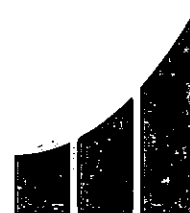


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**THE POLICY MAKING PROCESS OF TAX
REFORM IN LATIN AMERICA**

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1. INTRODUCTION

The main objective of this paper is to analyze the policy making process of tax reform in a selection of Latin American countries. This has been an important area of reform since the mid 1980s, mainly because countries have tried to offset the revenue losses from trade liberalization in a context of reduced tolerance toward monetary funding of fiscal deficits. In line with international trends, governments have also tried to improve the productivity -the ratio between the effective and the potential tax collection- and the neutrality – lower rates charged uniformly for all economic activities or agents - of the tax systems.

The average Latin American country enacted 2.5 significant tax reforms between 1990 and 2002. The VAT was the top item in the reform agenda, although congresses were also quite active in reforming the corporate income tax, and to a slightly lesser degree, individual income taxes. The intensity and frequency of reform –two unrelated dimensions- show a high degree of path dependence (countries most predisposed to reforms in the 1990s were also the greatest reformers in the late 1970s and 1980s), suggesting that the propensity for reform is related to longer-term institutional factors. However, the most significant reforms took place during the first half of the 1990s. Since then, many reforms have failed in the attempts to broaden the tax bases and eliminate the special exemptions and treatment that certain sectors enjoy. For example, after significant increases in VAT rates during the early 1990s, recent changes have been marginal, as legislative branches typically have resisted executive attempts to improve the efficiency of the tax, by broadening its base or raising the rates. Similarly, the reduction in (maximum) corporate and personal income tax rates has decelerated (and even reversed in several countries) since the mid 1990s.

Higher collections from direct taxes and VAT managed to turn around the decline in revenues from tariffs and taxes on foreign trade. Although the reform efforts achieved some success in raising higher revenues (especially until 1997), the main consequence has been a change in the composition by increasing the reliance on VAT while reducing other forms of taxation. The reforms were also relatively successful in achieving their goal of improving the efficiency of the tax systems. Although the greatest

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progress was made in terms of the productivity of the VAT, average productivity of corporate taxes and individual income tax also exhibit a positive trend. The neutrality of the tax systems tended to improve considerably between the mid-1980s and the early 1990s, with few significant changes thereafter. However, there is a very significant amount of variation across countries and time in terms of the outcomes of tax reform. Countries differ widely in terms of the frequency of reform, the intensity of the reform, as well as the results in terms of tax revenues, productivity and neutrality. For example, Argentina had a very significant amount of tax legislative activity between 1990 and 2002 –enacting important reforms in seven years during that period–. However, tax revenues did not change, and there was a reduction in neutrality. In contrast, Brazil did not have an important reform in the same period, but its tax revenues rose importantly (with a small improvement in neutrality).

Exploiting that variation across countries, this paper tries to underscore the fundamental determinants of tax reform and its outcomes. For that purpose, we use the policymaking process methodology, developed in Spiller, Stein and Tommasi (2003), Scartascini and Olivera (2003), and Spiller and Tommasi (2003). The basic idea of this approach is that political institutions affect policy outcomes through their impact on the process by which policies are designed, approved and implemented. Rather than mapping political institutions into policy outcomes directly, the methodology focuses on the relationship between political institutions and certain common features or qualities of policies, termed as *outer features*, which are systematically present in those policies:

In the specific case of tax reform and policy, the outer features refer to issues such as whether policies are *stable* and *predictable*. Stable policies are those that remain in place beyond the tenure of political officeholders. In the case of a tax reform, the tax code would become simpler, free of temporary clauses, temporary taxes or amnesties. Frequent changes and legislation reversing earlier reforms would be avoided. *Flexibility*, versus rigidity of policies, is another feature associated with the ability of policymakers to respond to changes in the underlying economic or social environment. In the case of tax reform, the flexibility or adaptability of tax policies might be related to whether tax reform is more or less responsive to changes in the economic environment or in the information available. For example, if earmarked taxes are being added, they would clearly increase the rigidity of the tax system. Stalemate in the legislative process, as a result of the interaction of veto players may also make the tax reform process rigid. Tax policies can also be *coherent* and *coordinated* (related to the degree of consistency among the actions taken by the several agents involved in the same arena of policymaking). The results of their actions would avoid, for example, a tax reform filled with complications and inconsistencies which would make the policy difficult to maintain. The policymaking process can generate incentives for increasing

efficiency in delivery (quality of the policies themselves, and quality of the policymakers and those in charge of implementation), which is an example of an investment-related quality. This is the case, for example, when the tax administration has been endowed with the resources and capacities to effectively implement the tax policies. Finally, policies can generate *broad* (as opposed to *concentrated*) benefits. In that case, policies are publicly regarded (resembling public goods), as opposed to being privately regarded. For example, tax policies are more publicly regarded when tax reforms lead to more horizontal and vertical equity. Using the PMP methodology is natural for tax policy analysis because defining an ideal tax regime is theoretically difficult, so the analysis should focus less on the content of the policies (there is no universally valid optimal tax reform), and more on the abovementioned features.

The paper proceeds as follows. In Section 2 we provide a detailed account of the main trends of the tax reform process during the 1990s, discussing the key changes in tariffs, corporate and personal income taxation, VAT, excise taxes, and administrative reforms. We also measure the outcomes of the reforms in terms of tax collections, productivity and neutrality of specific taxes, while briefly reviewing the studies on the distributional impact of taxation in the region. In Section 3 we explore in more detail the specific reform experience of nine Latin American countries (Argentina, Brazil, Chile, Colombia, Costa Rica, Guatemala, Mexico, Paraguay and Venezuela). We cursorily review the political institutions, key players and main features of fiscal policies in this group of countries. In Section 4 we establish a connection between the outcomes of policies as discussed in Section 2, with the characteristics of the policymaking process identified in Section 3. This is done through a panel of countries that allows the econometric testing of some of the main hypothesis. Section 5 concludes.

2. TRENDS AND OUTCOMES OF TAX REFORMS

2.1 The Objectives of the Reforms

The major thrust of tax reforms since the late 1980s has been to increase tax revenues without incurring high costs to government.² Tax reforms in earlier decades were also geared toward boosting tax revenues, but lower priority was accorded to the constraints on tax administration, while other goals, such as progressivity, got greater attention (Goode, 1993). The imperative to raise revenues since the late 1980s was a function of two major conditions: On the one hand, periodic bouts of high inflation in several

² Useful surveys of recent tax reform trends and outcomes in Latin America are Shome (1999), Stotsky and WoldeMariam (2002) and Tanzi (2003).

countries made it advisable to restore fiscal balance and avoid monetary funding of fiscal deficits (and, for this purpose, several countries invested their central banks with autonomy from the government administrations). On the other hand, import tariffs (and, in some cases, export taxes) ceased to be an important source of fiscal revenues as policies were adopted by all the countries to liberalize international trade. More generally, the strategy to integrate internationally limited the opportunities to tax cross-border movements of physical assets, financial resources, and proceeds from all mobile forms of capital, including human capital. Given that tax policy was largely driven by price stabilization and international liberalization, it is hardly surprising that the objectives of tax policy have become more modest.

Of course, raising more revenue (on a tax base limited by globalization) has not been the only goal driving tax reforms. Consistent with international trends in the tax area (Harberger, 1990; Goode, 1993), reforms proposed by governments in Latin America since the late 1980s have been geared toward improving tax neutrality and horizontal equity by reducing the difference in treatment of different sectors or revenue sources, and by reducing tax incentives and exemptions. Measures aimed at opening economies to international trade and trends in globalization have reinforced the need for tax structures that will not distort investment and production decisions. Neutrality is a less complicated objective when fiscal conditions are more favorable (when growth is robust or when, for example, there is a surplus of exceptionally high revenues from sales of natural resources). However, in practice, this objective has frequently been abandoned during the legislative process or the implementation of reforms, as we shall see below.

In general, the goal of neutrality is consistent with the objective of facilitating tax administration (and therefore reducing the unit costs of collections). Nevertheless, the opposite is seldom the case. In fact, several reforms, promoted by tax managers to facilitate collections, have frequently run into conflict with the goal of neutrality. The most significant recent instance is the taxing of banking transactions (which constitutes a cascading tax that affects disproportionately those activities that are the least vertically integrated and those with low value added per transaction). The same holds for more traditional selective excise taxes on certain consumer goods, such as tobacco, alcoholic beverages, and fuels (taxes which may be justifiable because they help to offset adverse externalities). Over the past two decades, some administrative practices frequently resorted to in the interest of streamlining tax administration have actually undermined neutrality and horizontal equity. Examples include tax withholdings, simplified tax systems for microenterprises, taxes on assets, and other taxes based on imputed income. In fact, it has been suggested that these mechanisms have been so abused that they have impaired the main objective of increasing the level of collections (Shome 1999).

A number of authors have called particular attention to what would seem to be an abandonment of redistributive goals as demonstrated by tax policies in Latin America (Agosin, et al. 2004; Lledo, et al. 2004). This trend is widespread in the developing world and among the “best practices” prescribed by international tax consultants (Goode 1993). Erstwhile optimism for a clear capacity of tax systems to achieve income distribution seemed justified by the postwar experience of European countries. But this view faded as recognition grew that tax administrations in developing countries had a limited capacity to handle steeply progressive tax schemes in politically adverse environments, where elites can undermine the application of this redistributive mechanism in practice. It is noteworthy that the highest income concentrations are found in the developing countries where tax burdens are the lightest (Agosin and Machado 2004). In past decades, this correlation would have been used to promote more progressive tax systems; at this time, however, it is more likely to be interpreted as evidence of the administrative and political problems that tax policies face in societies where incomes and wealth are highly skewed.

Even so, as contended below, the progressivity of a tax structure (that is, tax incidence by income level) should not be confused with its redistributive capacity, since the latter depends not only on incidence but the magnitude of public spending that may be financed by tax revenues. Even though the goal of progressivity ceased to hold sway, tax reforms in the 1990s managed to increase the redistributive capacity of the tax structures. In fact, public social spending as a proportion of GDP rose on average from 9.8% in 1990-91 to 13.5% in 2000-2001 (CEPAL, 2004). Chile and Colombia, in the early 1990s, and El Salvador and Guatemala, in the late 1990s, are examples of countries in which governments sponsored non-progressive tax reforms (based, as they were, on increases in value added taxes) for the explicit purpose of funding increases in social spending.

In the following sections of this chapter, we describe the major characteristics of Latin American tax reforms since the late 1980s; we assess the principal results in such areas as collections, neutrality, progressivity, and redistributive capacity; and we provide an overview of reform efforts and their major achievements and failures.

2.2 Principal Characteristics of Tax Reforms

Common traits and goals of tax reforms passed by Latin American legislatures in the late 1980s, include tax base expansion, rate increases in the value added tax (VAT), drops in income tax rates, and

streamlined tax structures. These trends in reforms were particularly notable until the mid-1990s. Thereafter, changes brought wide, if not erratic, swings in tax rates and changes to the tax base.

Tariffs

This article is concerned mostly with those tax reforms that require legislative action, as opposed to tariff reforms, which in most countries are the purview of the executive branch. However, since tariff cuts conditioned other aspects of tax policy, a brief summary of the changes in this area may be useful. Between the mid-1980s and the early 1990s, all the countries in Latin America launched programs to open their economies to foreign trade. As a consequence, tariff rates fell from an average 48.9%, prior to the reforms, to 10.7% by 1999, and dispersion was significantly reduced (Figure 1). By the late 1990s, only two countries (of the 24 for which data are available) maintained average tariff rates above 15% (Figure 2). These tariff declines were greater for industrial products than agricultural ones, which many countries still protect with higher or varying tariffs depending on price conditions. Nevertheless, high agricultural tariffs do not constitute a significant tax revenue source; they essentially fulfill a protectionist purpose. Tariff receipts have also reflected the proliferation of trade agreements that remove, either in whole or in part, tariffs on goods from specific countries. The public revenues forfeited under these agreements may equal several points of GDP³.

Taxes on business profits and capital gains

Corporate taxes have been an important target of the reforms since the mid-1980s. The most widespread and dramatic change has been the drop in tax rates on business profits, which typically fell from 42.0% in 1985 to 31.7% in 1990, and finally settled at 30.0%⁴ (Table 1). To avoid discouraging foreign investment, these rates tended to be set below the maximum rate in force in the United States (39.6% since the 1986 reform and 35.0% at present). As a result, rates tended to even out among the countries and stabilize over time. Between 1988 and 1995, tax rates for businesses changed 1.6 times, on average by country, however in the following seven years the average change per country was 0.4 times, and these changes were far smaller. In other words, during the 1990s the margin of action available for tampering with business tax rates narrowed considerably. As might be expected, changes proliferated in other areas.

³ To be precise, the reduction in tariff revenues between 1990 and 2001 was close to 1.0% of GDP.

⁴ To avoid skewing due to extreme observations, these figures refer to the medians of the 19 countries under consideration.

In effect, the emphasis seen on sector neutrality, which had been the hallmark of the first wave of business tax reforms until the early-1990s, tended to diminish thereafter. For example, in Central America it was common to waive duties on foreign capital in free trade zones where *maquila* assembly plants were established, and in sectors such as tourism, mining, and fishing. (This constitutes in practice a transfer of receipts to the countries of origin, since tax payments in other countries are deducted from those due in the country of origin; Agosín et al. 2004). Exemptions from income taxes in primary sector industries are quite extensive throughout Latin America (see Table 2).

Corporate profits have been usually taxed in most Latin American countries like any other income. However, in Bolivia, Paraguay, Peru, and the Central American countries, with the exception of Honduras, corporate profits are taxed at lower rates, if at all. In several cases (Bolivia, Costa Rica, El Salvador, Guatemala and Peru), the reforms that began in the mid-1980s afforded or reinforced favorable treatment of corporate profits; only in Nicaragua did the reform move in the opposite direction (Stotsky and WoldeMariam 2002).

To facilitate the management of business taxes, several countries long ago systems of “imputed income” on the basis of asset holdings, thus calculating minimum income tax payments as a percentage of asset holdings. Another common tool used to expedite collections is to withhold a fraction of some business income in lieu of future tax obligations. Nevertheless, the effectiveness of these mechanisms tended to decline in the 1990s as asset taxes were often modified and, in some countries, abolished; and withholding rates were generally reduced on corporate profits payments and foreign remittances of dividends, interest and royalties (Shome 1999; Stotsky and WoldeMariam 2002; Agosín et al. 2004).

Individual income taxes

The most significant reform concerning individual income tax was the reduction in the maximum rates. This trend was similar, albeit more pronounced, than in the case of business taxes, with the ceiling on individual income tax being lowered from a median rate of 50.0% in 1985 to 33.7% in 1990, and 25.0% in 2001 (rising in 2002 to 27.0%). Even though lower rates has meant less dispersion of tax rates among countries, disparities in individual income tax rates are greater than in business tax rates (Table 3). Changes in the maximum rates have become less frequent, declining from an average of 1.8 changes per country between 1988 and 1995 to 0.7 changes per country between 1995 and 2002.

Despite the appreciable drop in the maximum tax rate on individual income, the tax structures maintain important progressive aspects; exemptions are set for minimum levels of individual incomes, and different rates are charged according to the level of taxable income. The individual income tax exemption rose from an average of 60% of per capita income in the mid-1980s to 180% by the early 1990s, and to 230% in 2001 (Table 4). Moreover, the income levels to be taxed at maximum rates were lowered. On average, in the mid-1980s, the maximum rate was only charged when taxpayers declared incomes 121 times greater than the per capita income. These thresholds were decreased in the early 1990s to an average of 75 times per capita income, and in the late 1990s to 20 times per capita income. In theory, these changes tended to make personal income taxes more progressive as a whole. (However, progressivity within the lower and the higher income groups, when considered apart, was reduced). The increase in the personal exemption tended to shrink the universe of taxpayers, thereby streamlining collections and perhaps barely sacrificing any revenue.

Several attempts at reform sought, with scant success, to reduce the exemptions, discounts, and special treatment granted to specific sorts of individual income, which together seriously hamstringing the effectiveness of individual income taxes. Personal income taxes continue to be poorly integrated in many countries, because they rely on withholding mechanisms that differentiate between sources of income, and grant exemptions to different types of income, especially to financial returns and corporate profits (Agosin et al. 2004).

Consumer Taxes: VAT and excise taxes

The replacement of cascading sales taxes by value added taxes was the most significant tax reform in Latin America in the 1980s and early 1990s. In 1995, VAT systems were in place in 21 countries in the region. In theory, the VAT is charged throughout each stage of the production and distribution of goods, but taxes paid on investment or export goods are discounted or returned⁵. Consequently, the VAT functions as a tax on final consumption. However, in practice, the effectiveness of a VAT is undercut by the presence of informality and the difficulty to incorporate into the system small businesses and individuals supplying specialized services. Exemptions and differential tax rates on different products further reduce the effectiveness of the tax.

⁵ The obligation comes from the difference between the taxes charged for sales (tax debt) and those foregone on sales (tax credit). This structure encourages firms to take pains to ensure that suppliers from whom they purchase intermediate goods have paid the taxes that they should.

Until the late 1980s, the VAT-related reforms consisted either of introducing the system or strengthening it, and were less concerned with rate changes. The typical basic VAT rate was 10% until the late 1980s, but several reforms made in the early 1990s raised the basic rate to 15%. These rate changes were made ever less frequently, dropping from 1.5 times per country between 1988 and 1995, to 0.6 times in the following seven-year period. Thereafter, the most frequent changes were only at the margins, as legislative branches typically resisted executive attempts to improve the efficiency of the tax, by broadening its base or raising the rates of what is generally considered to be a regressive tax.

As opposed to the VAT, excise taxes and other minor taxes have tended to fade as sources of tax revenue. Through the early 1990s, interest in simplifying the system led to the actual elimination of hundreds of small taxes in many countries. In general, the only excise taxes preserved were those that raised the most significant revenues and were more easily justified by the nature of the goods being targeted (e.g., tobacco, alcoholic beverages, fuels). In contrast with other types of taxes, the difference in excise tax rates among countries has not narrowed, not even in countries whose economies are relatively well integrated, such as the Central American countries (Agosin et al. 2004). Though the excise taxes offer the opportunity for low-cost collections, they raise the opposition of the producers, which are usually a small group of well-organized and very vocal firms.

Administrative reforms

The goal of streamlining tax systems in order to facilitate tax administration was complemented over the past 20 years by a thorough modernization of the tax administrations. This was a break from the past, when attempts were being made to transplant tax systems wholesale from industrialized countries without bothering to adjust administrative practices or capacities. By 1990, the majority of tax administrations in the region had reorganized into a function-based structure (customer service, records, collections, auditing, and legal proceedings), instead of the previous organization by tax types. In the 1990s, administrative reforms involved for the most part functional rationalization, the creation of special taxpayer or customer service units, tracking of large taxpayers, the general implementation of standardized tax retention systems, and the introduction of simplified systems for small producers and firms (whereby a single combined payment is charged for income taxes, VAT, and excise taxes) (IDB 1996; Shome 1999). Not all these changes required legislative action, notwithstanding their importance in the effectiveness of the tax system. This is why it has been said that in developing countries, “tax administration is tax policy” (Bird and Casanegra 1992, as cited by Shome 1999).

2.3 Principal Outcomes of Tax Reforms

Bearing in mind that the priority of tax reforms in the late 1980s and 1990s was to boost tax revenues, a certain measure of success was achieved in reversing the direction of tax revenues, which had been declining since the mid-1980s. The reforms were also relatively successful in achieving their goal of improving the efficiency of the tax systems. The greatest progress was made between the mid-1980s and the early 1990s. Although the progressivity of the system was clearly reduced by the increased importance of the VAT, the redistributive capacity of taxes was improved by the increase in revenues.

Tax collections

Between 1985 and 1990, tax revenues tended to decline, in response to sluggish economic growth, the opening to international trade, and high inflation in some countries. Average tax revenues declined from 15.6% in 1985 to 12.9% in this period (and the median rate fell from 14.8% to 11.3%; see Figure 3). A recovery in income taxes, which soon began and continued until 1997, almost entirely eliminated these declines, as the average tax burden rose to 15.2% (and the median to 14.8%). Nevertheless, this progress was largely undone in the ensuing years, under the effect of slow growth in the region. Tax revenues in 2002 averaged 14.4% of GDP (with a median rate of 12.8%). These indicators suggest that the behavior of tax revenues is influenced by the economic cycle. However, even when one controls for the apparent impact of the economic cycle, these trends are still present, as can be seen in the same figure.⁶

Consequently, the objective of increasing tax revenues was accomplished but not sustained. Thus, governments managed to reverse the trend toward declining revenues seen in the late 1980s, but some of the gains achieved have eroded in recent years. When the 2000-2002 period is compared to the 1985-1989 period (both timeframes being periods of slow growth in the region), one finds that revenues (as a percentage of GDP) fell in 9 out of 19 countries. However, the trend was not uniform among all the countries. Bolivia, Brazil and the Dominican Republic managed to raise the tax burden by three points of GDP (Table 6). The differences among countries remain when calculations control for the impact of the economic cycle. Nevertheless, in the cases of Trinidad and Tobago and Venezuela, the behavior of tax collections also reflects oil price fluctuations.

⁶ The estimated elasticity of tax revenues/GDP to the business cycle (measured by applying the conventional Hodrick-Prescott filter to the log of GDP) in a panel regression with country-fixed effects from 1985 to 2002 is 0.88.

In light of the other factors influencing tax revenues, assessing the impact of reforms on the tax burden is no small matter. As indicated, the steps taken to open economies to international trade reduced the levels of tariff receipts, and the greater mobility of capital and other taxable bases narrowed the ability to tax firms and individual capital income. On the other hand, the greater price stability achieved by many countries reduced the debilitating effect of inflation on tax receipts in real terms, known as the “Tanzi effect.”⁷ Given the mix of factors, it makes sense to analyze not only the evolution of the total tax burden, but of the main taxes affected by the reforms. The revenues from direct taxes, which averaged 2.6% of GDP from 1985 to 1989, remained virtually the same in the following five-year period; nevertheless, it rose to 3.0% of GDP in the period from 1995 to 1999 and to 3.4% between the years 2000 and 2002 (Table 3). Even though these levels are low compared to international standards, they do represent significant progress within the region.⁸ As for the VAT, collections rose from an average of 3.0% of GDP in the late 1980s, to 3.8% in the following five-year period, to 5.0% in the late 1990s, and to 5.3% in the years 2000 to 2002. In this area, the tax yield is superior to global standards.⁹ Higher collections from direct taxes and VAT managed to turn around the decline in revenues from tariffs and taxes on foreign trade.

Neutrality

An interest in simplifying the tax structures and having tax systems that would avoid distorting production and investment decisions was the second goal behind the reforms. By definition, any tax exhibits greater neutrality when it charges lower proportional rates and is charged uniformly for all economic activities or agents. As we have seen, whereas VAT rates tended to increase, maximum rates on corporate profits and personal income taxes declined.¹⁰ Figure 4 summarizes these trends for the region as a whole.

To get an approximate measure of the uniformity with which taxes are charged, one may turn to the concept of productivity, understood as the ratio between the effective and the potential tax collection, given the basic or maximum rate. Thus, the productivity of the VAT is usually calculated as the ratio between the revenue raised by this tax as a proportion of GDP and the basic rate. In this way, if the entire final output of the economy were effectively taxed at the basic rate, then productivity would be 1.

⁷ This refers to loss in the real value of tax revenues between the time at which the obligation is assumed and the time when it is paid off.

⁸ According to IDB (1998, Ch. 8), the direct tax burden should be 8% of GDP, in accordance with global standards, for the income levels in Latin American countries.

⁹ The tax burden from sales taxes, according to global standards, is 4% del GDP. (Ibid.)

¹⁰ It makes sense to take the maximum income tax rate, instead of the average rates, because the maximum rate has a greater influence on production, investment, and work decisions.

However, the calculations presented below are not made on the basis of the entire GDP; rather, they are based on internal demand, because, as noted above, the VAT in the region is designed as a tax on consumption.¹¹ On average, the productivity of the VAT rose from 0.25 between 1985 and 1988 to levels of about 0.34 as of 1992 (Figure 5). In general, the most significant increases in productivity took place through the early 1990s, in the years when the tax was being consolidated. Several countries made some marginal improvements thereafter, but only Argentina, the Dominican Republic, and Ecuador registered significant improvements in productivity in recent years.

Average productivity of corporate taxes and individual income tax exhibited a similar trend. Beginning with productivity levels averaging 0.1 (or a median of 0.06) in the mid-1980s, improvements were seen by the mid-1990s (average of 0.15, median of 0.12), which have held rather steady ever since (Figure 6). Brazil, the Dominican Republic, Nicaragua, and Uruguay were the only countries that managed to raise income tax productivity in a significant way, beginning in the mid-1990s; whereas Trinidad and Tobago and Venezuela both experienced backsliding, due, at least in part, to the price trends in fossil fuels.

In order to summarize the neutrality of VAT and taxes on personal income and corporate profits in a single measure, we resort to the method used by Lora (2001), which employs an index combining the basic (or maximum) rates of the major taxes with their corresponding figures for productivity. Higher index values indicate lower tax rates (using a scale from 0 to 1 for each tax, wherein 0 corresponds to the highest tax and 1 to the lowest for the set of observations per year and country), and higher productivity rates (in this case, 0 corresponds to the lowest level of productivity, 1 to the highest). The results of this combined index show that the neutrality of the tax systems tended to improve considerably between the mid-1980s and the early 1990s, with few significant changes thereafter (Figure 7). Table 8 presents the values from the combined index of tax neutrality by country for the periods 1985-1989, 1990-1994, 1995-99 and 2000-2002. These values show that these trends were quite common in the majority of the countries. Nevertheless, whereas all countries were moving toward systems that were less distorting (and, thus, more similar to one another) significant differences remain among countries.

Progressivity and redistributive capacity

¹¹ Thus, strictly speaking, productivity should be calculated in terms of private consumption. Nevertheless, we have opted to use internal demand due to weaknesses with the data available on consumption.

The tax reforms of the past 20 years have been subject to frequent criticism over their regressive nature; specifically, over the greater share of overall tax revenues that VAT collections represent and the reduction in the rate ceilings for the taxes on corporate profits and individual income. The way this concept is usually understood, a tax is considered regressive when the lower income groups pay a larger proportion of their income or expenses than do the higher income groups. The implication is that the pre-tax concentration of individual spending or income (as measured by the Gini coefficient) is greater than the concentration of taxes according to income levels (using a quasi-Gini tax coefficient). This indicator is known as the Kakwani measure of progressivity or regressivity. As Table 9 suggests, on this account income taxes are strongly progressive: the median Kakwani measure for the seven studies considered is 0.15. It is not clear what the effect was from the reforms on the progressivity of this tax. The reduction in rates should have reduced progressivity, but this effect should also have been offset by the combined effects of having greater amounts subject to tax (which exclude a larger swathe of low-income persons) and the extension of the maximum tax rate to lower income levels (thereby raising the overall burden among the groups of highest earners).

Meanwhile, the same measure for the VAT suggests that, on average, this tax is highly regressive (-0.089). However, contrary to popular belief, in some cases such as Colombia (in 1994 beginning with the second income decile) and Guatemala, the VAT is a progressive tax. Furthermore, as the authors of these studies usually note, the calculations tend to accentuate regressivity, especially when the coefficients for concentration are calculated in terms of income and not spending,¹² and because only rarely are adjustments made to account for tax evasion.

The Kakwani measure does not take into account how much tax is collected. Alternatively, the Reynolds-Smolensky measure can be used, which does depend on the revenue collected, and which simply compares the Gini coefficient before and after paying the tax. Obviously, both measures yield the same sign for a given tax. By this measure, none of the 14 taxes considered produce any significant change in the level of income concentration, implying that the redistribution of income caused directly by the taxes alone is of minute importance.

However, the Kakwani and Reynolds-Smolensky measures of progressivity do not account for the redistributive potential of the taxes through the use of its revenues. This is a drawback, because it fails to recognize that a neutral tax (neither regressive nor progressive) that yields considerable revenue may

¹² For example, the measure is skewed when the lowest-income deciles include persons who have temporarily suffered a drop in income, but who maintain their spending apace with the permanent level of income.

hold greater redistributive opportunity than another extremely progressive tax (such as an income tax) that produces a scant revenue. In order to appreciate this redistributive potential, a third measure, inspired by Engel, Galetovic, and Raddatz (1997) is included in the table. The measure compares the Gini prior to the tax with a post-tax Gini that assumes that the proceeds of the tax are distributed to all income groups in equal amounts.¹³ As can be observed in Table 4, this measure indicates that the redistributive potential of the VAT is significantly greater than that of individual income taxes, which of course is due entirely to the VAT raising higher revenues.

This analysis is not as hypothetical as it may appear. Contrary to widespread belief, social spending grew by an average 3.7 % of GDP in all countries of the region during the 1990s, as mentioned. Considering the constraints on income tax collections and other means of raising public revenues, the increase in social spending would not have been possible had the declines in tax collections from the late 1980s not been offset by higher VAT revenues.

2.4 Reform Activity: Intensity, Achievements and Failures

The main objective of this paper is to assess the policy making process of tax reform in a selection of Latin American countries. Since most of that process takes place in the legislatures, it may be helpful to offer a simple measure that summarizes the extent of activity of the congresses in tax matters in recent decades. Taking the index that Mahon (2004) developed for the years 1977 to 1995, we have assigned quantitative values for each major congressional action beginning in 1990: a) the reorganization of the entire tax system (assigned a value of 0.2); b) establishment of a value-added tax (also 0.2); c) significant expansion of the tax base for the VAT (0.1); d) the increase in the basic rate of the VAT (0.1); e) elimination of minor taxes (0.1); f) significant expansion of the tax base for taxes on corporate profits (0.1); g) increases in the rate ceiling for this tax (0.1); h) significant expansion of the base for individual income taxes (0.1); i) increases in the rate ceiling for this tax; j) modernization of the tax administration; and k) introduction of the tax on banking operations, the tax on gross assets, or a simplified tax structure for small taxpayers (0.1). The assigned values (in parentheses) are intended to reflect the relative weight of each reform. Even though Mahon does not make available this level of detail for his original indexes, a comparison of overlapping years yields similar results for both scales.

¹³ Clearly, to the extent that public spending is allocated in a more redistributive fashion, the effect on the final Gini will be greater, but it makes more sense to assign this redistributive effect to the spending decisions instead of the tax structure. Incidentally, one notes that a "neutral" tax on 100% of income, which redistributes "flatly" throughout the entire population, would entirely eliminate any concentration of income.

