

PARAGUAY: TOWARDS A HEALTHY, FORMAL AND COMPETITIVE ECONOMY

PARAGUAY THRESHOLD COUNTRY PROGRAM: FOCUS AREA II
FORMALIZATION OF ECONOMIC ACTIVITIES • PROGRAM RESULTS 2006 • 2008



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Background

Paraguay Threshold Country Program

June 1, 2006 to November 30, 2008

The purpose of this report is to present the results of two years of implementation of the Threshold Program in the Republic of Paraguay.

The United States Government created the Millennium Challenge Corporation in order to make development assistance available to countries that demonstrate their desire to rule justly, invest in their people and foster economic freedom. The MCC awards grants to selected beneficiary countries, which are considered eligible based on pre-established criteria.

Some countries do not meet all of the criteria and must make progress in certain areas in order to qualify for critical development assistance. In view of this, the MCC, created the Threshold Program to assist countries still on the “threshold,” meaning that, while they are not eligible for the compact or principal programs of the Millennium Challenge Corporation, they have demonstrated a significant commitment to improving their performance according to the criteria.

In 2004, the Government of Paraguay expressed its desire to participate and to meet the eligibility requirements to obtain assistance from the Millen-

ium Challenge Account (MCA)¹ or the Millennium Challenge Corporation. Paraguay meets only three of the six required indicators. It received very low scores for the indicators on control of corruption, effective governance and the rule of law (8%, 16%, and 25% respectively, relative to countries with similar characteristics). Because of Paraguay’s demonstrated commitment, however, it was invited to submit a plan to the MCC’s Threshold Program.

Paraguay submitted a proposal for a Paraguay Threshold Program in October 2005, and it was approved in February 2006. The bilateral agreement between the United States Government and the Government of Paraguay was signed in May of that year. This agreement provides for a nonrepayable grant in the amount of \$34.65 million to support the country in an ambitious anti-corruption effort, a frontal attack on impunity, and in its struggle against economic informality.

The areas the Paraguayan government chose to address through the Threshold Program are consistent with its need to improve its performance indicators. Should it succeed in improving those indicators, the

country could be eligible for funding from the principal MCC account and would be able to access more development aid for poverty reduction.

The Paraguay Threshold Program addressed widespread corruption rooted, in part, in weak government institutions and a poorly functioning, distorted and exceedingly informal economy. Working on the dual fronts of impunity and informality—and enlisting the participation of all three branches of government: the Executive, the Judiciary and the Legislature, as well as the Public Ministry and the Comptroller General of the Republic—the Program proposed to carry out critical, sustainable reforms in key government institutions.

The following are some of the more salient aspects of the initiatives to fight corruption and informality through the Paraguay Threshold Program:

The Threshold Program achieved its goals in eight out of ten program components. Paraguay’s performance in the MCC’s corruption indicator gradually improved, rising from 8% in 2004, to 17% in 2007 and 30% in 2008.

¹ The Millennium Challenge Account is the principal account of the Millennium Challenge Corporation. These funds are made available to countries meeting 50% of the indicators to establish eligibility for the MCC.

Despite the progress made, Paraguay remained ineligible for funds from the MCC's principal account based on its performance in the corruption indicators.² Given its accomplishments, and the historic opportunity in the country, however, the MCC invited Paraguay to submit a proposal for Phase II of the Threshold Program. Accordingly, the Government of Paraguay submitted its proposal in September 2008, and it is currently under review by the MCC.

This report highlights the achievements of Phase I of the Threshold Program at the end of the implementation period and makes recommendations for the sustainability of the reforms already initiated. It also suggests activities designed to strengthen efforts to fight impunity and informality.

Focus area II: Formalization of economic activities

Government institutions worked through the Threshold Program to promote a healthy, formal and competitive economy in Paraguay and ensure that the country reaches the indicators established by the MCC and the Government of Paraguay. This was to be accomplished through a reliable legal framework to facilitate business activities, the impartial application of laws and procedures, interinstitutional cooperation, efficiency in the use of government resources, and greater transparency and dialogue between the public and private sectors.

A country's performance is determined by a number of factors, including its government's ability to pay for its own functioning and to provide public services. The main source of government revenues are taxes collected from individuals and businesses living and operating in the country. The most relevant taxes are the Value Added Tax (VAT) and those associated with imports and exports. When VAT revenues are lower than they should be, the resulting discrepancy is called the VAT "evasion gap." Studies conducted by the Office of the Undersecretary of State for Fiscal Affairs (SET), with the support of the Threshold Program, showed a significant fiscal gap in the payment of the VAT tax in Paraguay. This is attributable to a large informal sector that does not pay taxes and to the lack of sufficient controls to ensure tax compliance in the formal sector. The main objective of Focus Area II, therefore, was to aid the government in the process of formalizing economic activity in the country. This included reforming and streamlining the procedures to establish a business to boost the number of formal enterprises, attracting new sources of local and foreign investment, and helping the State enforce tax compliance in the formal sector.

In order to reduce VAT evasion, the Program supported the SET, which operates under the jurisdiction of the Ministry of Finance, in its control and investigatory duties to identify and punish VAT evaders. The goal was to reduce VAT evasion from 66.32% to 51.32%; According to official data

provided by the Undersecretary for Fiscal Affairs, due to the change from an external taxing index to a Paraguayan taxing index, the evasion gap is 45.27% which will be the new baseline for other reports. Based on available data as of December 2007, at the conclusion of activities, the level of evasion was 51.38%. Although the goal was met in practice, evasion levels must be assessed again at the end of 2008, to ascertain the program's overall impact on efforts to combat economic informality.

The Program helped the National Customs Office to combat export and import tax evasion—or illicit international commerce—by creating and training an interinstitutional force for the detection and seizure of contraband, and improving the efficiency of border control activities. This involved coordination between the National Police, the Paraguayan Navy, and the Public Ministry. The National Customs Office met the established goal by 102%, carrying out seizures valued at \$6,639,060.

Three investigative units were created—the Tax Investigation and Fraud Detection Department, the Office of the General Coordinator of Customs Investigation, and the Internal Investigations Department—to work in the areas of fraud detection and tax and customs infractions and invasion. Threshold Program assistance enhanced the capacity of these units to fulfill those objectives. In addition, tools for identifying acts of corruption within the Ministry of Finance were reinforced and preventive measures

² For more information, see the following websites: www.programaumbra.gov.py and www.mcc.gov.

How can a healthy, formal and competitive economy be achieved?

Strategy of the Threshold Program's Focus Area II:

- **Reorganization of public administration and the State.** A healthy economy is characterized by a clear legal framework, the impartial application of the law and interinstitutional cooperation.
- **Efficient administration.** This includes improving planning processes, the provision and adequate use of material and financial resources and ongoing monitoring and evaluation of programs and institutions.
- **Confidence in institutions.** Confidence in government is fostered by administrative transparency, the capacity to respond to the public and constructive public-private sector dialogue.
- **An improved national image.** By promoting favorable business conditions (policies, processes and capacity) and facilitating better access to markets.

Participating Institutions in Focus Area II of the Threshold Program

- Office of the Presidency of the Republic
- Supreme Court of Justice
- Public Ministry
- Ministry of the Interior
- Office of Migration
- Ministry of Finance
- Office of the Undersecretary of State for Fiscal Affairs
- National Customs Office
- Ministry of Industry and Commerce
- National Council of the Maquiladora Export Industry
- Ministry of Justice and Labor
- Social Security Institute
- Paraguayan Navy
- National Police
- Municipality of Asunción

instituted to reduce the possibility of recurrence. The emphasis throughout this process was on improving the technical expertise of those responsible for investigating such practices. It was buttressed by a hiring process designed to identify capable individuals with solid ethical values and a serious commitment to public service. These units referred more than 300 cases involving tax and customs offenses and internal corruption to the justice system, surpassing the Program's established goal of sending 73 investigated cases to the courts for prosecution.

The Program also helped streamline procedures for establishing a new business. It created a team headed by representatives of the Ministry of Industry and Commerce and comprising delegates from six other government agencies involved in the process, which

came together to operate in a single location and follow a streamlined procedure. The new process, known as the Unified System for Establishing Enterprises (SUAE), was installed in the offices of the Ministry of Industry and Commerce. With support from the Threshold Program, this initiative also surpassed the established goal of reducing the length, cost and complexity of the process. The length of time required to start a business was reduced from 74 to 15 days, and the cost from \$750 to \$80.

In order to attract investment (domestic and foreign), the Program actively promoted the country as an attractive location for companies to produce goods and services for export under the maquila system. The National Council of the Maquila Export Industry (CNIME) promoted

this system, domestically and abroad, among entrepreneurs seeking to expand their operations and export their products to other countries. Technical advisors advertised the advantages offered by the State to maquiladoras and promoted Paraguay as an ideal business location. At the end of the Program, the goal of 15 new businesses established and operating in the country from June 2006 on, had been met, and maquila exports had grown by 162%, relative to a goal of just 15%.

Paraguay and the MCC had set ambitious goals for the Threshold Program and the outcomes for Focus Area II speak for themselves: the VAT gap decreased, contraband seizures rose, the time, cost and number of procedures required to legally establish a business were reduced and new maquiladoras

were installed in the country. These are significant achievements, and the challenge in the years to come will be to continue to deepen the formalization process that has been set in motion.

The State and its institutions must undertake a constant self-examination process to continue to improve their efficiency, provide opportunities for everyone, and better serve the private sector and citizens. Whether we are members of the private sector, civil servants or every day citizens, we must continue to support government institutions by observing the laws—as individuals and as businesses—and by demanding that the State apply the law impartially and enforce compliance on the part of individuals and institutions.

The change is in us and we must recognize that change is an ongoing improvement process rather than simply a goal to be met.

Acronyms

BCP	Banco Central del Paraguay (Paraguay Central Bank)
CAIA	Office of the Administrative Coordinator for Customs Investigations
CNIME	National Council of Maquila Export Enterprises
CSJ	Supreme Court of Justice
DB2007	World Bank Doing Business 2007
DB2008	World Bank Doing Business 2008
DETAVE	Special Surveillance Department of the National Customs Office
DIT	Tax Investigation and Fraud Detection Department
DNA	National Customs Office
FAE	Formalization of Economic Activities
IDB	Interamerican Development Bank
IED	Inversión Extranjera Directa (Direct Foreign Investment)
IPS	Instituto de Previsión Social (Social Services Institute)
MCC	Millennium Challenge Corporation
MH	Ministry of Finance
MIC	Ministry of Industry and Commerce
MJT	Ministry of Justice and Labor
MP	Public Prosecutor's Office
OTA	Technical Assistance Office (United States Treasury Department)
PIB	GDP (Gross Domestic product)
REDIEX	Investment and Exports Network
SADEP	Customs System for Public Complaints with Judicial Protection
SEPRELAD	Money Laundering Prevention Agency
SET	Office of the Undersecretary of State for Fiscal Affairs of the Ministry of Finance
SUAE	Sistema Unificado de Apertura de Empresas (Unified system for Establishing Enterprises)
TTU	Trade Transparency Unit
VAT	Value Added Tax
UJ	Unidad Jeroviaha (Jeroviaha Unit)
USAID	United States Agency for International Development

“Several years ago my life was very difficult. I spent days on end worrying that I would lose all my merchandise and what little capital I had. My back was stressed by the weight of the flower boxes I carried every day across Puente de la Amistad Bridge, from Foz de Iguazú, Brazil to Ciudad del Este, Paraguay.”

Anastasia Ramos, flower vendor, currently a representative of the Multiflora international corporation.

Introduction

Anastasia's story aptly illustrates the transformation currently underway in the Paraguayan economy. This entrepreneur, who worked in the informal sector, lived in a state of constant anxiety over the risks associated with operating outside of the law, yet had no alternative employment options. By registering as an importer, she joined the still incipient process in Paraguay to consolidate a healthy, competitive economy. These steps towards formalization are a good start to enable the country to keep pace with the constant changes in the global economy.

Through a demanding reform program, coupled with the implementation of strategies to build a more healthy economy and increase formalization in the country, the Threshold Program has helped move Paraguay

towards a more efficient, less corrupt public administration model and create a more secure business climate that can generate new investments and economic growth. The Program showed that it is possible to begin to build this new model with government leadership, private sector cooperation and citizen support. In this report, we describe some of the practices that have been implemented to ensure a healthy, formal and competitive economy and relate experiences of change from the standpoint of the State and some of its citizens. The examples provided show that it is possible to aspire to a healthy economy, free from the scourge of illicit activity, and to a country situated to compete with its peers in conditions of greater transparency.

The lack of formalization—characterized by a large informal sector that does not pay taxes and poor control mechanisms to enforce formal sector compliance—contributes to the paucity of government resources needed to provide public services and diminishes public confidence in government institutions. Ultimately this discourages investment in the country. Formalization requires the design and application of effective sanctions and controls and promotion of conditions, policies and processes favorable for businesses. It is also necessary to build a



There is a strong correlation between the level of formalization in a country and the growth of its economy

What happens in a country where there are more informal businesses than formal ones?

Government services: The government ensures the provision of public services such as healthcare, social security and the maintenance of public spaces, including schools among others by levying taxes, contributions, and charges, and assessing official penalties for failure to observe the law. Informal businesses have a negative impact on the revenues the government requires to provide these public services. As a result, the government is unable to pay its civil servants a good salary, provide training, or provide them with the equipment they require to do their jobs

Formal businesses: They must compete with informal companies that do not pay taxes or benefits to their employees. As a result they are unable to compete with products offered in the informal sector.

Informal businesses: Because they operate outside the law, these companies cannot grow. Their merchandize and capital are undermined with no access to formal services, such as credits or insurance. In addition, they are more vulnerable to having to pay bribes that may exceed formal charges.

The general public: It suffers due to the poor quality of public services provided by poorly funded government institutions and ultimately must pay for services that should be provided by the government. In addition, people pay bribes or other informal charges solicited by public officials who are not adequately remunerated to provide a better service. In other words, the public pays three times over: formally, informally, and for services that the government is supposed to provide.

more healthy public administration—ensuring a clear legal framework and the impartial application of laws and sanctions—and improve its efficiency, in order to build public confidence in government institutions and project a positive image of the country to investors. Paraguay has acknowledged this reality and, in recent years, has taken steps to change the status quo, especially by strengthening government institutions and working to earn public confidence. One such initiative

is the Threshold Program. Program results show that economic formalization and reorganization activities have enhanced the country's competitiveness, which, in turn, spurs economic growth.

The concept of competitiveness is premised on the idea that investors and entrepreneurs (whether domestic or foreign) can choose where they want to invest and which businesses to launch, and they will invariably look

for optimum conditions. The economy, therefore, is more competitive insofar as it presents more favorable conditions. There is a correlation between the level of formalization in a country and the health of its economy, as well as between the confidence inspired by its institutions and its competitiveness. Conversely, the degree of informality has negative repercussions for competitiveness. The larger the informal economy, the less competitive the country.



The state of the art equipment used by DETAVE contributes to more rapid and effective anti-contraband operations.

The factors that characterize a healthy state are also conducive to the development of the formal economy: effective tax structures, greater transparency, an adequate legal framework, and the impartial application of laws and procedures. These are also important prerequisites for maintaining reasonable levels of public spending, efficiency in public administration, and judicial processes necessary to guarantee higher quality public service provision.

According to the Central Bank of Paraguay's (BCP) preliminary figures for 2007, the private sector—defined as “economic activities not produced by the public sector”—accounted for 85% of GDP.³ Formalization enables this critical sector for economic development to become better organized and more stable. Formalization in the private sector fosters business expansion and facilitates opportunities for contracts, investments, and market access. In the public sector, it leads to better resource administration based on tax collection, and monitoring and evaluating progress towards results.

