order that possible problem areas can be identified and to assure complete support from them.

In closing, I wish to express my sincere gratitude to the Director General, Sr. Don Hiram Suazo, Sr. Juan M. Chavarria, Sr. Barillas,

Sr. Cesar A. Ruiz, Lic. Roger Perez, and especially Lic. Jose E. Martinez, Section Chief of the "Sección de Apremios," with whom I worked very closely throughout my stay here. Also, I would like to single out Conrado E. Longoria, and Marion Coburn, the tax team members, who worked so closely with me on this project, and guided a novice through his first overseas assignment.

*Jesse Lee*

**Monday Morning Nov. 30**

- Gutierrez Luna, Director ICAP made opening remarks.
- Hugo Delfarco, Director CIET also addressed the delegation
- Barahona, Minister of Economy and Finance officially inaugurated the meeting.

After a short recess the delegates decided manner in which work would be carried out. Director of ICAP would be leader or moderator of the debates. Panama recommended an alternate to ensure continuation of business.

- Director suggested delegates be separated from observers to permit a better exchange of ideas.
- Work program was agreed.
- Papers would be presented in summary only. A work group composed of two or three delegates and one or two advisors would form a conclusions committee <sup>the conclusions</sup> which will be distributed to all members.
- Da Silva - regarding flight tickets said that through administrative problems and Thanksgiving Holiday they goofed in getting tickets to delegates. Review was made of the recommendations made at the first regional seminar on fiscal administration of 1964 and at the first meeting of Directors General in 1966. Those recommendations were:
  - I.- Regional Seminar on Fiscal Administration.

A.- Tax Policy

(See document 4143)

B.- Tax Administration

- 1.- Codify all tax legislation.
- 2.- Initiate extensive campaigns of taxpayer information
- 3.- Prepare manuals on administrative procedures.

- 4.- Provide more authority to tax agency to facilitate administration.
- 5.- Improve competency of tax agency employees.
- 6.- Create a training center for tax agency employees.
- 7.- Decentralization of operations and of authority at the same time to centralize tax administration.
- 8.- Establish automatic data processing systems.
- 9.- Provide more stability to the organization and its employees through legal disposition.
- 10.- Establish a cross control system.
- 11.- Gradually transfer the collection of certain taxes from tax office to banks.
- 12.- Establish a greater exchange of information on advances made in tax administration.

## II.-First Meeting of Directors General of C. A. & Panama.

### A.- Tax Policy

(See document 4143)

### B.- Tax Administration

- 1.- Promote uniformity in methods and administrative procedures conducive to a more efficient administration.
- 2.- Establish a system for the interchange of information between tax agencies of each country.
- 3.- Centralize tax administration into two components one for internal revenue and the other for customs.
- 4.- Establish within each tax agency a planning unit, and an OTM and technical studies unit.
- 5.- Structure the administrative organization on a functional basis and not by tax.

- 6.- Establish permanent systems for the dissemination of information concerning taxes.
- 7.- Decentralize the functions and attributes within the tax administration in order to bring about the necessary reforms.
- 8.- Provide adequate services for the presentation, and simultaneous payment of returns and adapt the legal and administrative aspects that will assist in the voluntary compliance of tax obligations.
- 9.- Strengthen the collection system by improving accounting methods to determine the tax owed by taxpayers and accelerating collections through specialized employees.
- 10.- Establish a complete master file of taxpayers.
- 11.- Adopt legal measures that will facilitate collection of tax by levy and seizure of assets of delinquent taxpayers.
- 12.- Adopt and apply a definite policy concerning penalties and abandon the practice of condoning penalties and interest.
- 13.- Review claims procedures, so that T/P's can expect just treatment and that the claims procedure is not used as a mean of delaying the payment of taxes.
- 14.- Develop adequate statistics with which to evaluate the administration, plan its effects and inform the public and other federal organizations.
- 15.- Efficient use of ADP equipment.
- 16.- Establish a personnel program that will bring about institutionalization of a career and merit system assuring a level of compensation in accordance with capabilities and responsibilities of employees.

17.- Provide for flexibility in the organization so that there is proper utilization of human resources.

18.- Increase level of competency of tax agency employees.

C.- Integral program of technical assistance and of personnel training.