In general, the reforms between 1990 and 2002, as compared to the previous 13 years, were quite similar in the degree of intensity, albeit more frequent: whereas reforms were enacted on average in 4.2 of the 13 years in each country in the latter period, between 1977 and 1989, reforms were on average passed in only 2.5 years in each country. Interestingly, one finds that the countries most predisposed to reforms (in terms of both intensity and frequency) were generally the same in one period as in the other, suggesting that the propensity for reform rests on longer-term factors. Looking at the list of 11 possible reforms (a-k) in the preceding paragraph, countries averaged 7.7 of 11 possible reform items. However, in some instances reforms were rescinded in whole or in part (after 1990), so the net number of reform items enacted was an average of 5.6 per country. Reviewing the breakdown of reform items offered in Table 10, we find that the VAT was the one item most frequently subject to reform. We find that congresses of countries in Latin America were also quite active in reforming the corporate income tax, and to a slightly lesser degree, individual income taxes.

From the results of reforms summarized in the previous section, we see that reform efforts were relatively successful in raising higher revenues and increasing the productivity and neutrality of these taxes. However, success fluctuated widely among the countries. As we have seen, attempts to increase revenues from indirect taxes were far more effective than in the case of direct taxes, to the detriment of tax progressivity, although without prejudice to redistributive capacity throughout the entire system. Where reforms have most seriously been frustrated has been in the attempts to broaden the tax bases and eliminate the special exemptions and treatment that certain sectors enjoy.

Furthermore, few countries demonstrated significant linkage between the results of reforms, on the one hand, and the magnitude of congressional effort, on the other (Table 11). In fact, the correlation between the index for reform activity and the increase in tax revenues between 1990 and 2002 is virtually null (-0.04), while the correlation between the frequency of tax reforms (the number of years with tax reforms) and the increase in tax receipts is actually negative (-0.20). What is even more discouraging is the negative correlation between the intensity of the reforms and the index of tax neutrality (-0.11), and the negative correlation between the frequency of reforms and the index of tax neutrality (-0.40).

Therefore, one finds that notwithstanding progress in revenue raising and tax administration, the greatest success did not occur in the countries with the greatest propensity for reform. On the contrary, the most reformist countries appear to have sacrificed neutrality in the process of enacting reforms. The remaining sections of this study attempt to understand these results by looking at how public policy decision-making affects the results of reform efforts.

3. THE POLICYMAKING PROCESS OF TAX REFORMS

Perhaps like no other area of public policies, tax policies are the outcome of complex intertemporal exchanges among political actors that participate in the policy making process. Typically, a tax reform involves short term political costs but potential long term gains if adequately designed. For example, the design, approval and implementation of a tax reform would depend on the interaction of the president, the finance minister, the tax bureaucracy, political parties, legislators, interest groups, multilateral institutions, academics, civil society, and the media, among others. Disentangling their incentives and payoffs from cooperation is helpful in order to understand the occurrence and quality of tax reforms. When their interests are not aligned, tax reforms are harder to enact, or when enacted have lower chances of success.

The general idea of the framework is that the ability to reach cooperative outcomes among the key political players affects the outer features of public policies. Political institutions—together with some particular aspects of the policies—determine whether cooperative intertemporal transactions are possible or not. When these transactions are feasible, public policies are more effective, more sustainable, and more adaptable. In contrast, when intertemporal political agreements are harder to strike and enforce, policies are either too unstable (in the sense of being subject to political swings) or too rigid (in the sense that players inefficiently tie their hands, rather than leaving some policy discretion). In the latter case, policies would not respond to changes in the socioeconomic conditions of the country. As in oligopoly games, the fewer the political actors, the higher the frequency of interaction between them, and lower immediate benefits from deviating are two key factors that facilitate cooperation. The observability of their actions and the existence of enforcement mechanisms are other important elements that need to be considered. Although mapping these abstract variables identified in the theory of repeated oligopoly games into aspects of the actual policymaking game is not trivial, a short tenure of key political actors (legislators, party leaders, ministers, etc.) is an indication of high discount rates, which makes cooperation less likely. The existence of an independent judiciary is an indication of the availability of credible enforcement technologies that play an important role in determining whether or not the political transactions environment is likely to lead to cooperation.

Before discussing in detail the political institutions, as well as the outer features of tax policies, it is important to understand who the key players in this arena are. Although there is some variation from country to country, especially between unitary and federal governments, in a well functioning democracy

it is expected that political parties, legislators, the President and cabinet, the media, experts within the government and the civil society groups play a key role in setting the agenda. The generation and selection of alternatives should be the area of greatest influence for qualified bureaucracy and the staff of legislators, as well as experts from within and outside the government. However, the decision making would involve primarily the president (with his/her cabinet) and legislators (with the support of their staff). In the implementation stage the key role is played by the government's specialized bureaucracies, while the evaluation and control should primarily be in the hands of the bureaucracies, judiciary and control entities, and experts outside the government. Based on work by Kingdon (1995), Lindblom (1991), Pressman and Wildavsky (1998) and Cortazar (2005), Table 12 provides a theoretical 'benchmark' of the role of each player in the tax policy area. The relevance of each player is ranked from 1 (negligible role) to 3 (maximum influence).

As mentioned in the introduction, the PMP methodology focuses on the relationship between political institutions (which determine the role and incentives of key players) and certain common *outer features*, which are systematically present in tax policies. As already discussed, these features refer to aspects such as the stability, adaptability, coherence, investment-like properties, and public regardedness of tax policies. However, these are still broad concepts that need to be made more analytically tractable. For the purpose of this paper, we associate *stability* with few tax policy reversals, few changes in the basic structure, and slow-moving and preannounced changes in taxation when necessary. *Adaptability* is greatest when there are few constitutional mandates on issues related to taxes, taxes are not earmarked, and the executive has some discretion to respond to changes in economic circumstances (e.g. a temporary reduction in the terms of trade allows the government to lower taxes in the export sectors). Tax policies are more *coherent* when the resulting tax structures are simpler and there is no tax competition between different levels of government. *Investment-like properties* are related essentially to a strong, independent, credible, and well-financed tax administration. These properties are reflected in low evasion and a positive attitude towards paying taxes. Finally, *public regardedness* refers also to simplicity, lack of loopholes and exemptions, ensuing horizontal and vertical equity.

Country analyses

We now turn into the analysis of the PMPs in the case of tax policies for a group of Latin American countries. The group of representative countries is: Argentina, Brazil, Chile, Colombia, Costa Rica, Guatemala, Mexico, Paraguay and Venezuela. The benefits of looking more in depth into these nine countries is that we are able to establish some patterns and construct some indices, which will add

richness to the following analysis. In each country case, we start by describing the actors that play a decisive role in shaping tax policy. We are interested in underscoring whether they are stable players –in the sense of having long tenures– or whether they change abruptly. Also, it is important to know who they represent and what their interests are. The role of interest groups, their capacity to organize and influence policy is another relevant aspect. Finally, in many countries tax policies are influenced by multilateral organizations, such as the IMF, the World Bank, and the IDB. In fact, much of the conditionality of IMF programs and multilateral lending hinges on fiscal issues. Therefore, we expect the IMF to be most influential in countries that have a program, where conditionality on fiscal reform is often central. Table 13 shows the frequency of IMF programs in the decades before and after 1990. Most countries have had more programs in the latter decade. In particular, this has been the case of Argentina, Brazil, and Colombia. The IMF favors the adoption and widening of the VAT, so we expect to see that countries under IMF programs introduce more reforms in this area. After describing the key players, we discuss the main characteristics the tax structure and the reform process since 1990. The purpose is to identify tax policies' outer features.

3.1 Argentina

Key players and the PMPs

According to Spiller and Tommasi (2003, 2005), Argentina is the prototypical example of a country where the political institutions are not conducive to effective political compromise and cooperation. The presidential regime makes the president the key player in the PMP. Legislators are elected in closed and blocked party lists under a system of proportional representation. The lists are controlled by governors and provincial party elites, making legislators relatively weak political actors. It is in the interest of these elites to rotate legislators. Contrary to first appearances, Congress does not have an important role in the PMP. The Supreme Court is not an enforcer of intertemporal agreements. According to Iaryczower et al. (2002), the Court has tended to be too aligned with the Executive. In addition to having substantial constitutional powers, governors generally control legislators. In relation to tax policy, governors favor the central collection of tax revenues in order to finance spending in the province. The purpose is to transfer the political cost of taxation to the executive (and congress), while retaining the political dividend of additional expenditures. The bureaucracy is dominated by a small group of political appointees that rotate very frequently, and are unable to coordinate various areas of policy. Lack of professionalization, motivation, and oversight makes the bureaucracy a very ineffective enforcer of political agreements. Table 14 shows the influence of key players in Argentina.

The tax burden in Argentina (including national and provincial taxes and social security contributions) has fluctuated around 21 to 22 percent of GDP between 1993 and 2001. In 2002 national taxes (consumption, income and international trade taxes) and contributions for social security represented 15.8 percent of GDP while provincial taxes (turnover tax, real state tax, automobile tax, stamp and other taxes) represented just 3,2 percent of GDP. The 2001 economic crisis caused a reduction in tax revenues to 19 percent of GDP, resulting in the creation of new revenue sources (tax on financial transactions and tax on exports) and the rise of the tax evasion level. Corporate income tax represented approximately two thirds of total income taxes. The tax on financial transactions and the tax on exports represented altogether around 10 percent of total government revenues and 20 percent of total tax revenues.

According to Lora and Panizza (2002), the effectiveness and fair-handedness of the tax system was undermined by several policies implemented before and after the crisis. On one hand, tax amnesties were reintroduced in 2000 despite the fact that these were supposed to have been eliminated with the establishment in 1997 of the permanent system of "spontaneous filing". Even more, the moratorium in 2000 reduced revenues by \$600 million in forgone payments. With the objective of increasing competitiveness and promoting investment, the tax on commercial borrowers' interest payments was reduced in stages the same year. Also, credits were launched for payment of VATs and several other taxes and the time available in which to use deductions for minimum business tax. In 2001 competitiveness plans for specific economic sectors introduced tax benefits (such as exemptions from employer charges and other taxes in recognition of VAT payments) and the use of tax credits to pay off debts to the central government.

Tax reforms have been a key component of the reform process since 1990. The executive initiates policies, but it requires the approval of most provincial governors, so that they instruct legislators to support the initiative. Their support is exchanged for political and fiscal favors, such as an increase in transfers from the central government to the provinces. The end result is a convoluted system of fiscal federalism. Although in theory subnational taxation should be important, in practice taxation is fairly centralized, generating a large vertical fiscal imbalance, which is covered through the negotiations between governors and the national executive. Those negotiations are characterized by the lack of cooperation and the incapacity to sustain intertemporal agreements. This results in large fiscal deficits and public indebtedness, bailouts of provincial finances, as well as the use of distortive taxes. The executive has the power to renege previous agreements, reducing the incentive of governors to reach agreements. In

turn, governors are not interested in the provision of national public goods and minimize subregional taxation, which reinforces their political power. Third-party or other enforcement mechanisms have been missing, because of limited independence of the judiciary and lack of power of the bureaucracy.

Outer Features of the PMP in Argentina

Stability: Although in general economic policy in Argentina is considered highly volatile, tax policy seems to be fairly stable. As mentioned, due to the nature of the electoral system, provincial politics is an important building block of national politics (Jones et al., 1998 and 2000). As an attempt to reduce the opportunistic incentives created by the fiscal vertical imbalance between the central government and the provinces, political actors have tended to reduce the capacity to adjust fiscal policy. Spiller et al (2003) explain that “these features have led to a rigid and convoluted federal tax collection and tax distribution, which has been christened the “Argentine Fiscal Labyrinth”.

Adaptability: As described above, tax policy has been relatively rigid.

Coordination/Coherence: Tax policy has been bounded by the lack of coordination between the central and provincial authorities. The huge transfers from the central government give little incentives to the provinces to increase their own revenue, which is low (3,5% of GDP). Argentina’s tax system has generated a great imbalance because provincial authorities obtain the political benefit of several fiscal expenditures (health, education, water supply and others) without incurring in the political cost of collecting taxes in their own jurisdiction.

Investment-related qualities/capacities: Regional governors, who are very influential in the legislature, have the distorted incentive to oppose tax reform while demanding more expenditures. They have little accountability in their fiscal situation. Tax administration has faced some evasion problems regarding income taxes. Some of the reasons have been the weakness and erratic policy of tax control, the lack of legal instruments available to the tax administration, and a long culture of tax evasion because of the frequent use of amnesties and whitewashing laws.

Public regardedness: Argentina’s tax system still embraces many exemptions and special treatments targeted to specific sectors that show a poor public regardedness of the tax policies. In addition to the remaining incentives and privileges on the VAT, exemptions are still extensive, including: private education, medical and funeral service rendered by unions, entertainments and shows, sport shows, taxi

services, location of houses and apartments, newspapers and magazines, books, medicines for human use, bread, milk and water. Furthermore, a large list of capital income and capital gains are exempted: dividends, interest from bank accounts, all capital gains for individuals, income from financial transactions for individuals, investments covered by promotion regimes (regional or sector investments incentives), and more. Several special regimes embedded on the “competitiveness plans” have broadened the horizontal inequity in Argentina’s tax system.

3.1 Brazil

Key players and the PMPs

According to Alston et al. (2005), the president has strong powers and is seen by the public opinion responsible of overall economic conditions in the country. The president negotiates with legislators top priority economic reform projects. The open lists electoral rules create a very competitive political system where legislators survive if able to fulfill the demands of their local constituency. In exchange for the approval of economic reform, legislators’ constituencies receive support from poverty alleviation programs sheltered from discretionary executive budget cuts. There is a bicameral Congress, which has the capacity to override the presidential veto. The independence of the Judiciary was enhanced by the Constitution of 1988, making the Supreme Court an important veto player due to its ability to control the constitutionality of laws. The Brazilian 1988 Constitution vests the states with substantial tax powers. The ICMS -Brazil’s version of the value added tax– is collected by the states and represents the single most important tax in the country (1/3 of all tax revenue). The indirect ways through which governors influence policy formation include *inter alia* lobbying activities in specific issues affecting states’ tax policy to their control over specific appointments in the federal bureaucracy. The constitution hard wired much of public policy, especially in relation to expenditures, making tax policy critical for fiscal stability. The Constitution of 1988 also mandated a gradual increase in the states and municipalities’ share of all public sector income. In relation to taxation, the bureaucracy is generally professional and powerful. It has been insulated from competitive politics. Table 15 shows the influence of key players in Brazil

Brazil has a well-established and clearly defined federal system, so when discussing the tax reform process, it is impossible to ignore the intergovernmental relations. According to Article 18 of the constitution, all members of the federation (i.e., the Union, the States, the Federal District and the municipalities) are autonomous. The tax powers of each level of government are explicitly defined, as are the revenue-sharing mechanisms of each level of government. Congress tends to approve much of the

policy reforms proposed by the Executive, yet Congress still holds checks on the powers of the President in return for some 'favor' in the form of regional 'pork'. It is this interaction that determines the qualities of policies, stable macro policies on the one hand and pork on the other. More than Congress, the independent court has restrained the will of the executive on tax matters, and explains in part the number of creative taxes at the federal level that have sprung up in recent years, many temporary in nature. However, within the context of a complicated fiscal federalism system, the court acts as an enforcer of intertemporal agreements, such as the constitution. The recent Law of Fiscal responsibility also permits the better enforcement of intertemporal agreements.

Brazil's tax burden has grown substantially and is invariably the highest in Latin America. Gross federal government revenues increased from an average of 16.5 percent of GDP in 1991–94 to 22.6 percent of GDP in 1999–2002. Total national revenues are 32 percent of GDP. The fiscal revenue increased markedly in the context of the external crisis in 1998–99, mainly through temporary taxes. The gradual loss of temporary revenues has been a great challenge because cuts in expenditure are difficult due to the high amount of constitutionally mandated expenditures. The best the government has been able to adjust was the permanent extension of a 2.5 percentage point surcharge on income tax for higher salary brackets.

The two major sources of additional revenues are the *Provisional Contribution on Financial Transactions* (CPMF) that was introduced as a tax at the end of 1993 and subsequently abolished and re-introduced several times since then; and the Social Security Financing Contribution (Cofins) that was associated with a series of court rulings favoring the government. Unlike others, the entire revenue gain of CPMF and Cofins remain with the federal government, as they are not shared with states and municipalities. In the case of the income tax and industrial products tax (IP) collected at the Federal level, the net revenue gain for the federal government is much reduced as about half of the revenues must be distributed to the participation funds of the states and municipalities. Other main tax bases for state governments are the motor vehicles taxes, and for the municipalities, service taxes and property taxes. Therefore, in terms of the distribution of responsibilities among governments, the legal basis is quite sound.

In the mid-1990s, the temporary or 'extraordinary' revenues became commonplace and widely used. All in all, extraordinary revenues peaked at over 3 percent of GDP in 1999, and continued to contribute on average with 2.5 percent of GDP in 2000–2002, suggesting that temporary taxes were a success in terms of revenues. However, the tax system may have indeed deteriorated in structure as a

result. According to Werneck (2002), exotic and low quality tax schemes raised revenue without having to be shared with lower-level governments. For example, turnover taxes moved from 22 percent of total tax revenue in 1989-93 to 39 percent in 2000.

The Fiscal Responsibility Law (LRF) approved in May 2000 was an effort to try to deal with the fiscal issue on the expenditure side, by imposing some order and accountability on States' spending. It set a general framework for budgetary planning, execution, and reporting, applicable to all levels of government. On revenues, the LRF mandates the withholding of discretionary federal transfers to states and municipalities that do not collect effectively their own taxes, and the publication of the impact of tax exemptions in the year they take effect and the two subsequent years. The LRF also requires that permanent spending mandates not be created without corresponding increases in permanent revenues or cuts in other permanent spending items. In the case of Brazil, this can act as a tool to make the system more stable and predictable. As a result of the LRF, the power of governors to influence national policies has weakened considerably, since the states have become more and more dependent on the Federal government because the voluntary (i.e. discretionary) transfers have become essential for their fiscal survival. This is so because the states' own revenues (tax and automatic constitutional transfers from the Federal Government) have since been devoted to producing the surpluses required to honor the refinancing contracts.

Outer Features of the PMP in Brazil

The case of Brazil illustrates the great difficulty in introducing tax reform, let alone getting it through Congress relatively intact without a major political feud. For example, in late 1997, the idea of tax reform began to float around. The government's considerations were quite radical: the main idea would be to discard turnover and cascading taxes as well as the state VAT taxes, and replace with three new ones: a consistent broad-based nationally-managed VAT, a new federal excise tax on a small number of goods and services and a local retail sales tax. However, it was only after the Asian and Russian crises, and the election to a second term, that the President decided to act. Over the next 18 months the tax reform issue dominated the political debate. Eventually, it was impossible to coordinate such a move: only opposition and stalemate resulted. While it may have superficially looked like a situation where the executive did not push hard enough on reform, once one considers the complexity of the change expected, it is not surprising. Werneck (2000) points out that there was uncertainty about the revenues that the new tax system would raise, uncertainty as to whether the agreed intergovernmental compensation rules would continue and whether the distribution across states would be preserved. It is therefore not surprising to see

that this was a non-cooperative equilibrium with too many competing interests. As Werneck puts it: “The tax reform debate [became] a noisy clash of conflicting views, increasingly marked by a strong aversion towards revenue losses. There [was] fear on all sides”.

In 2003 the new government of President Lula made a concerted effort to arrive at a consensus about tax reform once again. Originally the idea was to unify the main state tax, putting the 27 coexisting state codes under a single national VAT. The Cofins would be converted to a non-cumulative tax, and payroll taxes would gradually be replaced by a turnover tax to finance social security. It was specifically planned to be revenue-neutral at every level of government. As expected, the reform suffered some watering-down in Congress: the federal government decided that it would give the States a fourth of its CIDE¹⁴ revenue and the Manaus Free Trade Zone was extended for 10 years. Clearly, the government retreated and decided to concentrate on important measures that had a real chance of being approved, and postponed or shelved the most controversial aspects. The unification of the ICMS was thus postponed to 2005, and the number of allowed tax rates was reduced to five (as opposed to one). An important aspect was the conversion of the COFINS into a non-cumulative tax (although sectors to be negatively affected lobbied successfully to have their sectors continue to pay the COFINS under the old cumulative regime, or even exempted for some basic goods). Moreover, tax relief for exports and capital goods was granted. Partial success for the federal government came with the replacement of the payroll tax with a turnover tax and the extension of two temporary taxes, but also signified a transition to lower-quality taxes. The political elections calendar once again caught up and, with so many veto players and the complexity of the tax system (before and after), the reform process was temporarily shelved in 2004. The biggest obstacle has been to transfer the VAT to the federal the domain. The key question is for how much longer the country will be able to preserve its highly problematic state-level VAT arrangement. That is bound to be one of the main issues of the tax-reform debate over the coming years in Brazil (Werneck, 2004).

Stability: There is volatility and instability in tax policies. The 1988 constitution created more autonomy and leeway for the States to raise taxes, and also limited the type of taxes that the Federal government could impose (no Federal VAT). Although everyone wants to change the rules and the need of a radical reform has been floating since 1994, the government has instead resorted to many *incoherent* temporary taxes. The LRF is an attempt to impose stability in the Federal tax and expenditure system, as it allows the preservation of certain policies beyond tenure of certain officeholders or coalitions.

¹⁴ Contribution for Intervention in the Economic Domain (on the importation and commercialization of oil and derivatives, natural gas and derivatives, and combustible ethylic alcohol).

Adaptability: Tax policies have been relatively responsive to changes in the environment because the opening up of its capital markets and commitment to transparency has also required very strong discipline in the macro arena. However, there are various aspects, like the very large share of the budget financed by earmarked revenues that reduce the room to maneuver and adapt. However, to the extent that the FRL helps alleviate the primary fiscal deficits there may eventually be some room to reduce temporary taxes or eliminate others. Moreover, the well-designed LRF does allow for some flexibility of constitutionally mandated fiscal expenditures.

Coordination/coherence: States continue to use their tax systems to *compete* for business, so as a whole contribute to create an incoherent and volatile tax environment. The federal government, in its efforts to raise revenues has led to various low quality taxes. The 1988 constitution granted the states much a freer hand to introduce changes in their VATs. According to Werneck (2002) “Most of the uncoordinated changes were for the worst; they slowly transformed the pioneering, reasonably well-designed VAT scheme into a confusing disharmonic collection of 27 highly complex state tax codes. Competition to give generous tax breaks to investment projects has also been severe”.

Investment-related qualities/capacities: Tax administration has been continuously strengthened in the 1990s. A 2001 law allows bank secrecy to be broken for tax enforcement purposes. About 90 percent of personal income tax returns are filed via the internet, and all corporate income taxes are filed electronically. Brazil also has a relatively efficient tax collection system. Nonetheless, evasion has been facilitated by differentiated state tax systems and a cascading sales tax.

Public regardedness: There is a commons problem since every state tries to use its VAT tax rate to attract the best business, disregarding the macroeconomic effects. The result is the proliferation of other taxes and the pervasive use of exemptions, which result in considerable horizontal inequity. Indeed, the constitution establishes that there should be exemptions for religious organizations, unions, nonprofit educational and social assistance unions, paper, books and printing materials. There are also free trade zones and generous tax incentives for certain activities.

To sum, the tax policy process in Brazil has led to increasing tax revenues, as most expenditures are rigid and the executive is highly committed to macro stability. However, tax reform is not easy. The adaptability of revenues has favored temporary taxes, which lack the necessary properties of an efficient and coherent tax system. A structural reform has not been agreed by all the relevant players, although discontent with the current system is apparent. Consequently, it would be fair to characterize the

system as somewhat flexible, although inefficient and incoherent. Additionally, the large number of exceptions and special treatments question whether the policy is as *publicly-regarded* as it would be desired.

3.3 Chile

Key players and the PMPs

According to Aninat et al. (2005), Chile has a very powerful executive, with de facto control over the agenda and sole authority to initiate legislation in taxation. Legislators are professional and technically competent for Latin American standards. The electoral system has a twofold effect over the party system: it reduces the number of relevant actors by encouraging parties to coalesce and strengthens the national leadership of parties. The legislative electoral system does not have term limit provisions, which together with the need for candidates with strong local support encourages politicians to seek long legislative careers. Congress is bicameral, with supermajority thresholds required to change many laws (that enables various minorities to block policy changes) and, with the presence of Institutional Senators (nine non-elected senators appointed by different state institutions) and all former presidents who served 6-year long terms (lifetime membership in the Senate). Although there is an independent judiciary and non-partisan nominations, presidents nominate, appoint, and dismiss Supreme Court justices and one of the seven members of the Constitutional Tribunal with the senate's approval. The Constitutional Tribunal exerts ex-ante jurisdiction over legislation and sometimes is mandated to verify the constitutionality of legislation. The President directly appoints regional and provincial governors. Local governments (municipalities) have their own sources of revenues (land taxes and commercial permits) as well as resources that come through the Education and Health budgets. Municipalities are barred from borrowing by the Constitution. Perhaps the constitutional provisions that best reflect the strong powers vested upon the presidency are those governing the budget process, making Chile one of the countries with the most hierarchical budget institutions in Latin America (Alesina et al. (1999) and Vial (2001)). Moreover, the 1980 Constitution prohibits earmarked taxes. The bureaucracy is highly technical and relatively free from corruption even by the standards of the OECD. Table 16 shows the influence of key players in tax policy in Chile. It is important to highlight the importance of political parties in the decision making process.

In the area of tax reform, a reduction of tariff rates, a broadening of the VAT base and an increase in tax rates, as well as a reduction in the top marginal income tax rate were observed in Chile before other

countries in the region¹⁵. There are some taxes (excise tax on tobacco, surcharges on VAT for luxury vehicles and alcoholic content of beverages, jewelry, firearms, and a stamp tax, but they are relatively small). Import tariffs have declined markedly except for a few goods that remain protected: import tariffs are 6 percent for all goods not originating from countries with which it has a free trade agreement, but Chile imposes surcharges from time to time of between 5 and 24 percent. As with other reforms, the process was continuous. Due in part to healthy economic growth, and in part to measures put in place early to reduce evasion, as well as the virtual elimination of exemptions on the VAT, Chile has been able to maintain tax revenues above 22 percent of GDP since 1990.¹⁶

What distinguishes Chile's tax system from others in the region is: (i) minimal exemptions on all taxes (including a very small exempted personal income for income tax purposes); (ii) maximum profits tax rate is relatively low (16.5 percent) and payroll taxes are minimal; employers do not contribute to workers' pensions; (iii) although marginal tax rates for the personal income tax are progressive in nature, the real progressivity of the fiscal system is achieved through the expenditure composition, not the tax system. Chile has kept these principles in its tax system in the last 15 years. Legislation has worked to either change tax rates in some cases, as noted above, or 'fine tune' the system. The debate on tax reform is broad as there is significant and growing opinion from independent experts to which politicians and the public have easy access, as well as a rich economic debate in the media. Moreover, legislative procedures are relatively transparent. There are also a small number of veto players (President and bicameral Congress, with one party usually having a majority coalition). Politicians also have relatively long service terms (the president, who chooses his cabinet, serves for a period of 6 years, senators serve for 8 years, while deputies serve for 4 years). This encourages cooperative agreements, since the results of any reform most likely will be felt during a politicians' tenure, and electoral campaigns interfere less with policy decisions. Although the Christian Democratic Party has a majority in both chambers, both main parties are the sum of coalitions of smaller parties. Moreover, students, labor unions and other groups are relatively politically active, leading to policymaking processes where there is an incentive to reach consensus.

Outer features of the PMP in Chile

Stability: The tax structure has changed very little in the past 20 years. Reforms have been limited to some rate changes, so policies are very stable. The recent trend since 1990 has been to bring closer

¹⁵ There was a small increase of the profit rate in 2001, from 15 to 16.5 percent.

¹⁶ Chile is a centralized system, therefore municipalities collect only property taxes, motor vehicle duties and a few fees.

together the VAT rate and profit tax rate: The former was increased in 1992 from 15 to 18 percent, where it has remained ever since, and the latter was increased from 10 percent to 15 percent in 1993 and 16.5 percent in 2001. Moreover, as in other countries in Latin America, tariff rates have been reduced without policy reversals.

Adaptability: Chile recently adopted the idea of a structural budget balance, a policy designed not so much to be an automatic stabilizer, as much as a fine-tuning policy scheme in which tax rates are adjusted according to the state of the business cycle. This scheme, which allows for flexibility, requires extremely high quality statistics, good budgeting practices as well as a recent history of macroeconomic stability. The Copper Stabilization Fund and the infrastructure Fund are fully integrated into the budget. The lack of earmarking gives the budget more flexibility.

Coordination/coherence: Chile's division of responsibilities in policymaking and tax administration is clear, and because of the minimal exemptions, the system is simple and consistent and thus easy to administer.

Investment-related qualities/capacities: The tax administration is relatively strong. The revenue collection agencies (internal revenue, customs and Treasury) are governed by a framework law. Tax laws are relatively simple, and the president has the sole right to initiate them. Moreover, tax payers have clear rights and arbitration procedures. The staff running the regulatory the tax collection agencies tends to be more prepared, better trained and more professional than in other government agencies. Recently, all courts have been endowed with a tax unit to ensure a fair tax process as part of a larger reform of the judiciary.

Private versus Public Regardedness: As mentioned earlier, the process of debate about tax reform is fairly widespread, at the same time, special interests have not been able to step in and obtain exemptions¹⁷. The VAT tax of 18 percent is one of the highest in Latin America and has virtually no exemptions¹⁸. This is also true for the income tax: the exempted income is equal to 0.1 percent of per capita GDP, which is extremely low. The structure of the income tax is quite progressive but the highest marginal tax rate, at 25 percent, is not very high for international standards. The profit tax rate also has few exemptions (there are various clauses for small businesses, for example, vendors pay a portion of their sales). But the general principle is that everyone pays taxes.

¹⁷ With the exception of the military, a legacy of the Pinochet dictatorship, although this has been changing for the better.

¹⁸ Goods and services exempted are: mass transportation, schooling and charges of hospitals, imports by diplomats, donations to qualified institutions.

3.4 Colombia

Key players and the PMPs

According to Cárdenas et al. (2005), as it has been the case in most Latin American presidential regimes, an important number of constitutional prerogatives make the Colombian president the main agenda setter in most policy areas. This is true even after the 1991 constitution, which reduced presidential powers in a number of dimensions. The 1991 constitution deliberately curbed the legislative powers of the president by limiting to 90 days the declaration of either a state of internal commotion, or a state of economic emergency. These pro-tempore powers can be used to decree taxes, but decrees only remain in force after the emergency if congress enacts them in regular sessions. Legislators are, relative to the rest of the region, more specialized and professional, especially in the economic committees that deal with taxation. Incumbency rates for members of these committees are higher than for the rest of legislators. The symmetric two-chamber congress can be classified as reactive more than proactive, given the large legislative powers of the executive. Electoral rules (Hare system where the majority of seats are allocated to the largest remainders) generate incentives for parties to fragment into factions. The result is that parties have increased the number of lists over time, maximizing their seat share, while enhancing decentralization and fractionalization. The passage of legislation through congress has become more complex as a result of the increase in the effective number of parties. Since 1991, the Constitutional Court has been a key player in the policy-making process (it is more active and independent than its predecessor the Supreme Court). The main reason is that after the constitutional revision of laws many policy issues including taxes- have been elevated to the constitutional rank. Given the legislative procedure that a constitutional reform entails, transactions costs are now higher and the Court has a larger jurisdiction. Governors are not decisive in issues related to national taxes. As in Brazil, the Colombian 1991 Constitution is rich in detail and specificity, and many expenditure items are hard-wired into the Constitution. Like in Argentina, the Colombia bureaucracy is not powerful in the policymaking process. Political appointees have the real power. Table 17 shows the influence of key players in Colombia.