Formalization also ensures impartiality in the application of the law, and the attendant improvement in the rule of law. This is why formalization is not exclusive to the private sector. It must also include public administration so as to guarantee serious, trustworthy and efficient institutions that promote sustainable development and a more competitive economy offering a favorable business climate.

In keeping with its focus on formalization, building a healthy public administration and competitiveness (which are complementary factors), the Threshold Program worked with several government institutions. It worked with the Office of the Undersecretary of State for Fiscal Affairs (SET) to reduce value added tax evasion, with the National Customs Office (DNA) to increase its capacity to detect and seize contraband, and with the Ministry of Finance to investigate cases of fraud. The Program also collaborated with the Ministry of Industry and Commerce (MIC), and other related agencies, to streamline the procedures required to legally establish a business,

“The best business climate is a growing economy. Infrastructure, education and technological innovation are also important. But what companies always ask is: ‘just how easy is it to do business in the country?’”

Joseph Stiglitz,
2001 Nobel prize-winner for economics, during an interview with Clarin newspaper in Buenos Aires, shortly before his visit to Paraguay (April 29, 2008).

and assisted the National Council of Maquila Export Enterprises (CNIME) to attract investment in the country.

Main Results

After more than two years of Program implementation, working with fifteen different government institutions, the results observed are promising. The examples provided below illustrate the Program's impact on the work of these institutions.



³ Private consumption = 71% and Gross Private Capital Formation = 14%. Source: Central Bank of Paraguay.



Until November 2006, an entrepreneur wishing to open a business had to visit 17 divisions in seven different agencies. Today, he or she can use a one-stop service, involving a single procedure.

The Program helped establish three anti-contraband intelligence and operations units within the National Customs Office: DETAVE⁴, and CAIA⁵. It provided training for the units in contraband detection methods and in the use of modern equipment, technology and modes of transportation. It supported the DNA in the design of a more effective strategy to reduce contraband and evasion. The results were evident within a very short time.

BEFORE: The National Customs Office seized \$3.9 million in contraband from 2005 to 2006, prior to the activation of the DETAVE, and CAIA⁶ units.

TODAY: From May 2007 to November 2008, the National Customs

Office's anti-contraband operations led to the seizure and impoundment of goods valued at \$6.6 million.

With their highly trained human resources and modern, sophisticated equipment to detect contraband, and CAIA took in a total of \$14.7 million⁷, 10% of which corresponds to counterfeiting and pirating and 8% to seizures.

The Threshold Program launched an institutional modernization process in the Office of the Undersecretary of State for Fiscal Affairs and helped design strategies to reduce the fiscal gap in the payment of the Value Added Tax (VAT). One such strategy involves an innovative method for verifying the emission of legal sales records

by companies, which quickly began to produce results. Other efforts included strengthening a specialized investigation unit.

BEFORE: At the outset of its work with the Threshold Program, the Tax Investigation and Fraud Detection Department (DIT) of the Office of the Undersecretary for Fiscal Affairs had a baseline of zero for all indicators.

TODAY: Between 2005 and 2006, the DIT detected evidence of tax invasion involving 177 contributors, totaling \$9.7 million. Of the 73 cases investigated, the total recognized debt to the tax authority was \$3 million⁸. Most of that debt has since been paid.

⁴ Special Surveillance Department of the National Customs Office.

⁵ Office of the Administrative Coordinator for Customs Investigations.

⁶ The DETAVE unit initiated operations in May 2007, at about the same time as the Intelligence Unit currently known as CAIA.

⁷ These figures were provided in local currency by GOP (62,950,439,017 guaraníes at an exchange rate of 4.254 per dollar)

⁸ These figures were provided in local currency by GOP (57,590,140,783 guaraníes at an average exchange rate of 5.882 guaraníes per dollar and) 17,649,228,993 guaraníes at an average exchange rate of 5.882 guaraníes per dollar)



The formalization of economic activities creates jobs in Paraguay, so we can build a better country. Building site of Qin Yi America Factory, in Ciudad del Este, one of the industries attracted by the Threshold Country Program.

BEFORE: The estimated fiscal gap for VAT was 66.32%.⁹

TODAY: In September 2008, the 2007 fiscal gap for VAT was calculated at 51.38% based on data from the National Accounts of the Central Bank of Paraguay.

Seven institutions successfully streamlined their procedures for starting a business with the establishment of the Unified System for Establishing Enterprises (SUAE), under the Ministry of Industry and Commerce. Within a short time, the number of procedures, costs involved, and number of days necessary to complete the registration of a new company required of the entrepreneur had been reduced considerably.

BEFORE: Prior to November 2006, it took an average of 74 days to open a business. The entrepreneur was obliged to visit 17 offices in seven different agencies, and pay approximately \$750 (The World Bank, Doing Business 2007).

TODAY: Since November 2006, it has taken an average of 25 days required to register a business, and the total cost has been reduced to approximately \$80. Since December 2008 it takes less than 15 days. The procedures are done at a “one-stop service” window, in a single procedure.

Paraguay's National Council of the Maquila Export Enterprises (CNIME) launched an intensive campaign to at-

tract new investment and to promote the advantages the country offers in its production for export system, known as the maquila industry.

BEFORE: The benefits of Paraguay's maquila program—as a system for the production of goods and services for export—were little known inside the country or abroad. In the eight years preceding June 2006, 17 program proposals to establish maquilas were approved by the government of Paraguay.

TODAY: Between June 2006 and October 2008, more than 200 entrepreneurs from bordering countries have received information at their places of business concerning the advantages of Paraguay's maquila industry.

⁹ According to official data provided by the Undersecretary for Fiscal Affairs, due to the change from an external taxing index to a Paraguayan taxing index, the evasion gap is 45.27% which will be the new baseline for other reports.

The results are investment plans to establish 33 new programs, 23 of which already have received State approval to operate as maquilas.¹⁰ The 23 programs represent an investment estimated at more than \$13 million and will create approximately 1,200 jobs.

This report describes the results of the improvements implemented and their impact and potential for building a better future for Paraguay. Formalization is directly related to the construction of a healthier economy capable of growth and growing competitiveness. The progress made is proof that an interinstitutional commitment, along with the individual responsibility of government officials, can ensure the sustainability of the changes in the long term.

The chapters that follow detail key areas for ensuring a formal competitive economy in Paraguay. Chapter I addresses *Building a Healthy State and Efficient Public Administration*. Chapter II discusses the development of an *Achieving Competitiveness Through Efficient Administration*, and demonstrates how government institutions must take the lead in reform processes. Chapter III, *Cultivating Public Confidence in Institutions*, raises the issue of public confidence as a necessary prerequisite for galvanizing the productive sector. Chapter IV recommends *Promoting the National Image* through clearly defined formalization proposals that will showcase the changes accomplished in Paraguay on the international plane. Chapter V

Looking Towards the Future offers suggestions for consolidating the reforms and for cultivating stable, robust economic opportunities. This report titled *Paraguay: Towards a Healthy, Formal and Competitive Economy*, concludes that the first steps have been taken and it is important to carry them forward to ensure the sustainability of the reforms and aspire to a better future. Finally, an Appendix to the report contains descriptive figures and tables as well as a series of one-page descriptions of the individual components of Focus Area II: Formalization of the Economic Activities of the Threshold Program, and offers suggestions for ensuring the sustainability of these initiatives.

¹⁰ Several stages are involved in authorizing operations under a maquila system. State approval is the final authorization to begin operations.

CHAPTER I

Building a Healthy State and Efficient Public Administration

At the Threshold Expo 2008, young professionals admire development opportunities that offer a climate of legality, transparency and trust between the public and private sectors.





“I want—all Paraguayans want—a more developed Paraguay, where the young people grow up in a healthier, more honest environment. This is what we are seeking with our contribution.”

*Lieutenant Commander Marcos Gamarra Rodas,
commissioned to DETAVE by the Paraguayan Navy.*

The State is comprised of the people and the people make up the State. The slogan of the Threshold Program “a national cause,” followed by “the change is in us,” demonstrates that authorities and citizens must work together to build a healthier country and construct a society featuring favorable conditions that benefit everybody, together with clear operating rules and procedures.

The first key to a competitive economy in Paraguay is the health of public administration and of the State. The Threshold Program supported this process by promoting a clear legal framework and effective inter-institutional cooperation.

Clear Legal Framework and Impartial Application of Laws and Procedures

The Threshold Program strengthened laws governing economic issues, by drafting regulations, decrees and resolutions to increase the clarity and transparency of administrative and operational procedures to ensure that the law is applied impartially to all citizens regardless of their last names, family backgrounds, or access to capital. While the law already included provisions to suspend the economic activities of companies that fail to comply with their tax obligations¹¹ and to seize illegal goods brought into the country without a declaration or any documentation¹² when the Program began, there were no clear procedures or mechanisms in place by

Reorganization applies to the economy and to the State

Economists increasingly recognize that economic development is linked to the factors governing human behavior. Nobel Prize winners Amartya Sen (1998) and Joseph Stiglitz (2001) believe that ethics, values, and individual capacity are factors in a society's economic performance. This report is based on this premise insofar as it promotes the construction of a healthy, formal and competitive economy, in which the State facilitates opportunities for development in an atmosphere of legality, transparency and confidence between the public and private sectors.

The rule of law, characterized by respect for law and order, is essential for the development of transparent and trustworthy institutions with the authority to enforce laws and regulations.

¹¹ Law No. 2421/04 on “Administrative Reorganization and Fiscal Adjustment and Decree No. 8094/06 on the “Creation of the Jeroviaha Unit (UJ).”

¹² Law No. 2422/04, Customs Code.

The Jeroviaha Unit and “simulated purchases”

The Jeroviaha (a Guaraní word meaning “repository of trust”) are tax compliance officers working for the tax authority who operate undercover as everyday citizens seeking to purchase a good or service from an established business. If, upon paying for that good or service, they do not receive a sales receipt reflecting proper payment of the VAT, they identify themselves as government officials and fill out a report describing the situation. If there is a second instance of noncompliance during another monitoring exercise, a judge will order the three-day suspension of business activities, which can be extended for an additional three days. These verification exercises have revealed that numerous business fail to issue sales receipts, which in turn means that many businesses are not paying their taxes. The Jeroviaha Unit is based on the experience of a similar group known as *fedatarios* in the Ecuadorian tax administration.

which to apply these laws. To correct this situation, the Threshold Program worked with the Undersecretary of State for Fiscal Affairs (SET) to strengthen the monitoring and control capacity of its Jeroviaha Unit and with the National Customs, among other partner institutions, to develop a new legal framework to improve border control.



Members of the Jeroviaha Unit suspend the activities of a business that does not legally document its sales transactions. This is an example of the application of sanctions to ensure tax compliance.

The SET is responsible for collecting the revenues owed to the State by each person and company. Non payment of taxes creates a discrepancy between the resources the State should have, and those actually available to it. This fiscal imbalance hampers the State’s ability to provide quality services and guarantee public safety. This discrepancy is known as a tax gap and it is the SET’s responsibility to develop control mechanisms and tools necessary to discover the causes of the discrepancy. The institution, then, must have a thorough grasp of which companies are paying their taxes and which are evading them.

The SET created the Jeroviaha Unit for the fiscal control of businesses and to verify that they document legal sales. This means that companies must declare the real value of their sales and, as a result, their real income, and pay their taxes accordingly, as a result of the controls put in place by the SET. The consequences to entrepreneurs who fail to issue legal receipts include suspension of their business. This Unit also

took over the tasks previously assigned to the former Ministry of Finance inspectors or tax collectors and added these functions to its portfolio with a view towards promoting a trustworthy image of the Ministry of Finance.

In order to ensure that the Jeroviaha Unit has clearly delineated powers and that it always acts based on reliable information in a transparent manner, the Threshold Paraguay Program helped SET to improve its work methodology by ensuring legal backing of its enforcement activities and rigorous observance of tax laws and mechanisms to make others adhere to these laws. In terms of the application of laws, the Program professional staff helped to draft Decree 8594, that defines the mission and work methodology of the Jeroviaha Unit.

Decree No. 8594 also provided that when UJ agents purchase goods or services from a company without receiving a bill of sale, the Unit—pursuant to a court order and under the protection of the National Police—will



The Threshold Program helped design an appropriate legal framework for the fight against contraband. Members of the press corps report on the harmful effects of contraband and the work of anti-contraband units.

“We are not be competitive.”

According to the Sugar Growers Center [Centro Azucarero Paraguayo], political will is the only force that will help reduce contraband. In the meantime, “we are not be competitive,” asserts the organization.

According to the Center’s estimates, 55,304 tons of contraband sugar enter the country each year from Brazil and Argentina. This represents \$8.6 million in losses to the State only in customs duties and the Value Added Tax.

55,304 tons x \$320 dollars/ton
\$17,697,280
Freight dollars \$52/ton
\$3,871,280

Freight and costs value
\$21,568,560

This does not count insurance.

Tariff 30%
\$6,470,568

VAT 10%
\$2,156,856

(*) Values given in U.S. dollars. Exchange rate: 4,600 guaraníes/dollar or 39,686,150,400 guaraníes.

Data is for the 2007/2008 sugarcane harvest, published in the newspaper Última Hora on October 31, 2008.

suspend the activities of the offending company for a period of three days. The law empowers a judge to suspend a company’s activities for three days for the sole reason of failing to issue a legal bill of sale and the intent of Decree No. 8594 is precisely to clarify and establish a transparent and solid procedure. To ensure this, before proceeding with the temporary suspension of a company, the documentation is reviewed by the Supreme Court of Justice—the highest judiciary authority in Paraguay—to substantiate the legality of the procedures related to any dispute and to demonstrate that the UJ is treating all taxpayers equally. The law is very straightforward. It does not permit the negotiation of exceptions and does not include loopholes that would make it possible to avoid the consequences established by law, in other words, a three day suspension of business activities.

The Jeroviaha Unit began its verification work in the city of Asunción, focusing on legally established companies – presumed to be formal - rather

than places known to be operating in the informal sector. The companies selected for tax verification were chosen through a random lottery system, which is an example of the impartiality of the control measures. Through their activities, the UJ, the SET and the Supreme Court of Justice, implemented unprecedented, generalized controls in the country that targeted companies with good reputations and healthy cash flows. The ensuing suspensions had a ripple effect as people began to grasp the importance of these verification efforts and their right to obtain a record of legal sales.

What is more, companies began to review their systems, receipts and practices to document transactions, for fear of losing business revenues should they be subject to a three day suspension.

In the context of the Threshold Program, the government also incorporated a new legal framework and new procedures to improve fiscal compliance among individuals and companies

importing goods into the country. The National Customs Office, in conjunction with public security agencies, created the Office of the General Coordinator of Customs Investigation and DETAVE (Special Surveillance Department)—an inter-institutional force—to fight contraband at the national level. Customs officials already were empowered to seize nonregistered goods at the point of entry into the country (cases in which the

A single case investigated by the DIT generates over \$900,000 in revenues to the public treasury.

The investigations carried out in 2008 by the Department of Tax Investigation and Fraud Detection, elicited evidence of tax invasion in the amount of \$913,520 (exchange rate 4,000 guaraníes/U.S. dollar). This sum corresponds to a single case involving a contributor that acknowledged the evasion and the attendant debt to the public treasury and paid the back taxes in full.

Source: Report of the Research Institute for the Consolidation of the Rule of Law, Asunción, July 2008.

relevant fees and taxes had not been paid), but lacked sufficient resources and a legal framework for interinstitutional cooperation to systematically investigate where such goods were coming from and where they were headed, or to actively pursue smugglers in order to seize such goods.