1.- Recommend that ICAP include in its program of tax administration specific aspects on technical assistance and training of personnel of each country in its five-year plan.

2.- Take into account the recommendations made at the regional seminar when planning national improvements.

3.- Develop a regional plan to coordinate technical assistance through SIECA.

4.- Give technical assistance to countries in accordance with priority needs.

5.- In the training of personnel take into account courses at the following levels and objectives;

a) Regional courses to form technicians and high level administrators.

b) National courses for tax administrators of middle-upper levels.

c) National courses for the training of employees in administrative practices.

6.- Program regional and national seminars to discuss tax administration themes.

7.- Directors General should have annual meetings to evaluate progress of plans, make necessary changes and fix priorities with respect to administrative needs.

A work group was formed to determine the extent of progress made and to reassign priorities to those recommendations still pending.

**Monday Afternoon - November 30.**

**- Da Silva - Fiscal harmonization in the area of integration processes.**

**Possible Outline of a program in Tax Harmonization in Central America ( Unnumbered document)**

- 1.- Harmonize indirect tax systems attempting to uniform application to facilitate and promote regional trade.**
- 2.- Establish tax conditions that will permit greater movement of capital within the region.**
- 3.- Achieve neutral tax systems that will not interfere with rational location of investment.**
- 4.- Improve tax administration so that they will function efficiently and in harmony with the stated objectives.**

**SIECA asked that each country review the proposals and conscientiously indicate what areas are important. The document presented is an advance presentation of what OAS will formerly propose to the C. A. Countries. There was an exchange of opinions concerning the Role of foreign advisors vs. National advisors. Some delegates complained that foreign advisors made studies, presented in beautiful paper and then were abandoned by the host country. Jose Young of Panama backed Bill Newnam's recommendations for institutionalization establishing organizations within the Ministry, For tax policy a research group at the level closest to where tax policy is set. At the Director General level establish a Planning Office; a staff of legal advisors to work on legal problems affecting tax administration; and, a training office.**

**The conclusions were that the institution rather than individuals be responsible for carrying our improvements recommended. This is particularly desirable due to many changes in management.**

Da Silva then made a comparison of the problems of the Benolux countries and those of L.A. They are quite different. European countries were already developed when the common market was formed to create new opportunities for investment.

Tuesday - December 1.

Document 4155

Da Silva - Clasificación Latinoamericana Común de los Ingresos Tributarios y Paratributarios (CLACIT) Developed by Dept. of Finances, Joint Tax Program ~~SEA~~/BID. The idea of CLACIT is to standardize accounting to permit international analysis. The system can be used in conjunction with existing accounting systems. It permits tax structure analysis at international level.

In the addendum to 4155 the budgets of Costa Rica, Honduras, El Salvador, and Panama <sup>are shown.</sup> Most breakouts worked out very well, however, be improvements could/made by further detail, i.e. Income tax should be broken down to Individual and Business profits.

The information would be submitted to SIECA by the Isthmus Countries and Panama. SIECA in turn would prepare consolidated tabulations and then make them available to each country. Advisors should help each country set up the CLACIT system. Costa Rica and Honduras stated that it would be possible to furnish the statistics. Panama thought it double work because of having to work with two classifications. OAS representatives tried to explain the real simplicity of the system. It merely required taking present data and pouring it into the CLACIT classification. This could be done by the statistical section. Costa Rica's only observation was that the CLACIT was broader than the jurisdiction of the

**Director Generals of Internal Revenue.**

OAS further recommended that SIECA provide the form for each country to fill out, Da Silva said it should take no more than fifteen minutes. Countries should remember that they are consumers as well as producers of information. Countries would be interested in knowing how they stack up with other countries. The form prepared by SIECA could set the format for each country cross referencing the national classifications to the CLACIT classification. SIECA could send compilations immediately to each country showing both the country's monetary unit and also a comparison showing a C.A. monetary unit.

The idea was generally accepted so Gutierrez Luna formed a work group composed of members from Panama, Costa Rica, and ? to draw up recommendations for adoption of the CLACIT system.

Jose Acosta - Document 4145 - Comparative Analysis of Model Code with existing codes or projects.