During the 1990s the size of the state, and its mandate, grew considerably. The public sector was relatively small for regional standards (aggregate expenditures and revenues of the consolidated public sector were around 20% of GDP between 1960 and 1990). Aggregate public expenditures grew to 33.7% of GDP in 2003 from 21.2% 1990, reflecting a deliberate intention to increase in the size of the state and use fiscal expenditures for redistribution. The fact that total revenues grew to 29.7% of GDP in 2003 from

20.6% in 1990, suggests that there has been a deliberate, although insufficient, effort to raise revenues in order to finance larger expenditures. The analysis of the contents of recent tax reforms, as well as the formal objectives established in the draft projects, confirm that the major objectives of the executive in the tax reform process have been the increase in tax revenues as a means of reestablishing fiscal balances. Even though the priority has been the increase in fiscal revenues, the draft tax reform projects submitted to congress have given importance to the structure of the tax system, an area in which governments have been only partially successful. There has been an increasing reliance on the VAT: the tax rate has increased from 10% to 16% through the various reforms since 1990. However, the most recent attempts to widen the VAT base or raise the rate have had very limited success, in part because the legislative assigns a great priority to the progressivity of the tax system over its efficiency, regardless of the progressivity of the expenditure structure. This has severely limited attempts by the executive to reduce the number of VAT rates and the exemptions.

In the area of income taxes, Colombia is characterized by very high income tax rates: corporate income tax rate is currently 38.5 percent, one of the highest in Latin America, in addition to high payroll taxes that are also among the highest in the region. Personal income taxes are a 35 percent flat rate. Nonetheless, the exemptions are very high. Enterprises receive tax exemptions for various reasons, while there is a very high exemption level for personal income taxes, about 4 times per-capita GDP. Consequently, very few pay direct taxes, but those who pay have an excessive share of the burden. As mentioned earlier, the average VAT rate has been increased substantially, nonetheless, in the last few years the tendency has been to increase the number of rates so as to make it progressive, thus distorting it considerably. Colombia's policy has also moved towards the reduction of trade tariffs and the elimination of export subsidies.

As a consequence of congress' reluctance to widen the income and VAT tax base, the executive has introduced new –and highly distortionary– tax sources. In 1998, a temporary 0.2% financial transactions tax was adopted through an emergency decree, which was raised to 0.3% and made permanent in the 2000 tax reform, and raised again to 0.4% in the 2003 reform. In the same vein, the Uribe government adopted, through an extraordinary internal commotion decree, a transitory net wealth tax earmarked to the strengthening of democratic security in Colombia. This tax was extended for three additional years in 2003. The conclusion is that revenue pressures have led to decisions that disregard the basic principles of an equitable and efficient tax structure.

The role of congress as a political actor in tax reform has been significant. While in earlier decades, congress largely rubber-stamped the tax reforms submitted by the executive, oftentimes through emergency legislation, its involvement in the design of tax packages has been increasing since the early 1990s. On the positive side, congress has been exemplary, to the extent that it has passed eight tax reforms since 1990. Also, congress has a solid group of distinguished members with knowledge and expertise on fiscal affairs who lead the debate and who are influential in the outcome of the legislation. On the negative side, congress could be partly blamed for the insufficiency of revenues that resulted from the reforms, for the increase in expenditures and for the deficiencies in the structure of the taxing system. An analysis of tax legislation submitted by the executive reveals that congress tends to water-down the proposals excessively during the debates, both in terms of revenues, but, more importantly, in terms of the quality of the reforms.

The growing involvement of congress in fiscal issues is also illustrated in the significant number of sponsors that are assigned to the analysis of the draft proposals from the executive. As discussed above, the interest in becoming sponsor also has to do with the distribution of pork, or with benefits obtained from the private sector as a result of political favors. The Constitutional Court has also been a significant actor in tax policy outcomes. Tax issues have represented around 10% of the total legal claims on economic matters handled by the constitutional court since 1991. In 1999, the ruling on the financial transactions tax limited the scope in the use of resources. More recently, the constitutional court denied the approval of the generalization of the VAT and the taxation of specific activities. At the same time, the Constitutional Court has given its full legal support to important economic reforms.

In sum, tax reforms have been frequent (one reform every 20 months since 1990), have raised more revenues although at the cost of increasing the distortions of the existing tax system never closing the gap with expenditures. The situation of tax reform in Brazil and Colombia are very similar: in trying to get around the rigidities imposed by the constitution and deal with the immediate fiscal imbalances, the resulting 'reform' ends up introducing temporary patch-up revenue mechanisms that complicate and distort the system further.

Outer features of tax reform in Colombia

Stability: There has been a fairly steady increase in tax revenues, but recently there have been some policy reversals suggesting volatility: more exemptions, making the financial transactions tax permanent

and continuing with the practice of many VAT tax rates. Temporary taxes tend to become permanent after a year or two of their creation.

Flexibility: The important role of the courts in reviewing fiscal legislation has contributed to the rigidity of tax policy. Moreover, the importance the legislative gives to the progressivity of the tax system, and the very small component of the budget that is discretionary (about 19 percent) means that there is a tendency to pass tax reform that increases the rates for a small group of the population while exempting many others.

Coordination/coherence: While tax reform in Colombia has achieved an important increase in tax revenues to GDP since 1990, the system has become more complicated and distorted, and efforts to correct those distortions by the executive have sometimes led to others. There is also very little consistency between reforms.

Investment-related qualities: There is also a low capacity to adopt reforms that solve long-term problems with measures that have short-term upfront political costs, but high long-term payoffs. In other words, low investment qualities of tax reform. Although tax administration has consistently modernized, it is expected to handle an increasingly complicated tax system, which coupled with substantial payroll taxes may undermine the ability to effectively collect taxes.

Public regardedness: There have been important efforts in all aspects of fiscal policy to improve vertical equity, to the detriment of a serious erosion of horizontal equity, that is, a narrowing of the tax base. This has occurred not only because of exemptions, but because of the persistently high informal sector, which is outside of the tax network.

3.5 Costa Rica

Key players and the PMPs

Costa Rica has the longest history of democracy of any country in Latin America, with a centralized, presidential system. Unlike many Latin American countries, however, the legislature and judiciary effectively check the power of the president. The executive is constitutionally weak, as it has limited decree powers and cannot convene referenda single-handedly. Therefore, presidents use their partisan

powers to overcome constitutional limits on their authority. Because the legislative branch wields actual power, the composition of the legislature is important. Despite having proportional representative elections, Costa Rica evolved into a two-party dominant system. The two major parties, National Liberation (PLN) and Social Christian Unity (PUSC) have won, on average, 90% of the seats in the past five elections. However, parties not aligned with the PLN and PUSC won 37 percent of the vote in Congress.

The constitutional court has 22 magistrates elected by Legislative Assembly for renewable 8-year terms. A Constitutional Chamber of the Supreme Court ('Sala Cuarta'), established in 1989, reviews the constitutionality of legislation and executive decrees and all habeas corpus warrants. Additionally, the offices of the Ombudsman, Comptroller General, and Procurator General assert autonomous oversight of the government and interfere often in the policy-making process with considerable scrutiny, thus micromanaging checks and balances. As is often the case in small countries, subnational governments have very little power in national politics. In contrast, the bureaucracies in some public enterprises and the social security are relevant players and exercise some power. Table 18 shows the influence of key players in Costa Rica.

Revenues to GDP have oscillated between 10-12 percent of GDP since 1990, but have not grown beyond that, reflecting the slow process of reform. As in other Latin American countries, one of the obstacles to introducing certain taxes has been the Constitutional Court (Sala Cuarta). For example, most of the provisions of the 1994 tax reform –which increased the ability for the administration to sanction tax evaders, introduced the wealth tax, and allowed cross-checking of firms in the direct taxes chain- were declared unconstitutional.

The increasingly larger number of veto players, as well as somewhat weaker than average presidential powers has also contributed to the protracted processes of tax reform. Nevertheless, the process itself is democratic enough to lead to outcomes that are the product of a consensus. Veto players include various special interests or small groups that may be interested in blocking reform, and their petitions receive an audience from the constitutional court, however small the petition. The same is true for businesses located in the free-trade zone area, which have contributed greatly to economic growth.¹⁹

¹⁹ Costa Rica has had much success in attracting foreign direct investment, which is based in free trade, tax-free zones. The most prominent investment by far is the Intel plant which accounts for about 25 percent of exports and pays no taxes. Lack of taxation to FDI explains in part why the current fiscal situation is unsustainable.

The fundamental structure of taxes in Costa Rica has been changing for the better, but slowly. The income tax has not suffered much change. With regards to the sales taxes, there have been various frequent changes in the 1990s. The base has widened, albeit very slowly, and still does not include services in a systematic way. The VAT rate was changed several times between 1991 and 1996 (as planned), and in 1997 it was left at 13 percent, which explains why the VAT has been taking on an increasingly important role (it generated 45 percent of total tax revenues in the late 1990s from 30 percent in 1990). The opposite has occurred for tariffs, which have been successively reduced: the contribution of international trade taxes has fallen from 29 percent of revenues in 1990 to 7.3 in 2002. Although the average tariff has declined considerably (about 6 percent now), as in many Latin American countries, the effective tariff still tends to be higher for agriculture. There are also still export taxes on coffee, bananas, meat and cattle. With respect to excises, in 1994, in the context of a negotiating agreement denominated 'A Reasonable National Agreement', the government proposed to reduce the coverage of the excise tax from about 1500 goods to 700, and finally to 100 a year later. It took 4 years to actually get started, and the proposal finally passed with the 2001 *Law on Simplification of Tax Administration*. Some efficiency in tax collection has been achieved, albeit at a very slow pace. Another positive development has been to reduce the number of fuel taxes to one.

According to Cornick (2003), there is a consensus among leaders that the fiscal situation therefore needs to be addressed on the revenue side, as i) non-discretionary spending exceeds tax revenue by about 50 percent; (ii) expenditures are relatively low in terms of GDP; and (iii) adjustment of the budget has typically occurred through cuts in infrastructure spending. The problems of the low revenue and inefficiency of the tax system were the starting points to a national dialogue in the late 1990s. A group of ex-ministers of finance were commissioned to write a report looking at the fiscal problems in Costa Rica, and based on this report a well-lauded reform law was elaborated (*Proyecto Ley de Ordenamiento Fiscal*), which was introduced at the end of 2003 and continues to be discussed in the legislative assembly. The desired changes include using global as opposed to territorial income for income taxation purposes (the difference can be large for Costa Rica), taxing income from self-employment, pensions and dividends, establishing a uniform tax rate within and outside the free trade zones, transforming the current sales tax would change to a regular VAT system and services would also be taxed. In addition, the number of goods subject to an excise tax would be reduced to a minimum and a national tax agency would be created.

Given the urgent need to resolve the fiscal issue, a temporary, contingent law was introduced which would temporarily raise revenue while the more structural *Ley de Reordenamiento Fiscal* was

discussed in Congress. In December 2002, the *Fiscal Contingency Law* was approved with revenue measures amounting to 1 percent of GDP. However, it included a series of measures that exacerbated the distortions of the tax system. For example, a tax amnesty was installed for tax obligations prior to end-September 2002, eroding incentives for future compliance by tax payers. The law also introduced for 12 months a series of small new taxes and surcharges aimed at specific bases, for example, a 50 percent surcharge for luxury vehicles, an increase in taxes due for financial institutions operating a bank outside the territory (mostly with offshore branches), and an increase in the income tax rate of between 1.5 percent and 6 percent depending on the source. These measures not only reduced the quality of the structure of the tax system, but also eroded horizontal and vertical equity. Moreover, some of the taxes contemplated (such as for motels and cigarettes and alcoholic beverages) were earmarked to certain expenditures, increasing spending rigidity and not contributing to reduce the fiscal deficit. The *Fiscal Contingency Law* also increased authorization to the tax administration unit to reassess wage scales and buy new equipment.²⁰ The explicit decision to postpone a more structural reform poses the risk that the contingent measures in the Law will take on the air of permanence with the passage of time. It is not yet clear whether the permanent Law on Fiscal Reorganization will be able to pass before 2006 when the election campaigns begin.

Outer features of PMP in tax reform in Costa Rica

Stability: The reform process is stable and somewhat predictable. The political stability, which has attracted FDI and tourism, has also led to the preservation of certain policies beyond the tenure of certain officeholders, in many cases distortionary policies. The reform process is extremely slow and gradual, mainly because of the slow-moving consensus-building process. Despite Costa Rica experiencing many of the economic problems of the region (debt crisis, trade integration, financial liberalization) the policy making process has remained stable.

Adaptability: Very slow adaptability, and rigidity fuelled by inertia. Revenue earmarking is an issue in Costa Rica:²¹ tax revenues equal to 8.8 percent of GDP are earmarked to specific expenditures, out of a total of central government tax revenues of 13.4 percent of GDP in 2002. One of the biggest barriers of the very democratic political system is the difficulty of quickly arriving at a consensus: various factions of civil society are typically included in the discussion of reform, and the disagreement of a minority can be

²⁰ Nonetheless, the approval of these measures under the Law was more symbolic than substantive, as they could have been approved by the Executive without going through the legislature.

²¹ Costa Rica has two kinds of earmarking: i) constitutionally-mandated earmarking for education (6 percent of GDP) and the judiciary (6 percent of tax revenues or 0.8 percent of GDP); and (ii) legally-mandated earmarking in a number of other areas, totaling almost 2 percent of GDP.

given excessive weight. For example, if someone does not agree with a small aspect of a Law, even just a regular citizen, they are allowed to make their voice heard with the 'Sala Cuarta', which not only resolves constitutional controversies, but also can prevent bills from becoming law while they work themselves through the legislative process. Although policymakers understand the difficult fiscal situation since the early 1990s, actual reform has been minimal.

Coordination/coherence: There is a good consensus-building process, thus policies that are adopted are democratic and thus cohesive in nature. While policy coherence remains reasonably high, political coordination seems to have declined through time. In tax reform, there is a somewhat incoherent situation: the Fiscal Contingency Law, enacted temporarily, has complicated greatly tax revenue collection, since the deficiencies that already existed in the system were exacerbated, such as the reduced VAT tax base and the excessive number of excise and selected taxes. The tax system has thus become more difficult to administer, partially offsetting any measures included in the *Fiscal Contingency Law* to improve tax administration. The resulting system is also very inefficient: A study by Bolaños (2002) estimates the deadweight loss around 28 to 30 percent of revenue collected.

Investment-related qualities: Tax collection also remains rigidly low. Nonetheless, there have been gradual improvements in tax administration and the reform process is moving in the right direction. In 1992 and 1996 there was a new impetus towards modernizing tax administration, which was reorganized into four divisions: administration, collection, auditing and support services. Although there were improvements in all these fronts, there were still persistent problems of the quality of human resources, inefficiencies and insufficient financial resources. A recent IMF report noted that tax administration needed to be strengthened considerably, and urged the adoption of an action plan to tighten control of large taxpayers, improve cross-checking between taxes, and the give tax agency special powers to collect tax arrears. Nevertheless, although tax collectors and auditors now have the legal ability to sanction, in practice the administration does not possess the ability to be more pro-active in the collection process, and they have difficulties accessing information from the financial system. Recently they granted legal immunity to tax officials in matters pertaining to the conduct of their official duties.

Public Regardedness: Policies are publicly regarded as a result of the democratic tradition. Although the tax system is not broad and biased in favor of free trade zones, most Costa Ricans recognize that there has been an economic benefit from being hosts to companies in free trade zones. In terms of the redistributive aspect of the tax system, on average it is neutral but it can vary from year to year. However, if public regardedness in this context was defined on the broadness of the tax base, there is still substantial room

for improvement in Costa Rica. An IDB study by Cornick (2003) attempted to estimate the increase in revenues resulting from a complete widening of the base of various taxes without increasing tax rates. As is the case in various countries, the hypothetical revenue gains of widening the VAT are substantial, (while leaving the rate at 13 percent); Cornick calculates this would yield almost 4 percent of GDP. Similar gains are calculated if the other bases are widened.

3.6 Guatemala

Key players and the PMPs

The last two to three Presidential elections, which occurred after the signing of the peace accords, have been democratic, although a variety of procedural obstacles have historically reduced participation by poor, rural, and indigenous people. The unicameral Congress has 158 seats (the number of seats increased from 113 to 158) elected for four-year terms. The 1993 constitutional reforms increased the number of Supreme Court justices from 9 to 13, reduced the terms of office of central government branches of government and increased the term in office of mayors from 2 ½ to 4 years, thus in principle increasing the number of veto players. There are serious and worsening public corruption problems. Table 19 shows the influence of key players in Guatemala

The 1996 Peace Agreements defined the objectives of fiscal policy, finally materialized in the 2000 *Fiscal Pact*. The general goal of the *Fiscal Pact* was to increase the fiscal income in order to finance the necessary expenditure for the country's social development. The most important commitments introduced by the by the *Fiscal Pact* in terms of tax policy included enacting a reform in 2000 (which did not occur) in order to establish a stable, simple and certain tax system. A 12 percent of GDP tax burden should be achieved in 2002, and by 2001, the non-tax revenues should not exceed 15 percent of the total revenues. The tax exemptions, exonerations and other special treatments have to be approved explicitly by the parliament or eliminated. The tax system should be progressive, and in order to promote more confidence along the contributors, an Ethics Code should be implemented among the tributary authorities in 2001. Other similar administrative commitments were subscribed.

President Portillo's landslide victory in 1999 suggested possibilities for rapid legislative action. However, under the Guatemalan constitution of 1985, passage of many kinds of legislation requires a two-thirds vote. Passage of such legislation was not possible, therefore, with the president's party votes

alone. In 2001 the government attempted to increase several tax rates in 2001 in an attempt to meet the *Fiscal Pact* target of increasing its tax burden (at about 10.7% of GDP, currently the lowest in the region) to 12% of GDP. However, protestors took to the streets massively when the government sought further increases in August 2001, declaring their opposition to any new taxes until the Portillo administration provided better accountability for the taxes it already received.

Most of the recent literature on Guatemala's tax system agrees that few of the Pact's objectives have been achieved entirely. Although the tax burden has increased, the main goals established by the Pact have not been reached. While in 1995 the tax revenues represented roughly 8 percent of GDP, in 2002 the tax burden reached a historical high point at 10.6 percent of GDP (falling to 10.3 percent in 2003). Even so, Guatemala is below the Latin American average. The tax reform implemented during 2000-2003 did not contribute significantly with fulfillment of the other five commitments subscribed in the *Fiscal Pact*. For instance, few of the tax exemptions were eliminated, leaving effective special treatments inspired by the Constitution toward specific sectors. The *Superintendencia de Administración Tributaria* (SAT) estimates that in 2001 the value of the exemptions reached 8.7 percent of GDP.

The distribution between direct and indirect taxes has not changed significantly since 1996. Indirect taxes contribute with approximately 75 percent of the total tax revenues. Moreover, the VAT by itself contributed with roughly 49 percent of the tax revenues. The VAT rate was raised several times: from 7 to 10 percent in 1997 and to 12 percent in 2001. Revenues from indirect selective taxes have always been very low because they apply to few goods (fuels, petroleum derivatives, tobacco, and alcoholic beverages). The ISR (*Impuesto Sobre la Renta*) and the IEMA (*Impuesto a las Empresas Mercantiles y Agropecuarias*) represent almost the totality of the revenues from direct taxes. Among direct taxes the IRS has been the most important, although its participation in the direct tax revenue fell from 74 percent to 51 percent between 1996 and 2003. With the purpose of elevating direct tax revenues in 1998 the IEMA was created. Between 1998 and 2003 its participation in the total direct tax revenues rose from 30 to 51 percent. However, the IEMA was eliminated in February of 2004 by the Constitutional Court. As a result of this decision the direct tax revenues fell approximately 50%. Moreover, this setback on the objective of the tax burden augmentation implies the future inability of fulfilling the commitments subscribed in the Peace Agreement and the *Fiscal Pact*. The IEMA fell because the private sector filed a claim to declare this tax unconstitutional. This event reveals the weakness of the tax power of the government vis-à-vis the organized private sectors. The private sector's opinion is that the IEMA generated severe distortions that affected the efficient distribution of resources in the economy, and that the fiscal problem should be resolved through a reduction on public expenditure. Furthermore, the

organized enterprise sector considers that the inefficiency and corruption within the government has to be blamed for the failed attainment of the *Fiscal Pact* objectives.

Outer Features of the PMP in Guatemala

Stability: The breach or partial fulfillment of most of the commitments assumed by the Government in the *Fiscal Pact* has caused an atmosphere of economic uncertainty. Yet, the fact that the objectives established by the *Fiscal Pact* have not been modified, gives some grade of predictability.

Adaptability: Low adaptability and inflexibility. Guatemala's tax policy is not designed to respond to the state of the business cycle. Further, the guidelines established by the *Fiscal Pact* frames the tax policy towards a constant expansion of revenues in order to support the expansion of the social development expenditure, and toward a more progressive tax structure. Still, the achievements of the Pact's goal have been minimal.

Coordination/Coherence: Lack of coordination between the government and the private sector, and within government tax-related entities, has been present in the tax policymaking process. As mentioned, the private sector has gone in the opposite direction of the objectives established by the *Fiscal Pact*. This is a clear sign of the lack of coherence between the policies proposed by the government (following the dispositions of the 1996 Peace Agreements) and the interests of the private sector. There has also been a somewhat unusual but stark lack of coordination in the tax collection process. Studies about the performance of the fiscal administration in Guatemala reveal that before 2001 there was a remarkable absence of coordination between the SAT (the agency in charge of tax collections) and the Ministry of Public Finances (MPF) related to the elaboration and the revision of revenue estimates. This was translated, among other things, in a divorce between the tax goal formally presented by the MFP to the Congress of the Republic for its discussion and approval, and the goal that was used for the programming within the SAT.

Investment-related qualities/capacities: The tax administration in Guatemala has improved greatly after the institution of the SAT in 1998. The SAT has managed to establish firm bases for an effective tax administration. Nevertheless, the SAT is a relatively new institution and needs to work in several fronts to consolidate an efficient and productive tax administration. It has to develop better revenue collection mechanisms, a larger department for tax fraud investigations, and better coordination mechanisms with the MFP.

Public regardedness: Interest groups have played an important role in shaping tax reforms²², and their influence may have contributed to its slow application. Interest groups have obtained exemptions and special treatments. The SAT has estimated that the exemptions in 2004 would be 12.5 percent of GDP. In addition, the tax system does not seem to be moving towards a more progressive structure. According to *Instituto de Investigaciones Económicas y Sociales* (2004), the elimination of the IEMA illustrates how “businessmen, being a dominant social class, through history have known how to get rid of the direct fiscal loads imposed by the State”.

3.7 Mexico

Key players and the PMPs

According to Lehoucq et al. (2005), with the demise of the PRI, the president has lost its ability to direct policy change. The Mexican constitution makes the president more of a guardian of policy status quo than a promoter of policy change. However, the role of the president has not been limited to merely initiating legislation and waiting for Congress to generate new bills. By appealing directly to public opinion and wielding his veto, the president can shape the content of policy change. Until the 1990s, centralized nomination procedures and the ban on legislative reelection made senators and deputies dependent upon placating the demands of the president and of the corporatist sectors within the PRI. With a divided government, Congress has taken on a more proactive role in lawmaking that has changed the role of standing committees in the legislative process. Nevertheless, career incentives have not changed significantly with democratization and parties remain highly disciplined in contemporary Mexico. The prohibition on consecutive reelection still impairs Congress’s capacity to develop legislation.

After the 1994 constitutional reform, the Supreme Court continues to act, from time to time, as a veto player in the PMP. It does not appear to be ruling disproportionately in favor or against the government. What tends to happen is that when divided government persists and control over the presidency rotates among parties, a more experienced supreme court gradually shifts from being a veto player to being an impartial enforcer of inter-temporal agreements among parties. Unlike Argentina or Brazil, where national leaders render service to state-level elites in exchange for support of executive-

²² The most important groups are the Agrarian Owners Group or UNAGRO; Alliance Against Impunity or AAI; Committee for Campesino Unity or CUC; Coordinating Committee of Agricultural, Commercial, Industrial, and Financial Associations or CACIF; Mutual Support Group or GAM, and various other enterprise associations, civic and academic organizations.

based programs in the legislature, Mexico's municipal and state governments are not veto players in the PMPs. Although regional expenditures account for a large share of total government spending, local governments are highly dependent on federal revenues to fund their programs, as in Colombia. Constitutionally (see art. 115), state governments determine their own tax laws and collect revenue within their jurisdictions. Any taxes not reserved to the federal (or municipal) governments are fair game for states. States must finance municipal governments, but municipalities are free to impose some taxes not reserved to the federal government. The top-level bureaucracy exerts considerable political and economic power. The centralized PMP of the PRI era generated an asymmetry in its bureaucratic bodies. On the one hand, the presidential groups of the PRI era rewarded bureaucratic specialization on two top-level fronts: experienced political operators of the PRI, and highly educated policy and public management experts in the federal administration (Camp, 2002). On the other hand, middle and lower level bureaucracy is highly centralized, hierarchical, and overly regulated. Their human resource practices are mostly discretionary and not transparent. Table 20 shows the influence of key players in Mexico.

The tax policy and tax administration reforms introduced on the late 1980s and early 1990s established in Mexico a modern tax system comparable to other OECD countries. In the area of income taxation the reforms included the complete indexation for inflation, the integration of the personal and corporate income taxation (in order to avoid double taxation of dividends), and the creation of a minimum tax on gross assets. The structure of indirect taxes (VAT and excise taxes) is considered adequate, with tax rates similar to (or slightly below) international standards. With the reforms nuisance taxes were eliminated. Income taxes (personal, corporate and the gross asset tax) are the most important source of revenue for the federal government, representing 31 percent of total federal revenues in 1998. In 1998 VAT revenues represented 22 percent of total federal revenues. Hydrocarbon duties paid by PEMEX and excise taxes are also important.

However, the reforms did not improve the tax system's performance in its ability to raise adequate revenues. Tax revenues fell from 13,3 to 11,6 percent of GDP between 1990 and 2001, which is the lowest level of tax revenues in relation to GDP among the OECD countries (and lower than many developing countries).²³ Many factors are mentioned as potential causes of the steady deterioration in the tax effort. Martinez-Vasquez (2001) mentions three particular factors that, with varying degrees of importance, may account for the persistently low revenue performance. First, the structure of the tax system, and therefore its revenue capacity, economic neutrality, and fiscal equity, has been undermined by isolated ad hoc policy measures such as the special regimes for several economic sectors (including all

²³ This reflects in part the significant non-tax petroleum revenues, which mean it can afford such low tax collection rates.

agriculture and transport), the use of a compensatory system that complicates the personal income taxation, and the zero VAT rates for a wide list of domestic goods and services (including agricultural goods, foodstuffs, medicines and agricultural equipment). Second, the tax administration service has simply failed to modernize and, indeed, may have gone backwards in some of the institutional improvements achieved during mid 1980s. According to the estimates of the *Secretaría de Hacienda y Crédito Público* (SHCP), between 1985 and 1998 tax evasion of the VAT has represented around 30 to 46 percent. The level of evasion for the VAT reached a high point of 59 percent in the first half of 1996. Third, the Mexican authorities have pursued an implicit policy of keeping tax effort (the ratio of revenues to GDP) in the country at a relatively constant level. Increases in revenues (from a response to economic growth, the enlargement of the tax bases, or an increase of petroleum related revenues) are followed by policy measures such as tax rate cuts or special regime granting. (and sometimes the relaxation of tax administration effort). The private sector has supported too the idea of maintaining this relatively low tax effort.

Outer Features of the PMP in Mexico

Stability: Although there have been several tax reforms in Mexico (seven between 1990 and 2001), few of them have been major reforms, and changes on the tax structure have been relatively small. Reversals of tax reforms, like changes on the VAT rate, have responded to economic events and not political events. This means that the Mexican tax policy can be considered stable and predictable.

Adaptability: Indeed, tax policy in Mexico has responded to economic fluctuations (positive and negative). Yet, it cannot be regarded as an efficient built-in stabilizer for the economy. Tax policy adjustments have been possible following economic changes, though some of these adjustments have tended to dampen economic business cycles.

Coordination/Coherence: There seems to be a high coordination among different tax related political actors within the government. Nevertheless, as Martinez-Vasquez (2001) explains, “Mexico’s business elites appear to have been successful in blocking any permanent increases in the overall level of tax effort”. For instance, Berensztein (1998) concludes that the political factors that determined the success of Mexico’s tax reform in 1988-1994 were an economic crisis, the formation of a strong supporting coalition and preventing the formation of an opposing coalition.

Investment-related qualities/capacities: Tax administration efficiency is low. Tax evasion levels, and the perception of the inefficient revenue spending evidence a weak enforcement system and a legal certainty for taxpayers.

Public Regardedness: Some of the principal characteristics of the Mexican tax system lead to doubts as to whether the tax policy is publicly regarded. The extensive amount of exemptions toward specific sectors and special interest groups show a high horizontal inequity in the tax system. High levels of tax evasion augment the fact that the tax system is not taxing equally individuals with the same income level.

3.8 Paraguay

Key players and the PMPs

According to Molinas et al. (2005), the 1992 Constitution reduced the president's formal powers. The president can enforce policies unilaterally only if congress fails to address an urgent bill within sixty days, and his line-item veto can be overridden by an absolute majority of congress. There is no evidence of executive dominance in the key policy arenas for structural reforms. The executive dominates the formulation of nation-wide policies and policies related to the public sector (constitutionally, the executive has gatekeeping power over the initiation of the budget). In contrast, congress dominates the production of individual-level and local bills, and more surprisingly, the production of bills targeted to the private sector. Although congressional re-election is not banned by the constitution, the electoral context marked by competitive primaries, increasing party factionalism, and new political parties have created greater uncertainty about the political survival of legislators. Senators also are more representative of the economic elite, as many are involved in agro business. In other respects, the Paraguayan bicameral system is highly congruent—meaning that the partisan composition of the House and the Senate is usually quite similar (Lijphart 1999; Llanos 2002).