Establishing clear sanctions for non-compliance with the rules of the game is a critical part of establishing a clear legal framework and it is important to underscore the importance of attaching penalties to the illicit goods at the root of this extralegal business that so distorts the market. Tax and customs evasion is extremely dangerous to the society. While this type of offense may constitute an individual act, it has a

multiplying effect when the infraction goes unpunished. In the long run customers may not necessarily be paying a better price: the market is actually distorted and legal businesses cannot compete because they are unable to make the same profit margins as those who do not pay customs fees or taxes on goods. As the legal businesses cease to operate the resulting decline in government revenues means citizens receive fewer public services.

Since its creation DETAVE conducted more than 500 operations, but three major seizures in particular were widely covered by the media. These involved basic goods such as meat, sugar and tomatoes. While this may seem insignificant at first glance,

these are precisely the kinds of basic products that inflict the most damage on local companies. Smugglers do not pay import duties and this affords contraband goods an unfair market advantage, in the form of lower costs relative to legally imported goods. Thus, dishonest businesses reap higher profits, even though their products may not necessarily be of better quality. Smuggled goods can pose a health risk to customers because they lack phytosanitary certifications.

The objective of the new DETAVE, established by Decree No. 7980/06 on August 14, 2006, is to form an elite force to make sure that goods entering the country are legally registered, detect smuggled goods, and



Tomato smugglers from Argentina prepare to drop their illegal cargo into the river to eliminate incriminating evidence. DETAVE seizures prevented millions of dollars in losses to local tomato growers.

DETAVE's interinstitutional make-up is unprecedented in the history of the country's Customs Office. It has had a very positive impact on anti-contraband operations, having seized goods valued at over \$6.6 million.

proceed with the rigorous application of customs law. The establishment of the new Jeroviaha and DETAVE units enhanced the investigatory capability of their respective institutions and instituted and strengthened a hierarchical structure for other units involved in coordinating and complementing the work described earlier, including the following entities:

- The Tax Investigation and Fraud Detection Department (DIT), is responsible for the detection and investigation of instances of fraud and tax evasion, at the request of tax collection and control agencies (Decree No. 8209 of September 27, 2006).
- The Office of the General Coordinator of Customs Investigation (today

CAIA) is convened to investigate customs-related offenses, establish proof of illicit behaviors, and conduct undercover operations (Decree No. 7980 of August 14, 2006).

The main objective of the DIT and CAIA is to detect fraud and tax and customs infractions and evasion. Both of these legally established units are subject to clear internal procedures for the impartial application of the law.

These investigatory units detected cases of tax evasion and illicit operations conducted by companies and by *sacoleiros* (a Brazilian term for small scale smugglers who carry their goods in sacks) who smuggle contraband goods to Brazil either overland or in small boats. A case of large-scale sugar smug-

gling was detected in the city of Pedro Juan Caballero, near the Paraguay-Brazil border, a city known for smuggling. In order to ensure the sustainability of these achievements, the work that has begun must be carried forward with the support of the relevant institutions and authorities.

The achievements of the units charged with putting an end to impunity, law enforcement and penalizing individuals and companies, include:

- Over \$6.6 million in seizures and 520 anti-contraband operations (DETAVE), from May 2007 to October 2008 (source: DNA).
- A total of \$69.4 million in goods seized and adjustments through liquidation in anti-contraband operations (CAIA), from December 2007 to September 2008 (source: DNA).
- A \$5.3 million increase in tax revenues stemming from 227 audits (DIT) from January 2005 to September 2008 (source: SET).¹³
- The fiscal gap for VAT was reduced to 54% in 2006 and to 51.38% in 2007, compared to the 2003 baseline of 66.32%.¹⁴ The average in the South American region is a 2% reduction annually (Source: SET).
- Approximately 2000 inspections and 143 temporary suspensions of businesses through the implementation of an innovative methodology resulted in a 3% reduction in the fiscal gap for VAT from 2006 to 2007 (source: SET).

“Our seriousness, our competitiveness, is based on the quality of the products we offer. It was difficult to enter the international markets, but we have succeeded in doing so. Paraguay must make a constant effort to keep those markets open by protecting its health certification. Health and safety are essential to protect the industry. Contraband meats can harm our health certification and wreak havoc on the national industry.”

Maris Llorens, cattle rancher and exporter of beef products.

¹³ The Tax Investigation and Fraud Detection Department (DIT) was operating prior to the Threshold Program with support from a program of the Technical Assistance Office of the United States Department of the Treasury. The figure provided includes increases in tax revenues from January 2005 to September 2008.

¹⁴ According to official data provided by the Undersecretary for Fiscal Affairs, due to the change from an external taxing index to a Paraguayan taxing index, the evasion gap is 45.27% which will be the new baseline for other reports.



Interinstitutional cooperation helped enhance the efficiency of the institutions through an operational synergy. Each member of DETAVE plays a specific role in planning its future tasks.

“Our main advantage is that we work in a coordinated manner with forces that used to fight contraband individually, since joint efforts are always better. We have learned to work together, joining forces and skills. We have achieved this through training and modernization...”

Lieutenant Commander Marcos Gamarra Rodas, commissioned to DETAVE by the Paraguayan Navy

First Steps to Consolidate Institutions and Strengthen Institutional Links

Institutional linkages enable government agencies to cooperate and complement each other to create a healthy State. By establishing communication channels and mechanisms for information sharing and collaborative work, civil servants experienced the satisfaction of tangible successes.

Cooperation between institutions was the strategy used to reorganize institutions and to foster an operational synergy that would enable them to work more efficiently. Formal linkages between the anti-contraband efforts of the National Customs Office (DNA) and public security agencies led to unprecedented levels of inter-institutional cooperation for such operations. DETAVE operates under

the National Customs Office with the cooperation of the National Police—to make the necessary arrests and to protect people and equipment during contraband detection and seizure operations—and the National Navy, as the entity responsible for security on and around waterways. After a short period of operations the results achieved by DETAVE demonstrated that the government’s investment and changes in attitude implemented through the Threshold Program, helped reorganize anti-contraband efforts and contributed to formalization.

The decree creating DETAVE—an interinstitutional entity—spelled out the civilian nature of its law enforcement activities. Another innovative aspect of this decree is the inclusion and development of an intelligence-operation cycle: a collaborative effort based on intelligence systems and the

ability to pursue smugglers on land, on water, and through the analysis of the evidence obtained. In addition, the support, connectivity, and sharing of procedures with the Office of the General Prosecutor guaranteed from the outset that all relevant judicial entities were in accord about the legal process, so that the records kept during the course of such operations would comply with the laws in force.

Another example of successful interinstitutional cooperation is the creation of the Unified System for Establishing Enterprises (SUAE) which provides entrepreneurs a one-stop service that has drastically reduced the time period for registering new businesses. This new system, which operates under the jurisdiction of the Ministry of Industry and Commerce, brings together seven Paraguayan government agencies, all of

which signed an agreement to streamline and integrate their work. Each one of these institutions plays a particular role in the process of starting a new business.

The active participation of delegates from the seven institutions of the SUAE has ensured that cooperation among institutions will be ongoing. Each one offered proposals for changes in their own institution and engaged in a collective effort to learn about the processes in other institutions. The SUAE, which has been operating with increasing success since November 27, 2006, has demonstrated that interinstitutional efforts can lead to the establishment of better procedures within a short time frame. In just one year, Paraguay improved its ranking by 72 positions in the category of opening a new business accord-

ing to the World Bank report Doing Business 2008, which placed Paraguay among the countries that had shown the greatest improvement in this regard, by assigning it a ranking of 66th in this indicator. This shows that some forms of progress can have an immediate impact on competitiveness. The SUAE is testimony to the fact that it is possible for different government agencies to achieve efficient cooperation between institutions. In the long term, it would be helpful to develop a new legal framework that would further streamline the process to open a business. Meanwhile, however, by working together, each of the SUAE participating agencies pledged to reduce their processing time through regulatory modifications within each institution.

Institutions that make up SUAE and their functions

Institution	Agency	Procedure
1. MIC	SUAE	One-stop service window for document intake
2. Ministry of Finance	Treasury General Counsel	Legal opinion to register the articles of incorporation
	Office of the Undersecretary of State for Fiscal Affairs	Issue of the Single Taxpayer Registration [Registro Único del Contribuyente (RUC)]
3. Judicial Branch	Supreme Court of Justice	Payment of legal fees
	General Office of Public Records	Registration in the Legal Corporation Section and the Commerce Section
4. Social Insurance Institute	Worker – Employer Contribution Office	Worker – Employer registration
5. Ministry of Justice and Labor	Employer Registration Department	Employer Registration
6. Municipality of Asuncion	Urban Administration Department	Commercial patent and license
7. Ministry of the Interior	Office of Migration	Residency Card (Temporary-Permanent)

Tasks ahead: more interinstitutional cooperation

Today, operations to combat illicit activity are still frequently hampered by the lack of sufficient cooperation among institutions. During one particularly important anti-contraband operation in Ciudad del Este, the judge on call delayed four hours in issuing a search and seizure warrant. This damaged the operation by eliminating the element of surprise essential to such operations.

Although the Threshold Program opened the doors for greater cooperation among operational units, the Office of the General Prosecutor, and the Judiciary, much remains to be done.

Finally, in an example of what can be accomplished when inter-institutional coordination is taken to the international plane, the newly organized Office of the Administrative Coordinator for Customs Investigation (CAIA) is now able to detect cases of under-invoicing of goods in the DNA. Cases of counterfeit documents were detected by cross-checking information with foreign consulates and customs offices.

This contribution to the effectiveness of public administration and institution-building has left a promising model in place. It is the first step towards responding to the enormous demand for modernization and change so urgently needed by Paraguayan society.

This was evident in the words of Paraguayan President Fernando Lugo, on the occasion of his inauguration: *“The State that we are committed to building responds to the civic demand expressed at the voting booths last April 20. An initial action: to enhance the institutional strength of our Paraguayan government offices. Through their values. Their mission. Their efficiency. The civil servant’s sense of duty. Their absolute transparency. Their responsibility as government officials.”*

CHAPTER 2

Achieving Competitiveness through Efficient Administration

The Threshold Program helped to transform institutions into agile entities working to improve their productivity and effectiveness.



“Since the Threshold Program began, the attitude of many public institutions has changed completely. Now they meet our expectations. Our success is also their success.”

*Lilian Almeida,
Operations Manager of the maquiladora
MMKM in Ciudad del Este.*

These words highlight the productive sector's need to work with a public administration that is able to meet its needs in a timely fashion, thus galvanizing economic activities and production. An efficient public administration is critical to ensuring a competitive economy in Paraguay.

Improved interinstitutional cooperation, discussed earlier, played a very important role in enhancing the administrative efficiency of public agencies. The Threshold Program also contributed to greater efficiency in the public sector and had a positive impact on each institution by im-



For the first time, the struggle against contraband included Customs personnel, the Paraguayan Navy and the National Police in a coordinated effort to combat illegal imports. Deputy attorney general Alfredo Tauber explains the legal process associated with anti-contraband operations.

proving planning processes and the provision and use of resources, and introducing dynamic monitoring and evaluation of programs and institutions. A public sector that practices good planning, has sufficient and well managed resources and constantly monitors and evaluates its processes, activities and outcomes, is well situated to implement its activities efficiently. This is conducive to a better work environment, which in turn, enhances the country's competitiveness.

The Threshold Program acted as a catalyst for institutions to incorporate new strategic plans and tools. In this way, public institutions are gradually evolving into agile entities, focused on improving their productivity, efficiency and ability to find and anticipate solutions more effectively.

Planning

Without goals and objectives to focus on, many public institutions fail to achieve consistent outcomes because they are simply reacting to the problems that arise on a daily basis. The habit of "putting out fires" in the workplace, rather than operating based on a plan, creates problems and increases public frustration as citizens' expectations are not being met.

Planning

Planning addresses the ultimate purpose (what to do?) and the means (how to do it?). It defines the direction of the action plan, reduces the impact of change, economizes resources, and establishes criteria for designing the plan.

The planning process includes:

- **Identifying the organization's goals and strategies to achieve them.**
- **Creating a master plan for reaching goals and objectives.**



The Special Surveillance Department of the DNA (DETAVE) examines how contraband operates in Paraguay in order to fight illegal imports more efficiently and reduce the harm they cause to the country.

Therefore, a focus of the Threshold Program was to help instill good planning practices to improve the efficiency and effectiveness of participating government institutions.

Good institutional planning begins with an adequate assessment of the problem to be addressed, because without an understanding of the actual situation it is difficult to set objectives and design effective strategies to reach them. Institutions that introduced or strengthened good planning practices (based on initial assessments) include the Special Surveillance Department (DETAVE) under the National Customs Authority, the National Council of Maquila Export Enterprises (CNIME) under the Ministry of Industry and Commerce,

the Unified System for Establishing Enterprises (SUAE), also under the Ministry of Industry and Commerce, and the Office of the Undersecretary for Fiscal Affairs (SET) of the Ministry of Finance.

In the case of DETAVE, an assessment was conducted to look at patterns of contraband flows in the country. Based on the findings, the new entity was able to determine the most appropriate structure to efficiently fight contraband. This included the decision to integrate—for the first time ever—Customs, Navy and National Police personnel under a single inter-institutional umbrella to coordinate efforts in the fight against the illicit import of goods over land or on waterways. It also included a clear

definition of the roles and responsibilities of each participating institution based on their relative strengths and areas of jurisdiction.

In the case of CNIME, the planning process played a critical role in identifying business opportunities and generating more investment in Paraguay under a maquila system (a legal corporate status that offers financial benefits to certain companies that produce for export). Threshold Program advisors worked with officials on an in-depth analysis of the economic sectors and types of businesses that might have the most interest in the country's maquila system. Based on this analysis, specific strategies and work plans were designed to promote this system among sectors identified as having the

Change in progress

For several of the units created during the course of the Threshold Program, the modernization process continued after the assistance had ended. The Tax Investigations and Fraud Detection Unit (DIT), for example, prepared a procedures manual and developed job descriptions for its staff.

“There is no question that the performance of the units improved during implementation of the Threshold Program and the attitude of many civil servants working in the Ministry changed. Those who did not choose voluntary retirement understood that there would be no more opportunities to persist in inappropriate practices.”

Tito Ibarrola, Chief of the Department of Tax Investigations and Fraud Detection.



An entrepreneur registers his business using the SUAE's one-stop service window.

greatest potential. The outcomes of this assessment and planning process to date are reflected in investment plans worth over \$13.5 million for 23 new maquila programs, and in the ten additional companies currently in the process of registering in the country as new maquiladoras, with an investment level estimated at \$3.6 million.

The establishment of the SUAE—which consolidates the activities of all seven agencies involved in registering a new business in a “one-stop service”, in order to streamline this process and provide a higher quality service to entrepreneurs—led each individual institution to evaluate and identify ways to streamline its own business registration procedures. This planning and reorganization process

yielded more transparent structures able to detect irregularities and significantly reduce instances of corruption.

Finally, it should be noted that when the Threshold Program began, the SET did not have a tool to measure the VAT gap in the country. In other words, the SET was unable to measure the difference between tax revenues actually taken in by the State relative to potential revenues (the estimated total if all contributors paid according to their tax liability). Using the methodology introduced, data can now be compiled in statistical and index form to measure the efficiency of the tax system. This information can then be used in designing strategies to expand the tax base. The Tax Liability Index that was developed is a

calculation to measure the taxes levied on the country's economy based on data provided by the Central Bank of Paraguay. It includes the sales tax base, as well as taxes payable on purchases, and can be used to calculate the liability of each economic sector and its capacity to contribute annually, thereby generating useful information for planning processes in national institutions.