The Technical and Conceptual aspects are primary tasks to be undertaken in tax harmonization. Comparative studies of the tax systems are a good phase to start. The study concentrates on substantive norms leaving penalties for later. Penalties need not be identical merely compatible. El Salvador was not included in study because of absence of a code. All other countries (C.A.) have codes or projects.

Nicaragua and Panama have codes. Costa Rica, Guatemala and Honduras have projects. El Salvador has no code. El Salvador submit a compilation of its existing laws in order to proceed with a regional comparative analysis. Suggested measures necessary to advance the work in this area: Participation of legal advisors, a specialized

technical group to formulate concrete recommendations, promote adoption of codification projects now under study in Costa Rica, Guatemala and Honduras, cooperation of El Salvador in submitting compilation of its laws, conciliation by advisory organization of the studies on tax law.

### Conclusions

- 1.- It is possible to consolidate the basic norms of tax law in a legal group on general application of taxes.
- 2.- Nicaraguan and Panamanian codes do not contain important norms, a reexamination of its tax legislation seems in order

### Luis Illanes - OEA

Need for codification is recognized by most countries. Illanes discussed best way to approach harmonization. First codify all national laws then attempt the harmonization.

### Jose Bordon - OEA

Discussed procedure and planning that went into project to codify tax laws of Costa Rica. He stated objectives which in general were to improve Administration and equity in application of laws. With a few exceptions penalties are applied by the tax agency for better administration. Special penalties or outside jurisdiction of tax agency.

### Gonzalo Fajardo

Gave brief history of codification project. No new taxes or increase existing taxes until administration improved. Through code, tax agency acquired new powers but at same time guarantees for taxpayers were included. The code has awoken interest in tax law by all concerned. In the university it is required subject. Knowledge of tax

laws will be more generalized, taxpayers better advised, better compliance of tax laws. Fajardo discussed administrative procedure on assessments/ Tribunal Administrativo first hears case, taxpayer must pay 50% of assessment, this reduces delinquencies. 13% of assessments are abated by Tribunal Administrativo.

*Chasin* asked that Honduras and Guatemala give status of process to codify.

Efrain Suroz - Honduras

DGT began with income tax later expanded to cover all internal taxes. The need to codify become very apparent. OAS prepared a project called "Ley general de aplicación de impuestos". This will undoubtedly be the basis for the code. Internal political problems sometimes prevent tax legislation. Minister have to search for the right time to submit tax legislation.

Edison Gnazzo - C I A T

Code is desirable to put tax agency and taxpayers on the same legal plane. It would dispel idea that the cards against the taxpayer. The existence of a code is a real advantage to the private sector in this sense.

Guatemala - Mr. Santiago Castillo

Very little progress. A project has been in mill since 1987. The completed project was presented to Ministry and later submitted to congress where it seems to have stalled. Project will probably continue to sleep. Perhaps it would be opportune to review it and compare with Costa Rican code. Guatemala recognizes need for code, current tax laws are very old and difficult to administer. The code will improve this situation.

**Oscar**

**Issue - OEA - Sales Tax - Document 4150**

**General Principles in Tax Harmonization**

- a.- Principle of country of destine applies when goods consumed in the country are taxed whether imported or produced by the country and the goods exported are exempt. This principal has following affects:**
- 1.- Limits free trade if tax on imports from the region are collected by customs. This could be overcome if the tax is collected at time sale is made within the country.**
  - 2.- It will not affect competitiveness of regional products sold outside the region.**
  - 3.- True consumption capacity of each country is taxed.**
  - 4.- Generates more taxes for less developed countries.**
- b.- Principle of country of origin consists of taxing the products in the country in which produced. Under this system exports are taxed but not the imports. If this principle is adopted it would eventually facilitate free trade because intra-regional customs would not collect taxes. It would however, bring about following disadvantages:**
- 1.- Regional production would be less competitive in the international market.**
  - 2.- It could place national or regional production at a disadvantage with third countries if the tax is greater than the import duty.**
  - 3.- Less developed countries would be at a disadvantage with more developed countries because the taxable base would be less to the extent the commercial balance is unfavorable.**
  - 4.- Taxes would have to be the same in all member countries which would make this revenue source rather rigid.**

**Honduras and Nicaragua have a single stage sales tax system which is yielding**

good revenue. Guatemala has a 1½% cascading (multiple stage) system. Its a very effective, yield low.