The Judiciary is autonomous in theory, but in practice highly politicized and hardly competent. According to a survey conducted by the World Bank Institute in 1999, the Judiciary's institutional performance is relatively poor and its functionaries are perceived as being particularly corrupt (Plan Nacional Anticorrupción 2000). Historically, partisan politics in Paraguay has centered on the competition between two nineteenth-century organizations, the Colorados (or National Republican Association, ANR) and the Liberals (nowadays called Authentic Radical Liberals, PLRA). Smaller

middle-class parties (Encuentro Nacional, País Solidario, and Patria Querida) and a Colorado splinter (Unace) have been able to capture increasingly more seats in congress. At the same time, the “granitic unity” of the parties during the Stroessner era has given way to factionalism and increasing internal competition in the form of primary elections to define the candidacies and the composition of party conventions. Therefore, the cohesion of Paraguayan parties at the present is quite low. The 1992 Constitution facilitated the incorporation of new players into the policymaking process—and thus multiplied the number of veto points. The former 1949 constitution gave the executive branch excessive powers. Paraguay has not been able to develop an effective, relatively independent, yet accountable, bureaucracy. Public hiring practices are characterized by a high degree of patronage and arbitrariness. At lower levels, its main consequence is that the Paraguayan bureaucracy is plagued by corruption. Table 21 shows the influence of key players in Paraguay

Paraguay’s tax system has low rates, large exemptions and very high evasion rates (between 45 and 55 percent estimated for the VAT (IMF, 2004)), the latter reflecting a very weak and poorly-financed tax administration and a very high level of informality of the economy. Since 1990, when Paraguay transitioned to a democracy and witnessed the opening up of trade of its large neighbors, Argentina and Brazil, the paradigm from the previous 50 years of smuggling has broken down. Among the early reforms to address the large level of informality was tax reform legislation, Law 125/91. There was no personal income tax, and it was not particularly hard for small businesses to be exempt from the VAT. Initially the law had two features: it afforded considerable flexibility to the executive, who could decide which articles to apply, in some cases, the executive could decide the rate and the base of various tax rates to apply according to some parameters set out in the law. Nonetheless, various aspects of the law and its regulations were ambiguous and thus open to interpretation, and a series of laws amending Law 125/91 over the following decade (about 42 up to 2002 according to the World Bank (2003) added exemption after exemption, in particular to the industrial sector. The largest was the 5-year tax holiday on all taxes for firms that presented reasonable investment projects, even if they were never carried out. This clearly allowed any firm to be eligible for the tax holiday, and to continue reapplying.

The tax system displays large horizontal inequities. Although the profit tax rate was 30 percent, it was estimated that average firms effectively paid a tenth of that as a result of the exemptions and quasi-legal alternatives. Moreover, the politically and economically powerful agricultural class, represented in the government and Congress, prevented the update of land values for statutory purpose: land taxes are based on the assessed fiscal value of the property, yet the tax base value of agricultural land was on average only 5.6% of its market price (Molinas, 2004). The agricultural sector directly contributes less

very strong bargaining position to support the Law conditional on certain features alien to its special interests being removed. It became the main veto player. In the end, the Law was relatively watered down compared to its original form. The share of taxes to be paid by the agricultural sector increased, but was still relatively small. Nonetheless, it was estimated to increase the tax revenue yield by 1.3 percent of GDP in the long run (IMF, 2004) through its significant broadening of the tax base and the elimination of some egregious exemptions.

Although the new Law (*Ley de Reordenamiento Administrativo y Adecuación Fiscal*) clearly moved in the right direction, in practice, the traditional pressure groups continue to lobby for the postponement of some of the aspects of the law (the executive has the power to decide the timing of implementation of the articles of the law). Even before the tax law went into effect, the new government was able to increase tax revenues by 40 percent between August 2002 and 2003, in part due to some efficiency measures, but mostly as a result of better compliance and a reduction of internal corruption of the institutions.

Outer features of Paraguay's tax policies

Stability: Paraguay is a case where the characteristics of the former stability of economic policies, basically dictated by a small group of the ruling class, shifted completely to bring forth instead a much more democratic but stable process, where the various actors were forced to negotiate much more. Clearly the earlier form of stability was not desirable, (as there was no incentive to cooperate with other interested parties excluded from the political process)

Adaptability: Both the 1991 law and the 2004 tax laws give the executive branch some leeway in adapting the tax regime to given circumstances. For example, the law allows the executive to apply the Financial Transactions Tax at will, or to apply some articles of a law first and others later. De facto, however, the ability or willingness of the government to exercise that flexibility has not always existed in Paraguay, as there was not enough experience with democracy, nor enough fiscal problems for governments to ever feel the pressure to have to change the course of the slowly eroding tax base.

Coordination/coherence: The tax regime is full of loopholes and exceptions.

Investment-related qualities: Minimal resources for operation and inadequate wages and working materials for tax agents contributed to breed corruption within it. In that sense, the tax administration

lacks resources and independence. The recent successes in tax collection mentioned above are not sustainable unless the resources and powers of the tax administration are increased and maintained.

Public regardedness: The tax system has been prey to special interest, especially landowners.

3.9 Venezuela

Key players and the PMPs

According to Monaldi et al. (2005), since the approval of the 1999 Constitution the presidency has been significantly powerful. The president has the power to call for popular referendums to approve or eliminate laws, approve constitutional reforms, or call forth a Constitutional Assembly. As a by-product, the constitution is now extremely easy to change, if the executive is willing to do so and has the necessary popular support. Legislators are elected through proportional representation, but a small portion of the legislators are elected by plurality. Between 1989 and 2004, legislators have become less disciplined but more specialized. Factions within parties, and individual representatives, have been able to undermine the power of party barons on specific policy issues. The legislature has been able to play a more significant role in initiating legislation due to the decline of party elite agreements. The fragmentation of the party system and the decline in party discipline undermined the strong grasp that national party barons exercised over the judicial system. The Court took a more politically autonomous and activist role. During the Chávez presidency the government has generally controlled the Court that was appointed by the Constituent Assembly with an overwhelming government majority. Moreover, in 2004 the Chavista majority in the legislature passed a new Supreme Tribunal law adding new magistrates in order to obtain a firm grip on the Tribunal decisions. Key decisions at the national level (either by Congress or by executive decree) have to be negotiated with regional actors. The quality of Venezuela's bureaucracy has deteriorated and is clearly at the very bottom of the region. Table 22 shows the influence of key players in Venezuela.

Before 1990 there was essentially a balanced budget rule which meant that if oil income decreased, the government had to decrease expenditures. Non-oil fiscal taxation remained relatively low and stable (Santos, 2003), covering a very narrow group of economic agents through a relatively simple administrative structure. There was a favorable environment for long-term cooperative agreements. However, this stability was based on the existence of increasing or steady oil revenues (and to some

extent the fixed exchange rate). Once the oil revenues began to decline in the 1980s the stability turned into inflexibility. The subsequent administrations therefore found it hard to keep up with the fiscal rule and began to run deficits and acquire debt. Political instability also became commonplace, and it was hard to pass reform. By 1993 the government was facing a large fiscal deficit and so a tax reform was approved, which increased progressivity and introduced a VAT at 10 percent. However, in order to obtain the legislative support necessary to pass the law, a large share of the VAT revenues had to be earmarked for a special fund to finance the investments of regional governments (FIDES). For the first time in Venezuela's history, the governors and mayors had become a powerful force in the national legislature²⁴. The following administration, of Caldera came in the midst of some reforms and liberalization, but increasing economic and political instability. Public disputes between the executive and the legislature were common and tax reform was not allowed to pass. Nonetheless, by 1996 the economic deterioration, as well as special powers granted to the executive following the 1995 banking crisis, allowed Caldera to undertake some tax reforms, namely, an increase in the VAT to 16.5 percent. However, once again, concessions on the expenditure side almost counteracted any fiscal improvements that the tax rate increase could have generated. In particular, it was established that at least 15-20 percent of VAT revenues had to be transferred to the states, and the package included generous wage increases to the public sector.

During the Chávez administration (1999-present) policies have become more volatile and incoherent than ever before, in part as a result of political instability. There has been a reversal of many reforms implemented during the previous administrations. In particular, in 2003 a law passed which increased the number of income tax brackets substantially (the highest at 34 percent), and between 50-60 percent rates for profits from petroleum exploration. The VAT was left at 15 percent in August 2004 (8 percent for some agricultural imports). Cabinet turnover has significantly increased, while governance and institutional quality has dramatically declined (Monaldi, 2004).

Outer features of Venezuela's tax policies

Stability: Venezuela moved from exemplary stability, through a slowly degenerating political process, to extreme volatility. Even though an effective tax reform has been elusive, tax policy has been very volatile. Since 1992 the income tax law has been reformed five times, the value-added tax nine times, and

²⁴ Venezuela is a federalist state. Most subnational government revenue is oil-related: in addition to receiving 20-25 percent of total central government revenues through various schemes (i.e., the income tax), subnational government get 20-30 percent of oil royalties.

the tax on banking transactions has been “temporarily” established four times (Briceño, 2002). Part of this was the result of a higher level of involvement by the political actors.

Adaptability: Low adaptability. Some flexibility built into oil revenues but not in the case of non-oil revenues. When confronted with difficult fiscal problems, the policymakers have retracted instead of adapting the reforms.

Coordination: Until recently, coordination between the executive and congress was extremely difficult. Concessions have been made to achieve small change in the tax system, indicating that there was not much coherence in the policy-making process. Although the revenue-sharing system increasingly benefits the states, the regions seem to be in perpetual discontent about the arrangement and the amount of taxes allocated to them.

Investment-related qualities/capacities: Political instability has meant that there is considerable uncertainty as to whether a given tax policy will endure. Some authors point to the significant reduction in the quality of policy-making since the late 1990s.

Public regardedness: Moreover, the reversal of various market-oriented reforms has occurred with a bias towards the public sector (possibly patronage), and not necessarily benefiting the public at large. The concerns about the possible erosion of democracy would also play against this.

3.10 The Policymaking Process of Tax Reform: Main results

Key players

Based on the previous discussion, we can compute the overall importance of key political players in the nine countries under study. This can be done by averaging the data shown in tables 14 through 22. The results, shown in Table 23, suggest that relatively few players are decisive in specific stages of the PMP. For example, only the president and the cabinet have a central role in setting the tax agenda, while the weighting and selection of options is primarily in their hands and the legislators'. Decision making is concentrated in the president and legislators, while implementation involves all actors from the executive. Interestingly, evaluation and control rests primarily in the hands of the judiciary and control entities. How does this compare with the theoretical roles of these players depicted in Table 13? Table 24 shows a

measure of the deficit of influence of the selected players—differences between the players' actual importance and the expected level.

In the agenda setting of tax policies many players have a clear deficit of influence. This is the case of the media, civil society, government experts, political parties, and congress. In contrast, the bureaucracy and the judiciary have more influence than desired. Turning to the generation and selection of alternatives, experts, professional associations, and congressional staffers play a lower role than it is desirable. Conversely, the president, legislators, the judiciary, and especially political parties are excessively involved in this phase of the PMP. The decision making as such shows a deficit of influence from many groups, ranging from experts, civil society, the media, and the bureaucracy. In the case of implementation there is excessive influence from groups outside the relevant bureaucracy, while the opposite is true in the evaluation stage.

It is useful to introduce the concept of veto players in the policy game, which can make or break the approval or implementation of a tax reform. Based on evidence for OECD countries, we hypothesize that the number of veto players should be negatively correlated with the quality of tax reform. For the 9 countries analyzed, we constructed an index of effective veto players. Based on the discussion of the previous sections, we assign a value of 1 to those players that have a strong veto point, and 0.5 to those that are moderate veto players. Table 15 shows the index.

In all countries, except Costa Rica and Guatemala, the president is a strong veto player. In Argentina and Brazil, which have a federalist state, the regional and local governments are also veto players in tax policies. In both cases the executive is forced to negotiate with the state governors the desired structure of a tax reform before introducing legislation. This is not the case of Mexico—another federal government—mainly because governors play a role through political parties.²⁵ Governors have an increasingly important role in Venezuela as a result of the weakening role of the legislature. The judiciary is a strong veto player in Brazil, Colombia, Costa Rica, and a moderate veto player in Guatemala. The bureaucracies associated with state enterprises are a strong veto player in Costa Rica, a feature that is not observed elsewhere in the region. Interest groups are very important in Guatemala and moderately decisive in Colombia and Paraguay. Legislators are moderate veto players almost everywhere, with the exception of Chile and Paraguay. In Brazil they are strong veto players. Political parties are generally

²⁵ Unlike Argentina or Brazil, where national leaders render service to state-level elites in exchange for support of executive-based programs in the legislature, Mexico's municipal and state governments are not veto players in the policy-making process of tax reform.

deinstitutionalized –as we will discuss below-, implying that they are important veto players only in Paraguay. Civil society and social sectors are moderately important in Costa Rica and Guatemala.

In some countries, the role of the constitutional court as a major veto player seems to be associated with rigidity in tax policies. In Colombia and Costa Rica there is ample evidence of the importance of the constitutional court in reversing many decisions related to social spending and in delays tax reform. This has occurred because the constitution has given the courts an active role in fiscal policies. In Brazil the court has also had an important role in tax policies, although in many cases its decisions have sided in favor of tax reform. The constraints from the Constitution bind because the Judiciary has been relatively independent in ruling on issues of constitutionality. In Costa Rica the different instances where the court can intervene has clearly hindered the speed of the reform process. In other countries, such as Mexico and Guatemala, the constitutional court has intervened very sporadically, thus would not be considered a veto player.

The opposite is the case where the president or the executive power is one of the most important veto players, as in the cases of Chile, Mexico and Paraguay. These countries seem to have more adaptability and flexibility in tax policies, with various instruments available to adjust taxes according to the macroeconomic situation, and with a leading role of the executive in the initiation and support for tax reform. In Brazil, Guatemala, Venezuela and Colombia the President has more veto power than the legislature, but is limited by other veto players (be it the courts, interest groups, political parties, etc.)

In some countries the interest groups constitute increasingly important veto players. In Guatemala they have been able to block tax reform outside of the legislative process. In Argentina and Paraguay, and more so in Venezuela, interest groups exert their influence indirectly through legislators. In most cases businesses are interested in preserving the status quo and are able to either stall the reform process or get concessions through tax exemptions. Therefore, the public regardedness of the tax reform process suffers. Although this phenomenon is typical of all countries, in some countries special interests are powerful enough to become veto players.

In other countries the population at large (civil society) is well-represented in the tax reform process. Chile and Costa Rica seem to be the countries where the policy-making process itself seems to remain stable against economic shocks because of a well-woven social fabric and tradition of democratic participation. This allows them to stay the course and maintain some fundamentals in the presence of changes in the macro environment. All of these lead to credibility of the bureaucracy, active participation

of civil society in policy-making, and broad public debate, which are more likely to lead to a cooperative equilibrium or beneficial outcome. In the case of Costa Rica, continued chronic fiscal problems stem in part from the clear opposition of the population to privatization²⁶. In the case of Chile, the historical importance assigned to technocrats in the government has enabled the introduction of high-quality fiscal laws. There are other identifiable differences between Chile and Costa Rica: Chile has fewer effective veto players, has a much more transparent bureaucratic process and higher ex-post accountability standards. The two countries also have markedly different fiscal situations.

Outer features

Based on the case studies, it is possible to rank each country's outer features. The variable that we described as the features or qualities of the policy-making process is multi-dimensional and consists of a series of interwoven relations which are difficult to capture in an indicator. Nonetheless, the *index of quality of outer features* is an attempt to rank the countries in terms of these characteristics. This exercise requires a considerable amount of subjective judgment based on the information available, but it does allow us to identify some interesting patterns. Taken together, the trends do indicate that countries where there are a small number of clearly identified veto players, where there is clarity and consistency in the roles of the key players, and where the policy-making process is stable, adaptable, coordinated, is efficiently delivered and is mindful of the public good, the quality of the tax system should improve. At the top of the list is Chile, which has been very successful in all these fronts. Table 25 shows the index of the quality of each component of the tax policies' outer features (the score assigns a value of 4 for high quality and 1 for the lowest quality).

According to the results, tax policies are highly stable in Chile and Costa Rica, while Venezuela is an example of extreme volatility. The degree of adaptability is high in Chile, followed by Mexico and Paraguay. Costa Rica and Guatemala are examples of strong rigidity in tax policy. In terms of coordination, Brazil and Guatemala show the worst performance. In the case of Brazil, this is related the inability to reform the system in order to oblige all states to follow the same rules, especially in relation to the indirect taxation. In terms of investment qualities, Mexico, Paraguay and Venezuela seem to have the worst features, with weak bureaucracies and rampant evasion. Chile and Brazil, in contrast, have better tax administrations. Public regardedness is high in Chile and Costa Rica, where regimes are simpler and with fewer exemptions. Paraguay, Colombia, and Mexico stand at the other extreme in this front. The overall index of quality of outer features places Chile at the top of the list with 20 points. Costa Rica,

²⁶ This also explains why the autonomous public institutions are important veto players in fiscal policy in Costa Rica.

Mexico and Brazil are in a second group (with scores above 10). Venezuela, Argentina, Paraguay and Guatemala are at the bottom. Colombia is right in the middle.

The relationship between key political players and outer features

Political institutions have a direct impact on the policy making process (primarily affecting the possibility of reaching intertemporal agreements) by determining several key factors like the number of agents with influence over decision making, their potential interactions, their duration and their relative bargaining power, the arenas where decisions are taken, the enforcement mechanisms, etc. (Scartascini and Olivera, 2003). Based on the results presented in previous sections, here we present some simple correlations between the tax policies' outer-features and some variables that represent the workings of political institutions in each of the nine countries.

- (i) **Adaptability:** As one would have thought, the number of veto players involved in the tax PMP is negatively correlated with the adaptability of tax reforms (Figure 8). A higher number of veto players would complicate reaching intertemporal agreements that allow the executive to make some adjustments depending on fiscal situation. The importance of some key players can also be decisive for the adaptability of policies. For instance, Figure 9 illustrates how the adaptability of tax policies is lower in countries where business groups have a relatively high incidence on the decision process in this policy area, suggesting once again that business groups favor the status-quo. The structure and organization of political parties and party systems in general also represent a key determinant of the qualities of the tax policy making process. Jones (2005) has developed a *party institutionalization index* that measures if parties have programmatic politics, if they tend to compete based on policy proposals, if they have public policy consistency, and if their level of accountability is relatively acceptable and if they can be readily identified. Evidence suggests that democracies with the more institutionalized party systems have greater adaptability levels of the tax policy (Figure 10).
- (ii) **Coordination:** As expected, when more veto players are involved, the tax policy making process has less coordination and coherence qualities (Figure 11). Likewise, democracies where there is a greater effective number of legislative parties present low levels of coordination (Figure 12). On the other hand, democracies where there is a strongly institutionalized party system tax policies present high levels of coordination and coherence.

- (iii) **Investment Properties:** According to Figure 13, when the role of expert groups external to the government (including the IMF) have a great importance on the determination of the tax policy agenda the tax PMP presents more investment-related qualities. Then again, these investment-related qualities are lower in democracies where the effective ideological distance between the different parties is greater.
- (iv) **Public Regardedness:** Policies resemble public goods in those cases where political parties are more involved in the agenda setting (Figure 14).
- (v) **Outer Features Quality Index:** Figure 15 presents one of the most important results of this section. Evidence suggests that democracies with more institutionalized political parties and party systems in general have higher quality levels on their outer features.

To sum, the quality of tax policies is negatively related to the number of veto players. In addition, the evidence suggests that the number of players also has an impact on other areas of fiscal policy, such as the proportion of primary expenditures that is earmarked, meaning that fiscal sustainability is harder to achieve in environments where there are greater complications at arriving at a consensus in the policymaking process.

4. POLICY OUTCOMES, OUTER FEATURES AND POLITICAL INSTITUTIONS: EMPIRICAL EVIDENCE

Section 2 presented the stylized facts in terms of tax policy outcomes while Section 3 provided some analytical narrative on the outer features and the key players in the PMP. This section brings together these two pieces of information by analyzing how political institutions shape the interaction of key players in the policy-making process that can lead to certain desirable or less desirable outcomes. We start by establishing some correlations between the variables that describe the outer features of tax policy (discussed in the previous section) and the outcomes of tax policies (discussed in Section 2). We are well aware of the limitations of the exercise because with nine countries we have very few data points in order to establish clear-cut causal relationships. However, the exercise is useful because it suggests some relationships that we can test in a panel with annual data for 17 countries between 1980 and 2001.

It is a well established fact that income per capita is positively correlated with tax revenues (as a share of GDP).²⁷ However, for the nine countries analyzed in the previous section, there does not seem to

²⁷ See Acemoglu (2003).

be a relationship between the quality of tax policies' outer features and tax revenues to GDP. More concretely, the average share of tax revenue to GDP between 1990 and 2001 for each country, as well as the level of the VAT tax rate, do not seem to have much relationship with the outer features.²⁸ This is an interesting result because it suggests that there is no causal relationship between the quality of policies and tax revenues. The one possible exception is the index of investment-related qualities of tax reform, which according to our definition relates mostly to the quality of the bureaucracy of the tax collection administration. Moreover, it is consistent with the finding that the richest countries in the sample, Brazil, Chile and Argentina, all have high VAT tax rates and relatively high tax revenues to GDP.

In contrast, the outer features are related to the policy outcomes, such as neutrality and productivity. In fact, the higher the quality of the outer features the greater the average VAT productivity of the country (Figure 16). The correlations are stronger for some of the subcomponents of outer features such as stability, investment-related qualities and the public regardedness. The same is true for the neutrality index which is positively correlated with the degree of public regardedness, suggesting that better quality PMP result in better functioning tax systems, at least from the point of view of productivity and neutrality.²⁹ In addition, although we do not have enough information to make a strong conclusion, high quality outer features are negatively correlated with the cost of tax collection.³⁰ This is quite consistent with the idea that if the policymaking process delivers a system with high evasion, weak tax administration, exemptions, it likely to be less credible, which in turn makes collecting taxes more difficult (Table 26).

4.1 Econometric analysis

We now turn to more formal testing of the relationship between political institutions and policy outcomes. To the extent that political institutions determine the quality of the policy-making process, then good outcomes in tax reform should be positively related to political institutions after controlling for some economic variables. In particular, we are interested in explaining: (i) what motivates a government to initiate tax reform; (ii) to what extent political variables affect the 'policy outcome', in this case the productivity and neutrality of the tax system. Finally, we want to know if countries that face certain

²⁸ However, the degree of adaptability is positively correlated with the average change in the VAT rate between 1990 and 2001.

²⁹ It is interesting to note that better outer features are positively correlated with low corporate income tax rates.

³⁰ Incidentally, the cost of tax collection is higher in countries where people consider that taxes are too high, according to the Latinobarómetro surveys. The data also shows that the citizens are *less likely* to perceive that 'taxes are too high' when policies are more adaptable and coherent. More citizens are likely to believe that 'taxes are not well spent' the lower the index of outer features (in particular the lower the investment-related qualities and public regardedness).

political circumstances are more likely to resort to other types of taxes, different from income taxation and VAT.

Explaining the probability of tax reform

The first question to investigate is why certain countries are able to pass more tax reforms than others. We run a Probit model where the dependant variable is a dummy which takes the value of 1 when tax reforms were approved, according the definition of tax reform used in Section 1. The probability of reform should depend positively on the structural budget deficit, which reflects the need to raise taxes or improve the tax system in order to deal with fiscal sustainability. We use the share of interest payments in total revenues of the government, which is a proxy of the fiscal sustainability. The probability of passing tax reform should also depend positively on the year in the electoral cycle: there is evidence that a new government, especially if elected with a mandate, has a window of opportunity, typically the first year in office, to push through reform with less political resistance. Therefore, we use a variable that captures the number of years since the administration's inauguration. We postulate that the lower the value of the variable, the greater the chances of passing through reform.

Countries supported by an IMF program are expected to pass more tax reforms. However, the role of the IMF is a complex issue because there is some obvious endogeneity: countries that are more willing to reform are more likely to sign agreements with the IMF. We take the view that the IMF acts as an outside pressure in the legislative process, which can catalyze the passage of tax laws. This is captured by a dummy variable that takes a value of one when the government is under an IMF program involving conditionality. Finally, likelihood of reform should depend positively on the quality of the political and legislative process. Countries where there is a democratic and orderly way of arriving at decisions and where there are fewer extremes in terms of ideology are likely to be more successful in pushing through tax reforms. We use the variable *ideology*, defined as the distance between different ideologies that may exist in the legislative process, weighted by their relative importance. We also include the *Polity* variable, which captures the degree to which decision-making is made in an autocratic or democratic fashion (with more democratic means signifying a higher number on the polity index³¹). Finally, it may be the case that governments that receive a significant portion of their tax revenues from a natural resource (royalties from oil, copper or hydroelectric power, or taxes from companies that exploit these) may be in less need

³¹ The Polity Index of Democracy/Autocracy is a scale from -10 to +10 measuring the degree to which a nation is either autocratic or democratic. A score of +10 indicates a strongly democratic state; a score of -10 a strongly autocratic state. A fully democratic government has three essential elements: fully competitive political participation, institutionalized constraints on executive power, and guarantee of civil liberties to all citizens in their daily lives and in political participation. A fully autocratic system sharply restricts or suppresses competitive political participation. The chief executives are chosen by an elite group and exercise power with few institutionalized constraints. Polity IV Project Dataset User's Manual

to pass tax reforms than countries that do not have these. The results of the estimation, shown in Table 27, indicate that the probability of a tax reform is greater the smaller the number of ideologies represented in the legislative process, if there is IMF conditionality and if there is a fiscal sustainability problem. The first year of the administration is positive, as expected, but not significant at the 10 percent level. Neither is the presence of other revenues from natural resources.

Explaining the quality of the tax system

Following Mahon (2004) we investigate whether improvements in tax reform can be explained by variables that describe the political process in Latin America between 1977 and 1995. He finds that reform is predicted, in roughly descending order, by past inflation, explicit IMF performance conditions, a new administration, more authoritarian-elected governments, the dominance of the presidential party in the legislature, and established electoral systems. We follow the same basic structure in our regressions.

The dependant variables of interest are those that capture the quality of tax reform, and several have already been described in Section 2. While the *tax reform index* captures some of the positive trends that have been observed in tax reform in Latin America since 1985, it is possible that a country could have reduced the marginal income tax rate and increased its VAT rate, yet there is no change in the index. Consequently, while it encompasses a number of important areas, it may not always indicate adequately progress in tax reform. Ignoring these limitations, we use this measure of reform as the dependent variable. As in Mahon, we use *purchasing power loss*, an inflation-based index, which is a proxy for the level of macroeconomic stabilization on the country. It may also indicate the quality of other macroeconomic policies, which will also positively affect the quality of tax reform and tax policy. We include the dummy for *IMF conditionality*, which once again reflects an external key player in the policy-making game, exerting pressure at any given time to change taxes. We also include the administration's cycle year, again capturing the extent to which advancements in tax reform should be greater the first year of a specific administration. Finally, we include log of *income per capita* in the other specification to control for the fact that richer countries will be able to financially support a greater tax revenues to GDP and a more efficient tax administration. We choose two variables from the Polity IV (2004) project that capture certain elements of the policymaking process that may lead to cooperative outcomes. The first is the *executive constraint index*, a seven point scale used to isolate the political constraints on a government's executive branch. The coding for executive constraints was based on the degree of operational independence the chief executive of a country enjoyed during the years under observation. The measure presented in the dataset is the score for each country in each year of peace. If it is orderly,

and there are checks and balances, then this index has a high value. The second is the *polity* index described above. A high number captures the degree to which decisions are made by a broad group of people. A low number would capture an autocratic government. The higher the number of effective veto players, which according to the correlations seem to be negatively related to the likelihood of passing reforms, the higher the polity index. We also look at the *effective number of parties* as an indicator of the ability to reach consensus and cooperation in the legislative process, which may lead to better tax reform. Another variable used is *ideology* mentioned earlier, which may indicate the level of polarization in the policy-making process, thus making cooperation more difficult. Table 28 shows the results. The intensity of tax reform increases when the macroeconomic environment is unstable (losses of purchasing power), and the administration is at an early stage in its term. There is some weaker evidence suggesting that lower ideological polarization is more conducive to reform.

A simpler index is the VAT productivity (defined as the ratio of the revenues from the VAT as a proportion of GDP divided by the VAT rate). We prefer this index as a measure of the quality of the tax system and tax reform, at least for econometric purposes, for various reasons. First, as mentioned earlier, there is no 'ideal' VAT rate. Some countries may prefer to have a high rate, others a lower rate. As mentioned earlier, many studies show that the revenue to GDP is related to the level of development. Second, there is little dispute that an improvement in the efficiency of the VAT is desirable, and a higher VAT productivity is associated with fewer VAT exemptions and/or lower evasion, and/or more efficient the tax administration. Third, the overwhelming majority of tax reforms in Latin America during the relevant period have created a VAT, widened the VAT base or increased its rate, all of which would be reflected in a change in this index. Finally, it is a uniform tax applied in a similar manner across all countries, so the tax base, in an ideal state GDP, is comparable across countries.³²

Table 29 uses *VAT productivity* as the dependent variable, which for reasons mentioned above may be a better indicator of the quality of policy making and of policy implementation. The results are statistically significant and the coefficients have the expected sign. The fit of the equation also improves markedly. Equation 1, the preferred specification, shows that controlling for the level of development and the quality of the macro environment, the VAT productivity is higher the greater the executive constraints index and the effective number of parties (which proxy for the quality of the decision-making process, leading to cooperative equilibriums), but is greater the more 'autocratic' the political system, which we take as a proxy for a small number of veto players. It does seem to show some effect of the political

variables on the quality of the tax system, at least as it pertains to the VAT. Table 30 uses the Income tax productivity as a measure of the tax policy outcomes. Once we control for difference in the level of income, productivity seems to decrease with inflation and the effective number of political parties. Productivity increases with the degree of institutional constraints on the executive.

Lora's tax neutrality index is a good measure of the quality of tax policy.³³ Greater values of the index lower tax rates (using a scale from 0 to 1 for each tax, wherein 0 corresponds to the highest tax and 1 to the lowest for the set of observations per year and country) and higher productivity. When we use this measure as the dependent variable, the result show that neutrality is greater in environments where there is lower inflation, a larger number of effective parties, and the executive is less constrained. It is somewhat puzzling to see that the greater the ideological divide between the relevant political parties, the greater the neutrality of the tax system.

Other Taxes as a Means to Raise Revenues

In the previous chapter one of the patterns that came through, at least for some of the countries analyzed was a tendency of countries that are fiscally constrained (either because of a sustainability problem, or the inability to lower expenditures due to legal or political constraints) will be more likely to resort to creative ways of raising revenue, such as tweaking with taxes, imposing temporary taxes and surcharges that become permanent or using methods that require less involvement from Congress to raise revenue. Therefore, we define the variable *other taxes* as the share in total current revenue of revenue from taxes other than the VAT and direct taxes. This would include payroll taxes, property taxes, excise taxes and other cascading taxes.

Table 32 shows the results after controlling for countries that receive a large share of current revenues from natural resources. We find that the structural fiscal balance, which captures the severity of the fiscal problem, is highly significant and negatively related to the share of other taxes, as expected. We also find that this variable higher for countries that have an unstable macroeconomic environment, as proxied by purchasing-power-loss, possibly signifying the need for more 'desperate' measures under certain circumstances. More importantly, the results show that the lower the executive constraints index

³² As opposed to an income tax, where the maximum tax rate fails to capture the marginal rates scales, the exemption levels and the treatment of income such as capital gains. In the case of excise taxes, for example, most countries tax a heterogeneous list of goods.

