

PD-AAA-72-G1

AID 1020-25 (10-70)

5190032-5
A.I.D.

Reference Center REPORT U-446
Room 1656 NS

PROJECT APPRAISAL REPORT (PAR)

PAGE 1

1. PROJECT NO 519-11-740-032.1	2. PAR FOR PERIOD: 2/11/69 TO 12/31/70	3. COUNTRY EL SALVADOR	4. PAR SERIAL NO. 71-2
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TAX ADMINISTRATION IMPROVEMENT

8. PROJECT DURATION: (Begin FY 65, End FY 72)	7. DATE LATEST PROP 6/25/70	8. DATE LATEST PIP 12/1/68	9. DATE PRIOR PAR 2/10/69
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10. U.S. FUNDING	a. Cumulative Obligation Thru Prior FY: \$ 504,000	b. Current FY Estimated Budget: \$ 89,000	c. Estimated Budget to completion After Current FY: \$ 65,000
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11. KEY ACTION AGENTS (Contractor, Participating Agency or Voluntary Agency)

a. NAME	b. CONTRACT, PASA OR VOL. AG. NO.
Internal Revenue Service	LA (TA) 05-65 Amend- ment No. 8

I. NEW ACTIONS PROPOSED AND REQUESTED AS A RESULT OF THIS EVALUATION

A. ACTION (X)			B. LIST OF ACTIONS	C. PROPOSED ACTION COMPLETION DATE
USAID	AID/W	HOST		
			<p>1. The Tax Advisor should rewrite the PIP with special attention paid to the output indicators of Part II of that document. They should be chosen in such a way that their successful accomplishment would contribute directly to the project purpose as defined in Section IV. A herein. Modified and updated as required these targets would largely be drawn from actions shown in Part I of the existing PIP with greater stress on qualitative factors. For assistance in differentiating between the work schedule (Part I) and selected output indicators (Part II), the Tax Advisor should consult AID Manual Circular 1026.1 including Supplement I.</p> <p>As presently constituted, the targets of Part II of the PIP more closely relate to the programming goal of Section V herein, than to the project purpose.</p> <p>It is recognized that at this late date in the life of the project and the already heavy time-demands on the single Tax Advisor, rewriting of the PIP might be deferred. The failure to do so, however, would leave inappropriate benchmarks against which the success or failure of the project would ultimately be measured; moreover, the preparation</p>	

D. REPLANNING REQUIRES

REVISED OR NEW: PROP PIP PRO AG PIP/T PIP/C PIP/P

E. DATE OF MISSION REVIEW

PROJECT MANAGER: TYPED NAME, SIGNED INITIALS AND DATE: Ronald A. Witherell 26 JAN 1971

MISSION DIRECTOR: TYPED NAME, SIGNED INITIALS AND DATE: Albert J. Linstad

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PAR CONTINUATION SHEET

This sheet is to be used for any Narrative Sections for which sufficient space has not been provided on the form. Identify each narrative by its Part and Section Designation.

I. New Actions Proposed and Requested as a Result of this Evaluation

B. List of Actions (Continued)

of the 1971 annual work plan required under the IRS Impact System will facilitate this task.

2. The annual work plan for 1971 mentioned immediately above should be limited to fewer projects, more realistically matching resources with expectations. The scopes of work outlined in the Annual Work Plans for 1969 and 1970 have been too detailed and ambitious for what was a two and is now a one man tax team. As a consequence, the several projects delayed or postponed simply for want of time misleadingly detracts from what has been a successful project. This recommendation has been discussed with and has the support of the Tax Advisor.

3. Given the enthusiasm expressed by the newly-appointed Minister and Subsecretary of Finance for institutionalizing tax administration improvement plans and the potential benefits accruing therefrom, the Tax Advisor should devote as much time as possible in assisting the Ministry of Finance in completing a written reform plan by the earliest possible date. June 30, 1971 has been suggested as a deadline, which would leave the present GOES administration one year for implementation.

The Ministry's plan is expected to incorporate virtually all of the major actions contemplated by the Tax Advisor. Therefore, priority should be given to its completion and backstopping even though it may entail postponement of other planned activities. Project postponements and changes evolving from this should be approved by and properly documented with the USAID.

4. In conjunction with a country-wide fiscal cadaster provided for in a law passed March 12, 1970, a loan paper is now being drafted for consideration by AID/W, which would accelerate cadaster activities. While 45-60 days of TDY assistance have already been planned between now and June 30, 1971, additional technical assistance, will probably be needed by the GOES for the planning and most certainly for the implementation phase of the work. Careful attention must be given by the Tax Advisor in establishing the proper priority for time spent on Cadaster vis-a-vis other projects. The Mission should be kept informed of priority conflicts so prompt action may be taken to either provide more assistance or adjust the work schedule. Moreover, the IRS need not necessarily be the T.A. source during implementation.