The general import of sales taxes on harmonization. In general a cascading tax system may be disadvantageous to national production. In El Salvador the rate *OF .1% was later increased to one percent.*  
~~is 1% per thousand. When it was increased the result was a rate of 1½ per~~

hundred. The former low rate did not reveal the problem that really existed.

Costa Rica, Honduras and Nicaragua now have a single stage system. Panama, Guatemala and El Salvador have a stamp tax type of tax not an independent sales tax law.

Honduras began with a single stage tax system, later went to a hybrid single stage and value added. The result was to reduce the number of responsible for the tax. However, it becomes a little more difficult to administer the value added tax. The question arises as to the logic of the value added hybrid system, because since it falls on a merchant with lower sales it would seem that level of merchant would be less equipped to carry good accounting records.

Mr. Carlos Muniz - related Nicaraguan sales tax experience. The problems were minimal. The tax agency developed a master file of responsible. There are 683 enrollments. A problem arose in that importers of raw materials were enrolled and not required to pay tax. Muniz feels there is evasion with these importer/manufacturers and asked for comments on his problem. No comments were made.

There followed much discussion concerning which principle is best. Some favored blurring up customs because they are a nuisance, anyone traveling can readily recognize the inconvenience they create.

Delegates did not arrive at any concrete conclusions. The work group will submit a series of conclusions to the delegation before the end of the conference.

Wednesday Morning December 2, 1970

Informe Sobre la Renta

- Document 4183 -

The discussion centered around the many variations in treatment given to tax on income that affect the harmonization approach. There are conceptual differences that affect taxable income. There are also differences in the basic levels of taxation. Also, there are differences in the many fiscal incentives of each country. There were discussions on the principles of taxing income; i.e., the "Principio Mundial" and the "Principio Territorial".

With respect to deductions there are also many differences. Depreciation was cited as a good example, this allowance varies from country to country.

It is important that foreign companies who are very mobile and invest throughout Central America receive equal tax treatment from each country.

Suazo of Honduras gave a brief outline of how income tax operates in Honduras.

Antonio Ramirez of El Salvador, expressed in his opening remarks that he was much at a loss notwithstanding the brilliant presentations. He was not as well prepared as those presenting the papers. He went on to give his concept of tax on business profit tax.

He sought answers on how much to tax each type of activity taking into account the effect this has on the economy. El Salvador has a particular problem of development. They offer incentives primarily to the agriculture sector. Each country has its own problems therefore taxes accordingly which makes tax harmonization very difficult.

Coralia de Moreno of Panama - Gave a series of reasons why Panama uses the "Principio Territorial" and not the "Principio de Domicilio". The latter would put national firms at a disadvantage in her opinion.

José Jordón - CAS

Asked that El Salvador tell its experience on using the principal of "Renta Mundial".

Due to time limitations the chair opted to go ahead with next paper;  
El Convenio Centroamericano de Incentivos Fiscales al Desarrollo Industrial"  
"Central American Agreement on Fiscal Incentives for Development of Industry"/  
The narrator gave a brief explanation of the agreement; its history, actual benefits  
and coordination.

Fiscal incentives are tied in to important taxes that apply to raw materials and  
equipment. This is generally true because important duties are relative high, so  
countries provide full and partial exemptions to new industry. The Better approach  
would be to lower import taxes on that type of material to reduce number of special  
requests for exemptions by industry.

Incentives are applied to bases not entirely clear. It would be interested to  
hear some dialogue on the subject. Nicaragua suggested that countries of the  
Common Market make an agreement with US concerning American investors so that  
Fiscal Incentives for US firms do not place the CM countries at a disadvantage.  
Each country uses incentives to attract new investment. These also imply market  
guarantees. Guarantees are accomplished by placing import quotas on that certain  
product. In Panama raw material is exempt for new industry. The market guarantee  
is assured by import quotas or by high import taxes. There is an awareness of  
capital flight however, it is compensated by savings deposits which are tax exempt  
as are certain bonds. Problems/ <sup>in administration</sup> arose when special contracts between firm and  
government established <sup>different</sup> ~~the~~ tax rates. Panama feels that US firms don't care where  
or to who they pay taxes it should therefore be the host country that receives  
the revenue.