Provision and Adequate Use of Resources

The assessments and evaluations conducted revealed that, in some cases, the annual plans of some institutions did not correspond with the resources available. When a public administration lacks the necessary resources to implement its plans, its efficiency and



The Office of the Undersecretary of State for Fiscal Affairs demonstrated that it is possible to transform a public institution and render it more efficient in order to respond to increasingly high public expectations.

Modernization of the SET

By contributing the necessary technology and advisory services, the Threshold Program facilitated procedures conducive to establishing an efficient administration and improving public confidence.

Electronic updating of taxpayer information: With state of the art technology, taxpayer information can be updated in the same place where other verifications are carried out.

Internet filing of sworn declarations: Sworn tax declarations can be submitted electronically.

Electronic tax payments: A secure electronic tax payment system was implemented and operates through a commercial bank.

Electronic issue of certificates of shipment: This system has made Paraguay one of the few countries with enhanced security for cargo transportation.

competitiveness decreases. An aim of the Threshold Program, therefore, was to make sure participating governmental institutions had sufficient human, material and financial resources to meet their objectives.

In terms of human resources, planning must necessarily be accompanied by an effective staff selection and training process. Government institutions must make work force professionalization a priority to ensure greater efficiency and the proper use of State resources. In the context of the Threshold Program, the Paraguayan government sponsored training programs for DETAVE, the Jeroviaha Unit (UJ), the Of-

fice of the Undersecretary for Fiscal Affairs (SET) and internal investigation units of the Ministry of Finance and the National Customs Office (created to investigate and report corruption by civil servants and customs violations). Staff development included practical field training and observation missions to other countries to learn from experiences at the regional level.

DETAVE is made up of specially selected and trained personnel. Human resources training included rigorous theoretical and practical instruction. Participants were subject to a criminal history check and scrutiny of their professional and personal

backgrounds, including the application of a voluntary polygraph test. Training of UJ staff benefited from the existence of a similar unit in Ecuador with a proven track record of success. Under the auspices of the Threshold Program, some members of the UJ participated in two observation missions to Ecuador. The first visit focused on understanding the unit's general functioning and identifying areas applicable to the Paraguayan situation and objectives. During the second visit, participants examined route control practices. Personnel from investigative units also participated in observation and training visits to Colombia, Puerto

Monitoring and Evaluation

This is the process of compiling information about the functioning of an organization or project. A monitoring plan is a basic—and critical—tool for making appropriate decisions concerning the design, implementation, administration and evaluation of an organization's activities.

Evaluation entails an objective and systematic examination of an entity's performance and measures its efficiency and impact. Its ultimate aim is to:

- Compile the lessons learned from the project's experience in order to improve the quality of the entity's work.
- Improve the design of future activities and processes.
- Demonstrate to the public the entity's merits, processes, strategies and activities.

Together, monitoring and evaluation help ensure that the institution is operating efficiently and reaching its goals.

Rico and Washington, D.C. to study best practices from around the world.

An important aspect of the adequate use of material resources in the new DETAVE and Jeroviaha Unit involved training in the use of new equipment necessary for the operations of each institution. The Program equipped DETAVE with several pieces of specialized equipment for the detection of concealed contraband, without the need to open boxes, trunks, and other containers. Some of this equipment uses sophisticated technology and has special use and maintenance requirements. Part of the staff development

process, therefore, included specialized training in handling these devices and in procedures to store and safeguard them when they are not in use.

Another contribution to the effective operation of the Jeroviaha Unit was the provision of Wap cellular telephones,¹⁵ which facilitate immediate access to the SET database and enable the UJ to conduct control activities directly from the verification site. This system increases the efficiency of verification operations and offers enhanced security and guarantees to the taxpayer. The use of this technology ensures the objectivity and transparency of procedures because the taxpayer can use a special code to verify the legitimacy of the operation.

The state of the art tool most essential to the performance of the investigative units CAIA and DIT was a software package containing programs such as i2, the Analyst's Notebook and Arcview. These programs correlate and organize data, such as photographs, maps, telephone calls, and other data inputs, to offer investigators a clearer view of which avenues to pursue. With them, investigators and analysts can process large quantities of information into useful intelligence. Arcview is a Geographic Information System (GIS), used to capture, store, analyze and present data related to geographic locations. It facilitates data analysis and mapping activities to detect similarities and patterns. The i2 is an advanced investigations system that can link seemingly unrelated data. Personnel responsible for operat-

ing these programs attended specific training sessions on their use.

The PARIS system, also acquired and adapted through the Threshold Program, is a management software package for the investigative units. This system helps efficiently administer the work of investigators and case management, as well as the unit's contacts and database. This tool was another important contribution to the Threshold Program's Focus Area on Formalization of Economic Activities, in the context of knowledge transfer for updating and presenting statistical data.

To facilitate the application of a more proactive, transparent advocacy effort CNIME began to implement the Customer Relationship Management (CRM) system to systematically monitor promotional efforts targeting national and foreign companies and to generate statistical inputs such as the average time it takes an investor to decide whether to become involved in the maquila industry after an advocacy effort has been made. This tool will help CNIME institutionalize its contacts and maintain background information in a unified database to ensure that sensitive information is not lost during personnel rotations or staff turnover.

To ensure that equipment such as radios, vehicles and watercraft provided to these institutions was used properly, the counterpart institutions issued the relevant regulations and user guidelines to effectively control the

¹⁵ Wap Cellular phones provide direct access to SET database from anywhere in the country.

equipment, supervise its maintenance, and make sure it is used exclusively for the established purpose.

During its implementation period, the Threshold Program contributed to the development of human resources and the provision of equipment. Building on this foundation, the training and equipping of the public sector will be an ongoing process requiring adequate funding, which will be a future challenge for the Government of Paraguay. One way to ensure that the State has the ability to adequately fund public agencies is by reducing tax evasion and using the collected taxes to continue fortifying the public sector.

Dynamic Monitoring and Evaluation

Even the most careful planning process may not produce the desired outcomes for a number of reasons. Changes in the context or environment in which the planning process occurs may undermine its effectiveness, and inefficiency or gaps in the

implementation of a work plan may derail it from its objectives. It is therefore important to conduct periodic monitoring and evaluation activities to determine whether objectives and goals are being met and, if they are not, to pinpoint any necessary adjustments to strategies, implementation methods, or previously established objectives.

With the support of the Threshold Program, public institutions as diverse as the SUAE and the SET applied these principles in an effort to improve their efficiency. In the case of the SUAE, the first step was an assessment of the business registration process and the requirements of each participating institution. Based on this assessment, the SUAE was designed to improve efficiency and to reduce the cost of business registration from the outset. After one year of operation, another assessment was conducted, which identified additional improvements that were both necessary and feasible to further enhance efficiency,

without enacting a new law. The institutions that make up the SUAE have continued to work in a coordinated manner to apply the recommendations of the assessment and individually to more efficiently process their parts of business registration applications within the established time frames. The Program provided additional resources (such as computers and software) to facilitate and expedite the flow of information between those institutions.

One of the most significant achievements of this undertaking was the design of a single form to register a business. The form was created after months of negotiations and numerous adjustments to policy and procedures, formats, and information classification systems within each institution. Working with a computer company, the software used by the SUAE was adapted and adjusted. As a result, the SUAE will provide a better public service with the aim of reducing the average time to open a business to 15 days.



DETAVE is made up of specially selected and trained personnel. The training process included theoretical and practical instruction.



In cases where equipment was provided, the participating institutions instituted control systems and regulations to ensure its proper use.



Post-operation analysis is essential for monitoring activities. Periodic and short-term evaluations help achieve goals and objectives, detect shortcomings and apply corrective measures in a timely fashion.

The outcomes of these myriad efforts show that it is possible to transform a public institution to enable it to respond to increasingly high public expectations. This success was achieved by helping the institution determine its objectives, set goals, and create a work plan to move forward. The indirect impact is reflected in an openness to reflection and analysis that enabled the institution to identify and resolve weaknesses in its organizational structure and resource administration.

These are examples of single, consolidated forms used by the SUAE to open sole operator and limited liability companies and to obtain legal corporate status.





CHAPTER 3

Cultivating Public Confidence in Institutions

The Threshold Program supports initiatives that ensure direct access to information in a clear, quick and transparent manner.



“We request that the authorities inform us about the formalization process and tax compliance efforts, and that they listen to civil society’s call for government budgets that invest in the basic needs of our population.”

*Statement issued by civic organizations in favor of formalization.
Ciudad del Este, Paraguay, July 7, 2008.*

Similar appeals can be heard across the country: citizens are demanding more transparency in the administration of government institutions and more access to information about their activities, as a first step towards placing confidence in the GoP. Citizens are seeking more opportunities to oversee the use of funds and to ascertain whether their demands have been taken into account. The Threshold Program worked towards increasing openness as a basic requirement for building confidence in government institutions. To this end, it promoted initiatives to improve transparency in public institutions and fostered a constructive public-private sector dialogue.

When we ask ourselves exactly what elements must be perceptible in government institutions in order to build public confidence in them—besides increased transparency, mechanisms to respond to the public, and dialogue with the private sector—we see that the institution must operate in a sound and efficient manner to make sure that information is shared, responses are received and dialogue takes place in a legal framework with clear and impartially applied procedures. It is not surprising that the same elements that foster public confidence in government institutions also make

An institution inspires confidence when:

- **Its administration is transparent: it offers the public more access to information, and has the capacity to investigate accusations of fraud or corruption brought against public officials.**
- **There is a constructive dialogue between the public and private sectors.**
- **Steps are taken to promote a positive image.**
- **The reforms are supported by measures to reorganize and streamline public administration.**

the country more attractive to foreign investment.

Administrative Transparency

In order to improve public access to information, the Threshold Program developed mechanisms to handle the inquiries, comments and reports or complaints received by government agencies. It also reinforced institutional capacity to detect and investigate cases of fraud or corruption committed by public officials.



Several public education campaigns took place during the course of the Threshold Program to inform citizens about benefits of program activities, such as the development of a simple, one-stop service for registering a business.

A few examples of how institutions improved transparency in the framework of the Threshold Program are provided below:

- Access to tax information was improved by the installation of a Call Center under the auspices of the SET. Under this new system, calls from the general public are channeled to a centralized answering services where simple consultations are handled by an automated service and others are referred to the appropriate departments. In the past, it was difficult to obtain assistance and people did not know what numbers to call.
- As part of its support to the SET, the Threshold Program helped establish simpler, more transparent and user-friendly taxpayer services, including procedures such as electronic tax payment, electronic updating of taxpayer

information and other innovations, as described in previous chapters. All of these mechanisms are designed to facilitate public access to the information available on its website:

**www.set.gov.py
and its Call Center in Paraguay
(595 021-417-7000).**

- The SUAE created a website containing information about the requirements for starting a new business: **www.suae.gov.py
and a telephone number to answer questions (595 021)-525-885.**

Once the process is begun, the customer is assigned an access code on the website, which can be used to monitor the status of the process. In the past, tracking a registration process and inquiring about the status of applications meant personally visiting all seven institutions now working

together under the SUAE umbrella to enquire as to the status of the registration documents.

- The establishment of SADEP, the Customs System for Public Complaints with Judicial Protection, is an automated complaint mechanism accessed through an Internet portal of the National Customs Office:



The Threshold Program helped streamline, facilitate and enhance the transparency of procedures for many institutions. In this example, a businessman is using the electronic tax payment system to update his taxpayer information electronically.



A team of SET officials works with private sector tax specialists to improve the tax audit system.

as applying to register a business and the existence of a professional force to fight contraband, given that illegal activities are extremely damaging to formal companies in the country.

Internal Investigation

Adequate information and transparency in public services administration must be accompanied by the capacity to investigate cases of fraud or internal corruption. In this area, the Program helped to develop capacity for impartial investigations of reports involving civil servants, which facilitate the subsequent application of the penalties established by law. This element helps bolster confidence in government institutions and reinforces other initiatives to improve public administration.

The Ministry of Finance's Internal Investigation Unit (UIIH) is responsible for investigating accusations of fraud, corruption and other offenses committed by public officials. The following are examples of the types of internal investigations conducted under the auspices of the Threshold Program, that have helped build public confidence in government institutions:

- The UIIH was responsible for investigating irregular travel expense reports submitted by members of the anti-contraband units of the National Customs Office. The investigation elicited sufficient evidence to remove those found guilty from their posts. In September 2008, the office of the special prosecutor for corruption cases filed

www.aduana.gov.py
and telephone: (595 021)-616-2000.

The system guarantees that the identity of the complainant will be protected and provides resolution of the complaints.

- Several public education campaigns were included in the Program design to inform the public about the re-

forms and the process of formalization, reorganization and competitiveness of the Paraguayan economy. Some of the institutions' public messages encouraged people to participate in the reform process by requesting invoices and records of legal sales to combat the common practice of VAT evasion. Another initiative was to raise awareness of new government services such

“There are no corrupt institutions, but rather officials who become corrupted.”

Remark by President Fernando Lugo on the occasion of his inauguration, August 15, 2008.

“The institution (DNA) was hijacked by informality. If an entrepreneur lacked connections, his process would not move forward. Bad customs praxis is still a reality.”

DNA investigator.

charges against 37 civil servants and they are currently being prosecuted. As a result of the investigation, the DNA adopted a series of reforms on the provision and use of funds.

- A report filed by a taxpayer whose company's activities were being verified by the Jeroviaha Unit led to the removal of an inspector from the Office of the Undersecretary of State for Fiscal Affairs. The latter had offered to "wipe clean" the company's file in exchange for an irregular payment. In a public statement, the SET encouraged other taxpayers to follow this example and report corrupt officials.
- A high-level official of the Ministry of Finance chose to resign after the Internal Investigation Unit opened a case concerning his activities.
- In August 2007, a customs officer accused of corruption was sentenced to two years in prison.

These examples show that freedom of information mechanisms are insufficient without the other elements discussed in previous chapters. In other words, better access to information is not enough: citizens also require a legal framework featuring clear and impartial procedures, administrative efficiency and the capacity to investigate complaints. Similarly, investigations into accusations of fraud or corruption must be part of a proactive government monitoring and evaluation process to pinpoint opportunities to improve internal processes and procedures in order to prevent fraud and corruption.

The case of irregular travel expense reports submitted by DNA officials described earlier led to corrective measures in processes to administer and monitor the use of travel allowances. This example shows that the reforms described in this report interact for the common good. The investigation process had an additional deterrent effect on other civil servants, who began to take the travel expense report process more seriously.

Nonetheless, it is still difficult to institute self-correction mechanisms within government agencies to combat the contaminating influence of internal corruption networks that impede progress towards a formal, healthy and competitive economy. In recognition of this situation, the incoming customs director said "We are committed to the people, obligated to carry out our work with efficiency and quality. Our slogan "zero tolerance for corruption," is a promise that we will not betray the people's hopes and the confidence placed in us." (DNA website, August 19, 2008).