5. The Tax Advisor should be cautioned against involving himself in the internal personnel matters of the Ministry. Through the

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I. New Actions Proposed and Requested as a Result of this Evaluation

B. List of Actions (continued)

absence of any negative comment to the contrary, the previous PAR implicitly condoned such a practice when it noted that "with some encouragement from A.I.D.", a new Director General was appointed in May, 1968.

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II. PERFORMANCE OF KEY INPUTS AND ACTION AGENTS

A. INPUT OR ACTION AGENT CONTRACTOR, PARTICIPATING AGENCY OR VOLUNTARY AGENCY	B. PERFORMANCE AGAINST PLAN							C. IMPORTANCE FOR ACHIEVING PROJECT PURPOSE (X)					
	UNSATISFACTORY		SATISFACTORY			OUT-STANDING		LOW	MEDIUM			HIGH	
	1	2	3	4	5	6	7	1	2	3	4	5	
1. Internal Revenue Service (IRS)					X							X	
2.													
3.													

Comment on key factors determining rating

B.5 - Many basic reforms have been accomplished as scheduled in Impact Annual Work Plans submitted by the Tax Advisor for calendar years 1969 and 1970. On a day-to-day basis, the use of modern management tools has become a way of life in the Director General's Office and the Audit Division of the Direct Tax Office. These include current production statistics, regular staff meetings, appraisal of results, etc. Inter-related manuals for supervisors including instructions for both the classification and examination of returns are either in effect or planned which will supplement written guidelines already adopted.

(Continued on page 2 (i))

4. PARTICIPANT TRAINING	1	2	3	4	5	6	7	1	2	3	4	5
					X						X	

Comment on key factors determining rating

B.5 - Training courses scheduled in the PIP contained the following caveat, "INTAX courses not definitely scheduled. Participation will depend upon courses offered and the content of the courses."

(Continued on page 2 (iii))

5. COMMODITIES	1	2	3	4	5	6	7	1	2	3	4	5

Comment on key factors determining rating

6. COOPERATING COUNTRY	a. PERSONNEL	1	2	3	4	5	6	7	1	2	3	4	5
	b. OTHER				X						X		

Comment on key factors determining rating

a. (B.4) - At the office and division level, the performance of key individuals has varied. The Director General of the Direct Office, appointed in April, 1969, has remained enthusiastic toward administrative project. Developed under his direction have been the Project Control and Statistical Reporting Systems mentioned above (see C.6 under "Contractor, Participating Agency, or Voluntary Agency"). He has, moreover, been a supporter of expanded participant training.

Notwithstanding these positive factors, the Director General has a tendency to become overly involved in technical vis a vis admin-

(Continued on page 2 (v))

7. OTHER DONORS	1	2	3	4	5	6	7	1	2	3	4	5

(See Next Page for Comments on Other Donors)

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Participating Agency (Continued from Part II A.1, page 2)B.5

Overall, the Tax Advisor's assessment that the management building phase has gained momentum appears warranted.

An Informal Appeals System, encouraged by the Tax Advisors, is functioning on an experimental basis in the Direct Tax Office. Project Controls and Statistical Reporting Systems have also been introduced. Two major disappointments have been the failure to increase the number of auditors and to move more rapidly in fully reestablishing the delinquent returns program which was abandoned in December, 1968. On either account, however, the tax advisor's responsibility is secondary at best. (See Section 6 - "Cooperating Country"). It is worth noting, however, that, limited actions for identifying new taxpayers commenced late in 1969 and that the expansion of these activities holds a very high priority with the new Minister and Subsecretary.

In the training area, participant training has expanded significantly (see Section 4, "Participant Training"); and awareness of the need for internal training and actions for its fulfillment appear to have taken a positive turn. This is evidenced by the introduction in late 1969 of a home study course in accounting for auditors; the execution in CY 1970 of a supervisory training course; and an audit technician orientation course.

For the supervisory course, 12 RTAC training films supplemented 21 hours of classroom instruction for the 25 supervisors who attended. Given to the newer and less experienced personnel, the orientation course consisted of nine 2-hour meetings.

All three of these courses involved the direct or indirect participation of the Tax Advisor. One, the home study course in accounting, has been beset by problems which are described in the section immediately below.

At the Minister's request, the Tax Advisor has recently requested TDY assistance to identify in-house training needs of auditors and to assist in designing and implementing a course to fill these needs. Finally, and most important in an institution-building sense, he has asked the Tax Advisor for assistance in preparing internal training plans for 1971.