ICAP said it had studied the application of the countries of Ley de Fomento Indus-  
trial and of the agreement on fiscal incentives.

In some countries the directors generals do not have voice nor vote on fiscal

incentives. There is also a lack of organization to give life to the <sup>incentive</sup> agreement. Administrators should be more interested in fomenting industry because it will have a <sup>salutary</sup> ~~secondary~~ effect in the economy of each country.

Buzo mentioned that directors are called variously collectors or directors of revenue. In Honduras through audits the administration determines how incentives, are being used, by firms which enjoy them. He asked what controls could be suggested to control the incentives given to foreign investors so that national industry is not placed at a disadvantage and at the same time guarantee the continuation of the foreign company. The reply was that the agreement did not treat this issue. On the question of how countries assure that the tax that has been exempted is not paid to the country of origin, it was recommended that attention be given this issue at the time the contract is being prepared.

Administration and evaluation of fiscal incentives will be discussed at the CIAT Seminar which should provide some answers <sup>FOR</sup> ~~to~~ the directors general.

On equalized development - El Salvador wanted an explanation of this concept. The idea is to give preferential treatment to less developed countries.

De Silva - made a very good exposition on the pros and cons of fiscal incentives. His presentation is to be reproduced and distributed.

Honduras said that an evaluation should be made of the incentives. From these evaluations could be learned which incentives are no longer advantages to the respective countries.

#### Tributación Del Capital Extranjero

#### Taxation of Foreign Capital

Document (4161) no discussion was held on this subject.

Acosta La Multiple Tributación Internacional; sus Implicaciones en Relación a los países del Istmo Centroamericano.

Multiple taxation is a greater barrier to free movement of capital. The region is

an importer of capital. Double taxation occurs when the capital exporting country taxes under the principle of "Renta Mundial" and the Capital importing country taxes under the principle of "Renta Territorial." This conflict more generally occurs on income tax.

Much discussion was held over the two principles some delegates felt that the capital importing countries should tax and the capital exporting countries should ~~forget~~<sup>follow</sup> the tax, to further help developing countries.

The chair asked the U.S. delegation to comment on their feelings on double taxation. Ormerod, Newsum and Gonzales all explained that the subject/related to tax policy <sup>is</sup> and therefore did not feel free to comment. There was further discussion on the two principles. Pepe Acosta made a the point that the ones that must adjust to the problem are the capital importing countries because it will be illusory to expect that capital importing countries change their tax legislation.

Da Silva - Asked Nicaragua to comment on the idea that SIECA and ICAP collaborate on a project model on income tax with the first objective to establish rates and the second to establish recommended incentives. The project would be a preliminary project which would be distributed for evaluation and approval to each country, then converted into a model which the countries could use to gradually change their legislation. The chair clarified that there would be no commitment made by countries upon approving the preparation of a first project but merely using the approval of the delegation so that the project can be initiated by the international organizations. No vote was taken, but there was general agreement that ICAP, SIECA proceed with the project. Da Silva said the AID/BID Joint Program would offer its full support in preparing the proposed manual.

Da Silva also proposed that SIECA and ICAP make a study of incentives and he assured that related information concerning US could be readily obtained.

Also that information be gathered to prepare a model contract between capital

-4-

importing countries and capital exporting countries. The one prepared by UN was made here for agreements between developed countries and therefore not suitable for Latin America.

of

A work group was formed to summarize the conclusions/today's proposals.

Layton

Thursday Morning      December 3rd.

**Basis for improvement of Tax Administration - Document No. 4154**

It is very difficult to rely on <sup>additional</sup> taxes as a way of solving fiscal problems.

The best <sup>solution</sup> way is to improve administration thereby improving compliance and at the same time reduce the cost of administration.

This is not a new theme many recommendations have previously been made

However, not many of these recommendations have been put into practice.

Honduras has made some inroads as has Panama and Guatemala but there

remains much to be done. Some of the remarks will not always apply depending upon the progress made by each country.

**Split Administration-**

There ~~is~~ still remains the problems of split administration/taxes. Some countries still maintain two directorates one for direct taxes one for indirect taxes.