Facilitating Private Sector Participation in Public Sector Reforms

Healthy, formal, competitive economies enjoy active private sector participation (from individual citizens, civil society organizations and private enterprises) in the reform of government institutions. When it is constructive, this participation helps strengthen administrative transparency and foster reforms to improve public sector organization and efficiency. The

participation of private sector actors in public sector activities and most importantly, in the reform process, can help make reforms to public administration more responsive to the needs and wishes of citizens. The Threshold Program facilitated this type of participation through a number of different activities:

- *Monthly meetings between private sector representatives and counterpart institutions of the Threshold Program, through an Advisory Council.* These meetings were intended to facilitate ongoing private sector involvement in monitoring the progress made by public institutions and their activities to attain Program goals.
- *"Train today to formalize tomorrow."* The Paraguayan-American Chamber of Commerce project supported the training of educators from the provinces emphasized the importance of the formalization processes underway in Paraguay and trained educators in basic economics.
- *"The role of citizens in building government capacity to fight corruption."* This Institute for the Consolidation of the Rule of Law project examined the role of investigative units (DIT, CAIA, and UIIH) in anti-contraband efforts and published this information to raise public awareness about the importance of this struggle.
- *"We pay taxes so the State can do its job."* [Tributamos para que el Estado cumpla]. This Institute for Comparative Studies in Criminal and Social Sciences (INECIP) project designed training workshops on economic

Additional testimonies from the private sector:

Much to the surprise of the authorities, many citizens noticed that the SET was operating as a serious institution and applauded the new controls, even acquiescing to the sanctions. *“Under no circumstances are we to think the system can function without controls. As distasteful as they may be, they are necessary,”* asserts Carlos Mersán, a well-known tax attorney who, just months before the Threshold Program intervention, had vigorously criticized the SET’s strategy to implement new controls as being, in his view, unconstitutional.



Juan Vera, president of the Association of Customers and Consumers of Paraguay, during the SET’s Call Center inauguration.

“Anything that contributes to the simplification and clarification of procedures is welcome. The public is realizing that the SET has made a lot of progress in improving its services. People can see substantial improvement.”

reflects a significant change in public perception of the SET which, in the past, had been perceived as inefficient at best and, at worst, an institution that simply ignored flagrant cases of fraud by its public officials.

Similarly, the private sector involvement in reform promoted by the Threshold Program led to better customer service on the part of public institutions, which further increased private sector confidence in these institutions. The streamlining of procedures to start a new business, through the creation of the Unified System for Establishing Enterprises (SUAE) facilitated the access of entrepreneurs to this public service and helped enhance the quality of services provided to the public. Those interested in opening a new business learned that they could do so by means of a single procedure and that only the requirements set forth in the law were being asked of them. The system is designed to promote transparency, and the SUAE website provides information on the exact cost and requirements to start a business. Once the process has begun, an individual can follow up on the status of the documentation by telephone or by Internet. Specialized ongoing training resulted in a tangible positive attitude among civil servants assigned to the SUAE, who demonstrated a stronger commitment and responsibility towards resolving the problems that arose on a daily basis. The SET Call Center experienced a similar change. At first, callers did not have a clear understanding of the utility of a service designed to answer tax-related questions. At the same

formalization for small merchants in Ciudad del Este. At the end of the process, a partnership was established between INECIP and the Chamber of Electronics Importers of Paraguay to ensure the continuity of this effort.

- *Transparency Paraguay helped to design and implement the SADEP (the Internet-based public complaint system described earlier) and organized trainings for young people on the work of the National Customs Office.*

- *Decree regulating the activities of the Jeroviaha Unit. A team of SET officials worked with private sector tax experts to arrive at an amendment to Decree No. 8094/05. The changes were applied through Decree No. 8594/06, which regulates the activities of the Jeroviaha Unit and corrects certain deficiencies, including some that had been hampering the unit’s work. This strategic partnership with the private sector became stronger over time. Several weeks before the Jeroviaha Unit proceeded*

with the first temporary suspensions of businesses, a series of meetings were convened with accountants, tax attorneys, and notaries to explain the suspension procedure and the anticipated results. The latter included such specific outcomes as reducing the high rate of noncompliance in issuing sales receipts, which was estimated at 80% in 2007. These meetings played a critical role in securing the acceptance and commitment of the private sector, which supported the SET’s verification efforts.

On May 2, 2008, the Undersecretary of State for Fiscal Affairs received a note from the People’s Defender, Manuel María Páez Monges, which states as follows: *“... We request ongoing and intensive control efforts by the Jeroviaha Unit in view of the public indignation that has been expressed over tax evasion by commercial establishments in Asunción.”* This note directly illustrates the degree of public confidence in the SET’s control operations. Moreover, it



The SUAE is conducive to transparency. One can look up the requirements for starting a business and verify the status of the procedure on its website: www.suae.gov.py

“Today our office operates transparently. Our clients can see it and they go away satisfied. Many entrepreneurs think the SUAE is a private enterprise, or a service that has been outsourced, because it is effective and quick and we provide good customer service. This is the image we want to foster, in order to maintain our credibility.”

Alba Narváez,
municipal delegate to the SUAE,
from 2006 to 2008.

time, the civil servants involved had little experience dealing with the public. The learning process for the public and the SET employees occurred in a parallel fashion. Over the course of several months, SET staff learned to respond courteously and diligently to citizens' questions. This improved the institution's image which, in turn, bolstered public confidence. Today, a growing number of citizens nationwide use this SET service, which currently receives an average of 8,000 calls per month.

The presence of the Threshold Program served as a seal of confidence for the parties. It fostered dialogue and facilitated joint initiatives involving citizens and the institutions. The sustainability of the changes is contingent on the involvement of the public, and on public officials being committed to reining in tax evasion and contraband

and to promoting more investment and businesses. The public must remain vigilant and raise its voice when institutions take a step backward. Citizens must demand the allocation of necessary resources, the transparency and effectiveness of processes, and the universal application of clear rules.

Just as the Threshold Program helped build confidence to enable institutions to take ownership of their work, it also enhanced the credibility of those institutions in the eyes of citizens. A merchant whose business was being investigated by the Jeroviaha Unit reported to the SET that he had received a dishonest offer by an inspector from that institution. The case was investigated and the civil servant in question turned out to be guilty and was arrested. But most importantly, the case showed that the SET was beginning to earn public confidence.

There has been a change in public perception of the seriousness of certain institutions and their capacity to receive complaints.

These examples illustrate the efforts that have been made to facilitate constructive private sector participation in the public sector's operations. The private sector's active participation in reforming the public sector is helping strengthen mutual trust. *“The government is going to be responsible for opening the doors to investors from around the world. But if we have the bad reputation of being smugglers, or corrupt, or drug or arms traffickers, who is going to want to invest in our country? This is what we have to change so that people believe in Paraguay.”* Epifanio González López, Chief of DETAVE up until August 2008, who has worked for 32 years in the operations area of the National Customs Office, has no-

“We have achieved more transparent and efficient management, we have more and better information, and this contributes to improved relations with the public. This customer service center enables us to provide a better service to taxpayers with increasingly high expectations. We can better serve people throughout the country and engage in direct communication without the need for face to face contact between the taxpayer and tax officials. Calls are taped and monitored for quality assurance.”

Gloria Páez, former Undersecretary of State for Fiscal Affairs, on the formal inauguration of improvements to the SET Customer Service Center in August 2008.

ticed the increased trust in his institution. Mr. Gonzalez is familiar with the reality of merchandise flows and the image people have of customs officials, but has observed that the negative perception is slowly changing. Both he and all citizens hope the change will be sustainable. By engaging the private sector, the Threshold Program contributed to a more positive image of the country and helped transmit that image to domestic and foreign investors.



CHAPTER 4

Promoting the National Image

The Qin Yi America set up operations in Ciudad del Este, shifting its focus from imports to the textile industry. Now their blankets bear the “Paraguayan Industry” seal and are exported to Brazil.



“Contact with the maquila industry, promoted by the Threshold Program introduced us to the real Paraguay. In Brazil, we used to have a distorted image of reality. We saw Paraguay as a disorganized and corrupt country. Today we find a structured country, with a significant incentives policy for establishing new enterprises and new investment opportunities. We also see an enormous desire for growth in the country’s efforts to galvanize the formal economy.”

Letter from two entrepreneurs who already began the process to establish a maquiladora in Paraguay: Rodrigo Henrique Probst of Itu Tava S.A. and Gilmar Darolt, of Junior Comercial de Cereais Ltda., State of Santa Catarina, Brazil.

This testimony shows that Paraguay can project—and is projecting—a more positive and trustworthy image, which is improving the country's position in the world economy. Today Paraguay is still in the bottom ranks of global indices, such as the World Economic Forum's, that measure competitiveness, transparency, institutional solidity, the business climate, and other indicators. Nonetheless, as a result of the advocacy strategy implemented by CNIME under the Threshold Program, potential investors can see that a formalization process is underway in Paraguay: its legal framework is increasingly straightforward, government administration is more efficient, and formal enterprises enjoy more support to pursue their activities. Today, the State exercises more effective control over businesses that evade taxes or fail to declare their goods when enter-

ing the country. And, it applies the law in an impartial manner, which helps enhance competitiveness.

The emerging image of Paraguay as a healthy, formal and competitive country able to develop formal businesses of all types is the result of the advocacy efforts undertaken with the support of the Threshold Program. The Threshold Program's Country Plan [Plan País] was developed by the Government of Paraguay, which has worked to improve public administration and operations. In the framework of the Threshold Program, the Ministry of Industry and Commerce worked diligently to promote the country's image through favorable investment policies, focusing especially on the maquila system. This strategy led to the formalization of many enterprises, which provide real value added to society and to the economy, under competitive conditions, through job creation and labor force training.

Promotional materials:
"Maquila in Paraguay"



The Maquila System

The Threshold Program focused on the maquila system pursuant to a decision by the Government of Paraguay, which views it as a tool with enormous potential to galvanize the economy, attract foreign capital and create jobs in the short term. It is



Cooperation and coordination with institutions and entrepreneurs from bordering countries is essential to ensuring that investors receive information on the advantages of the Paraguayan maquila industry and business opportunities in Paraguay. This photograph depicts one such key meeting involving the private sector (entrepreneurs from Paraguay, Brazil and Argentina), local and national authorities, and facilitators from the Threshold Program.

important to recall that Article 4(b) of Decree No. 10.337 “Government Policies and Priorities,” contains the strategic objective of improving the economic structure and consolidating the shift towards production for the export market, with a priority on job creation. The concept of the maquila system is consistent with these objectives. Moreover, because it is geared towards the export of the goods and services produced, domestic production must meet international standards of high quality at a competitive price. This leads to the enhanced competitiveness of local businesses participating directly (maquiladoras or submaquiladoras) or indirectly (inputs and service providers) in the system, as well as of the labor force it employs.

The Executive Secretariat of the National Council of Maquila Export

Enterprises (CNIME) is responsible for diverse functions to ensure compliance with the maquila regulatory framework. In this context, CNIME must monitor the management of companies operating under this system to ensure they do not deviate from their stated programs. This entity also acts as a liaison between the maquiladoras and other government agencies. In addition, the Executive Secretariat is actively involved in the preliminary review of new programs (projects submitted by businesses wishing to operate as maquiladoras) and in overseeing CNIME’s approval process.¹⁶

One of CNIME’s objectives is to effectively promote the system to increase the number of new maquiladoras. From its establishment in early 2001 to June 2006, CNIME’s work was constrained by the lack

of adequate funding to carry out promotional trips and provide sufficient accompaniment to investors visiting the country. It also lacked funds to pay specialized promoters and remunerate personnel engaged in research, proactive advocacy activities and follow-up with the businesses contacted in order to promote the benefits of the maquila sector. The shortage of resources limited CNIME to “reactive” tasks, such as receiving the few investors who visited their offices with some prior knowledge of the system and a modicum of interest in investing in the country.

In order to rectify this situation, CNIME, with assistance from the Threshold Program, developed a strategy to attract investment based on the identification of sectors and specific enterprises that stood to benefit most from the maquila

¹⁶ CNIME comprises representatives from several government institutions. It is chaired by the Ministry of Industry and Commerce and includes the Ministries of Finance and Foreign Affairs, the Central Bank of Paraguay, and the Technical Planning Secretariat.



With Threshold Program assistance, the CNIME developed a strategy to attract investment and to identify sectors that might benefit from the maquila system, such as the clothing sector.



The maquila system is a means of modernizing production systems in Paraguay. This system makes it possible to develop skills among the local labor force and also facilitates technology transfer.



The maquila system promoted by the Threshold Program is a major source of direct and indirect jobs.

system. The promotional plan implemented by CNIME included the following activities:

- Preparation of more than 30 studies and research projects on countries and sectors, and papers addressing specific questions raised by companies interested in operating under the maquila system because of its advantages.
- Analysis of information on the characteristics of specific businesses, to identify companies with the particular profiles identified in the studies and research projects.
- Development of promotional presentations and materials describing the benefits of the maquila system and the advantages of doing business in the country.
- Direct contact with the companies identified, initially by email or

telephone, followed by on-site visits based on a previously established agenda when internal visits, including at least five confirmed interviews with interested companies and contact information for more than 10 previously identified potential companies.

- Follow-up with companies that expressed interest in operating under the maquila system and ongoing evaluations of the sectors that had been approached with information about the system's advantages.
- Research papers and documents to respond to specific questions or requests for information concerning tariffs or business plans for creating a maquila program.¹⁷
- Preparation of meeting agendas to give international investors the opportunity to interview members of

the CNIME Executive Secretariat and visit potential service providers and facility sites.

- Respond to all of the investors' questions and consultations and the provision of any additional information requested.

Each investor that decided to enter the maquila sector received assistance to develop a maquila program. The future operator was accompanied throughout the legal process, which involved the approval of the maquila program through a binisterial resolution (Ministry of Commerce and Industry and Ministry of Finance) and other required steps to launch operations under this system. This assistance was meant to ensure and expedite the establishment of the companies, in view of the many requirements associated with setting up a maquiladora and the difficulty

¹⁷ A production plan required by GoP to grant authorization to factories to operate under the maquila system.

foreign investors might face in learning to operate expeditiously in a new country. Without the proper, specialized assistance to guide the entrepreneurs through the relevant processes and provide reliable data for decision-making, the start-up process might have encountered excessive delays and possibly might never have been accomplished.

Streamlining the Process to Establish a Business

Promotional efforts in support of the maquila system and other beneficial policies for businesses could all be in vain unless the actual process to establish a business is not sufficiently responsive. According to the World Bank's *Doing Business* report, a key factor in a country's competitiveness is the fact that a business can be opened quickly, with a minimum of paper work, and at a low cost. Following the World Bank methodology, the Ministry of Industry and Commerce requested that each institution submit an analysis of its procedures for establishing a business so as to identify ways to streamline the process. The findings of this analysis, and the implementation of the ensuing proposals, led to the creation and inauguration of the Unified System for Establishing Enterprises (SUAE) in November 2006. As a result of the creation and success of the SUAE, Paraguay rose 72 positions, from 138th in 2007 to 66th in 2008, in the rankings for starting a new business,

as indicated in the *Doing Business* 2008 report.¹⁸

These types of efforts reflect a genuine interest in promoting the creation of new business which, in turn, has helped project a positive image of the country.

Concrete Outcomes and Impacts

The Threshold Program provided assistance in developing maquila programs at no cost to the entrepreneur and guaranteed the continuity of this service throughout the development and installation process, provided by CNIME, to all companies that had already expressed an interest in operating under this system. The Threshold Program's technical advisors assisted businesses with each step of the start-up process up to the initiation of export activities. Unfortunately, with its current funding levels, CNIME will not be able to continue to provide this level of services to its clients. Analyzing the cost-benefit to the State reveals a tangible need to revise the agency's budget to ensure that CNIME can continue to provide the same quality of services to investors.

During the life of the Program, 33 maquiladoras began the registration process to establish their businesses in Paraguay, and 23 have already received approval from the State. The investment of those already approved is worth upward of \$13 million and

their programs will create nearly 1200 jobs. The ten programs still in the approval process represent an anticipated investment of approximately \$3.6 million.