³³ The definition of Lora's Tax Neutrality Index is developed in section 2.

and the higher the polity variable, the easier it is for the government to raise other types of revenues; presumably because it is less subject to various checks and balances.

5. CONCLUSIONS

What are the features of 'good' tax policies? Why some countries have better working tax systems than others? Why some countries are more able than others in reforming their tax systems? This paper tries to answer these questions by applying the policymaking process methodology to the recent experience with tax reform in Latin America. This framework provides the answer to the first question: high quality policies are those that do not change in response to political shocks -but that are responsive to economic conditions-, that are not captured by special interests, and that are coherent and efficient. To a large extent, countries that are able to deliver better tax policies have better political institutions, in the sense of engaging various actors in the policymaking game, but restricting the use of veto powers as much as possible. When these players are institutionalized and have long-term perspectives the results tend to improve significantly. This is the case, for example, when political parties not only are relevant in the policy game, but also have programmatic politics, compete based on policy proposals, have public policy consistency, their level of accountability is relatively acceptable, and can be readily identified. Results also tend to improve when the executive is more constrained. That is, when the system of checks and balances works well in the sense of preventing policy swings. However, successful reforms provide some discretion so that some parameters of the tax system can be adjusted rapidly to changes in economic conditions.

This means that successful reforms are difficult to achieve because they require a complex process of consensus building between many players. When reforms take place too frequently, policy reversals and incoherencies are common. There is a fine line, because with too many powerful players the game can easily end in stalemate and gridlock. This is the scenario of protracted reform, typical of many countries in the region. It remains to be explained why this has been the case in many countries since the late 1990s.

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Appendix 1: Variable definitions

Variable	Definition	Source
Mahon's Tax Reform Index	A measure of the extent of tax reform passed by Congress made up with the following components: tax system overhaul (0.2), VAT creation (0.2), VAT expansion (0.1), VAT rate increase (0.1), corporate income tax rate increase (0.1), broadening corpo	Taken from Lora.
Tax Reform Dummy	Takes the value of 1 for the year where any of the above has taken place.	Taken from Lora.
IMFcond1	Dummy for year when program with IMF starts	Taken from Lora.
IMFdisb	Dummy for year when IMF disburses money	Taken from Lora.
Tax Neutrality Index		GFS and article IV.IMF
VAT Productivity Index		GFS and article IV.IMF
Income Tax Productivity Index		GFS and article IV.IMF
VAT Tax Rate		Price Waterhouse Coopers
Personal Income Tax Rate		Price Waterhouse Coopers
Corporate Tax Rate		Price Waterhouse Coopers
Personal Exemption Level		Taken from Stotsky et al 2002
Tax Revenues	Tax revenues as percent of GDP.	GFS and article IV.IMF
Votes of Incumbent	Percentage of votes that elected the incumbent that is finishing term in the year indicated.	Taken from Lora.
Votes outgoing Incumbent	Percentage of votes for the party of the president that is finishing term in the year indicated.	Taken from Lora.
Legislative Votes outgoing Incumbent	Percentage of votes of the incumbent majority party.	Taken from Lora.
Administration Cycle Year	Period trend. Note that the period begins next year after the elections (this for fiscal budgetary purposes).	Taken from Lora.
Ideology	It classifies parties on a left to right scale according to their economic ideology.	Taken from DPI (2002) and Coppedge (1994 and 2001).
Coalition	Equals 1 if it is a coalition government, where coalition means that opposition parties also hold positions in the executive, such as cabinet positions.	Taken from Chelub et al. (2003).
Effective number of parties	It is the effective number of parties of that year's presidential election calculated using the electoral results from Payne et al. (2002).	Taken from Lora and Olivera (2004).
Polarization Index	It calculates the effective ideological distance between the different parties.	Taken from Lora and Olivera (2004).
Promises	The promises variable takes values on a scale 0-1, where higher values mean more efficiency-oriented campaign messages.	Taken from Lora and Olivera (2004).
Democracy Index	The Democracy Indicator is an additive eleven-point scale (0-10).	Polity IV Database
Polity Index	Combined Polity Score: The Polity score is computed by subtracting the Autocracy Index score from the Democracy Index score; the resulting unified polity scale ranges from +10 (strongly democratic) to -10 (strongly autocratic).	Polity IV Database
Executive Constrains Index	This variable refers to the extent of institutionalized constraints on the decisionmaking powers of chief executives, whether individuals or collectivities. Such limitations may be imposed by any "accountability groups."	Polity IV Database
Openness of Executive Recruitment Index	Openness of Executive Recruitment: Recruitment of the chief executive is "open" to the extent that all the politically active population has an opportunity, in principle, to attain the position through a regularized process.	Polity IV Database
Taxes well spent	Are taxes well spent? - %no.	Latinbarómetro
Taxes too high	Are taxes too high?	Latinbarómetro
Extent and Effect of the Tax System	The level of taxes in your country (=1 significantly limits incentives to work or invest, 7= has little impact on incentives to work or invest)	Global Competitiveness Report
Efficiency of the tax system		Global Competitiveness Report
Adjusted Fiscal Balance	It is the fiscal balance of the central government adjusted by the endogenous influence of the economic cycle and terms of trade changes on fiscal revenues.	Taken from Lora and Olivera (2004).
Purchase Power Loss	Calculated from CPI.	Taken from Lora and Olivera (2004).
Cycle (LogGDP)	From State's H-P filter	Taken from Lora.
Crisis	When cycle is negative, which means that GDP is below its trend.	Taken from Lora.
Unemployment		Taken from ECLAC yearbook (various years)
Social Expenditure	Expenditure on education and health.	Taken from CEPAL Panorama económico y social (various years).

Table 1
Corporation's Income Tax Rate

Country	1985	1990	1995	2000	2002
Argentina	33%	20%	30%	35%	35%
Bolivia	30%	0%	25%	25%	25%
Brasil	45%	40%	25%	25%	25%
Chile	10%	10%	15%	15%	16%
Colombia	40%	30%	35%	35%	35%
Costa Rica	50%	30%	30%	30%	30%
Ecuador	40%	25%	25%	25%	25%
El Salvador	35%	30%	25%	25%	25%
Guatemala	42%	34%	25%	31%	31%
Honduras	46%	46%	40%	25%	25%
Jamaica	45%	33%	33%	33%	33%
México	42%	36%	34%	34%	35%
Nicaragua	45%	..	30%	25%	25%
Paraguay	30%	30%	30%	30%	30%
Peru	55%	35%	30%	20%	27%
Dominican Republic	49%	49%	25%	25%	25%
Trinidad and Tobago	50%	40%	38%	35%	35%
Uruguay	30%	30%	30%	30%	30%
Venezuela	50%	50%	34%	34%	34%

Source: PriceWaterHouseCoopers: Corporate Taxes. Worldwide Summaries. Several years

Table 2
Financial and Fiscal Incentives to Production and Investment

Country	Horizontal tax incentives	Tax incentives to specific sectors	Tax incentives to particular regions
Argentina		Mining, forestry	
Bahamas	X ^(a)	Hotels, financial services, spirits and beer	
Barbados	X ^(b)	Financial services, insurance, information technology	
Belize	X	Mining	
Bolivia		Mining	
Brazil			X ^(c)
Chile	X ^(d)	Forestry, oil, nuclear materials	X
Colombia			X ^(e)
Costa Rica		Forestry, tourism	
Dominican Republic		Tourism, agribusiness	
Ecuador		Mining, Tourism	
El Salvador			
Guatemala			
Guyana		Agribusiness	
Haiti	X ^(f)		
Honduras			
Jamaica		Motion picture industry, tourism, bauxite, aluminum, factory construction	
Mexico	X ^(g)	Forestry, motion picture industry, air and maritime transportation, publishing industry	
Nicaragua		Tourism	
Panama		Tourism, forestry	
Paraguay	X ^(h)		X ⁽ⁱ⁾
Peru		Tourism, mining, oil	X ^(j)
Trinidad & Tobago	X ^(k)	Hotels, construction,	
Uruguay	X ^(l)	Hydrocarbons, printing, shipping, forestry, military industry, airlines, newspapers, broadcasters, theaters, motion picture industry	
Venezuela	X ^(m)	Hydrocarbons and other primary sectors ⁽ⁿ⁾	

Source: IDB 2001. Table 17.3 in The Business of Growth. Economic and Social Progress in Latin America 2001 Report.

Notes: 1) The notation X(ip) means that there are credit lines for entire investment projects and, a portion, for discrete capital goods. The plain X indicates that only loans for discrete sets of fixed assets are available.

a) Income is tax-free and imports to be used in investment projects are duty-free.

b) The tax incentive is for foreign investors. Offshore companies are taxed at a rate significantly below the rate for local companies.

c) There are federal tax investment incentives for the Northeast and Amazon regions.

d) There are two main horizontal forms of tax incentive to investment (including re-investment of profits): 1) Accelerated depreciation is granted for new fixed assets acquired domestically and for imported fixed assets; 2) personal income tax and Additi

e) There are two special tax regimes that favour particular regions recently affected by natural disasters. They are the Pérez Law and the Quimbaya Law. The first is applicable to the zones affected by the flooding of the Pérez River in 1995 and the seco

f) Haiti has a comprehensive tax-holiday scheme.

g) Through the Sector Promotion Program (PROSEC), firms in twenty-two industries in the manufacturing sector can import goods at a preferential rate to be used in the respective manufacturing sector to produce final goods either for the external or the

h) Paraguay has a five-year-duration tax-holiday for new investments.

i) The duration of the tax-holiday mentioned in footnote 15 is longer (ten years) if the company making the investment locates in the Departments of Guairá, Casapá, Neembucú, Concepción, or in the Eastern Region.

j) Manufacturing enterprises operating in the border provinces and in the Amazon region are exempt from the income tax, the VAT, and the excise taxes.

k) Trinidad and Tobago grants comprehensive tax holidays of up to ten years.

l) A tax exemption is available on profits reinvested in manufacturing firms, farming, and hotel facilities. In addition, there is a partial relief from capital tax through computing the fiscal value of industrial equipment at fifty percent.

m) New investments in manufacturing industry, agriculture, fishing, fish farming, livestock, and tourism receive a tax rebate of 20 percent. Furthermore, the capital gains tax is one percent.

n) New investments in hydrocarbons production enjoy a tax rebate of 8 percent. The purchase of capital equipment and services for new investment in oil, mining, agriculture, and fisheries is exempt from the wholesale tax.

Table 3
Individual's Income Tax Rate

Country	1985	1990	1995	2000	2002
Argentina	45%	30%	30%	35%	35%
Bolivia	30%	10%	13%	13%	13%
Brasil	60%	25%	35%	28%	28%
Chile	50%	50%	45%	45%	40%
Colombia	49%	30%	35%	35%	35%
Costa Rica	50%	25%	25%	25%	25%
Ecuador	40%	25%	25%	25%	25%
El Salvador	60%	50%	30%	30%	30%
Guatemala	48%	34%	30%	31%	31%
Honduras	46%	46%	46%	25%	25%
Jamaica	58%	33%	25%	25%	25%
México	55%	35%	35%	40%	40%
Nicaragua	53%		30%	25%	25%
Paraguay	30%	30%	0%	0%	0%
Peru	50%	45%	30%	20%	27%
Dominican Republic	73%	73%	25%	25%	25%
Trinidad and Tobago	70%	35%	38%	35%	35%
Uruguay	0%	0%	0%	0%	0%
Venezuela	45%	45%	34%	34%	34%

Source: PriceWaterHouseCoopers: Individual Taxes. Worldwide Summaries. Several years

ax Exemption Level and Upper Income Bracket (Multiples of per capita GDP)

Personal Exemption Level					Upper Income Bracket				
1985	1991	1997	2000	2001	1985	1991	1997	2000	2001
0.8	0.5	1.2	1.3	1.7	21.4	13.7	14.5	15.5	16.5
1.0	0.5	...	...	...	10.1	0.5	...	...	...
0.3	1.2	2.1	1.7	1.5	10.1	2.8	4.2	3.3	3.1
0.2	2.3	0.1	0.1	0.1	2.8	22.6	1.3	1.2	1.2
0.0	0.4	2.7	4.4	4.1	20.5	25.3	12.0	11.7	16.6
1.2	2.9	1.1	0.8	0.8	1.4	5.3	5.6	4.1	3.7
1.1	0.2	0.1	2.6	2.3	413.5	74.3	34.3	6.5	5.8
0.4	2.9	1.8	0.9	2.4	29.2	35.8	22.7	11.3	8.3
...	2.3	1.4	1.2	1.2	171.7	32.5	12.7	11.4	11.0
0.9	2.3	6.3	5.3	5.0	356.0	31.7	17.5	14.7	22.5
0.0	6.9	5.2	3.9	3.6	600.4	686.8	103.4	39.1	36.0
0.7	0.2	0.1	0.1	0.1	21.3	11.7	5.0	36.8	44.0
1.7	...	6.6	8.3	7.7	56.9	9.9	47.4	49.9	61.2
0.3	0.5	0.9	0.9	0.9	89.0	97.8	63.1	58.9	57.8
0.5	...	...	...	...	10.4	...	...	...	...
...	...	2.6	2.8	2.9	...	...	20.1	21.5	22.3
...
...	...	0.0	0.0	0.0	...	...	0.0	0.0	0.0
0.6	1.8	2.1	2.3	2.3	121.0	75.0	24.2	19.0	20.7

Table 5
Value-Added Tax Rates

Country	1985	1990	1995	2000	2002
Argentina	18%	13%	21%	21%	21%
Bolivia	10%	10%	13%	13%	13%
Brazil	30%	30%	31%	31%	31%
Chile	20%	18%	18%	18%	18%
Colombia	10%	12%	14%	15%	16%
Costa Rica	10%	10%	10%	13%	13%
Ecuador	10%	10%	10%	12%	12%
El Salvador	0%	0%	13%	13%	13%
Guatemala	7%	7%	7%	10%	10%
Honduras	5%	5%	7%	12%	12%
Jamaica	0%	0%	13%	15%	15%
Mexico	15%	15%	15%	15%	15%
Nicaragua	15%	15%	15%	15%	15%
Paraguay	0%	0%	10%	10%	10%
Peru	11%	16%	18%	18%	18%
Dominican Republic	6%	6%	8%	8%	8%
Trinidad and Tobago	0%	15%	15%	15%	15%
Uruguay	20%	22%	22%	23%	23%
Venezuela	0%	0%	13%	15%	15%

Source: PriceWaterHouseCoopers: Corporate Taxes. Worldwide Summaries. Several years

Table 6
Tax Revenue as GDP percentage

Country	1985-89	1990-94	1995-99	2000-02	2000-02 Vs 1985-89
Argentina	11.6%	11.6%	12.5%	9.5%	-2.1%
Bolivia	8.0%	9.9%	14.0%	13.1%	5.1%
Brazil	16.5%	18.2%	19.7%	24.4%	7.9%
Chile	19.3%	18.4%	18.7%	16.7%	-2.6%
Colombia	11.2%	11.8%	10.4%	12.9%	1.7%
Costa Rica	20.2%	18.4%	17.9%	12.5%	-7.7%
Ecuador	14.4%	15.5%	9.8%	12.5%	-1.8%
El Salvador	12.3%	9.8%	11.6%	10.8%	-1.5%
Guatemala	7.9%	7.4%	8.9%	10.2%	2.3%
Honduras	13.6%	15.5%	16.9%	16.2%	2.6%
Jamaica	23.5%	21.4%	22.3%	25.6%	2.0%
México	14.3%	13.5%	11.9%	12.0%	-2.3%
Nicaragua	25.3%	11.0%	13.6%	14.1%	-11.2%
Paraguay	8.5%	9.4%	10.6%	9.7%	1.2%
Peru	10.8%	13.4%	14.8%	12.6%	1.9%
Dominican Republic	11.8%	13.2%	14.8%	15.5%	3.8%
Trinidad and Tobago	24.8%	19.2%	20.4%	15.3%	-9.6%
Uruguay	21.9%	25.7%	26.2%	24.0%	2.1%
Venezuela	17.0%	15.9%	14.1%	11.9%	-5.1%

Source: IMF. Data from Government Finance Statistics and Article IV. Several Years

Table 7
Tax Revenues

Item	1985-1989	1990-1994	1995-1999	2000-02
Total Tax Revenue (% GDP)				
LAC average *	15.4%	14.6%	15.1%	14.7%
LAC median *	14.0%	14.2%	14.3%	13.2%
LAC average (1)	14.8%	14.5%	15.0%	14.7%
LAC median (1)	13.7%	14.0%	14.5%	13.3%
Income Tax Revenue (% GDP)				
LAC average *	2.7%	2.8%	3.5%	3.9%
LAC median *	2.3%	2.0%	3.0%	3.4%
LAC average (1)	2.6%	2.5%	3.0%	3.4%
LAC median (1)	2.5%	2.1%	3.0%	3.3%
VAT Tax Revenue (% GDP)				
LAC average *	3.2%	4.0%	5.3%	5.5%
LAC median *	2.6%	3.6%	4.7%	5.0%
LAC average (1)	3.0%	3.8%	5.0%	5.3%
LAC median (1)	2.7%	3.4%	4.5%	5.2%

Source: Own calculations based on IMF. Data from Government Finance Statistics and Article IV. Several Years

(*) Includes Argentina, Brazil, Chile, Colombia, Costa Rica, Ecuador, El Salvador, Guatemala, Honduras, Jamaica, México, Nicaragua, Paraguay, Peru, Dominican Republic, Trinidad and Tobago, Uruguay and Venezuela.

(1) Includes Argentina, Brazil, Chile, Colombia, Costa Rica, Ecuador, Guatemala, Honduras, Mexico, Nicaragua, Peru, Dominican Republic and Uruguay.

Table 8
Neutrality Tax Index

Country	1985-89	1990-94	1995-99	2000-02	1985-89 Vs 2000-02
Argentina	29.1%	37.4%	35.8%	33.7%	4.6%
Bolivia	55.8%	66.3%	56.1%	54.0%	-1.8%
Brazil	22.8%	35.0%	38.9%	40.9%	18.1%
Chile	49.6%	49.3%	50.9%	52.6%	3.0%
Colombia	47.8%	50.1%	42.7%	44.5%	-3.4%
Costa Rica	42.9%	51.3%	50.1%	51.3%	8.4%
Ecuador	39.1%	51.5%	51.3%	56.5%	17.4%
El Salvador	25.9%	42.1%	52.5%	54.2%	28.2%
Guatemala	42.7%	50.6%	53.4%	52.2%	9.6%
Honduras	42.5%	47.0%	54.0%	56.7%	14.1%
Jamaica	38.8%	62.8%	66.5%	67.7%	28.9%
Mexico	33.8%	45.7%	41.8%	41.3%	7.5%
Nicaragua	.	35.9%	42.7%	49.6%	...
Paraguay	32.8%	47.6%	62.8%	60.9%	28.1%
Peru	36.5%	35.2%	45.8%	52.8%	16.3%
Dominican Republic	27.5%	45.7%	55.7%	60.9%	33.4%
Trinidad and Tobago	32.0%	52.1%	52.8%	48.0%	16.0%
Uruguay	52.2%	48.7%	56.8%	55.6%	3.4%
Venezuela	30.2%	41.9%	49.1%	45.3%	15.1%

Source: Own calculations based on IMF. Data from Government Finance Statistics and Article IV. Several Years

Table 9
Summary of Income and Value-Added Tax Incidence Studies

Country and study	Year of calculations	Gini before taxes	Revenue (ratio to income or expenditure)	Quasi-Gini of tax	Gini after tax	Gini after tax and equidistribution of revenue	Kakwani measure	Reynolds Smolensky measure	Engel, Galetovic, Raddatz measure
	(a)	(b)	(c)	(d)	(e)	(f)	(d)-(b)	(b)-(e)	(b)-(f)
Income taxes									
Argentina: CEB (1997)	1996	0.470	0.050	0.625	0.470	0.438	0.156	0.00008	0.031
Chile: Engel et al (1997)	1994	0.543	0.018	0.882	0.543	0.528	0.338	0.00006	0.016
Dominican Republic: Santana and Rathe (1992)	1989	0.497	0.038	0.751	0.497	0.469	0.253	0.00010	0.028
El Salvador: Acevedo and Orellana (2003)	2000	0.502	0.011	0.645	0.502	0.495	0.143	0.00002	0.007
Guatemala: Bahl et al (1996)	1993	0.565	0.014	0.651	0.565	0.556	0.086	0.00001	0.009
Honduras: Gómez-Sabaini (2003)	2000	0.539	0.044	0.551	0.539	0.515	0.011	0.00001	0.024
Peru: Haughton (2004)	2000	0.470	0.012	0.627	0.468	0.462	0.157	0.00197	0.008
Median							0.156	0.00006	0.016
Value-added taxes									
Argentina: CEB (1997)	1996	0.470	0.062	0.329	0.470	0.449	-0.141	-0.00009	0.021
Chile: Engel et al (1997)	1994	0.543	0.087	0.454	0.543	0.504	-0.089	-0.00008	0.040
Colombia: Steiner & Soto (1998)	1994	0.543	0.039	0.592	0.543	0.519	0.050	0.00002	0.023
El Salvador: Acevedo and Orellana (2003)	2000	0.502	0.054	0.265	0.502	0.488	-0.237	-0.00013	0.014
Guatemala: Bahl et al (1996)	1993	0.565	0.040	0.641	0.565	0.539	0.076	0.00003	0.026
Honduras: Gómez-Sabaini (2003)	2000	0.539	0.079	0.420	0.539	0.506	-0.119	-0.00009	0.033
Peru: Haughton (2004)	2000	0.470	0.056	0.455	0.471	0.445	-0.015	-0.00088	0.025
Median							-0.089	-0.00009	0.025

Table 10**Main Types of Reform 1990-2002 (Absolute number of reforms in 17 countries)**

	Gross	Net
(a) Tax system overhaul	11	11
(b) VAT creation	1	1
(c) VAT base broadening	17	15
(d) VAT rate increase	29	21
(e) Elimination of minor duties	5	5
(f) Personal income tax base change	14	14
(g) Personal income tax rate change/reduction	16	8
(h) Corporate income tax base change	9	7
(i) Corporate income tax rate change/reduction	23	5
(j) Comprehensive administrative reform	5	5
(k) Creation of other taxes (excises, bank debits, gross assets)	9	9
Average of reform items by country	7.7	5.6
Average of reform years by country	4.2	

Source: Own calculations as explained in text based on IMF Article IV Reports and questionnaires applied to Tax Administration officials in some of the countries.

Table 11
Indicators of Tax Reforms and Outcomes

Country	Amount of legislative activity		Number of years with legislative activity		Number of years with a tax reform reversal		Change in tax revenues 1990-2002, % GDP	Change in neutrality Index, 1990-2002
	1977-1989	1990-2002	1977-1989	1990-2002	1977-1989	1990-2002		
Argentina	1	2.4	7	8	0	0	0.0%	-4.9%
Bolivia	0.8	0.7	1	6	0	0	4.9%	-10.4%
Brazil	0.3	-0.1	2	6	0	3	5.6%	6.0%
Chile	0.1	0.1	3	7	1	2	0.4%	6.7%
Colombia	0.6	0.7	2	7	0	0	1.7%	-5.0%
Costa Rica	0.6	0.6	3	8	0	2	-6.8%	1.6%
Dominican Republic	0.4	-0.3	2	5	0	3	5.1%	33.1%
Ecuador	0.4	0.7	2	5	0	0	1.0%	6.0%
El Salvador		0.2		6		3	1.8%	24.6%
Guatemala	0.5	0.9	2	9	0	1	3.8%	5.5%
Honduras		0.7		7		1	1.3%	7.3%
Mexico	1.1	0.1	5	7	0	3	-0.7%	-0.9%
Nicaragua		0.3		8		3	12.5%	28.1%
Panama	0.5	0.2	3	2	0	0		
Peru	0.2	0.8	2	8	0	2	0.4%	19.3%
Paraguay	0	0.3	0	2	0	1	0.0%	28.1%
Uruguay	0.4	0.2	3	6	0	2	1.1%	7.8%
Venezuela	-0.1	0.6	1	7	1	3	-7.7%	10.1%
Averages	0.45	0.51	2.53	6.33	0.13	1.61	1.4%	9.6%
Correlation with amount of legislative activity		1.00		0.41		-0.57	-0.21	-0.48
Correlation with number of years with legislative activity		0.41		1.00		0.23	-0.02	-0.38

Table 12
Players' ideal / theoretical importance in the Tax PMP

Considered Players	Agenda Setting	Generation and selection of alternatives	Decision making	Implementation	Evaluation and control
Political Parties	3	-	2	-	1
Legislators	3	2	3	-	2
Legislators' Staff	2	3	3	-	1
President	3	2	3	1	1
Ministerial Cabinet	3	2	3	2	2
Bureaucracy	1	3	2	3	3
Judiciary and control entities	-	-	1	2	3
Subnational Governments (only for unitary governments)	1	1	1	2	2
Business	2	2	2	2	-
Media	3	2	2	1	2
Experts (within the government)	3	3	3	1	2
Experts (outside the government, including the IMF)	2	3	2	1	3
Labor Unions	3	1	2	2	2
Professional Associations	1	2	1	2	1

Table 13
Frequency of IMF programs

Country	Frequency of IMF Programs	
	1980 - 1990	1990 - 2001
Argentina	3	4
Bolivia	1	6
Brasil	1	3
Chile	0	0
Colombia	0	1
Costa Rica	3	3
Ecuador	1	2
Guatemala	2	0
Honduras	0	1
Mexico	2	2
Nicaragua	0	2
Paraguay	0	0
Peru	1	5
Rep Dominicana	1	3
Salvador	0	3
Uruguay	3	5
Venezuela	1	1

Table 14
Argentina: Players' importance in the Tax PMP

Considered Players	Agenda Setting	Generation and selection of alternatives	Decision making	Implementation	Evaluation and control
Political Parties	2	1	2	1	1
Legislators	3	2	3	1	1
Legislators' Staff	1	1	1	1	1
President	3	3	3	2	2
Ministerial Cabinet	3	3	2	3	1
Bureaucracy	2	2	1	3	2
Judiciary and control entities	1	1	2	2	3
Subnational Governments	3	2	3	1	1
Business	1	1	1	1	1
Media	2	1	1	1	2
Experts (within the government)	2	3	2	1	1
Experts (outside the government, including the IMF)	2	2	1	1	3
Labor Unions	1	2	2	1	2
Professional Associations	1	1	1	1	1

Table 15
Brazil: Players' importance in the Tax PMP

Considered Players	Agenda Setting	Generation and selection of alternatives	Decision making	Implementation	Evaluation and control
Political Parties	2	2	3	1	1
Legislators	3	3	3	1	1
Legislators' Staff	1	2	2	1	1
President	3	3	3	3	2
Ministerial Cabinet	2	3	1	3	2
Bureaucracy	2	2	1	3	1
Judiciary and control entities	1	1	3	2	3
Subnational Governments	2	3	2	3	2
Business	1	1	1	1	1
Media	2	1	1	1	2
Experts (within the government)	3	2	2	2	1
Experts (outside the government, including the IMF)	2	1	2	1	3
Labor Unions	1	1	1	1	1
Professional Associations	1	1	1	1	1

Table 16
Chile: Players' importance in the Tax PMP

Considered Players	Agenda Setting	Generation and selection of alternatives	Decision making	Implementation	Evaluation and control
Political Parties	1	2	3	1	1
Legislators	1	2	3	1	1
Legislators' Staff	1	2	1	1	1
President	3	3	3	3	2
Ministerial Cabinet	3	3	2	3	2
Bureaucracy	3	2	1	3	3
Judiciary and control entities	1	1	1	2	3
Subnational Governments	1	1	1	1	1
Business	1	2	1	1	2
Media	2	1	1	1	2
Experts (within the government)	2	3	1	2	2
Experts (outside the government, including the IMF)	2	2	1	1	2
Labor Unions	2	1	1	1	2
Professional Associations	1	1	1	1	1

Table 17
Colombia: Players' importance in the Tax PMP

Considered Players	Agenda Setting	Generation and selection of alternatives	Decision making	Implementation	Evaluation and control
Political Parties	1	2	1	1	1
Legislators	2	3	3	1	2
Legislators' Staff	1	1	1	1	1
President	3	3	3	2	2
Ministerial Cabinet	3	3	2	3	2
Bureaucracy	1	2	1	3	3
Judiciary and control entities	3	1	3	1	3
Subnational Governments	1	2	2	1	2
Business	1	2	2	1	1
Media	1	2	1	1	2
Experts (within the government)	1	2	1	2	3
Experts (outside the government, including the IMF)	2	2	1	1	3
Labor Unions	1	2	1	1	1
Professional Associations	1	2	1	2	1

Table 18
Costa Rica: Players' importance in the Tax PMP

Considered Players	Agenda Setting	Generation and selection of alternatives	Decision making	Implementation	Evaluation and control
Political Parties	1	2	1	1	1
Legislators	2	3	3	1	1
Legislators' Staff	2	1	1	1	1
President	2	2	3	3	2
Ministerial Cabinet	2	1	1	3	2
Bureaucracy	2	1	1	3	3
Judiciary and control entities	1	3	3	1	3
Subnational Governments and entities 1/	1	3	2	3	2
Business	1	2	2	1	1
Media	2	1	2	1	2
Experts (within the government)	2	2	1	2	2
Experts (outside the government, including the IMF)	2	2	1	2	1
Labor Unions	2	3	2	1	1
Professional Associations	1	1	1	1	1

1/ Public sector entities like the Central Bank, public enterprises and the Social Security Institute. Subnational governments have little power.

Table 19
Guatemala: Players' influence/role importance in the Tax PMP

Considered Players	Agenda Setting	Generation and selection of alternatives	Decision making	Implementation	Evaluation and control
Political Parties	2	1	1	1	1
Legislators	2	3	3	1	1
Legislators' Staff	1	2	1	1	1
President	2	3	3	3	1
Ministerial Cabinet	2	2	2	3	1
Bureaucracy	2	1	1	3	1
Judiciary and control entities	1	1	3	1	2
Subnational Governments and entities	1	1	1	1	1
Business	2	2	3	1	2
Media	1	1	1	1	2
Experts (within the government)	1	2	1	1	1
Experts (outside the government, including the IMF)	2	2	1	1	2
Labor Unions 1/	2	2	2	1	3
Professional Associations	1	1	1	1	1

1/ Groups that support the fiscal pact after the Peace Agreements.