- Structure by function rather than by tax.

- Need for delegation - High levels of administration are handling ordinary operations. This detracts from the true work of administering the overall operation.

- Insufficient Support - High levels of the administration need more support, additional units such as:

a.- Programming

b.- Tax Studies

c.- Statistics on Taxation

d.- Systemization.

e.- Taxpayer information - need to arouse a tax conscientiousness in the public.

f.- Training.

- **Need for operating manuals.**

- **Salary Systems** - This is a very serious problem in the public sector but most particularly for tax administration. Anyone involved in collection should be well paid because from his work results the revenue for the budget. Attrition leaves the least desirable employees, the better ones, seek improvement and better salaries.

- **Excessive Geographic Centralization** - District Offices have very limited responsibilities.

- **Deficiencies in control over taxpayers**

ARODY Robles of ICAP made a strong recommendation that each tax agency establish a technical group with sole objective to improve tax administration. Group should be composed of highly specialized people in, audit, registers, accounting of taxes, data processing.

In looking at the organization the following aspects should be considered:

- Consolidation of the various taxing entities.

- Director of Taxes should have a high level position within the Ministry.

- There should be a clear distinction in functions

a.- Management Area

b.- Advisory Area

c.- Administrative Area

d.- Operations Area

Already mentioned but a point worthwhile repeating is the personnel problem.

Tax agencies should have very strict selection procedures. Many high ~~salaries~~ employees with responsible jobs have <sup>sub</sup> standard education. Salaries are very low. Even when Civil Service and job classification exist these do not adjust to reality. Many employees are hired because of political pressures. The better employees leave for private industry. In general there are no

retirement systems.

Illanes said Honduras had made great progress in most points mentioned in the document. That it was a sink or swim situation brought about by a decree to reorganize. He favors violent changes rather than piece meal structural changes.

Gnazzo said tax administration is a means to an objective in many cases the administration cannot execute the tax laws passed by the country and ceases to be the means and turns into an obstacle.

Panama said changes must be agreed upon at higher level agreements are hard to get. There is much resistance to change. Changes in management leave many plans on the *drawing* board. Changes must be made very slow, violent changes cause chaos, Changes made in Panama were made very slow and insidiously Also important is that planning groups be established to make constant necessary changes, set goals, control production. Without the planning group the tax agency will be hard pressed to meet its goals. Panama has an organization by tax rather than a functional organization which is working very well.

Regional directors have been given more authority. There are organizations at the national levels that control the operations of regional offices.

Decentralization requires centralization of controls.

Panama asked at what level control of exemptions should be placed. The reply was that it would vary according to the structure of each tax agency. In the case of Panama perhaps at the normative level.

Da Silva said probably the best way to improve tax administration in central america is to employ more women of the caliber of Coralia de Moreno of Panama (the compliment was well deserved).

Suzo said we should determine how to go about putting recommendations already made into practice. <sup>Many</sup> ~~any~~ times changes made by Directors General may cost him his job unless he has full backing of the Ministry. The Minister must also

have the backing of the Presidency, Nonetheless changes in legislation are very hard to bring about because one has to rely on the varying interests of the congress.

Virgilio Caseres indicated that one of the most important factors is well trained personnel to carry out the work of the tax agency.

Newnam made the observation that exemptions are strictly audit problems and therefore belong in audit. He further stressed the need for a planning group and a legal advisory unit. Paper shuffling takes up much time that should be dedicated to compliance. Norman Novak's book says "the work that comes to you tends to drive out the work to which you must go". The quote by Newnam was to stress the need to identify and pursue the important objectives in tax administration and to dispense with paper shuffling.

**III**

Mario Polinaris, Costa Rica. It should be a requirement that the tax agency be contacted on every tax exemption granted by congress or other higher levels of the Government. He proposed that Carlos Barboza present his work on government accounting, internal controls and the manual on administrative procedures.

Barboza said that the largest firm in the country is the government and therefore should have a good accounting system. On administration the objectives are

- improved taxpayer service
- work flow
- forms design and use
- Plan of accounts to determine cost of administering taxes
- Accounting of taxes
- Flow charts on accounting work. These are designed for a 360/25.
- End of year accounting of taxes and the activity for year.
- Audit programs
- General disposition, reference material on general administration.