The Threshold Program directly assisted¹⁹ 16 of the 33 maquiladoras to be established in country, and six of these are already set up and have initiated operations. Of the companies assisted by the Program, seven have 100% foreign capital, five have mixed capital (both foreign and domestic) and four have 100% domestic capital. To give some perspective on this, prior to June 2006, just one company, Megaplásticos, had established itself in Paraguay under the maquila system with 100% foreign capital.

The new companies contacted by the Threshold Program contributed to the training and specialization of labor of Paraguayan workers, through invitations to visit their factories abroad, specialized courses, and machinery donated to local training centers, such as the National Professional Promotion Service of Hernandarias, which received equipment from two maquiladoras to aid in training its new machine operators.

¹⁸ The ranking for 2007 is important for the SUAE, since it is based on information from 2006, when the SUAE was established, and covers the period from that time until mid 2007.

¹⁹ A program advisor assisted the companies from the initial presentation of the system's advantages through the initiation of operations.

Paraguay reaped the following benefits through the establishment of enterprises operating under the maquila system:

- An opportunity to develop the skills of the local labor force.
 - Technology transfer.
 - Generation of national value added as a prerequisite of the transformation process.
 - Increase in exports.
 - Product diversification.
 - Market diversification: in 2007, Paraguay exported products to 34 countries under the maquila system.
 - Contribution to job creation for Paraguayans in their own country, with the guarantees set forth in existing labor laws (minimum wage, social security and other benefits found in the Labor Code).
 - Positive contribution to the image of “made in Paraguay.”
 - Contribution to the formalization of economic and commercial activities in the country.
- The maquila program and the activities involved in its implementation are taxed through a single contribution of 1% (one percent), which is paid monthly with a sworn declaration.
 - Minimized risk of tax evasion on the part of the maquiladora, due to the existence of a joint regulatory entity (CNIME-DNA) that controls the entry of raw materials and capital assets and the outflow of the finished product.
 - Employer contribution by the maquiladora to the Social Insurance Institute (See Table I).
 - Development of new production chains in Paraguay, that include submaquiladoras and providers.
 - Attraction of more foreign capital to the local economy.

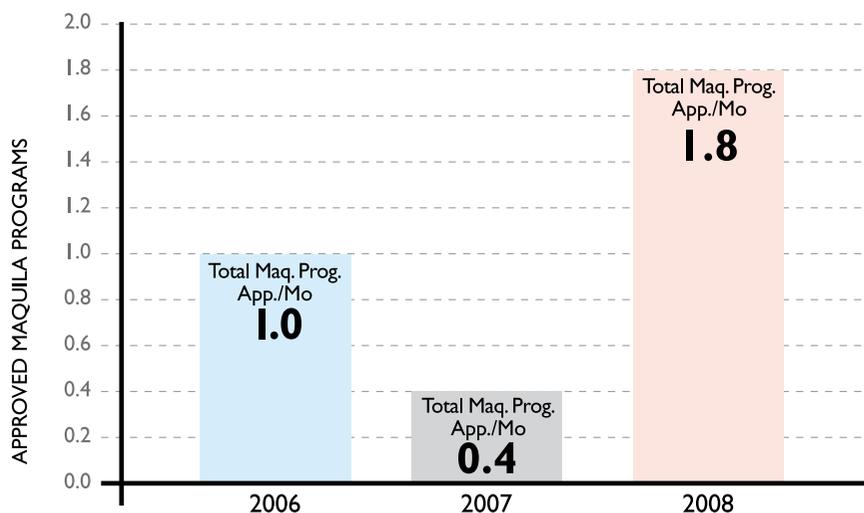
Advantages of the maquila system

The maquila system for the production of goods and services marketed abroad helps make Paraguay an advantageous place to attract and establish national and foreign investment.

Low tax liability: Single Maquila Tax of 1% of the value added in-country.

Flexible legislation: allows foreign specialized staff to remain in the country to train local workers.

Figure 1: Historical behavior of approved maquila programs/month, during the period from June 2006 to September 2008, still in effect. Source: CNIME.



The graph shows the average number of maquila programs approved monthly during the life of the Threshold Program. The number of programs approved declined markedly in 2007, and rose significantly again in 2008.

The 2007 decline could be related to the CNIME's financial difficulties from March to December 2007, as well as to the natural course of investment promotion, in which it usually takes about 24 months for the investment to be operational. The Program launched coordinated, proactive promotional efforts in 2007. The 2008 increase is attributable to the Threshold Program's contribution.

Table I. Totals in U.S. dollars for the following categories: total exports from the country, exports under the maquila system, national value added, Single Maquila Tax, worker-employer contribution, and net wages of the labor force directly employed by the maquila system for the period 2001 – 2007.

Year	Total exports ²²	Total maquila exports ²³	National value added ²⁴	Total Single Maquila Tax ²⁵	Worker -employer contribution under the maquila system ²⁶	Net wages of direct employees of the maquila system ²⁷
2001	990,205,013	1,184,351	0	0	0	2,763,995
2002	950,581,348	2,001,062	0	0	774,526	3,337,783
2003	1,241,503,654	7,930,838	3,472,282	34,723	657,573	2,919,507
2004	1,631,570,586	8,407,641	1,462,226	14,622	773,244	1,112,911
2005	1,671,703,992	27,566,128	4,683,955	46,840	311,101	4,116,198
2006	1,920,026,579	54,688,664	13,948,536	139,485	1,262,950	7,961,169
2007	2,784,726,946	74,734,358	24,518,726	245,187		

²² Source: CNIME

²³ Source: CNIME

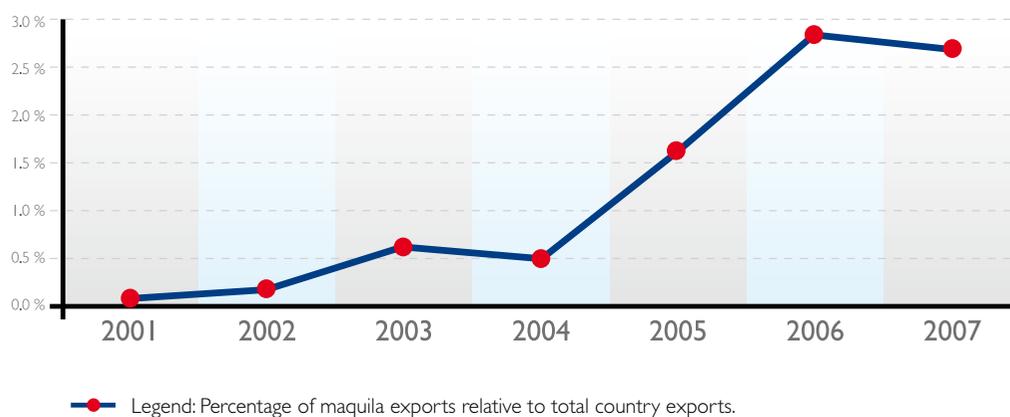
²⁴ Calculated based on the total Single Maquila Tax

²⁵ Source: General Collections Office, Office of the Undersecretary of State for Fiscal Affairs, Ministry of Finance.

²⁶ Source: Office of Worker-Employer Contributions, Social Insurance Institute

²⁷ Calculated based on the total Worker-Employer Contribution.

Figure II. Percentage of Maquila Exports relative to Total Country Exports. Source: CNIME



In conclusion, tangible outcomes of efforts to attract new companies under the maquila system include technology transfer, industrial growth with value added, and increased foreign capital flows. Other positive outcomes include increased tax revenues for the State, growth in national exports, market diversification, and the development of new production chains. It is important to remember that the objective of the Millennium Challenge Corporation (MCC) is to reduce overall poverty by promoting sustainable economic growth. This is premised on the principle that assistance is most effective when good governance, economic freedom and social investment are strengthened. Laying the groundwork for good governance is insufficient without efforts to promote the benefits and policies that might be attractive to potential investors.

The implementation of the Threshold Program demonstrated that when diverse government institutions join forces, they can produce excellent results for the country and its people. It also demonstrated the importance of systematic promotion of these outcomes, which is beneficial for development and enhances Paraguay's image. Many potential investors changed their perception of Paraguay as a corrupt country, governed by illegality and devoid of guarantees for businesses to a more positive image investment promotion activities, coupled with the fight against corruption, helped to disseminate current investment, economic information and change perceptions of the country.



CHAPTER 5

Looking towards the Future: Recommendations for Progress Towards a Healthy, Formal and Competitive Economy

The maquiladoras have contributed to job creation and to the training of Paraguayan workers.



“Roikoteve la autoridad openami orerehe” (we need the authorities to pay attention). We must teach our compatriots how to demand their rights. Because rights are something you demand, you don’t beg for them, and the authorities have the obligation to listen to us. I demand work. If there is work, then there will be health, education and bread.”

*Sara Servián,
President of the Association of Housewives of Paraguay.
From an interview published in the newspaper ABC Color,
May 18, 2008.*

These are the sentiments of a committed leader whose life's work is to advocate for the rights of housewives in Paraguay. Her appeal can be interpreted in broader terms: citizens hope for a country that offers more opportunities and more efficient use of public resources, with increased spending on health and education. They want a more productive country, with trustworthy institutions and impartial application of the law, and a professionalized and efficient public administration, whose planning process takes into account future generations. They want a country that can compete with others on a level playing field.

This report describes some of the concrete achievements that furthered the process of economic formalization, improved public administration, and enhanced competitiveness conducive to expanded economic opportunity. Not only did the institutions involved overcome their initial resistance to the proposed changes, they demonstrated sufficient political will during the course of the Program to change some of the attitudes and practices that can hamper their potential development. While the country has made enormous strides, it must keep moving ahead at a good pace if it is to further the formalization process and make sure the population perceives the benefits of this progress.

Looking ahead, the main challenge is to determine, and follow, the appropriate course so that the outcomes reach future generations. Opportunities must be available to the majority

and reforms must respond to the interests of society as a whole. An institutional presence must be felt throughout the national territory, through local governments, where central government agencies must be represented and active.

What follows are a number of recommendations for Paraguay to continue moving firmly forward in this transformative process towards a formal and competitive economy. The appendices at the end of the report offer indicators from each partner institution and data from each of the Threshold Program's work areas. There is also a one-page description of activities and a summary of recommendations which, should they be implemented, could ensure the sustainability of the reforms instituted and progress made in recent years.

Reorganization of Public Administration and the State

In this context, the institutions clearly were mutually strengthened by working together. Accelerated progress was made in establishing a clear legal framework responsive to the needs and objectives of the institutions and ensuring the impartial application of the law. The changes instituted, in turn, fostered confidence in the State on the part of citizens who have benefited from government services and those who find themselves affected by its actions.

The Threshold Program demonstrated that institutions are capable of working collaboratively and updating their

legal frameworks and procedures on an ongoing basis in order to reach their established goals and objectives. The following recommendations are offered with a view towards ensuring the assimilation and sustainability of these innovations:

Clear Legal Framework

The SUAE is based on an interinstitutional agreement between the seven participating agencies. In the short and medium terms, mechanisms must be in place to make sure the legal framework governing SUAE is brought up to date and procedures are further simplified. In the long term, legislative changes are required to regulate the establishment, registration and closure of businesses. The bill currently under examination could expand the SUAE's

sphere of action, by incorporating the procedures of all institutions involved in the registration process of new businesses in order to offer a more complete service to those interested in formalizing their companies. The Threshold Program recommends that the draft law be approved as soon as possible.

When it comes to the modernization of other institutions, it is also important to update the regulatory framework to include procedural changes and cutting edge technologies. This is the case with the SET, where the new draft Tax Code should include rules on the authorization and monitoring of cash registers, automatic receipt printing systems and the use of cellular telephones to facilitate remote access to fiscal databases, to give just

a few examples. In addition, the SET is requesting an amendment to Decree No. 8594, to make appropriate changes to the working conditions of UJ employees in order to improve the Unit's functioning.

Impartial Application of the Law

The Judicial Branch should be included in interinstitutional agreements in order to secure closer cooperation from judges in the civil and commercial spheres. During the course of the Threshold Program, some shipments seized by DETAVE were released and there were cases of unwarranted delays in obtaining search and seizure orders, as well as technical errors related to the verification tasks performed by the Office of the Undersecretary of State for Fiscal Affairs. If the institu-

The need to update legislation on communications technology. A law that supports optimum use of the SET/UJ's material resources:

The experience of the past two years has demonstrated the importance of communications in the activities carried out by units receiving Threshold Program support.

It would be helpful to update legislation prohibiting the payment of cellular telephone service for use by civil servants, so that technology such as WAP cellular telephones, can be used to facilitate control efforts and other operations. Similarly, special frequency radios should be provided, as they facilitate and speed up internal communication. Another recommendation is to update radio operator licenses and include those costs in the General Expenditures Budget.



A new approach to efficiency in public institutions gave entrepreneur Qin Yi America Lisa Xiang confidence to invest in Paraguay.

tions are to preserve their authority and respect, the judiciary must be a continual presence in control and verification activities.

Paraguay's new government has declared **“zero tolerance for corruption.”** This must be the basis for institutions to dignify the role of the civil servant and ensure that those who engage in wrongdoing are not allowed to continue in their posts unpunished and are not allowed to return to the civil service. Some of the tasks undertaken by the Threshold Program—such as updating legal framework for effective law enforcement, instituting mechanisms for the imposition of penalties, creating a career civil service, and promoting values such as integrity, responsibility and respect for the public welfare—must be carried forward to ensure a healthier public administration.

Interinstitutional Coordination

The SET is a good example of institutional modernization. During the course of the Threshold Program, it successfully applied many of the recommendations included in this chapter to strengthen its administration and performance. Building on these advances, interinstitutional coordination between the SET and the Treasury Counsel under the Ministry of Finance should be strengthened to expedite corrective measures on delinquent taxpayers and to avoid a backlog of files. The SET's Jeroviaha Unit must also have the support of other agencies to facilitate operations such as shipment control. Coordi-

nation is also suggested with other institutions that might benefit from the electronic remittance advice shipment documents and similarly advanced technologies implemented by the SET, so as to avoid duplication of efforts. To this end, trust and cooperation at all levels must be strengthened.

Trust and cooperation must also be strengthened between the National Customs Service, other supporting institutions and the Public Ministry, in relation to the intelligence-operations cycle of anti-contraband efforts. The assignment of a Junior Public Prosecutor to the National Customs Office should be made permanent to ensure the specialization of this judicial agent, an efficient liaison with the Public Ministry, the prompt issuance of warrants for search and seizure and impoundment, and procedural soundness, among other things. The presence of this public prosecutor also serves as a constitutional safeguard for those accused of wrongdoing.

An Efficient Administration to Achieve Competitiveness

Progress towards competitiveness involved, among other things, working with institutions to shape a new, more efficient style of public administration. The new work philosophy enabled government institutions to adapt to challenges and lend their concerted support to private sector initiatives. In order to maintain efficiency in government administration, the institutions must continue to develop their planning capability, making optimum use of their human, material, and financial

Professionalization of civil servants.

The outstanding results obtained with the Jeroviaha Unit confirm the need for ongoing training and refresher programs in the use of technology and other tools.

The institutions should incorporate modern methods for the selection and classification of civil servants that facilitates their professional development and strengthens their commitment to their jobs. Ethical conduct must be part of their training, as well as a basic requirement for joining the civil service. This experience applies to all other institutions. In view of the specialization of anti-contraband forces, Focus Area II of the Threshold Program proposed a plan for “Training the Trainers,” within the DNA, which already has its own Customs Training Center. Salaries must be adjusted to fit duties and responsibilities and must be competitive with the private sector. The Threshold Program recommends an examination of the outcomes obtained in countries where the Fiscal Administration has its own development and training center.