Table 20
Mexico: Players' importance in the Tax PMP

Considered Players	Agenda Setting	Generation and selection of alternatives	Decision making	Implementation	Evaluation and control
Political Parties	2	3	3	1	2
Legislators	1	2	3	1	1
Legislators' Staff	1	2	1	1	1
President	3	3	3	3	1
Ministerial Cabinet	3	3	2	3	1
Bureaucracy	2	1	1	3	2
Judiciary and control entities	1	1	2	1	3
Subnational Governments	1	2	2	2	2
Business	1	1	2	1	1
Media	1	1	2	1	1
Experts (within the government)	2	2	1	1	2
Experts (outside the government, including the IMF)	1	1	1	1	1
Labor Unions	1	1	1	1	2
Professional Associations	1	1	1	1	1

Table 21
Paraguay: Players' importance in the Tax PMP

Considered Players	Agenda Setting	Generation and selection of alternatives	Decision making	Implementation	Evaluation and control
Political Parties	3	2	3	1	1
Legislators	2	3	3	1	1
Legislators' Staff	1	2	1	1	1
President	3	3	3	3	1
Ministerial Cabinet	3	3	2	3	2
Bureaucracy	1	1	1	2	2
Judiciary and control entities	1	2	1	2	1
Subnational Governments	1	1	1	1	1
Business	2	1	1	1	1
Media	1	2	1	1	2
Experts (within the government)	1	1	1	1	1
Experts (outside the government, including the IMF)	1	3	2	2	3
Labor Unions	1	1	1	1	1
Professional Associations	1	1	1	1	1

Table 22

Venezuela: Players' importance in the Tax PMP

Considered Players	Agenda Setting	Generation and selection of alternatives	Decision making	Implementation	Evaluation and control
Political Parties	2	2	2	1	1
Legislators	1	3	3	1	1
Legislators' Staff	1	2	1	1	1
President	3	3	3	3	1
Ministerial Cabinet	2	2	1	3	1
Bureaucracy	1	1	1	3	1
Judiciary and control entities	1	1	1	1	2
Subnational Governments	1	2	2	3	2
Business	1	1	1	1	1
Media	1	1	1	1	2
Experts (within the government)	1	1	1	1	2
Experts (outside the government, including the IMF)	1	1	1	1	2
Labor Unions	2	1	1	1	2
Professional Associations	1	1	1	1	1

Table 23

Average of the nine selected countries: Players' importance in the Tax PMP

Considered Players	Agenda Setting	Generation and selection of alternatives	Decision making	Implementation	Evaluation and control
Political Parties	2	2	2	1	1
Legislators	2	3	3	1	1
Legislators' Staff	1	2	1	1	1
President	3	3	3	3	2
Ministerial Cabinet	3	3	2	3	2
Bureaucracy	2	1	1	3	2
Judiciary and control entities	1	1	2	1	3
Subnational Governments 1/	1	2	2	2	2
Business	1	1	2	1	1
Media	1	1	1	1	2
Experts (within the government)	2	2	1	1	2
Experts (outside the government, including the IMF)	2	2	1	1	2
Labor Unions	1	2	1	1	2
Professional Associations	1	1	1	1	1

Table 24

Deficit of influence of the selected players—differences between the players' actual importance and the expected level

Considered Players	Agenda Setting	Generation and selection of alternatives	Decision making	Implementation	Evaluation and control
Political Parties	-1	2	0	1	0
Legislators	-1	1	0	1	-1
Legislators' Staff	-1	-1	-2	1	0
President	0	1	0	2	1
Ministerial Cabinet	0	1	-1	1	0
Bureaucracy	1	-2	-1	0	-1
Judiciary and control entities	1	1	1	-1	0
Subnational Governments 1/	0	1	1	0	0
Business	-1	-1	0	-1	1
Media	-2	-1	-1	0	0
Experts (within the government)	-1	-1	-2	0	0
Experts (outside the government, including the IMF)	0	-1	-1	0	-1
Labor Unions	-2	1	-1	-1	0
Professional Associations	0	-1	0	-1	0

Table 25**Components of the tax policies' outer features (the score assigns a value of 4 for high quality and 1 for the lowest quality)**

Outer Features	Venezuela	Argentina	Guatemala	Paraguay	Colombia	Brazil	Mexico	Costa Rica	Chile
Stability	1	2	2.5	3	2.5	3	3.5	4	4
Adaptability	2	2	1	3	2	2	3	1	4
Coordination	2	3	1	2	2	1	3	3	4
Investment qualities	1	1	2	1	2	3	1	2	4
Public regardedness	2	1	3	1	2	2	2	3.5	4
Total	8	9	9.5	10	10.5	11	12.5	13.5	20

Table 26
Outer Features and credibility of the tax system

Country	Taxes are well spent? (% no)*	Taxes are too high? (% yes)*	Extent and effect of taxation**	Efficiency of the tax system***	Outer Features Quality Index
Argentina	75%	36%	2.4	1.9	9
Bolivia	83%	27%	2.6	3.1	
Brazil	76%	60%	1.9	1.8	11
Chile	62%	19%	4	4.3	20
Colombia	81%	67%	2.8	2.6	10.5
Costa Rica	75%	60%	3.4	3.7	13.5
Dominican Republic			2.9	2.6	
Ecuador	92%	47%	2.5	2.4	
El Salvador	66%	58%	4.6	5	
Guatemala	74%	55%	3.1	2.5	9.5
Honduras	64%	50%	2.5	3.3	
Mexico	89%	32%	2.8	2.1	12.5
Nicaragua	71%	59%	2.3	3.1	
Paraguay	84%	44%	3.8	3.7	10
Peru	85%	49%	2.4	2.6	
Uruguay	76%	64%	2.4	2.6	
Venezuela	74%	48%	3.4	3	8
Correlation with the Outer Features Quality Index	-0.50	-0.55	0.44	0.60	1

Source: * Latinbarómetro, ** Global Competitiveness Report and authors' calculations.

Table 27
Econometric Results: Tax Reform Probability

Explicative Variables	Tax Reform Dummy		
	(1)	(2)	(3)
IMFconditionality	0,424* (1,84)	0,511** (2,10)	0,533** (2,16)
Administration's Cycle Year	-0,118* (-1,71)	-0,094 (-1,27)	-0,097 (-1,31)
Interest Payments (% of Revenues)		0,019** (2,24)	0,019** (1,97)
Polity Index			0,021 (0,43)
Ideology	-0,184* (-1,86)	-0,244** (-2,33)	-0,254** (-2,27)
Dummy natural resources			0,114 (0,81)
Constant	0,580 (1,44)	0,348 (0,85)	0,135 (0,21)
Prob > chi2	0,0219	0,0025	0,0087
Number of Observations	190	166	166

* Significant at 10%

** Significant at 5%

*** Significant at 1%

z-statistic in parenthesis

Table 28
Econometric Results: Determinants of tax reform intensity

Explicative Variables	Mahon's Tax Reform Index (Taxref)		
	(1)	(2)	(3)
Adjusted fiscal balance		0,578 (1,26)	0,443 (0,94)
GDP per capita	-0,000007 (-0,65)	-0,000006 (-0,57)	-0,000007 (-0,55)
Purchasing Power Loss	0,019* (1,73)	0,263** (2,14)	0,247* (1,96)
IMFconditionality	0,050* (1,92)	0,048* (1,85)	0,024 (1,17)
Administration's Cycle Year			-0,023*** (-3,57)
Effective Number of Parties			-0,0017 (-0,12)
Executive Constrains Index	0,014 (0,83)	0,010 (0,60)	(-0,00007) (-0,00)
Polity Index			0,007 (0,39)
Ideology	-0,021* (-1,83)	-0,018 (-1,52)	-0,022 (-1,59)
Constant	0,022 (0,23)	0,022 (0,22)	0,129 (0,97)
Adjusted R-square	0,0935	0,2275	0,1625
Number of Observations	186	180	176

* Significant at 10%

** Significant at 5%

*** Significant at 1%

t-statistic in parenthesis

Table 29
Econometric Results: Determinants of VAT productivity

Explicative Variables	VAT Productivity				
	(1)	(2)	(3)	(4)	(5)
GDP per capita	0,00003*** (2,70)	0,00002** (2,29)	0,00003*** (2,80)	0,00004*** (3,48)	0,00003** (2,35)
Purchasing Power Loss	-0,20** (-2,22)	-0,19** (-3,12)	-0,20** (-2,49)	-0,195** (-2,57)	-0,23*** (-2,71)
IMFconditionality	0,057** (2,25)	0,047** (2,11)	0,055** (2,32)	0,055** (2,41)	0,055** (2,27)
Effective Number of Parties			0,041*** (2,87)	0,0267** (2,22)	0,041*** (2,63)
Executive Constrains Index	0,0014 (0,13)	0,062*** (3,81)		0,0478** (2,46)	0,057 (2,63)
Polity Index		-0,020*** (-2,73)		-0,026*** (-3,27)	-0,020*** (-2,89)
Ideology	0,0022 (0,22)		0,0025 (2,21)		0,0242** (2,15)
Constant	0,246*** (3,54)	0,119* (1,70)	0,0516 (0,48)	0,0465 (0,43)	-0,112 (-0,79)
Adjusted R-square	0,6441	0,5841	0,6383	0,6259	0,6744
Number of Observations	174	242	173	200	173

* Significant at 10%

** Significant at 5%

*** Significant at 1%

t-statistic in parenthesis

Table 30
Econometric Results: Determinants of Income tax productivity

Explicative variables	Income Tax Productivity	
	(1)	(2)
GDP per capita	0,00002*** (2,99)	0,00002*** (2,80)
Purchasing Power Loss	-0,169*** (-4,22)	-0,198*** (-4,38)
IMFconditionality	0,014 (1,10)	0,059 (0,43)
Effective Number of Parties	-0,027** (-2,44)	-0,0065 (-0,84)
Executive Constrains Index	0,027** (2,10)	0,025** (2,03)
Polity Index	-0,0119** (-2,36)	-0,0064 (-1,35)
Ideology		0,000 (0,01)
Constant	0,175** (2,29)	0,072 (1,31)
Adjusted R-square	0,7528	0,8115
Number of Obsevation	200	173

*** Significant at 1 percent

** Significant at 5 percent

* Significant at 10 percent

t-statistic in parenthesis

Table 31
Econometric Results: Determinants of the Tax Neutrality Index

Explicative variables	Tax Neutrality Index	
	(1)	(2)
GDP per capita	0,000013** (2,00)	0,00013** (1,98)
Purchasing Power Loss	-0,093* (-1,86)	-0,0926* (-1,85)
IMFconditionality	0,0114 (0,88)	0,0115 (0,88)
Effective Number of Parties	0,028*** (3,17)	0,028*** (3,15)
Executive Constrains Index	0,0159* (1,83)	0,0154 (1,19)
Polity Index		0,0003 (0,06)
Ideology	0,0190** (2,09)	0,019** (2,08)
Constant	0,173** (2,00)	0,173* (1,95)
Adjusted R-square	0,6320	0,6295
Number of Obsevation	173	173

*** Significant at 1 percent

** Significant at 5 percent

* Significant at 10 percent

t-statistic in parenthesis

Table 32
Econometric Results: Determinants of the use of "other" taxes

Explicative Variables	Other Taxes (% of current revenues)	
	(1)	(2)
Adjusted fiscal balance	-0,219*** (-2,92)	-0,233*** (-3,15)
Purchasing Power Loss	0,058*** (5,01)	0,060*** (5,14)
Effective Number of Parties	0,0037 (1,56)	0,005** (2,09)
Executive Constrains Index	0,0019 (0,72)	-0,010* (-1,73)
Polity Index		0,0059** (2,32)
Constant	0,004 (0,23)	0,027 (1,31)
Adjusted R-square	0,7514	0,7592
Number of Observations	173	173

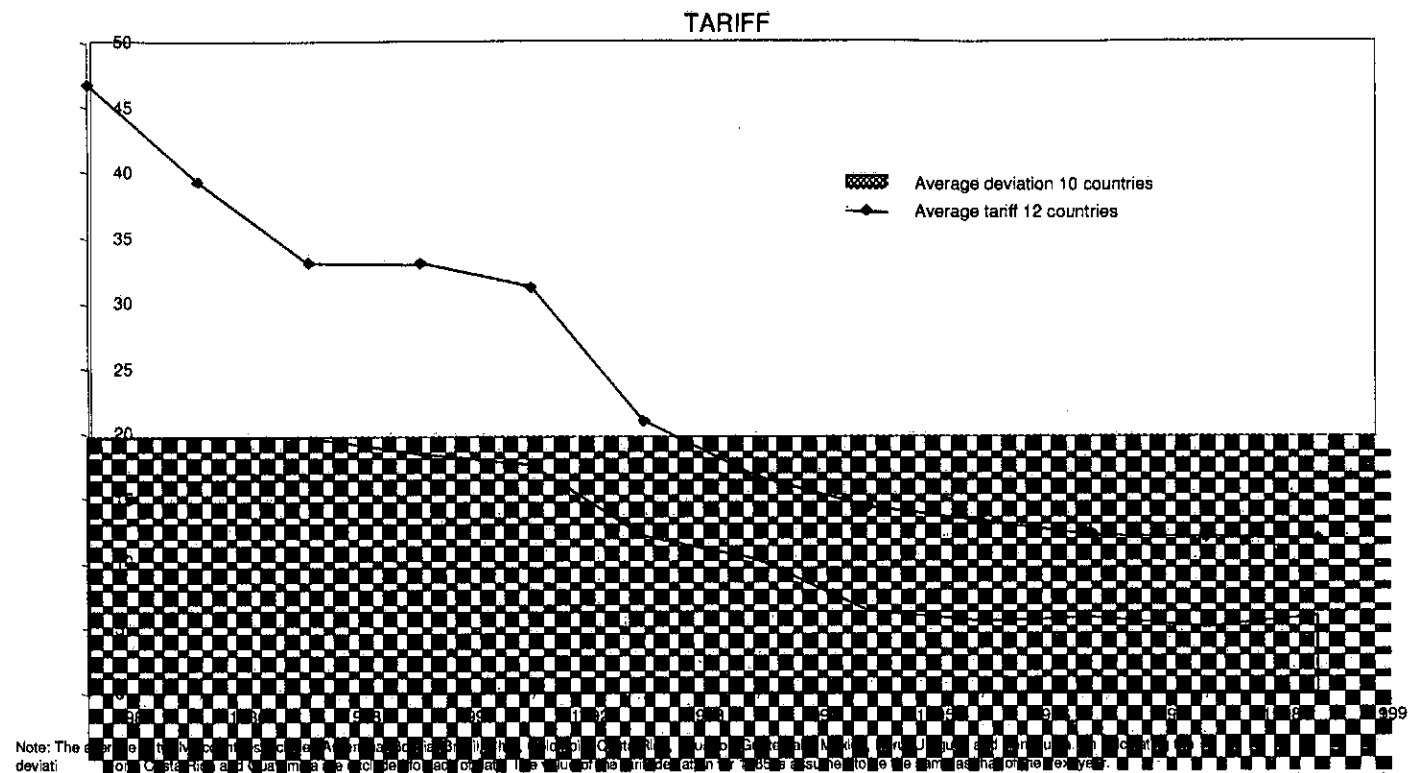
* Significant at 10%

** Significant at 5%

*** Significant at 1%

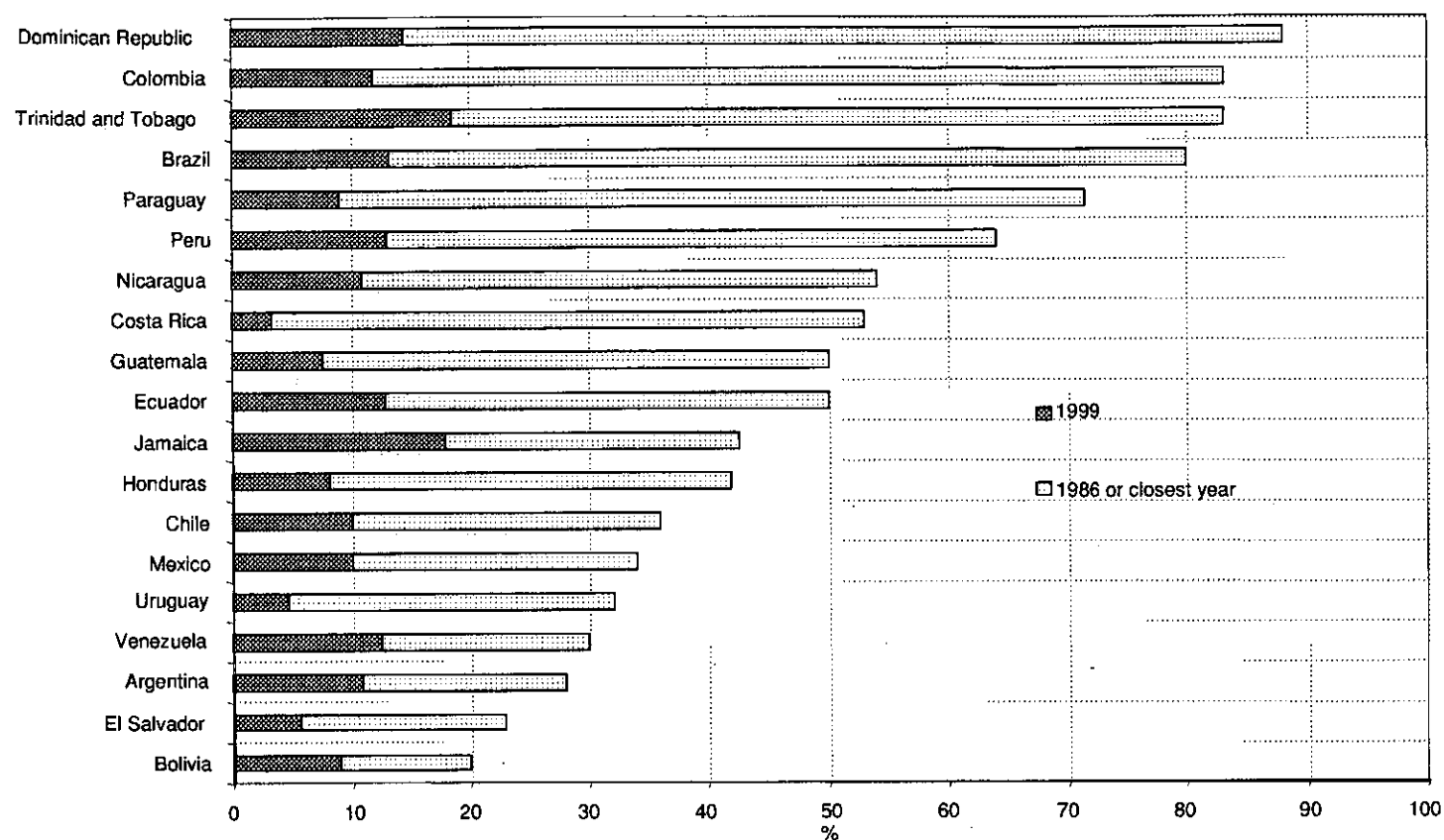
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Figure 1.
Tariff Liberalization, Latin America



Source: IDB Research Department WP 466. See Appendix 1.

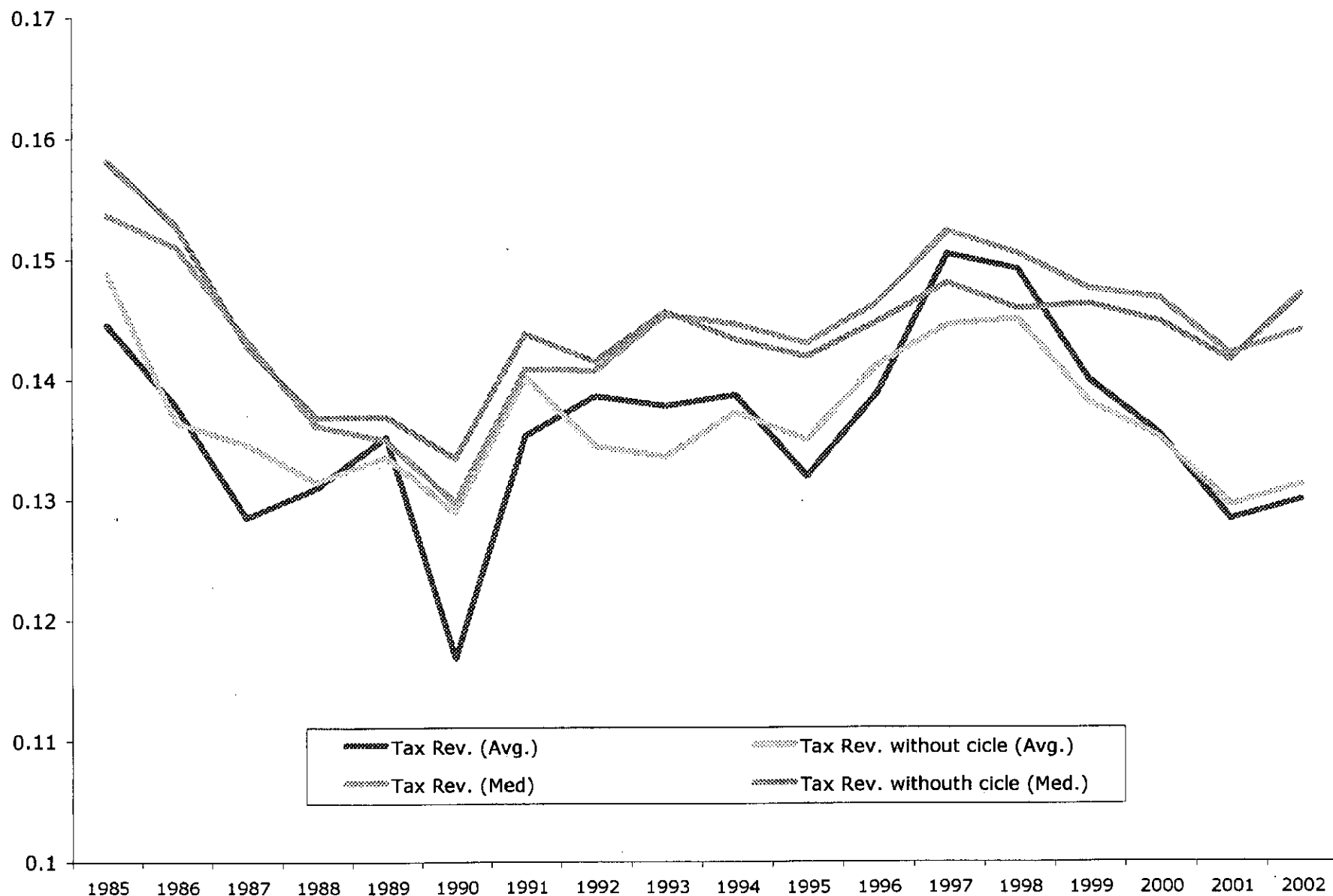
Figure 2.
Tariff Reduction in Latin America, 1999 vs. 1986



Source: IDB Research Department Working Paper 466. See Appendix 1.

Figure 3

Tax Revenues as gdp percentage*
(Average and Median)

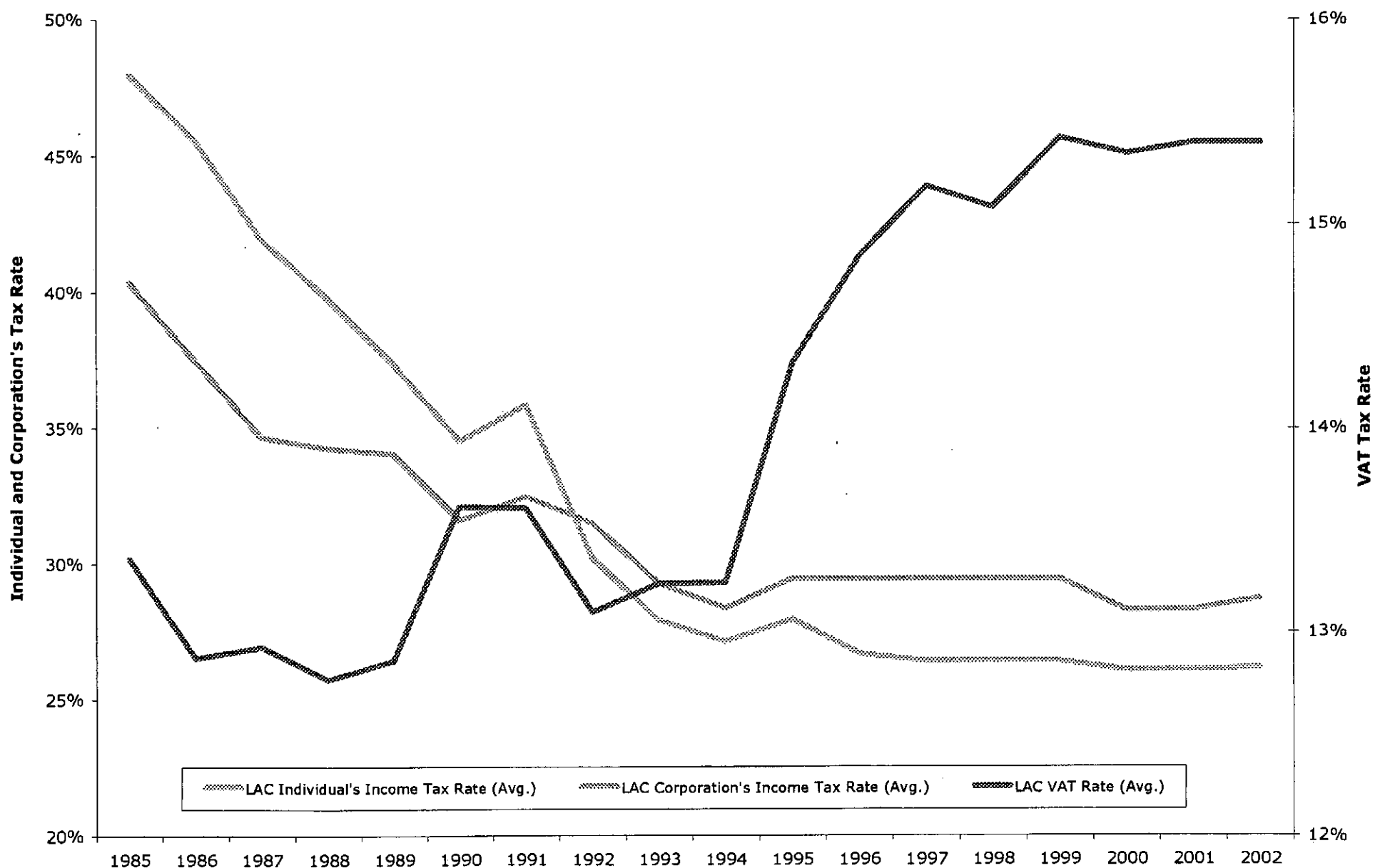


Source: IMF. Data from Government Finance Statistics and Article IV. Several Years

(*) Includes Argentina, Brazil, Chile, Colombia, Costa Rica, Ecuador, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, Paraguay, Peru, Dominican Republic, Uruguay and Venezuela.

Figure 4

Tax Rates: Value-Added Tax, Individual's Income Tax, Corporation's Income Tax*



Source: PriceWaterHouseCoopers: Individual Taxes and Corporation Taxes. Worldwide Summaries. Several years

(*) Includes Argentina, Brazil, Chile, Colombia, Costa Rica, Ecuador, El Salvador, Guatemala, Honduras, Jamaica, Mexico, Nicaragua, Paraguay, Peru, República Dominicana, Trinidad and Tobago, Uruguay and Venezuela.

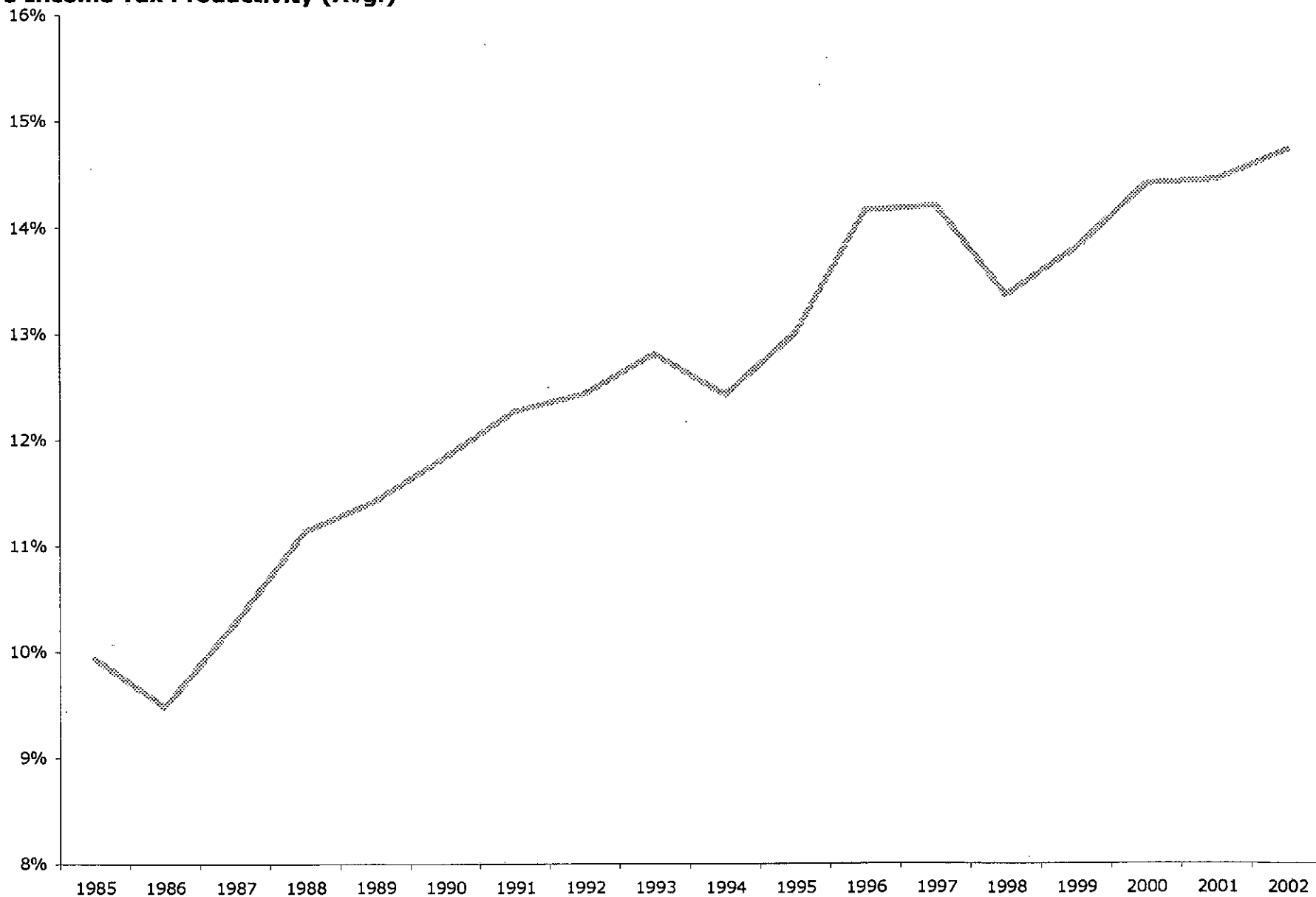
Figure 5
LAC's VAT Productivity (Avg.)*



Source: IMF. Data from Government Finance Statistics and Article IV. Several Years. PriceWaterHouseCoopers: Individual Taxes and Corporation Taxes. Worldwide Summaries. Several years

(*) Includes Argentina, Brazil, Chile, Colombia, Costa Rica, Ecuador, El Salvador, Guatemala, Honduras, Jamaica, Mexico, Nicaragua, Paraguay, Peru, República Dominicana, Trinidad y Tobago, Uruguay y Venezuela.