Da Silva discussed document.

**4156 - Regional Aspects of the Systemization of Data in the Tax Administration  
of Central America & Panama**

**4156 - Systems on Tax Registers.**

Proposes a program for exchanging information among the countries on their <sup>compatibility</sup> experience in ADP. Try to achieve more ~~availability~~ in equipment. This compatibility would facilitate the integration being sought and also provide cross referenced data. It would also facilitate training for the entire region because of similarity of equipment.

In the case of Master Files and property tax rolls. Taxpayer Master Files are essential in tax administration. It is not only a number that is assigned to a taxpayer but has a very important function in tax administration.

The number could have a series of codes to identify firms and individual, also codes to group certain types of taxpayers.

Suggest separate registers for individuals and corporations. Establish a uniform system of numbering part of the number would identify the country. This would provide a census of all firms in Central America provide cross referenced information on sales taxes and custom taxes.

In the discussion that followed the ADP systems experts present opined that the idea was good except that it would require much more compatibility than we now have. Leo Jusseaume said that compatibility is not easily achieved density of data ~~tax~~ varies, similar configurations may use cards and other may use tape.

Not only is there a need for ~~an~~ compatibility in Configurations but there must also be compatibility in systems and also in the capacity of developing adequate systems. With respect to the output of regional data it would be feasible to exchange some outputs. So that each country knows what the other country's outputs are.

The tendency is to mix ID numbers with classification codes. The result is that we overload our ID numbers.

Young of Panama thought there was no problem of compatibility that with adapters the data of different countries could be read by others. Further making all equipments alike would mean giving all the business to one manufacturer. The ID number should be one not issued by the tax agency - used a number already available and maintained by some other agency. He also made some observations of the problems of maintaining and updating regional master file of taxpayers.

Newnam IRS recommends that each tax agency have its own computer configuration and not one that is centralized because of problems of control over the use of the equipment.

Raul Humberto Ramos of Nicaragua recommended a value added tax as a bridge for the contemplated integration. To use a value added tax in lieu of a consumption tax for the reasons stated. No comment was made on the proposal because it was not the subject being discussed.

#### Fuentes Mohr - Summarization

- Establish a mechanism for the Harmonization Tax Administration.
- Organizing and training of personnel responsible for carrying out the tax harmonization process.
- Codification of tax laws
- Identify areas that can be worked on where legislation is not required.
- The principle of "destino" was the most acceptable principle.
- On income tax there was a lot of discussion and it was agreed that a tax model on income tax would be developed for possible use in future legislation.
- A series of investigations will be made on the double taxation and fiscal incentives.

**- Organization needed to move the harmonization program ahead.**

- a.- It was agreed that technical assistance should be better coordinated.
- b.- Exchange of information.
- c.- Training of technical personnel
- d.- Directors should meet once a year.
- e.- Meetings of technically specialized groups.
- f.- Institutionalize national groups to continue the work started by foreign advisors.
- g.- Need to train technical personnel that would work on harmonization as part of a general training program of ICAP.
- h.- A group of instructors should be formed drawing people from ICAP, SIECA and from the respective tax agencies.

Acosta, OAS - Document 4152

Orientation for an ~~an~~ integral policy of training on taxation for C.A.

Training is very important in improving tax administration and therefore training centers should be formed nationally as well as regionally. Management should make studies on the needs of each country so that national and regional organizations can plan the courses needed.

Gutierrez Luna, ICAP said that the governments have already shown interest in centralizing the training. ICAP fulfills the mandate of the Ministers of C.A. countries on training needs. In Panama there is a seminar for high level officials to arouse interest in administrative reforms. Same seminar was held in El Salvador.

We have seen with great satisfaction that many international organizations are channelling their training assistance through the central american organizations. Each country needs to set up their own training facilities for priority needs. The reason that ESAPAC was changed to ICAP WAS that formerly the training

not well coordinated with technical assistance. ICAP training now more tied to administrative reform and technical assistance. ICAP would like to host the Annual Meetings of directors to further promote training programs. The assistance of other International Organizations would help to coordinate the training needs. ICAP will help each country develop training courses. DeMarco of CIET - CIET will also collaborate in developing national training courses as well as regional training courses.