The updating and impartial enforcement of the law, coupled with control mechanisms, guarantee a better future for many Paraguayans who are obliged to pursue informal job opportunities.

resources and paying more attention to ongoing monitoring and evaluation of their activities.

Planning

In some cases, a gap exists between the resources available to governmental institutions and the activity planning process. Therefore, an institutional consensus should be in place to adapt resource levels to achieve goals and objectives and ensure sufficient flexibility to assign civil servants to posts where they are needed. Adequate planning of equipment use is also important to ensure the effectiveness of staff and achievement of institutional objectives.

Provision and Adequate Use of Resources

While the institutions made some progress in this regard, all of the units supported by the Threshold Program require assistance in resource management, particularly in relation to the use of funds for fuel and travel

expenses. The recommendation here is to continue using electronic control mechanisms, such as the fuel cards used during Program implementation, for the effective monitoring of fuel use and replacement throughout the country.

Equipment Inventory and Monitoring

The public must have assurances that the investment in government institutions is being used appropriately. Systematic control of the use of equipment and tools is recommended to avoid unnecessary damage or losses, and protect procurements made with public funds. The systems applied during the Threshold Program to monitor the use and condition of equipment and to ensure its proper care and maintenance should be continued. Public oversight mechanisms, such as a complaint line, should also be set up. In some cases, long term solutions to safeguard equipment must be found. For example, as of October 2008, the DNA did not

have an appropriate location to store boats used for river-based anti-contraband operations. Permanent docks should be installed to protect these vessels in Asunción, Encarnación, Salto de Guairá and Ciudad del Este. It is also important to make existing facilities and procedures secure. With regard to the security of electronic information, the recommendations from the electronic information security consultancy in the SET should be applied and extended to other government agencies.

Ongoing Training and Refresher Courses for Civil Servants

Those who received instruction through the “training of trainers” program should transfer their knowledge to their colleagues using a rotation system through different departments in all institutions. Technical staff should update procedures manuals on a regular basis to ensure that all civil servants are using the same set of rules and to ensure the effectiveness and clarity of procedures. Some units should be reorganized based on work demands. Internal training is essential, therefore, as are efforts to build on the learning that has already taken place. Available talent should be recognized and leveraged for training purposes and other activities.

Appropriate Remuneration

This is applicable across the board, but it is most pressing in areas where civil servants are working in hazardous positions. The salaries of DETAVE personnel and other similar positions



Ilda Beatriz Notario is an instructor with the National Professional Promotion Service in Hernandarias.

“It was a unique opportunity. The clothing industry offers a lot of job opportunities which we have yet to fill. In the SNPP we only offer three instruction sessions with room for twelve students, as we do not have enough machines or materials. We appreciate the donations of machinery from the maquiladoras. This will enable us to train dozens of young people for their first job.”



Carmen Agusti de Petras is a skilled artisan from Ypacaraí, who specializes in chala handicrafts, which are made from banana leaves. She formalized her business through the SUAE and is sure to expand her marketing opportunities.



The Threshold Program helped improve conditions for the development of the formal economy. In the process, new jobs were created for many Paraguayans.



Paraguay can progress towards a more healthy economy by strengthening its resolve and applying new strategies to improve its ranking in world competitive indices. This is the great challenge for Paraguayans and for their authorities.

do not reflect the level of responsibility they require. While some civil servants may be offered certain incentives, proper remuneration is essential to ensure that they do not feel the need to resort to illegal methods to augment their income. They should also receive the benefits set forth in labor laws (pension and health insurance) as well as life insurance or disability insurance.²⁰ It is also important to improve and expedite the distribution of incentives to those participating in anti-contraband activities.

General Recommendation: Government Funding

Public institutions currently rely to a great degree on international cooperation and diverse grants, particularly

when it comes to financing reforms, staff training and expanding service networks. However, some of the changes undertaken could be vulnerable inasmuch as they are contingent upon internal resolutions or the “good faith” of the authorities. One of the main recommendations, therefore, is that these expenditures be considered capital expenditure and incorporated into the annual budget of the institutions. The potential to have funding available for a more efficient administration of the institutions will, in the long term, ensure better planning and control of the reform process.

Monitoring and Evaluation to Ensure Integrity

Considerable government savings can result from efficient control mechanisms and the ability to apply appropriate penalties as needed. During Program implementation it became clear that there was a need to improve internal institutional controls through ongoing audits, cross-referencing data and better control of funds disbursed to individuals. The Program instituted innovative methods to ensure the integrity of public officials, including polygraph tests. Continued use of polygraph tests, at least twice a year, will permit direct monitoring of the ethical behavior of members of operational and investigative units. This procedure encourages

²⁰ Currently, not all the civil servants hired on short term contracts receive these benefits.

civil servants to observe dignified, disciplined, honest and law-abiding conduct.

Fostering Public Confidence in Institutions

During the life of the Threshold Program, the participating institutions redefined their mission: they cultivated an objective vision of society's needs and they learned to listen to complaints and respond with satisfactory solutions. On some occasions, they were able to garner the constructive participation of certain sectors of society, such as notaries, attorneys and accountants in the SET and the SUAE, industrial associations in the customs sphere, and investors in the case of CNIME. This operational model grounded in private sector participation in reform is necessary to improve the well being of citizens and to situate the country in the global economy in conditions of equality, since public confidence in their institutions and authorities is one of the indicators that must continue to improve in order to increase competitiveness.

While the Program helped to develop communication tools between the public and private sector, this is not enough. What follows are some of the elements that need to be incorporated by institutions to enhance their public credibility.

Administrative Transparency

Transparency in internal processes is also one of the requirements to ensure the credibility of anti-contraband operations, (as well as of other

government activities? The Program did not become involved in the task of assessing the value of seized goods within the DNA, for example, but it did observe the need to expedite and improve the transparency of those procedures, and make sure the public is aware of them.

More Public Service Mechanisms

Successful customer service initiatives such as those undertaken by the SUAE and the SET Call Center should be replicated. Operator training, innovative telephone services and other related investments require funding. The SET's positive experiences indicate that this sort of initiative should be applied in other government agencies.

Public Complaint Systems

Mechanisms such as SADEP (the Customs System for Public Complaints with Judicial Protection), should be maintained in order to receive and investigate complaints of wrongdoing using a secure, interactive electronic format. This tool will enhance credibility in public administration and elicit valuable information for the respective investigative units. As an additional safeguard for the individual making the complaint, SADEP is monitored by the nongovernmental organization *Transparencia Paraguay*, which operates as an independent watchdog to ensure the transparency of the system. It is essential that *Transparencia Paraguay* continue to serve in this role as an observer and a safeguard.

Consolidation and Updating of Economic Information and Statistics

A basic condition for any investor is that clear and accurate information be available and accessible. It is important to provide accurate information to those interested in investing in the country. The Program recommends, therefore, that the government continues to carry on research on specific topics that could contribute to informed decisions concerning the sector-specific advocacy strategy. Moreover, it is recommended that the country's statistical databases be developed, updated and consolidated, along with other information that may be useful to entrepreneurs, in order to ensure coherence among data from the Central Bank of Paraguay, the Ministry of Finance and the National Customs Office. More work should also be done to update, upload and publish those statistics on the websites of various government institutions. The information made available must be reliable and easy to locate and interpret.

Facilitate Private Sector Participation in Public Sector Initiatives: Civil Society and Fiscal Education

The Threshold Program also recommends continued efforts to integrate other sectors into the institutional modernization process. This can be accomplished with a communications policy that includes an open door policy vis-à-vis society. This might involve the continuation of existing collaborations with nongovernmental organizations to consolidate fiscal education

and raise awareness about the benefits of formalization. When institutions are able to show that resources have truly been used to benefit the public, then people will develop a more positive opinion of formalization efforts.

Promoting the National Image

A country's image is constructed on a daily basis. Every situation, every decision made, influences the perception of the international community, and particularly that of potential investors. The authorities must be vigilant at all times, since a diverse array of studies are constantly measuring indicators and variables that are used to inform investors worldwide. The Threshold Program proposes redoubling efforts and continuing to promote competitiveness, bearing in mind the following aspects:

Vigorous Advocacy to Attract Investment

Paraguay should continue developing maquila programs and providing free assistance with the procedures and steps involved. A minimal investment to aid entrepreneurs could reap enormous benefits for the entire country in terms of new jobs and business opportunities. There is no better advertisement than a satisfied customer and, within a short time, these new investors might just become the country's most effective advocates.

Resources for Advocacy, Research and Follow-Up

Paraguay must have adequate funding in place for the research, advocacy,

negotiations and follow-up required to bring in investors. Tools to facilitate relations with entrepreneurs should be applied continuously, including paying for promotional trips, the development of research materials, and following up on the various administrative procedures. The department responsible for attracting investment should be assigned the resources it needs to perform its duties. It is recommended that investment promoters be able to devote themselves exclusively to that function and assist potential investors through the entire process up to the actual initiation of export operations.

Harmonizing Policies to Make Paraguay More Competitive

What has been accomplished through the creation of the SUAE in terms of streamlining and expediting the process to start a business, while reducing the cost, is evidence that, with sufficient political will and a limited amount of resources, it is possible to surmount obstacles and promote business activity. This model of interinstitutional teams should be tapped to streamline other sorts of procedures. The experience of the SUAE can be replicated in other government agencies.

Streamlining Procedures for Operations under the Maquila System

Threshold Program promoters learned by experience that entrepreneurs wishing to start up a maquiladora in the country were required to visit some 30 institutions and carry out approximately 80 steps which could take as long as 5,000 hours. This



To ensure a professional and dedicated staff, the institutions must offer salaries and benefits commensurate with the level of responsibility required.

protracted and cumbersome process included steps from the registration, approval and establishment of the business, up to the actual initiation of operations. Without assistance, the investor could fall prey to improper requests to "expedite" paperwork. CNIME signed a number of agreements with other institutions to facilitate paperwork for entrepreneurs interested in the maquila system, but more remains to be done to streamline procedures. The institution has plans to further streamline the process by means of draft legislation and additional decrees, and by enhancing the operational system. Streamlining also can be accomplished by incorporating new technologies such as electronic payment vouchers now used mainly by collection agencies such as the SET and the National Customs Office.



Appendix

Threshold Program Indicators

Focus Area II: Formalization of Economic Activities

Component 6: Reducing VAT evasion gap

Indicator	Baseline	Outcomes until October 2008	Anticipated outcomes by Program end	Observations
Number of registered VAT contributors	0	83,887 new contributors (May/08)	40,000	Percentage achieved: 209.7
Reduction in the % of non-submission of sworn declarations	51.79% (base-proposal fiscal year Jan/06-07)	45.03% ²¹	47.21%	Percentage achieved: 147,6%
Reduction in the % of failure to submit documentation	70%	47%	40%	Percentage achieved: 76,7%
Reduction in the % of goods in transit without proper documentation.	85%	72%	65%	Percentage achieved: 65% ²²
VAT evasion gap	66.32%	51.38%	51.32%	Percentage achieved: 99,6%

²¹ Data until of September 2008.

²² These indicators might improve once the Jeroviaha Unit resumes operations.

NOTE: According to official data provided by the Undersecretary for Fiscal Affairs, due to the change from an external taxing index to a Paraguayan taxing index, the evasion gap is 45.27% which will be the new baseline for other reports.

Component 7: Modernization of Customs Services (Border Control)

Indicator	Baseline	Outcomes until November 2008	Anticipated outcomes by Program end	Observations
Value of goods seized and impounded on land or waterways	0	\$6,639,060	\$6,500,000	Percentage achieved: 102% (520 operations were conducted and 423 reports made) ²³

²³ According to DNA reports, a seizure worth approximately \$8 million has yet to be valued.

Component 8: Department of Fiscal Investigation and Fraud Detection (DIT)

Indicator	Baseline	Progress until October 2008	Anticipated outcomes by Program end	Observations
1. Number of investigated cases sent for judicial review	0	143	30	
2. Time spent in the detection of potential fraud cases	0	0	10 days	Difficult to estimate
3. Number of cases investigated	0	234	1	
4. Number of intelligence reports on financial crimes sent to SEPRELAD	0	284	30	
5. Accusations of criminal activity by public officials presented by civil society	0	27	36	Probable involvement of civil servants in criminal behavior

Component 8: Administrative Coordination of Customs Investigation (CAIA)

Indicator	Baseline	Progress until October 2008	Anticipated outcomes by Program end	Observations
1. Number of customs-related internal corruption cases submitted to the UIIH	0	33	15 cases	
2. Number of customs-related criminal cases submitted and sent to the District attorney	0	124	30 cases	
3. Number of intelligence reports on financial crimes sent to SEPRELAD	0	19	15 cases	
4. Reports of criminal activity involving civil servants presented by civil society	0	2	36 cases	

Component 9: Streamlining the Business Registration Process

Indicator	Baseline	Progress until October 2008	Anticipated outcomes by Program end	Observations
Days to register a business	74	15	36	The SUAE ²⁴ has registered 191 businesses since November 2006.
Cost of registering a business	\$750	\$80	\$250	This means a savings of \$670
Steps to register a business	17	6	9	With the establishment of the SUAE, the number of steps has been reduced to 6.

²⁴ Unified System for Establishing Enterprises (SUAE)

Component I0: Establishment of new maquiladoras

Indicator	Baseline	Progress until October 2008	Anticipated outcomes by Program end	Observations
Number of programs approved with a current biministerial resolution	17	23 new programs with a current biministerial resolution	15 additional programs	The goal of 15 programs approved with a biministerial resolution was surpassed by 153%, since from June 2006 to October 2008, 23 new programs were approved as a result of the joint efforts of the Threshold Program and CNIME. ²⁵
Increase of 15% of exports	Exports since the maquila system began in May 2006: \$68,003,518	Export value at 29 months of the Threshold Program (June 2006 to October 2008) \$178,051,650	+ 15%	+ 162% (until October 2008). The 15% of exports goal was surpassed 15 months into the Threshold Program, in August 2007.

²⁵The CNIME actively engaged in promotion and coordination activities to attain 23 new maquila programs approved with a current biministerial resolution since the start of the Threshold Program (June 2006). Six of these programs are the direct result of the Threshold Program; two are new programs by existing enterprises. As a result of the Threshold Programs proactive promotional efforts, ten new companies (seven of which are already registered as maquiladoras) are currently in the process of requesting authorization to operate under the maquila system.

Summary Sheet by Component

A component is understood as each of the Threshold Programs work areas.

COMPONENT 6: Reduction of Value Added Tax Evasion

Background:

At the end of 2004, 1500 taxpayers accounted for 90 percent of tax revenues. The VAT gap was estimated at 66%.²⁶

Objectives:

- Reduction of the margin of VAT evasion.
- Institutional strengthening.
- Simplification, standardization and generalized use of records documenting the sale and transfer of goods.

Main Activities:

- Support the development of a regulatory framework for the Jeroviaha Unit's control operations.
- Support recruitment and training of Jeroviaha Unit staff.
- Technical support and outfitting of the Jeroviaha Unit and other SET departments.
- Specialized consultancies to modernize SET procedures.

Achievements:

- VAT evasion reduced by 15 percentage points.
- 48% increase in declared sales (based on a sample of suspended taxpayers).
- Suspension of 143 business establishments.
- 1426 simulated purchases.
- 607 inspections of cargo vehicles en route.
- 342 inspections of self-printing cash registers.
- 344 training hours for SET personnel.
- 30 specialized consultancies for the SET.
- Design of policy on electronic information security.
- Design of tax schedule.
- Design of electronic tax payment system.
- Design of a system that provides electronic remittance shipment documents.
- Building and equipment upgrades for the Jeroviaha Unit and Call Center.