(C.4). As defined in the revised PROOP of June 25, 1970, "the principal objective of the project is to assist in increasing tax revenue through:

1. Modernization of tax administration procedures and techniques,
and

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Participating Agency (Continued from Part II A.1, page 2 (1))

(C.4)

2. Improvement of the capabilities of tax administrators and technicians."

While not specifically stated in the PROP, these elements constitute two essential ingredients of this project's purpose; namely, to help build within the Ministry of Finance an efficient and effective system of tax administration.

Material included under B.6 above noted several examples of very real progress toward achievement of these objectives; and it seems fair to say that, in the absence of the tax team, many improvements during the past two years would probably not have been made.

Also within the Direct Tax Office, the daily contacts between the Salvadoran administrators and technicians with the tax advisor(s) have undoubtedly been an assist in upgrading the skills and effectiveness of the former as managers and workers, respectively. As the services of the advisor(s) have been increasingly sought during this period, it can be assumed this learning process has accelerated.

In a more direct fashion also, the Tax Advisor has contributed to the second of the two elements of project purpose listed above. His efforts have been instrumental in expanding participant training (see Section 4 - "Participant Training") and internal training within the Ministry itself (see "B.6" above).

Of the Ministry-sponsored training sessions mentioned above, one, the home study course in accounting, did not progress satisfactorily. Owing to complaints among the 40 enrolled auditors that the course did not fully meet their needs, it was suspended several months ago when about 65% completed. The Tax Advisor has expressed doubts over the merits of their arguments and would prefer the course be continued. However, while an IRS employee will arrive in February to assist in designing a training program for the Audit Section, it has not been decided what role, if any, the accounting course will play.

Summary: The institution building process in the Direct Tax Office, owing in large part to the efforts of the tax advisors, has advanced considerably since the last PAR of February, 1969. Somewhat offsetting this progress has been the scant attention afforded the Indirect Tax Office although the Tax Advisor recently initiated discussions with the Director of that office concerning their plans to develop a stronger audit capacity. Without the latter, effective enforcement of the September, 1970 Stamp Tax Law will not be possible.

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4. Participant Training (Continued from Part II. A.4, page 2)

B.5

From an evaluative standpoint, then, little can be gleaned by posturing that, of the five courses and conferences listed, three were attended, one wasn't, and one was cancelled. A qualitative, but more useful approach compares the general importance now of participant training within the Ministry of Finance vis-a-vis its position there 1½ years ago.

Against this measure, participant training receives very high marks. In FY 1970, one participant attended each of three INTAX courses; 1) Middle Mgt. Dev.; 2) Supervisory Dev.; 3) Administrative Services. In September 1969, when the senior Tax Advisor first reported to Washington the intention of the Ministry to be represented at these courses (and one other not subsequently attended), he noted, "The Ministry has not nominated a participant for one of these courses for the past two years".

This breakthrough has picked up added steam in FY 1971. In December three INTAX participants returned from the Supervisory Development Seminar. During the first half of CY 1971, one INTAX participant each is scheduled to attend the Middle Management, Training Administration and Public Relations seminars. Three participants have also been selected for the forthcoming INTAX course in Investigative Techniques.

This outlook has not confined itself exclusively to INTAX courses. The Ministry sponsored one attendee to a CIAT organized ADP seminar held in Bogota last December. Another Ministry participant recently completed a five month CIET course in Argentina on general tax administration.

On the negative side, the GOES was not represented at the annual CIAT Conferences held in Mexico City and Montevideo during May of 1969 and 1970.

(C.4). A review of the summaries prepared by the Senior Tax Advisor from the follow-up contacts with the three INTAX participants indicates their training is contributing significantly to the two key elements of the project purpose mentioned above in Section C.4 on "Participating Agency".

Chief of Audit - (Middle Management Development) - "In summary, it appears that material covered in the INTAX training course is closely related to work that he does and there are indications that his participation should make him a better executive."

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4. Participant Training (Continued from Part II. A. 4, page 2 (iii))

(C.4)

Group Supervisor in Audit Division (Supervisory Development) - "In summary, Mr. Mendoza seems to have gotten a good grasp of the principles to which he was exposed in the INTAX course and is enthusiastic toward introducing them in his present position."

Chief, Coordinator for the Director General's Administrative Reforms Council - "At this point, there seems to be little doubt that he is applying his knowledges and new skills effectively."