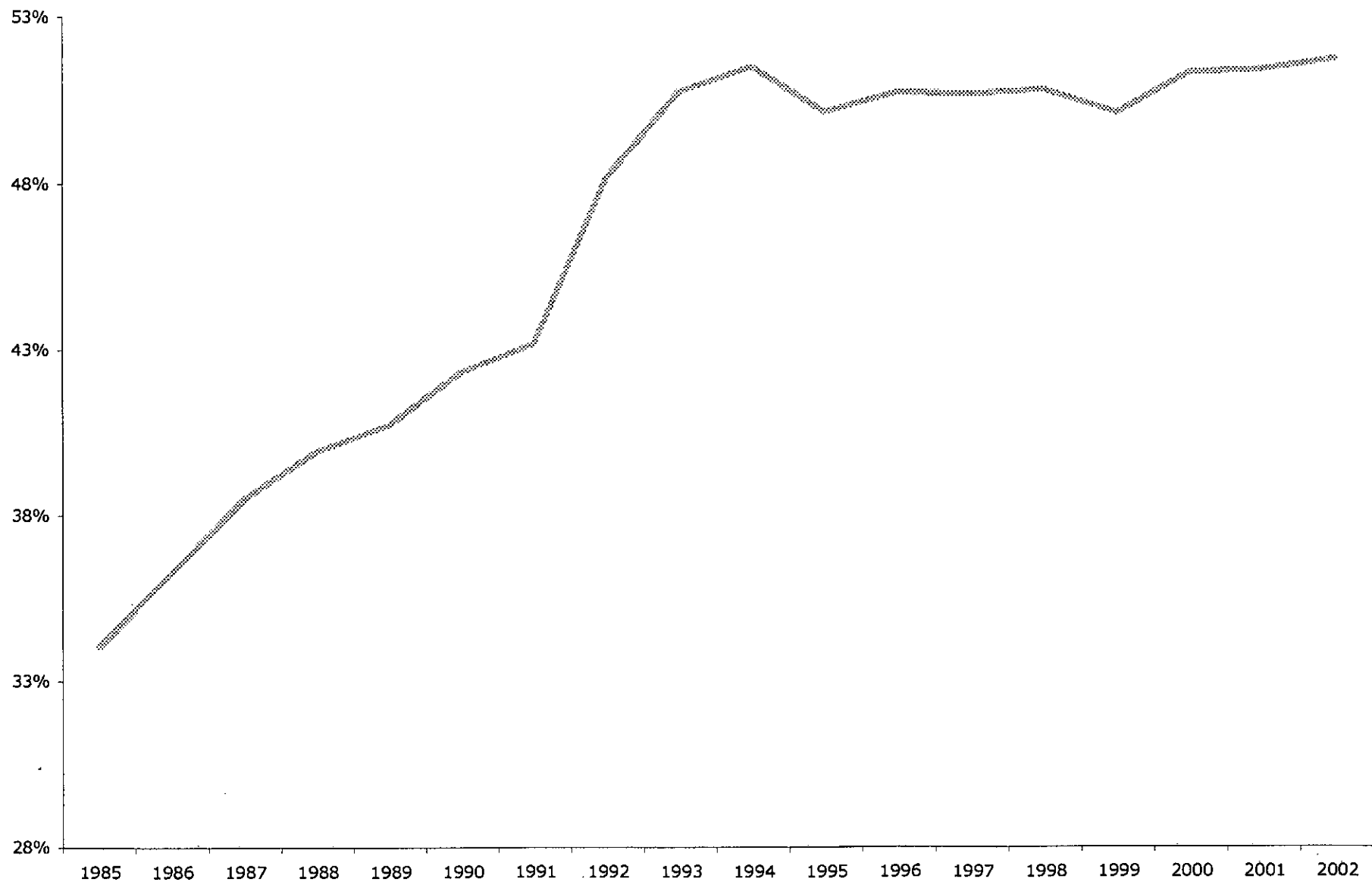
Figure 6
LAC's Income Tax Productivity (Avg.)



Source: IMF. Data from Government Finance Statistics and Article IV. Several Years. PriceWaterHouseCoopers: Individual Taxes and Corporation Taxes. Worldwide Summaries. Several years

(*) Includes Argentina, Brazil, Chile, Colombia, Costa Rica, Ecuador, El Salvador, Guatemala, Honduras, Jamaica, Mexico, Nicaragua, Paraguay, Peru, República Dominicana, Trinidad and Tobago, Uruguay and Venezuela.

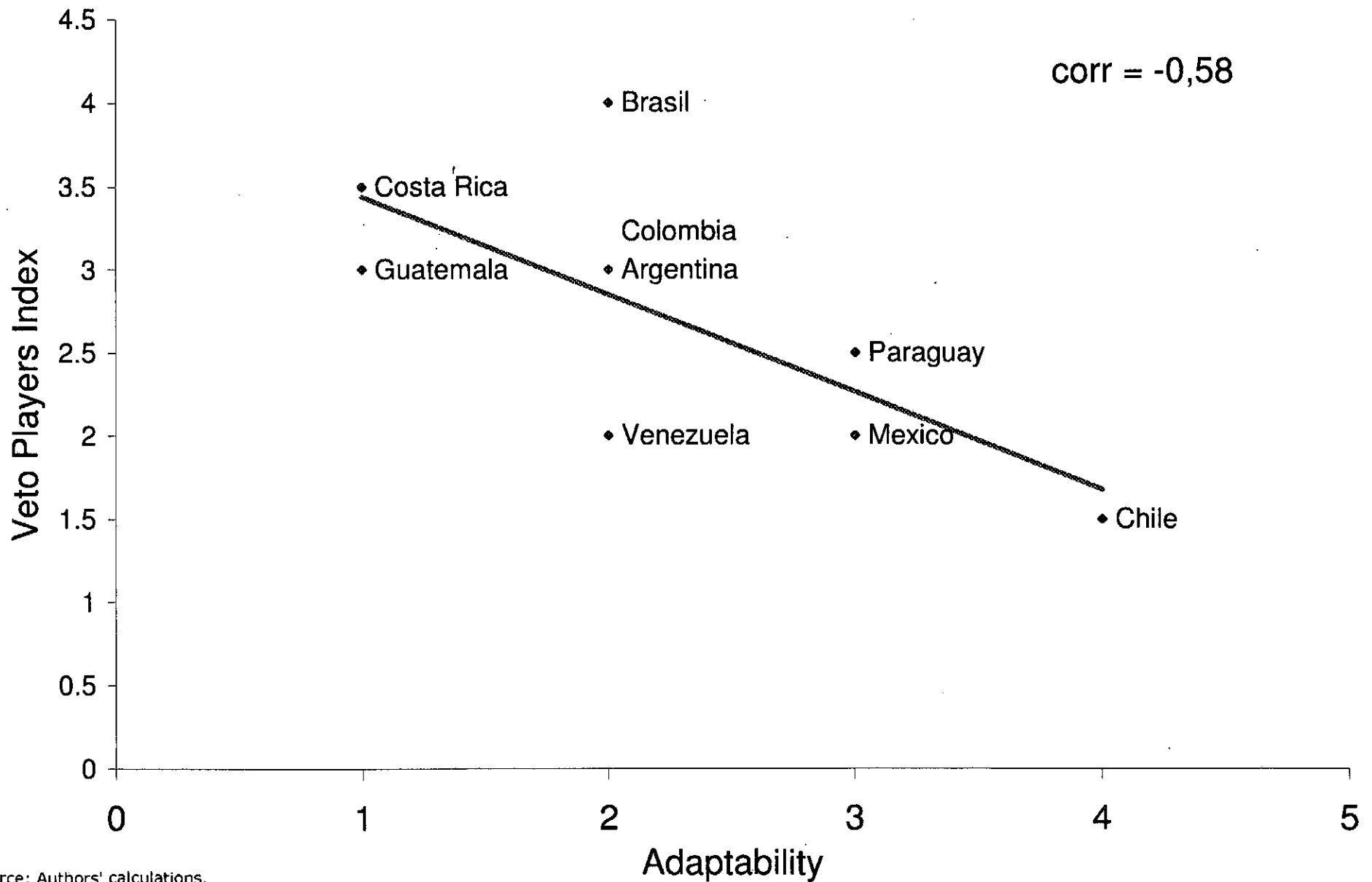
Figure 7
Neutrality Tax Index (Avg.)



Source: IMF. Data from Government Finance Statistics and Article IV. Several Years. PriceWaterHouseCoopers: Individual Taxes and Corporation Taxes. Worldwide Summaries. Several years

(*) Includes Argentina, Brazil, Chile, Colombia, Costa Rica, Ecuador, El Salvador, Guatemala, Honduras, Jamaica, Mexico, Nicaragua, Paraguay, Peru, República Dominicana, Trinidad and Tobago, Uruguay and Venezuela.

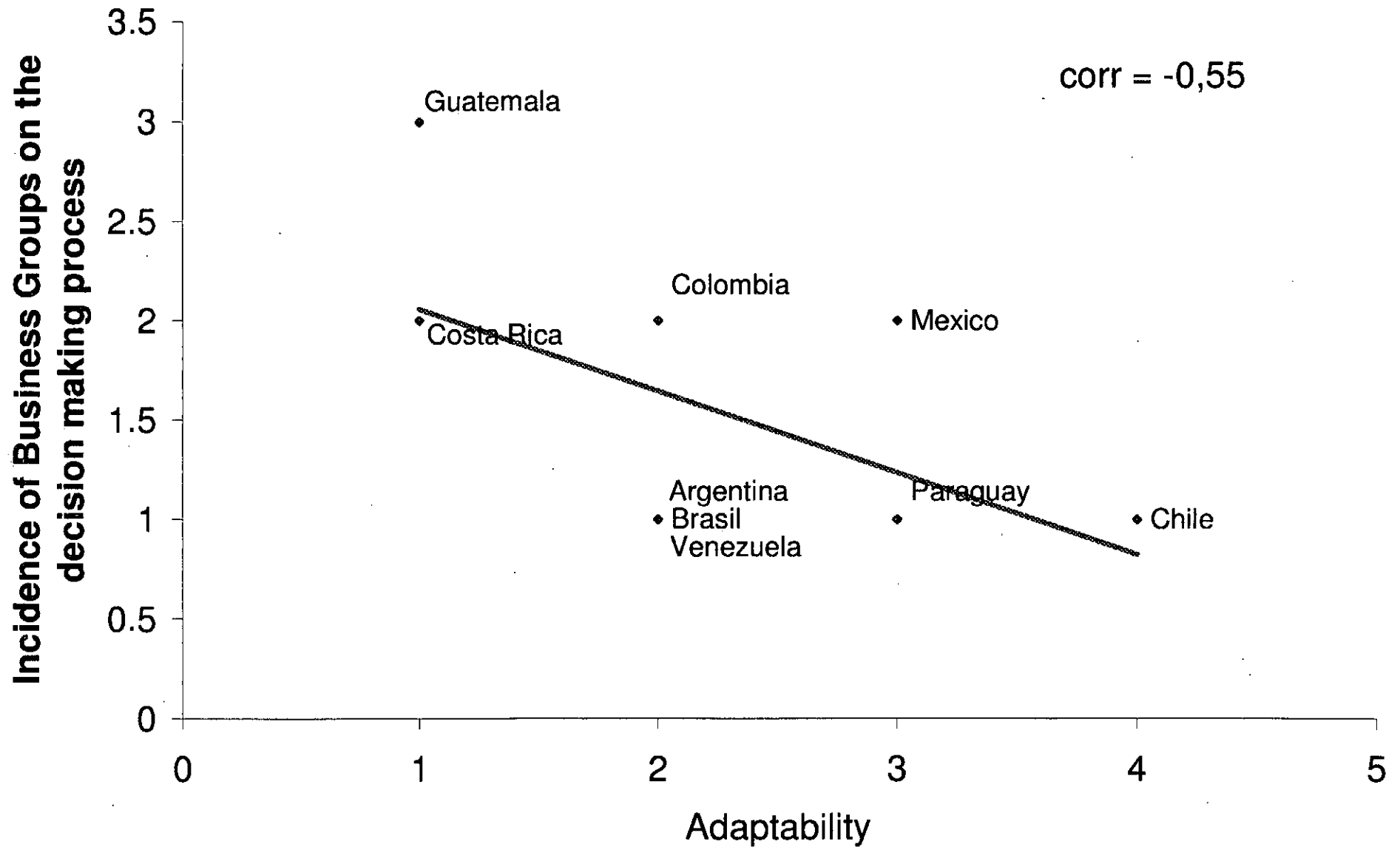
Figure 8
Adaptability vs. Veto Players Index



Source: Authors' calculations.

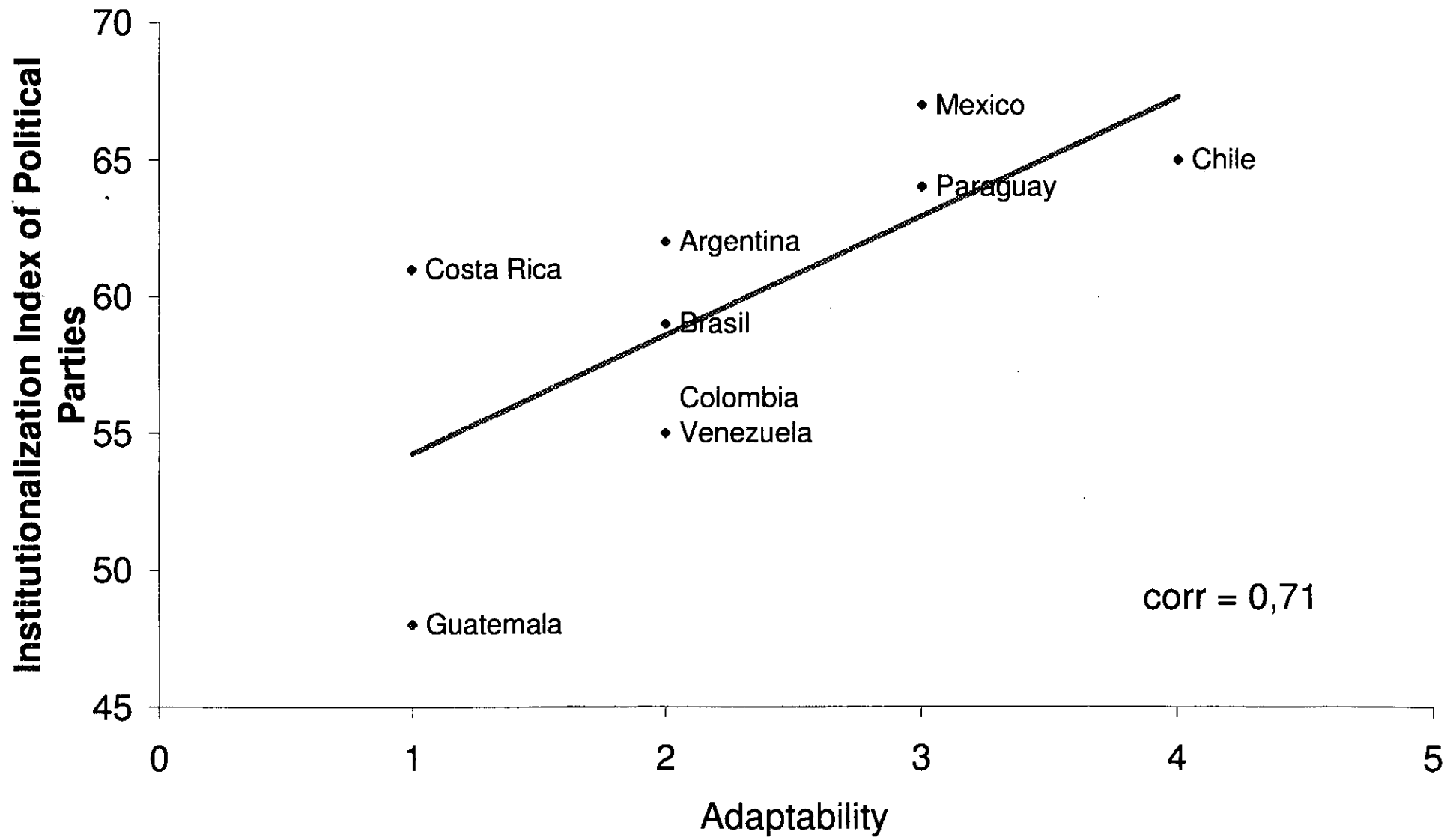
Figure 9

Adaptability vs Incidence of Business Groups on the decision making



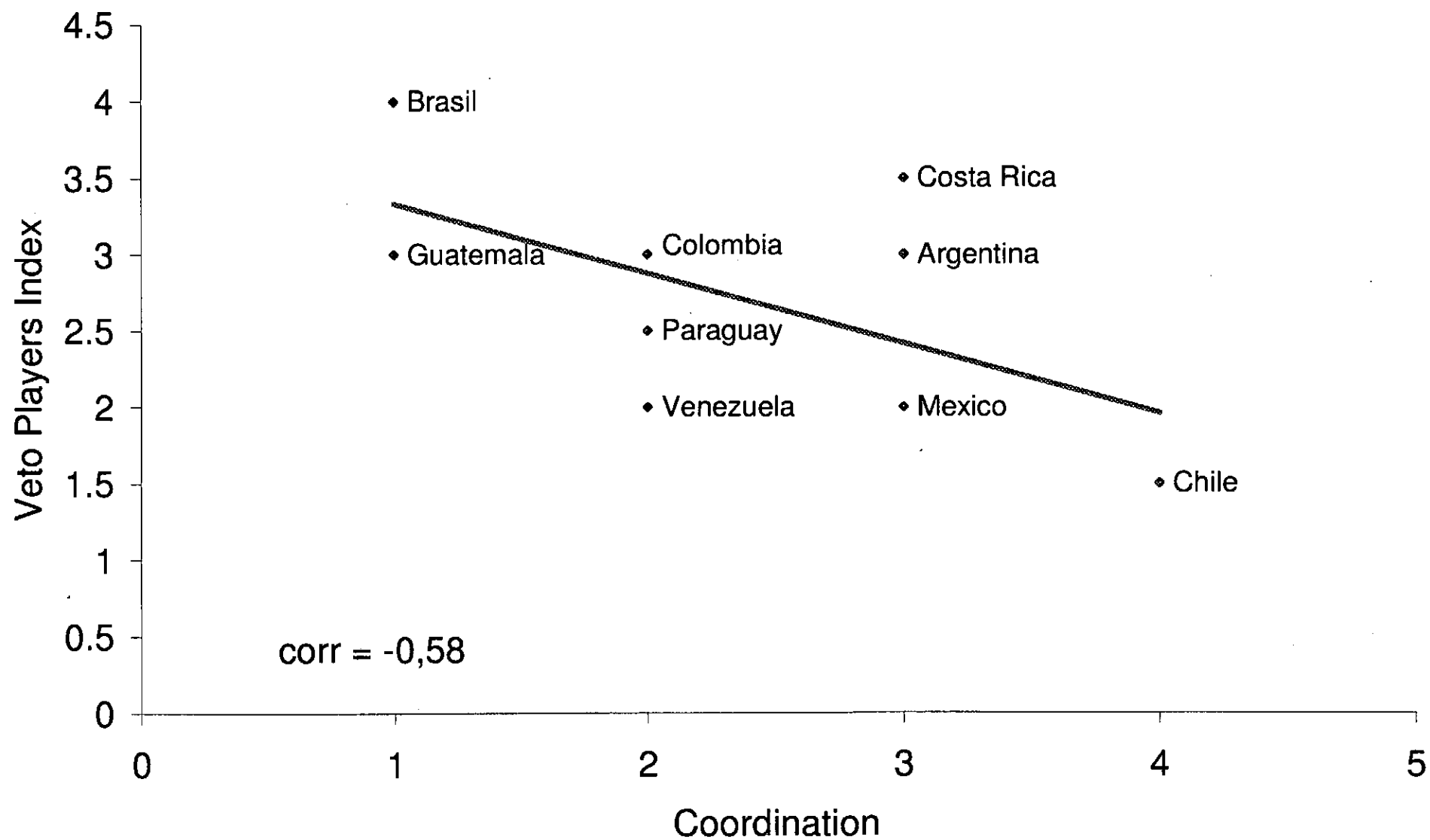
Source: Authors' calculations.

Figure 10
Adaptability vs Institutionalization Index of Political Parties



Source: Jones (2005) and author's calculations.

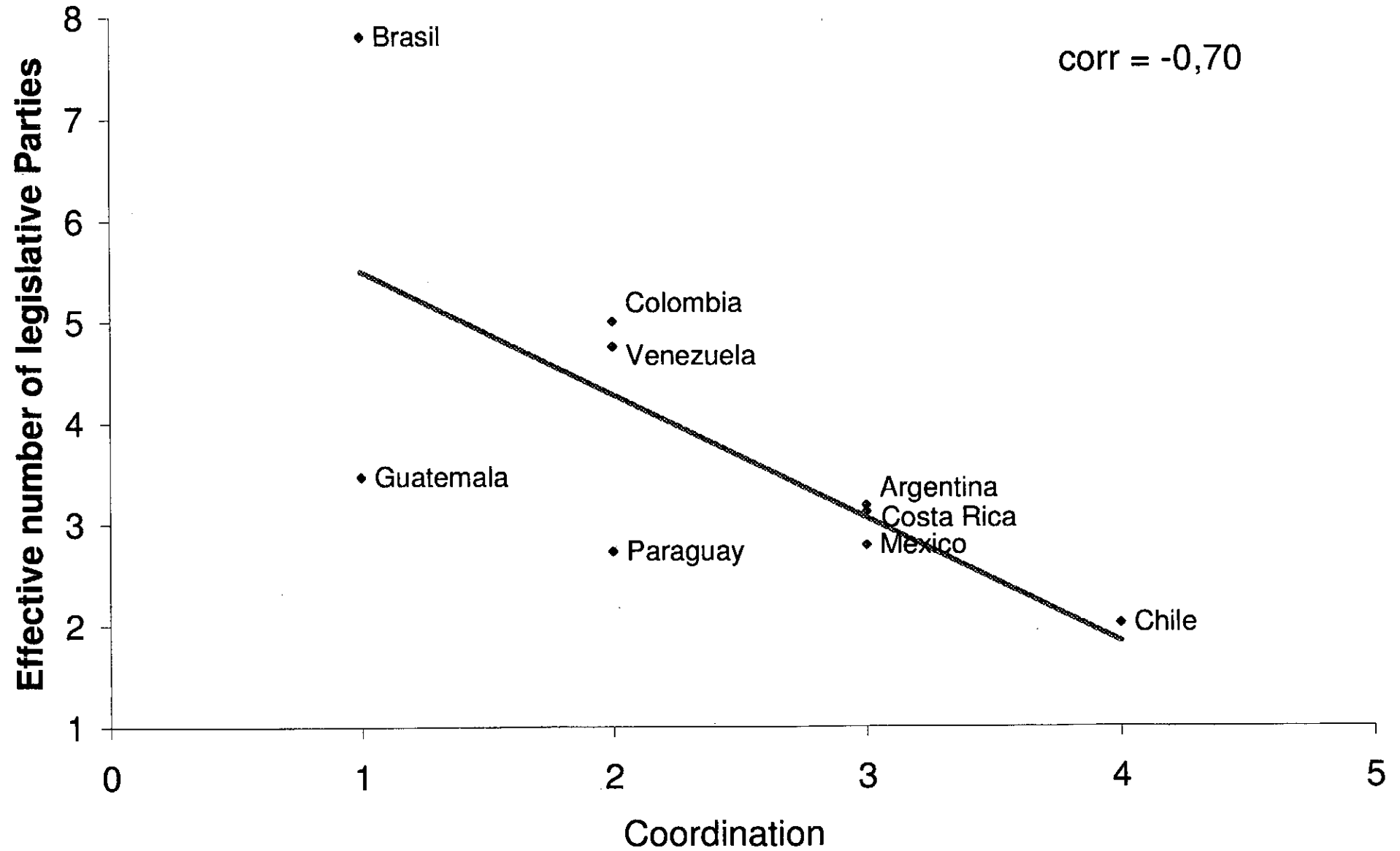
Figure 11
Coordination vs Veto Players Index



Source: Authors' calculations.

Figure 12

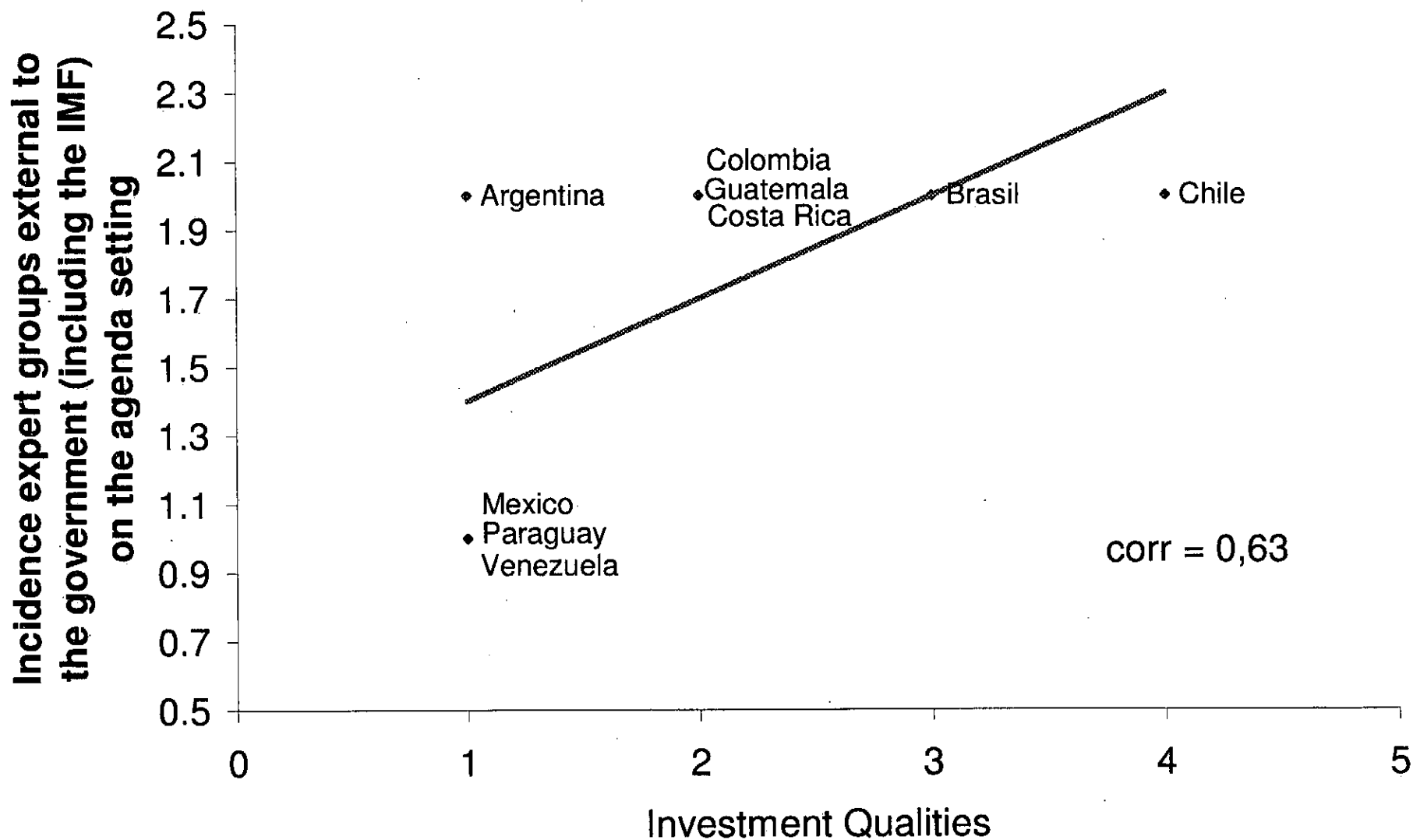
Coordination vs Effective number of legislative parties



Source: Jones (2005) and author's calculations.

Figure 13

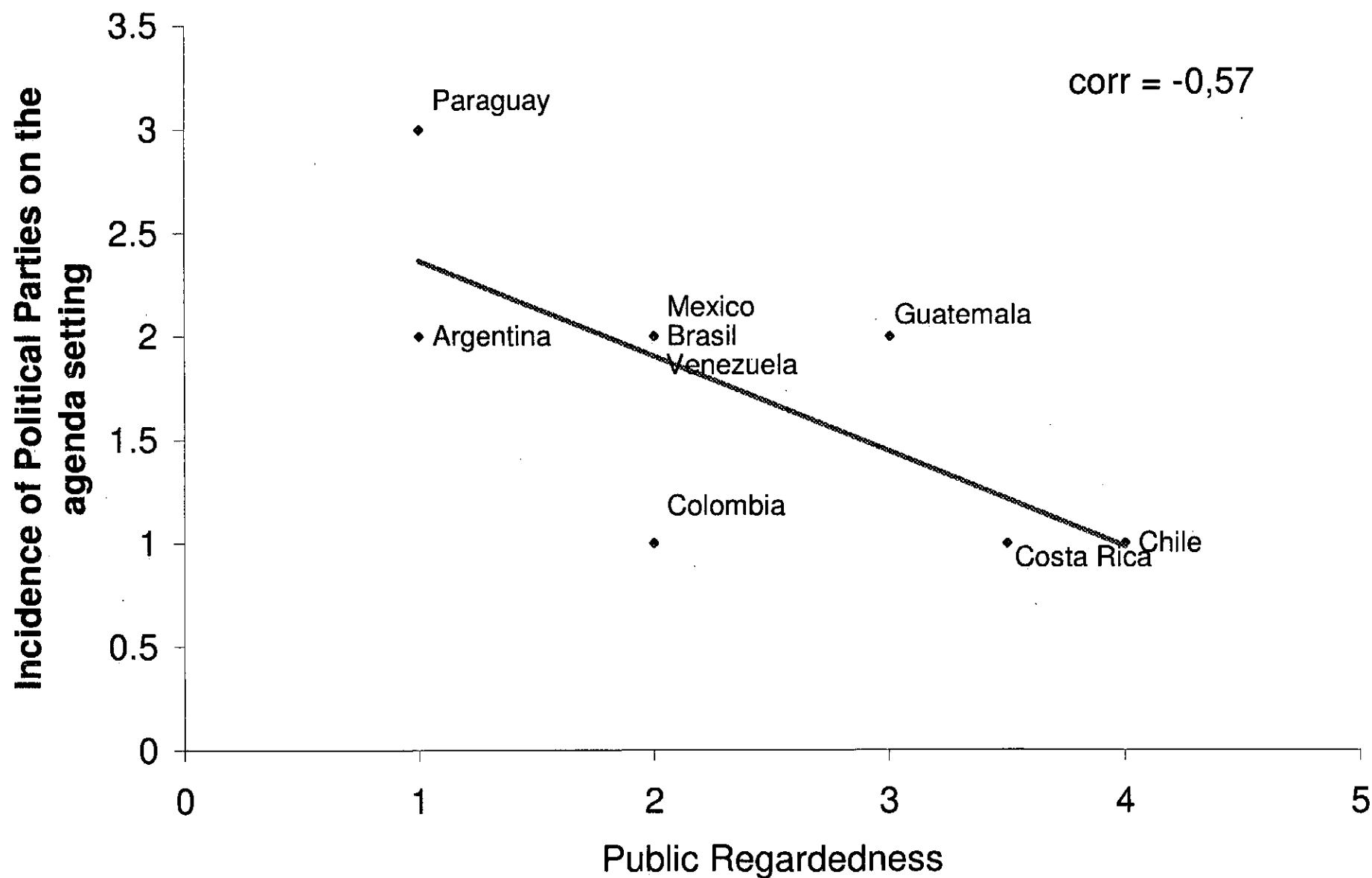
**Investment-related qualities vs Incidence of expert groups external to the government
(including the IMF) on the agenda setting**



Source: Authors' calculations.