²⁶ According to official data provided by the Undersecretary for Fiscal Affairs, due to the change from an external taxing index to a Paraguayan taxing index, the evasion gap is 45.27% which will be the new baseline for other reports.

Sustainability of the Jeroviaha Unit and other SET departments

In order to fulfill the main objective of Component 6, Reduction of Value Added Tax Evasion, the Jeroviaha Unit was established under the Office of the Undersecretary for Fiscal Affairs (SET) and received Threshold Program support. Below are some of the aspects that should be kept in mind to ensure the sustainability of the Jeroviaha Unit and enable it to continue to conduct the necessary operations:

- Obtain an adequate budget to cover the UJ's operational expenses so that it can continue to conduct operations such as simulated purchases and control of documentation of goods in transit. Establish categories and schedules for updating Jeroviaha salaries: categories include simulated purchases, future recruitment and training of new members, timely inspections of cash registers and self-printing systems, training teams of auditors, travel expenses for National Police officers for activities countrywide, fuel for vehicles, severance packages for members who leave the Jeroviaha Unit and a reinsertion program for Jeroviaha members who transfer to other departments of the SET.
- Ensure regular updating of computer systems to improve the controls implemented by the Unit. This includes electronic tax payments and certificate of shipment systems.
- Make sure the laws are amended in keeping with UJ operations in companies located in and around the capital city as well as in the provinces.
- Strengthen the Internal Control Department: The main function of this department, which was incorporated into the SET's 2007 organigram, is to support sustainability by monitoring the activities of the institution's various areas or units. This included measurements of indicators during the course of the Threshold Program as well as other management indicators.
- SET Communications Area: this area must be strengthened through the incorporation of human resources and a planning process to improve media relations and its public image.
- Internal communications equipment: upgrade for use and create expense categories for cellular telephone service coverage. The experience of the past two years of the Threshold Program has demonstrated the importance of communications support for UJ activities. Therefore a line item for communications equipment for the Jeroviaha Unit should be included.
- Specific support/coordination with other institutions: activities relating to the implementation of the Electronic Certificate of Shipment System.

COMPONENT 7: Modernization of Customs Services (Border Control)

Background:

In late 2004, the National Customs Office did not have the capacity to control the entry of goods overland or by river. Smugglers operating throughout the country took advantage of this situation by moving all sorts of goods back and forth across the border.

Objectives:

- Improve border control overland and via waterways.
- Control in-country transit of goods.
- Strengthen the system to monitor, control and suppress contraband.
- Establish an operational anti-contraband unit: DETAVE (Special Customs Surveillance Department).
- Institutional strengthening.
- Public oversight of customs activities.

Main Activities:

- Develop a regulatory framework for the intelligence-operation cycle of anti-contraband activities.
- Support training of DETAVE personnel through specialization courses.
- Technical support and outfitting of DETAVE: provision of vehicles, watercraft and transport trucks.
- Provision of work tools.

Achievements:

- \$6.6 million in seizures of illegal goods; 520 anti-contraband operations from May 2007 to November 2008, reflecting improved government capacity to combat illicit activity.
- Installation of a Customs System for Public Complaints with Judicial Protection.

Sustainability of DETAVE:

In order to fulfill the main objective of Component 7—improved border control to decrease contraband, the National Customs Office formed the Special Surveillance Department. The following are some of the aspects that should be taken into account to ensure the sustainability of the unit's work:

- Continue with border control activities of land and water routes.
- Tighten controls on in-country transit of goods.
- Strengthen the system to monitor, control and suppress contraband.
- Facilitate public oversight of customs activities.
- Regular updating of the regulatory framework for the intelligence-operations cycle of anti-contraband activities.
- Refresher training for DETAVE members through specialization courses and the addition of new members.
- Gradual increase in resources for the DETAVE unit.
- Follow-up and investigation of complaints received through the Customs System for Public Complaints with Judicial Protection (SADEP).

- Remuneration: develop an adequate incentives plan to encourage optimum performance and enhance employment longevity.
- Promote the integrity and proper management of the unit through:
 - Training: develop an effective, participatory methodology
 - Recruitment: comprehensive personnel recruitment and selection programs
- Strong political will: to foster real, sustainable change.
- Resources: strategic planning for proper resource administration.
- Ensure the integrity and ethical conduct of the investigators through ongoing training and polygraph tests.
- Strengthen ties/networks: promote shared responsibility, build responsible, respectful collaboration among the following stakeholders:
 - Customs
 - Navy
 - Police
 - Office of the General Prosecutor, Economic Crimes Unit
 - Transit Police

COMPONENT 8: Investigative Units

Background:

In late 2004, the Ministry of Finance, the Office of the Undersecretary for Fiscal Affairs and the National Customs Office did not have effective units in place responsible for investigating cases of tax and customs fraud, tax invasion and corruption among public officials.

Objectives:

- Strengthen investigatory capability.
- Detect and investigate tax and customs offenses.
- Detect and investigate internal corruption offenses to enhance the integrity of the Ministry of Finance, the SET and the DNA.

Main activities:

- Train unit members.
- Provide office equipment, investigative tools, computerized information systems, and vehicles.
- Advisory services and evaluation of investigatory activities.

Achievements:

- SET tax revenues increased by \$12.7 million.
- Proceeds on the DNA administrative summary sheet: \$14.7 million.
- 124 cases of criminal Customs offenses presented and sent to the Public Ministry.
- 33 internal corruption cases in the Customs Office brought before the Internal Investigations Unit.
- 19 intelligence reports on financial crimes sent by Customs to SEPRELAD.
- 25 internal corruption cases in the SET brought before the Internal Investigations Unit of the Ministry of Finance.
- 2 reports from civil society on possible criminal activity by civil servants.
- 227 cases investigated by the DIT.
- 143 investigated cases sent by the DIT to the courts for review.
- 264 intelligence reports on financial crimes sent by the DIT to SEPRELAD.

Sustainability of investigative units:

The Threshold Program provided support for the investigative units to strengthen their capacity to investigate and control corruption and fraud in government institutions responsible for tax collection. The following are essential to ensure their sustainability:

- Support of the national authorities in case investigations.
- Operational funds for the units, particularly in the areas of travel expenses, fuel, communications equipment, and equipment maintenance.

- Clear internal organization: make sure coordination is taking place between intelligence and operational units. This coordination should occur at all levels of the institution to improve the efficiency and productivity of anti-contraband operations and fraud detection investigations.
- Adequate remuneration, in addition to incentives distributed in a transparent manner.
- Ensure the autonomy and physical safety of the investigators.
- Ensure the integrity and ethical conduct of the investigators through ongoing training and polygraph tests.
- Provide ongoing refresher training for human resources.

COMPONENT 9: Streamlining the process to start a business

Background:

In the World Bank's 2006 Doing Business report, Paraguay's ranked 138 for ease of starting a business. The procedures were drawn-out, time-consuming and expensive, and this had a negative impact on one of the main indicators to measure the business climate.

Objectives:

- Reduce the number of steps, the cost and the time involved in starting a business.
- Install a "one-stop service" for starting a business.

Main activities:

- Study of the process for registering a business.
- Design and implementation of a Unified System for Establishing Enterprises (SUAE).
- Evaluation of the internal processes of each institution and the SUAE.
- Communication of the changes and benefits associated with the establishment of the SUAE.
- Workshops to promote the SUAE among associations in the sectors involved in establishing enterprises. More than 700 people received direct information on the benefits of the SUAE.
- Customer service training for public officials and delegates from the various institutions.

Achievements:

- Installation of a "one-stop service" system for starting a business.
- Process to start a business reduced from 17 to 7 steps.
- Time period to start a business reduced from 74 to 15 days.
- Cost of starting a business reduced from \$136.80 to \$77.60.
- International status of Paraguay rose 72 positions in the World Bank's Doing Business ranking system following the installation of the SUAE.
- Internal regulations (administrative provisions, resolutions, agreements, decrees) of the institutions that make up the SUAE were amended to improve processes associated with starting a business.
- Institution officials became more aware of the importance of expediting and streamlining the process to start a business.

Sustainability of the SUAE:

The main objectives of the "one-stop service" are: to make the process more user friendly, streamline requirements and establish electronic systems for the procedures. This requires a series of actions on the part of those responsible for the "one-stop service" that must be carried out in a dynamic and continuous fashion in order to gradually improve the system. The following are some of the aspects that should be kept in mind for the sustainability and continuous fine-tuning of the Unified System for Establishing Enterprises (SUAE):

- Funds for the SUAE included in the annual budget of the Ministry of Industry and Commerce.
- Immediate response capability to proceed with the necessary improvements to equipment, systems, staff, Internet and physical space.
- Regular monitoring of compliance with established time periods internal and external to the SUAE.
- Dynamic communication between the SUAE administration and its participating institutions for speedy problem-solving at different stages of the process to start a business.
- Maintain a massive communications campaign to inform potential consumers of the benefits of the SUAE.
- Establish an administrative oversight system of SUAE management.
- Conduct “simulated test” to evaluate the quality of customer service. The caliber of customer service offered by the delegates is as important as a positive image of the locale’s physical attributes. The delegates must be familiar with the processes in order to clearly inform consumers about the requirements and procedures to start a business.
- Bear in mind the job descriptions found in the SUAE operations manual when selecting civil servants. Delegates, directors and contact people within the institution must be willing and able to solve problems on the spot. While the ultimate objective of a unified system is to transfer processes to a computerized, automated format, the SUAE’s performance is contingent on the good will of the institutions in general, and staff members in particular.
- Ensure that the executive management of SUAE is familiar with all of the relevant procedures and laws in order to detect potential obstacles or bottlenecks that may arise at different stages, and propose solutions. The latter should be shared with all of the institutions and civil servants involved and implemented in a proactive way by the executive management of the SUAE.
- There should be adequate computer support, with a technician responsible for trouble-shooting problems as they arise. In the final stage of the Threshold Program, the systems of several of the SUAE’s participating institutions were digitalized for the eventual integration of their information systems.

COMPONENT 10: Installation of 15 new maquiladoras in Paraguay

Background:

Paraguay's potential in the maquila industry was being wasted. In 2006, the resources available to the CNIME resources were insufficient to effectively promote the maquila system and attract investment to this sector:

Objectives:

- Installation of 15 new maquiladoras in Paraguay.
- 15% increase in exports between June 2006 and October 2008.
- Preparation of documents to facilitate the establishment in the country of investments directed towards the maquila system.

Main activities:

- Develop an efficient strategy to attract investment under the maquila system.
- Market research by country and sector.
- Domestic and international advocacy in support of the maquila system.
- 21 promotional visits abroad and 4 trips to develop 5 maquila programs.
- Scheduling and accompaniment of 40 visits by foreign entrepreneurs.
- Assistance for these maquiladora operators in establishing themselves in the country, incorporating their business, opening a bank account, registering as maquiladoras, developing their maquila programs and installing the factory for production and export.
- Training of CNIME staff.
- Strengthening of the CNIME infrastructure, investigative tools and development of a database for potential maquiladora operators.

Achievements:

- 23 new maquila programs approved with a current biministerial agreement (countrywide).
- 16 companies decided to operate a maquila in Paraguay with the direct support of the Threshold Program; 13 of these are already registered as maquiladoras and the programs of 6 of them have been approved through a biministerial resolution. Seven of these companies set up operations in Ciudad del Este.
- Exports rose 162% (June 2006 - October 2008).
- Approximately \$8 million worth of short term investments by the 16 maquiladoras attracted through the Threshold Program.
- Creation, in the short term, of approximately 1200 jobs.
- Ten market research studies and over 20 studies in response to specific consultations.
- Mapping of the procedures to install and operate a maquiladora in Paraguay.
- "Supply Portfolio for Paraguay" targeting investors.
- Strengthening of the CNIME's advocacy department.

Sustainability of the CNIME:

The National Council of Maquila Export Enterprises established under the Ministry of Industry and Commerce is the promotional engine of the maquila system. The maquila is a mode of capturing foreign investment to produce goods and service in Paraguay for export. Any agency established to promote investment, if it is to be effective, must be managed as a private commercial enterprise. The following actions are necessary to ensure the sustainability of the CNIME:

- Design, adhere to, and constantly update a plan that includes a mission, vision, and strategy.
- Establish specific, attainable goals with reasonable time frames.
- Develop a procedures manual for operations.
- Maintain a high quality professional staff with specific areas of expertise and skills. Hiring should be done using a merit-based system and not through patronage or political connections.
- To ensure success, the training of civil servants must be: a) frequent, dynamic and up-to-date, b) focused on relevant technical subject matter (opening a business, the maquila system, advantages in the country, competitiveness, rules of doing business, investigative tools), c) focused on marketing, communications and negotiation.
- Prepare market research: sectors with potential in the maquila industry and countries with capital and investors interested in diversifying and expanding.
- Implement adequate marketing and communications strategies and tools: a) macro audience: country advantages, competitiveness, the system's functioning and advantages; b) specialized audience (by request): specific information on sectors and tariffs, requirements for registration under the maquila system and information on the local supply of appropriate sites, available staff, providers, subcontracts, associates, raw materials, infrastructure services, transportation and logistics, and financial services; c) adequate information for local governments on the impact and importance of direct foreign investment as an engine for local development and the benefits of participating actively in promoting the system.
- Advocacy plan at the domestic and international levels.
- Schedule of visits for investors and companies interested in the maquila industry.
- Assistance for investors throughout the process, from starting the business, through each procedure or step, until it begins operations.
- Systematic evaluation of the performance of technical staff, officials and the CNIME itself. Use the findings for decision-making processes and to make changes as necessary to reach the established goals.
- Periodic reporting of outcomes a) accountability: balance, annual report; b) system operations (number of companies, investment figures, job creation, export totals, tax revenues generated); c) specific, updated information on the target audience.
- Cultivate a positive image of the CNIME. This image is projected in its actions and the quality of the services it provides, and is just as important as the image of the country as a whole.

List of Beneficiary Institutions by Component

COMPONENT 6 - Jeroviahá Unit

1. Office of the Undersecretary of State for Fiscal Affairs

COMPONENT 7 - DETAVE

1. National Customs Office
2. Paraguayan Armed Forces - Navy
3. National Police

COMPONENT 8 - Investigative Units

1. Office of the Undersecretary of State for Fiscal Affairs
2. National Customs Office

COMPONENT 9 - Unified System for Establishing Enterprises (SUAE)

1. Ministry of Industry and Commerce (MIC) - SUAE Director
2. Ministry of Finance, Treasury General Counsel and Office of the Undersecretary of State for Fiscal Affairs
3. Judicial Branch, Supreme Court of Justice and General Office of Public Records
4. Social Insurance Institute, Worker – Employer Contribution Office
5. Ministry of Justice and Labor, Employer Registration Department
6. Municipality of Asunción, Urban Administration Department
7. Ministry of the Interior, Office of Migration

COMPONENT 10 - Installation of 15 new maquiladoras in Paraguay

1. National Council of the Maquiladora Export Industry (CNIME)
2. Ministry of Industry and Commerce

**Our photos were
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Unidad Jeroviaha

The Paraguay Threshold Country Program is a reform initiative of the Government of Paraguay with the involvement of 34 government agencies and technical assistance provided by the United States Agency for International Development. The Program was financed with a donation of \$34.5 million from the Millennium Challenge Corporation (MCC).