In a later report, the tax advisor summarized the positive benefits accruing to the Direct Tax Office from their training. "In the INTAX areas (L-III-5), all three participants who returned during this period seem to be using their training to good advantage. One of them, the Chief of Audit, has an active role in six of our major projects; a second, the Tribunal's Coordinator, in three; and the third, the Office Audit Branch Chief in one."

A recent promotion within the Ministry supports an apparent intent on their part to utilize the newly acquired skills of returned participants. Previously an attorney in the appeals section, the Ministry's representative at the May-September CIET course (see C.6 under this section) in Buenos Aires has recently been appointed to a key tribunal position, a job commanding nearly twice the salary he had been receiving.

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6. Cooperating Country (Continued from Part II A.6, page 2)

a. (B.4)

istrative matters. This has occasionally left a void in decision making at the Director's level with final action being decided either at the operating or Ministerial levels. More recently, the new Subsecretary of the Ministry has become more involved in the development of reform plans mentioned herein. An excellent administrator himself, it is expected that he will more clearly delineate the Director's role in the near future.

For their part, the Chief of the Audit Division, a June, 1969 appointee and his principal subordinate, Chief, Office Audit Section, have spearheaded the many operational and procedural improvements within the Audit Division. Both received INTAX training in February-March, 1970.

Strong support at the Ministerial level, at least until recently, was not present. The basically passive reaction by the recently departed Minister and Subsecretary to a reduction in the tax team, was generally construed to reflect a lack of interest at that level in administrative reforms. This was further evidenced by their failure to increase enforcement activities through additional auditors or delinquency follow-up personnel.

This situation has reversed itself under the new Minister and Subsecretary, both of whom took office on September, 1970. They are moving to broaden the tax reform program; and under the close observation and direction of the Subsecretary, a longer range and more comprehensive reform plan than the existing one is being developed. Implementation of priority projects has already begun.

a. (C.3). The positive effects on the project purpose of most actions made during the reporting period were partially offset by three factors: 1) The delay in providing more personnel for assessment and collection of delinquent taxes; 2) the failure to provide for an effective increase in the number of auditors in the first six months of 1970; and 3) the hesitancy, so far, of the Director General to take a firmer position in the decision making process.

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II. 7. Continued: Comment on key factors determining rating of Other Donors

III. KEY OUTPUT INDICATORS AND TARGETS							
A. QUANTITATIVE INDICATORS FOR MAJOR OUTPUTS		TARGETS (Percentage/Rate/Amount)					
		CUMU- LATIVE PRIOR FY	CURRENT FY		FY ____	FY ____	END OF PROJECT
			TO DATE	TO END			
The Impact Progress Re- port for the period ended 12/30/70, reflects key outputs. A copy has been forwarded to the Desk Officer for refer- ence purposes.	PLANNED						
	ACTUAL PERFORM- ANCE						
	REPLANNED						
	PLANNED						
	ACTUAL PERFORM- ANCE						
	REPLANNED						
	PLANNED						
	ACTUAL PERFORM- ANCE						
	REPLANNED						
B. QUALITATIVE INDICATORS FOR MAJOR OUTPUTS	COMMENT:						
	1.						
	2.						
3.							

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IV. PROJECT PURPOSE

A. 1. Statement of purpose as currently envisaged.

2. Same as in PROP? YES NO

To help build an efficient and effective system of Tax Administration within the Ministry of Finance.

B. 1. Conditions which will exist when above purpose is achieved.	2. Evidence to date of progress toward these conditions.
Taxpayer compliance judged to be between 80 and 90% of taxes owed.	Ministry has expressed desire to establish tests to measure compliance.
Formal written audit procedures and investigative techniques, including identification and treatment of fraud.	Office audit procedures are in effect and field audit guidelines are partially completed.
Permanent system for identifying training needs and a cadre of at least three instructors to fulfill them.	Participant scheduled to attend INTAX Training Administration Seminar in mid-1971 will be charged with overall training responsibility in the Direct Tax Office. Three mid-1971 participants in INTAX Investigative Techniques Seminar will develop Audit Investigations Course.
Formal written guidelines for Supervisors.	Partially prepared. Recently returned INTAX participants are scheduled to complete them.

(Continued on page 4 (i))

V. PROGRAMMING GOAL

A. Statement of Programming Goal

Increases in tax revenues of the GOES.

B. Will the achievement of the project purpose make a significant contribution to the programming goal, given the magnitude of the national problem? Cite evidence.

The February 1969 PAR noted that the sector goal of increasing direct tax revenues by 15% a year between 1964 and 1969 would not be achieved. It pointed out that between 1964 and 1966, revenues actually fell by 4.6%; and that the situation reversed itself in 1967 and 1968 with gains of 14.3 and 32.1%. However, these increases were due largely

(Continued on page 4 (ii))

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IV. Project Purpose - B.1. (Continued from page 4)

B.1. Conditions which will exist when above purpose is achieved.

2. Evidence to date of progress toward these conditions.

Informal conferences resolving at least 60% of audited cases prior to assessment of additional taxes.

Pilot informal conference being conducted.

A permanent group of at least five personnel to follow-up on delinquent taxpayers (non-filers) with at least 4,000 contacts annually and an estimated 1,600 new taxpayers until compliance reaches a satisfactory level (see item 1 above).

Cross-checks being conducted in Direct Tax Office. Plans for delinquency follow-ups, using master file, are being made.

A formal collection force of at least four personnel to follow up on all unpaid assessed taxes within one year of non-payment.

Listings of all overdue taxes being made for notification by mail and personal contact, if necessary.

Cadastral plan implemented, including formation of a group large enough to maintain evaluation files and to assure the accurate assessment and collection of net worth taxes.

Work plan being developed.

Full time services of at least one person to work solely on public information, taxpayer assistance and education activities.

Participant planned for INTAX Seminar in Public Relations is expected to establish this office.

A permanent group of at least three personnel to make management studies and implement desirable organization and methods improvements.

Interest expressed by Ministry in this function. No formal action to date.

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V.B. (Continued from V, Programming Goal, page 4)

to changes in methods of accounting (1967) and an increase in the net worth tax rate (1968). In 1969, a one-time emergency tax accounted for another sizable increase.

Because of these several exceptions, the amounts for total direct tax collections in the table below do not portray a true picture of the collection performance of the Tax Offices. Accordingly, adjusted totals and percentages are shown.

For 1970 also, a cautionary note should be made. The July, 1969 conflict between El Salvador and Honduras occasioned a severe profit squeeze for many Salvadoran commercial and industrial enterprises. As a consequence, 1970 income tax assessments grew very little, as reflected in the low (3.3%) increase in total direct taxes on an adjusted basis.

Owing to this abnormal situation, any relationship between improved administration and the level of total direct collections for 1970 must be considered tenuous.

<u>Year</u>	<u>Total Direct Taxes (\$)</u>	<u>% Increase (Decrease)</u>	<u>Adjust- ment (\$)</u>	<u>Adjusted Total (\$)</u>	<u>Adjusted % Increase (Decrease)</u>
1964	18.4	-	-	-	-
1965	17.8	(3.3)	-	-	-
1966	17.6	(1.3)	-	-	-
1967	20.1	14.3	(1.8) ^{1/}	18.3	4.1
1968	26.5	32.1	(2.6) ^{2/}		
			(4.0) ^{3/}	19.9	9.0
1969	28.9	9.1	(4.0) ^{3/}		
			(3.7) ^{4/}	21.2	6.3
1970	25.9	(10.4)	(4.0) ^{3/}	21.9	3.3

1/ Withholding Tax transfer of \$4.5 million (\$1 - \$2.50)

2/ Withholding Tax transfer of \$6.5 million.

3/ Estimated additional net worth taxes of \$10 million due to change in rate.

4/ One time emergency tax of \$9.3 million.

Projections which were revised in Part II of the PIP (dated 12/1/68), were met for 1969 and 1970 as disclosed by the following:

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PERFORMANCE SHEET

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V.B. (Continued from V. Planning and Control, page 3 (ii))

	1968	1969	1970
Projected Revenues	21.8	24.9	29.7
Actual Revenues	20.0	25.2	28.8

1/ Adjusted for 13.7% emergency tax.

As regards auditing, one of the major areas of expenditure out the project's life, some comparative data are available:

	1968	1969	1970
Returns Audited	1,200	1,500	2,500
Additional Taxes Recommended	100	150	300
Estimated Collections from Audit Actions	50	75	150

The sharp drop in returns received in 1968 and 1969, and recommendations in both 1968 and 1969, were nullified because of a change in the law which actively placed some of these recommendations beyond the scope of limitations. Estimated collections from audit actions fell sharply in 1970, however, indicating that a detailed and high quality audit may be developing. Also, in 1970, it is noted the fact that the emergency tax (13.7%) was expected to double the expected amount of 11 million and the Audit Division was the group most responsible for its administration.

In light of the unusual events of the last two years, the 0.5% and 3.3% increases recorded over the last two years may be considered as satisfactory. If a faster growth rate can be realized, continued strong improvement in collections resulting from audits and new vigorous efforts to identify non-payers and collect delinquent accounts are essential. Strong action in the identification and collections areas will test the resolve of the Ministry of Finance and the GOES as a whole.

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