Figure 14

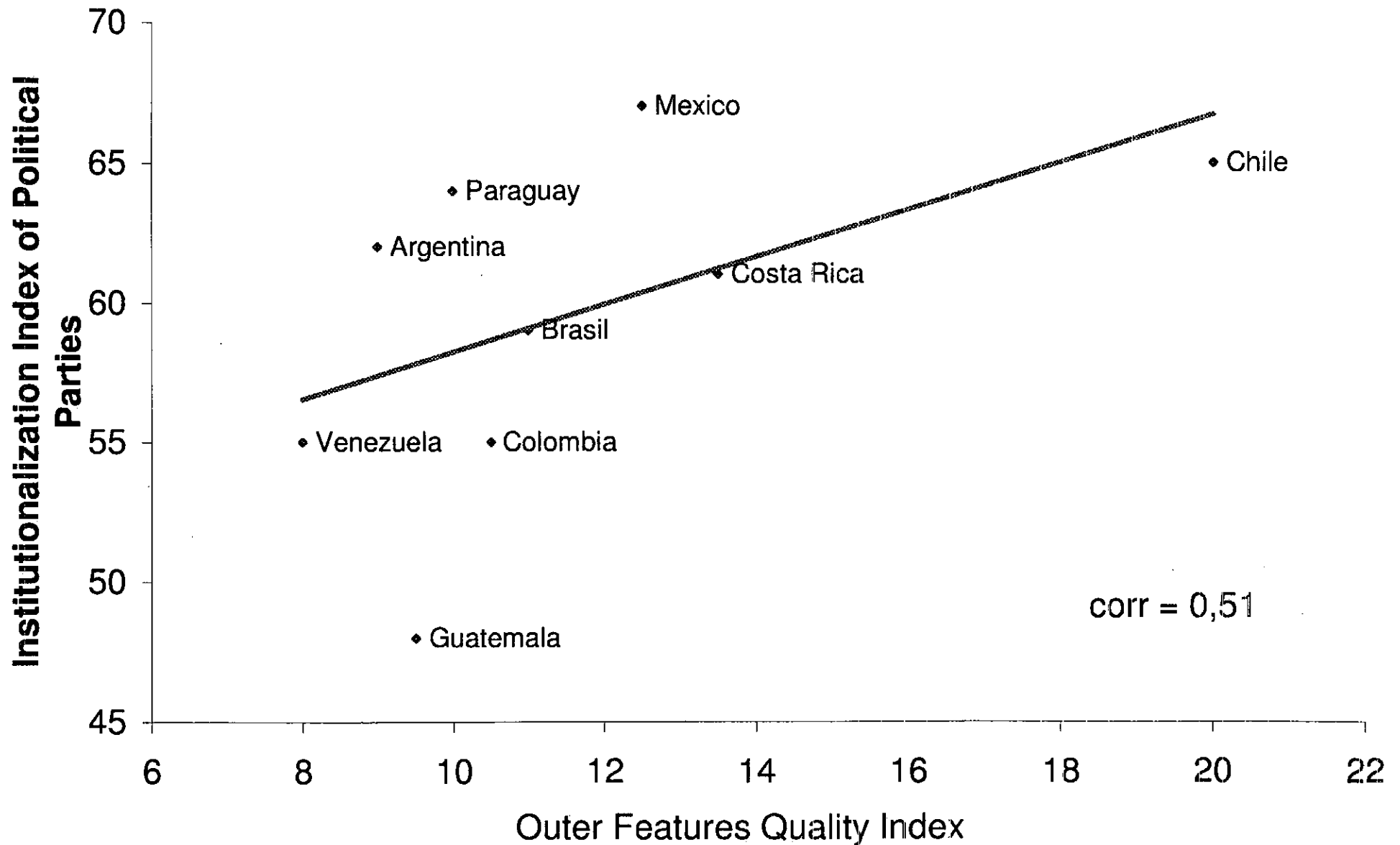
Public Regardness vs Incidence of Political Parties on the tax policy agenda setting



Source: Authors' calculations.

Figure 15

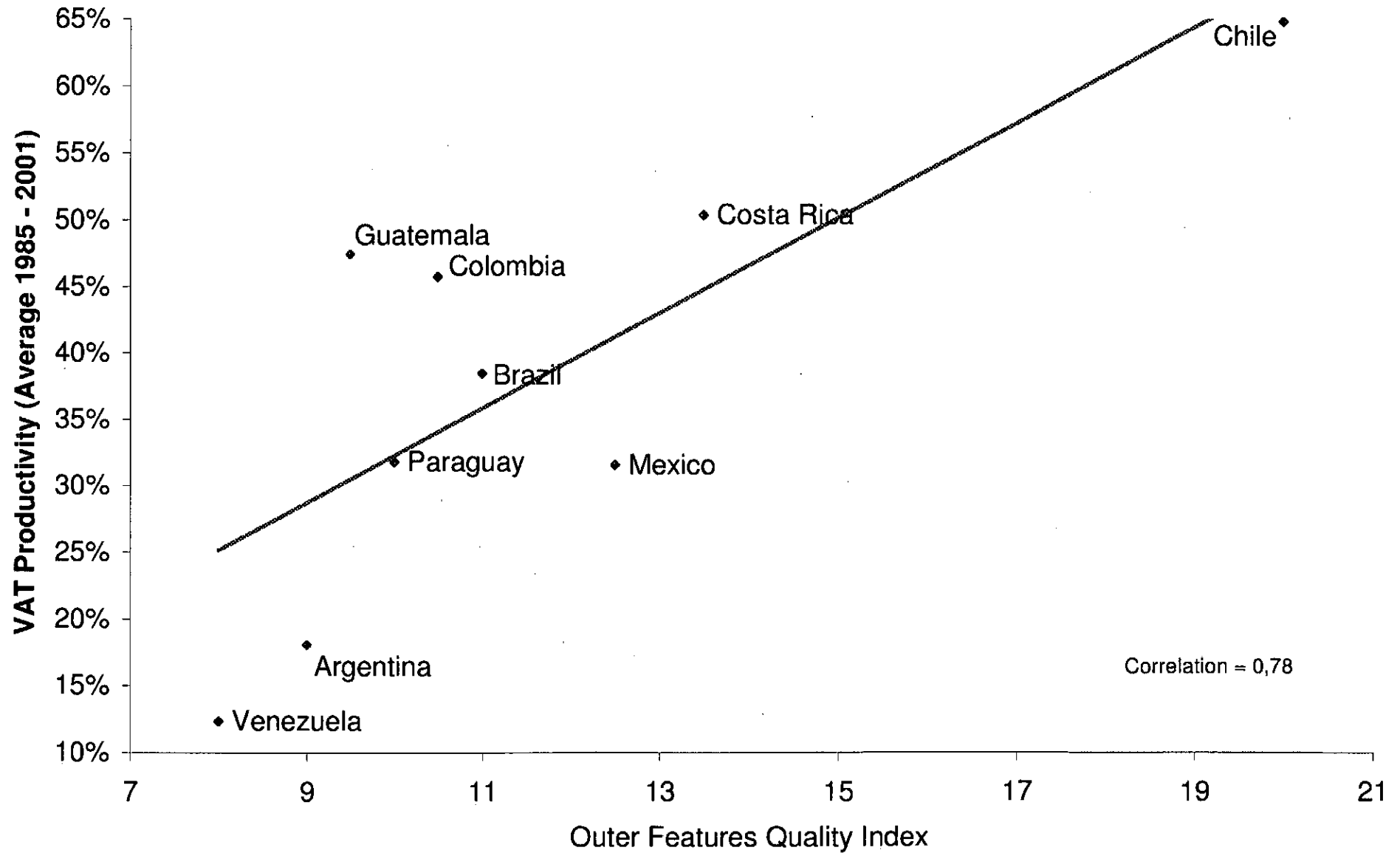
Outer Features Quality Index vs Institutionalization Index of Political Parties



Source: Jones (2005) and author's calculations.

Figure 16

Outer Features Quality Index vs Average VAT Productivity



id	country	year	Tax Rev. (/txr_hp		txr_trend	Tax Rev. with txr_strlac_med	
19	ALC_MEC	1985	0.144574	0.005125	0.133371	0.1488538	0.1523536
19	ALC_MEC	1986	0.137779	0.005522	0.13606	0.1364394	0.1427523
19	ALC_MEC	1987	0.12856	0.002209	0.138828	0.1346585	0.1300807
19	ALC_MEC	1988	0.130986	-0.008083	0.141419	0.1314705	0.1327827
19	ALC_MEC	1989	0.135253	-0.006664	0.139325	0.1335605	0.1374495
19	ALC_MEC	1990	0.116868	-0.008418	0.137277	0.1289991	0.1210013
19	ALC_MEC	1991	0.135385	-0.001353	0.135234	0.1402435	0.1392487
19	ALC_MEC	1992	0.138675	0.003662	0.133831	0.1344981	0.1377444
19	ALC_MEC	1993	0.137828	0.001287	0.13512	0.1336309	0.137815
19	ALC_MEC	1994	0.138741	0.001211	0.138205	0.1372696	0.1375317
19	ALC_MEC	1995	0.131963	-0.001063	0.140425	0.135017	0.1292332
19	ALC_MEC	1996	0.138906	-0.000254	0.140806	0.1412556	0.1352474
19	ALC_MEC	1997	0.150466	0.007156	0.137714	0.1445733	0.1443664
19	ALC_MEC	1998	0.149162	0.005997	0.134174	0.145101	0.1438345
19	ALC_MEC	1999	0.140021	0.00051	0.136528	0.138145	0.1377604
19	ALC_MEC	2000	0.135475	-0.000538	0.136972	0.1351869	0.1329148
19	ALC_MEC	2001	0.128408	-0.003238	0.137081	0.1295765	0.1280151
19	ALC_MEC	2002	0.13	-0.003325	0.131812	0.1313011	0.13275

id	country	year	Tax Rev. (/txr_hp		txr_trend	Tax Rev. w txr_strlac	
18	ALC	1985	0.153703	0.007557	0.1461467	0.158152	0.150201
18	ALC	1986	0.151057	0.006314	0.1447422	0.152841	0.146045
18	ALC	1987	0.143375	-3.87E-05	0.1434133	0.142946	0.134534
18	ALC	1988	0.136163	-0.006135	0.1422987	0.136822	0.131011
18	ALC	1989	0.134981	-0.006556	0.1415366	0.136974	0.131745
18	ALC	1990	0.129798	-0.011406	0.1412042	0.133461	0.121173
18	ALC	1991	0.140941	-0.000372	0.1413127	0.14385	0.139124
18	ALC	1992	0.140769	-0.000991	0.1417595	0.141514	0.137145
18	ALC	1993	0.145389	0.002951	0.1424384	0.145661	0.139299
18	ALC	1994	0.144629	0.001396	0.1432329	0.143362	0.135813
18	ALC	1995	0.143037	-0.001019	0.1440564	0.141925	0.135567
18	ALC	1996	0.146351	0.001515	0.144836	0.144814	0.138556
18	ALC	1997	0.152368	0.006879	0.1454888	0.148067	0.139298
18	ALC	1998	0.150473	0.004526	0.1459467	0.14592	0.136533
18	ALC	1999	0.147593	0.001382	0.1462109	0.146322	0.140277
18	ALC	2000	0.146807	0.00048	0.1463275	0.144867	0.13741
18	ALC	2001	0.142155	-0.004202	0.1463565	0.141647	0.135345
18	ALC	2002	0.144084	-0.002279	0.1463627	0.147066	0.143476

TASA IVA/ Value-Added Tax Rate	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002
LAC VAT Rate (Avg.)	0.133571	0.128692	0.129231	0.127643	0.128571	0.136133	0.136063	0.130944	0.132368	0.132395	0.143184	0.148447	0.151868	0.150816	0.154237	0.153447	0.153974	0.153974
LAC median	0.105	0.1	0.1	0.1	0.1	0.13	0.1335	0.1	0.11	0.1	0.13	0.15	0.15	0.15	0.15	0.15	0.15	0.15
LAC AVERAGE (1)	0.133571	0.128692	0.129231	0.127643	0.128571	0.135143	0.137643	0.136214	0.138571	0.138607	0.149321	0.156464	0.156464	0.155036	0.160036	0.160036	0.16075	0.16075
LAC MEDIAN (1)	0.105	0.1	0.1	0.1	0.1	0.125	0.1335	0.11	0.12	0.115	0.145	0.15	0.15	0.15	0.15	0.15	0.15	0.15
Tasa máxima de tributación personal (%) / Maximum Personal Tax Rate	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002
LAC Individual's Income Tax Rate (Avg.)	0.4795	0.455727	0.419628	0.397961	0.373517	0.345183	0.358595	0.301842	0.279211	0.271316	0.279474	0.266842	0.264211	0.264211	0.264211	0.260789	0.260789	0.261842
LAC median	0.5	0.48	0.45	0.45	0.38	0.33665	0.34	0.3	0.3	0.26	0.3	0.3	0.3	0.3	0.3	0.25	0.25	0.27
LAC AVERAGE (1)	0.46325	0.44825	0.397692	0.383077	0.353077	0.329231	0.348571	0.3025	0.289643	0.2825	0.288571	0.273571	0.27	0.27	0.27	0.265357	0.265357	0.266786
LAC MEDIAN (1)	0.495	0.48	0.45	0.45	0.36	0.3	0.32	0.3	0.285	0.28	0.3	0.3	0.3	0.3	0.3	0.25	0.25	0.26
Tasa máxima de tributación de las empresas (%) / Maximum Business Tax Rate	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002
LAC Corporation's Income Tax Rate (Avg.)	0.403684	0.374737	0.346572	0.34235	0.340406	0.315961	0.324753	0.314805	0.292568	0.283621	0.294542	0.294542	0.294542	0.294542	0.294542	0.282805	0.283158	0.287368
LAC median	0.42	0.42	0.35	0.345	0.345	0.31665	0.3333	0.3333	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3
LAC AVERAGE (1)	0.397857	0.358571	0.327692	0.321846	0.322615	0.296462	0.309786	0.292714	0.280393	0.26825	0.285214	0.285214	0.285214	0.285214	0.285214	0.271429	0.272143	0.277857
LAC MEDIAN (1)	0.42	0.41	0.35	0.34	0.34	0.3	0.32	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.25	0.25	0.26

piva carlosa brazil all	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002
Argentina	12.7%	13.1%	11.4%	3.3%	4.6%	8.2%	8.8%	13.2%	18.1%	18.5%	16.8%	18.4%	17.5%	17.6%	17.6%	19.7%	15.7%	27.2%
Bolivia	5.4%	3.6%	15.4%	25.1%	26.2%	24.7%	29.4%	29.5%	31.9%	37.6%	35.4%	50.0%	49.1%	47.7%	31.9%	31.3%	32.0%	39.2%
Brasil All	24.1%	28.0%	26.2%	24.6%	27.9%	35.4%	31.2%	30.4%	28.1%	28.8%	29.1%	30.0%	27.0%	25.7%	27.0%	27.3%	29.7%	30.3%
Chile	41.5%	43.5%	42.0%	49.3%	45.5%	40.4%	44.8%	47.0%	47.0%	48.2%	46.5%	47.9%	42.7%	41.9%	43.0%	44.9%	44.6%	46.3%
Colombia	28.0%	29.1%	29.5%	29.0%	29.5%	27.5%	31.1%	35.2%	37.2%	32.7%	27.2%	27.8%	28.3%	26.9%	27.7%	32.9%	30.5%	27.1%
Costa Rica	27.4%	32.8%	30.1%	20.0%	18.9%	28.2%	30.2%	42.1%	36.3%	37.2%	39.8%	35.0%	33.0%	36.3%	35.3%	35.8%	37.0%	36.0%
Ecuador	17.2%	27.5%	25.2%	28.7%	29.1%	31.0%	31.1%	32.3%	33.7%	33.4%	31.3%	31.6%	33.5%	33.7%	29.5%	46.0%	50.9%	48.8%
El Salvador								33.4%	41.6%	42.5%	36.6%	40.1%	36.7%	37.2%	36.4%	40.8%	45.1%	44.4%
Guatemala	27.0%	28.2%	31.3%	32.6%	32.7%	31.7%	27.9%	34.3%	34.6%	33.6%	37.6%	34.4%	36.9%	39.5%	42.6%	43.2%	39.5%	42.2%
Honduras	29.0%	28.6%	29.2%	30.2%	35.5%	52.2%	39.5%	39.0%	39.2%	35.8%	47.2%	47.7%	51.0%	65.4%	43.2%	42.6%	38.5%	39.5%
Jamaica							16.7%	67.7%	67.0%	60.2%	59.2%	57.3%	46.8%	53.2%	52.5%	55.7%	56.4%	57.7%
México	20.0%	19.9%	21.7%	20.6%	20.7%	23.8%	22.2%	25.8%	25.4%	25.8%	19.3%	19.4%	20.5%	20.3%	21.6%	22.6%	23.4%	23.6%
Nicaragua	24.4%			22.1%	26.7%	22.9%	14.3%	23.0%	29.0%	28.8%	19.1%	20.8%	24.5%	27.6%	29.4%	31.0%	30.0%	31.5%
Paraguay								17.1%	30.9%	33.6%	37.5%	35.4%	39.1%	38.8%	38.2%	37.2%	36.9%	34.7%
Perú	23.1%	21.7%	17.5%	25.0%	17.0%	9.9%	15.4%	20.6%	27.1%	32.3%	33.0%	32.9%	34.8%	34.8%	34.2%	35.1%	34.1%	34.8%
República Dominicana		15.8%	20.4%	20.9%	22.7%	24.8%	24.2%	32.6%	41.8%	40.5%	30.6%	24.5%	34.6%	34.0%	35.8%	35.1%	45.6%	48.1%
Trinidad y Tobago						34.2%	33.7%	30.8%	33.4%	37.2%	37.6%	30.5%	29.2%	35.8%	30.5%	28.4%	29.1%	27.9%
Uruguay	33.4%	33.4%	31.3%	36.5%	32.5%	25.7%	26.4%	27.3%	24.4%	24.0%	26.0%	26.6%	37.9%	38.8%	38.9%	26.5%	26.7%	26.4%
Venezuela									6.1%	28.0%	36.2%	42.5%	35.7%	32.1%	31.5%	31.1%	29.6%	32.2%
LAC's VAT Productivity (	24.1%	25.0%	25.5%	26.3%	26.4%	28.0%	26.7%	32.3%	33.3%	34.7%	34.0%	34.4%	34.7%	36.2%	34.0%	35.1%	35.5%	36.7%
Median LAC	24.4%	28.0%	26.2%	25.1%	27.3%	27.5%	28.7%	31.5%	33.4%	33.6%	35.4%	32.9%	34.8%	35.8%	34.2%	35.1%	34.1%	34.8%
Average LAC (I)	24.1%	25.0%	25.5%	26.3%	26.4%	27.6%	26.9%	30.9%	32.4%	32.7%	31.4%	31.9%	33.7%	35.0%	32.7%	33.9%	34.2%	35.8%
Median LAC (I)	24.4%	28.0%	26.2%	25.1%	27.3%	26.6%	28.7%	31.4%	32.8%	33.1%	30.9%	30.8%	34.1%	34.4%	33.1%	34.0%	33.0%	35.4%

Source: IMF. Data from Government Finance Statistics and Article IV. Several Years. PriceWaterHouseCoopers: Individual Taxes and Corporation Taxes. Worldwide Summaries. Several years

(*) Corresponde a Argentina, Brazil, Chile, Colombia, Costa Rica, Ecuador, El Salvador, Guatemala, Honduras, Jamaica, México, Nicaragua, Paraguay, Perú, República Dominicana, Trinidad y Tobago, Uruguay y Venezuela.

(1) Corresponde a Argentina, Brazil, Chile, Colombia, Costa Rica, Ecuador, Guatemala, Honduras, México, Nicaragua, Perú, Rep. Dominicana y Uruguay. La omisión de países se debe a la ausencia de datos en ciertos años.

	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002
income per capita																		
Argentina	0.019623	0.024269	0.030395	0.010173	0.015656	0.009939	0.009987	0.012348	0.040774	0.052737	0.048204	0.057475	0.061741	0.072687	0.075528	0.069074	0.070685	0.052396
Bolivia	0.007209	0.010832	0.060138	0.120493	0.147629	0.133782	0.151474	0.160263	0.129385	0.076267	0.021568	0.058413	0.066251	0.069446	0.077626	0.073392	0.063047	0.079136
Brasil	0.093656	0.092013	0.086285	0.095314	0.137656	0.152107	0.10973	0.119579	0.119719	0.145817	0.14	0.145455	0.157842	0.201692	0.196	0.179048	0.190476	0.224762
Chile	0.1	0.1	0.1	0.096667	0.09	0.070054	0.112092	0.112773	0.112034	0.119478	0.120862	0.133793	0.129873	0.129772	0.116667	0.136667	0.15	0.157143
Colombia	0.058421	0.091436	0.115702	0.114224	0.117276	0.1242	0.194841	0.198617	0.149988	0.133374	0.114842	0.109393	0.125383	0.124245	0.120816	0.122603	0.146099	0.152858
Costa Rica	0.052445	0.048017	0.084476	0.083594	0.081963	0.082207	0.07661	0.059975	0.071491	0.076313	0.081459	0.078908	0.080794	0.08886	0.106309	0.098419	0.110086	0.111465
Ecuador	0.031083	0.04	0.04	0.035	0.0425	0.048	0.056	0.052	0.052	0.056	0.068	0.064	0.068	0.06	0.028	0.072	0.088	0.088
El Salvador	0.049747	0.06637	0.058662	0.051038	0.044403	0.051011	0.057743	0.045281	0.076811	0.103126	0.122569	0.123037	0.108686	0.103788	0.119161	0.116567	0.096733	0.119873
Guatemala	0.021984	0.024273	0.032133	0.06017	0.050703	0.043453	0.064728	0.054427	0.073595	0.045331	0.058294	0.076312	0.077515	0.070139	0.077854	0.079463	0.082729	0.096666
Honduras	0.071857	0.071436	0.078031	0.080085	0.07712	0.074631	0.088572	0.106062	0.097801	0.084993	0.114216	0.115494	0.10639	0.125611	0.10528	0.130066	0.14282	0.140762
Jamaica	0.249656	0.285891	0.310506	0.323096	0.332314	0.357952	0.321626	0.329407	0.337415	0.317309	0.342224	0.314014	0.333262	0.333412	0.392722	0.383503	0.350706	0.353389
México	0.084536	0.086598	0.0886	0.103066	0.115139	0.132173	0.133052	0.147131	0.157437	0.151244	0.120154	0.117293	0.13204	0.136926	0.146072	0.136109	0.133333	0.135592
Nicaragua							0.031024	0.055226	0.048554	0.036651	0.055557	0.06085	0.070416	0.071455	0.074355	0.094176	0.096496	0.112787
Paraguay	0.040893	0.039554	0.046586	0.041637	0.041338	0.03796	0.037907	0.091202	0.097011	0.13302	0.150483	0.148415	0.136522	0.134574	0.152224	0.118486	0.108767	0.1219
Perú	0.026421	0.061523	0.045757	0.069492	0.037991	0.017027	0.023383	0.041659	0.060596	0.085415	0.095593	0.121387	0.121162	0.120737	0.114523	0.165973	0.171543	0.119959
República Dominicana	0.03412	0.037552	0.035738	0.04106	0.048874	0.042106	0.039368	0.080185	0.093377	0.088684	0.100442	0.099628	0.112034	0.110705	0.118284	0.121796	0.158233	0.150501
Trinidad y Tobago	0.37403	0.289489	0.297356	0.316869	0.31492	0.327575	0.408832	0.330253	0.27372	0.270843	0.359822	0.402567	0.30988	0.243922	0.219873	0.200337	0.206752	0.226903
Uruguay	0.119999	0.135407	0.123206	0.127954	0.105556	0.10728	0.099366	0.122538	0.14444	0.136828	0.17472	0.24491	0.232719	0.251809	0.274293	0.279671	0.25749	0.275499
Venezuela	0.353247	0.201199	0.214601	0.234445	0.254941	0.31857	0.31404	0.243436	0.297157	0.246681	0.181254	0.220106	0.269528	0.089442	0.108619	0.160488	0.122124	0.078702
LAC's Income Tax Productivity (Avg.)	0.099385	0.09477	0.102676	0.111354	0.114221	0.118335	0.122651	0.124335	0.128069	0.124216	0.130014	0.141655	0.142107	0.133643	0.138116	0.144097	0.144532	0.147279
Median LAC	0.055433	0.068903	0.081253	0.089454	0.085982	0.078419	0.088572	0.106062	0.097801	0.103126	0.114842	0.117293	0.121162	0.120737	0.116667	0.122603	0.133333	0.1219
Average LAC (1)	0.099385	0.09477	0.102676	0.111354	0.114221	0.118335	0.127742	0.128174	0.132486	0.129081	0.13415	0.146145	0.14609	0.137098	0.141658	0.14687	0.147201	0.149195
Median LAC (1)	0.055433	0.068903	0.081253	0.089454	0.085982	0.078419	0.093969	0.109418	0.104918	0.111302	0.117498	0.11934	0.123272	0.122491	0.117475	0.126334	0.138076	0.128746

Source: IMF. Data from Government Finance Statistics and Article IV. Several Years. PriceWaterHouseCoopers: Individual Taxes and Corporation Taxes. Worldwide Summaries. Several years

(*) Corresponde a Argentina, Brazil, Chile, Colombia, Costa Rica, Ecuador, El Salvador, Guatemala, Honduras, Jamaica, México, Nicaragua, Paraguay, Perú, República Dominicana, Trinidad y Tobago, Uruguay y Venezuela.

(1) Corresponde a Argentina, Brazil Chile, Colombia, Costa Rica, Ecuador, Guatemala, Honduras, México, Nicaragua, Perú, Rep. Dominicana y Uruguay. La omisión de países se debe a la ausencia de datos en ciertos años.

tax_index/indice_tributario 2005	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002
Argentina new	29.2%	29.6%	29.4%	25.8%	31.3%	40.0%	37.9%	34.2%	37.2%	37.9%	34.8%	35.8%	35.7%	36.3%	36.4%	33.6%	32.4%	35.1%
Bolivia new	37.7%	48.2%	59.8%	65.8%	67.5%	66.4%	68.7%	66.9%	65.3%	64.4%	51.9%	58.3%	58.4%	58.1%	53.6%	53.2%	52.9%	55.9%
Brasil all new	18.8%	19.9%	21.8%	21.8%	31.7%	36.6%	33.2%	33.4%	32.7%	38.9%	36.0%	37.9%	38.9%	40.7%	40.8%	39.4%	40.7%	42.6%
Chile new	47.6%	48.3%	47.8%	53.0%	51.5%	47.3%	49.0%	49.7%	49.7%	50.9%	51.3%	52.4%	50.6%	50.3%	50.0%	51.6%	52.2%	54.1%
Colombia new	38.4%	49.2%	50.6%	50.3%	50.6%	48.8%	53.5%	54.9%	47.6%	45.4%	43.6%	42.0%	42.9%	42.4%	42.5%	44.9%	44.6%	43.9%
Costa Rica new	34.0%	35.5%	50.6%	47.4%	47.0%	49.9%	50.2%	53.1%	51.1%	52.4%	53.4%	48.0%	47.4%	50.4%	51.0%	50.7%	51.7%	51.4%
Ecuador new	36.2%	39.8%	39.1%	39.9%	40.4%	50.9%	51.3%	51.5%	51.9%	52.0%	51.9%	51.8%	52.6%	52.3%	47.9%	55.2%	57.5%	56.9%
El Salvador new	25.7%	26.5%	26.2%	25.8%	25.4%	30.3%	30.7%	38.3%	54.2%	57.2%	52.6%	53.7%	52.0%	51.9%	52.4%	53.6%	54.0%	54.9%
Guatemala new	38.1%	38.6%	40.0%	48.5%	48.1%	47.4%	47.3%	48.8%	55.5%	53.8%	54.3%	51.9%	52.8%	53.2%	54.6%	52.4%	51.4%	52.9%
Honduras new	41.9%	41.7%	42.2%	42.6%	44.1%	49.2%	46.5%	47.2%	46.9%	45.2%	50.2%	54.8%	55.4%	60.8%	49.0%	57.0%	56.4%	56.6%
Jamaica new	28.1%	36.6%	42.2%	43.1%	44.1%	46.4%	54.7%	73.2%	71.5%	68.4%	69.3%	67.3%	63.1%	65.1%	67.8%	68.4%	67.1%	67.6%
México new	31.0%	31.1%	33.9%	35.7%	37.3%	42.2%	42.1%	47.8%	48.2%	48.4%	41.0%	40.9%	41.9%	42.1%	43.0%	41.4%	41.2%	41.3%
Nicaragua new						22.3%	22.3%	41.2%	47.1%	46.4%	40.5%	41.3%	42.9%	43.9%	44.7%	49.3%	49.1%	50.4%
Paraguay new	32.8%	32.7%	33.1%	32.8%	32.8%	32.6%	32.6%	53.7%	58.3%	60.9%	63.0%	62.2%	62.8%	62.6%	63.3%	61.3%	60.7%	60.7%
Perú new	28.8%	39.7%	40.5%	40.4%	33.1%	28.9%	32.1%	32.3%	39.0%	43.8%	44.5%	45.8%	46.3%	46.3%	45.8%	55.0%	55.0%	48.2%
República Dominicana new	24.7%	26.8%	28.1%	28.4%	29.4%	29.7%	29.4%	52.8%	58.3%	58.3%	54.9%	52.9%	56.7%	56.5%	57.4%	57.3%	62.4%	62.8%
Trinidad y Tobago new	31.9%	27.7%	28.2%	34.7%	37.6%	53.8%	57.6%	52.8%	47.6%	48.7%	56.3%	57.0%	52.0%	50.8%	48.0%	47.4%	48.0%	48.6%
Uruguay new	52.5%	53.3%	51.3%	53.1%	50.8%	48.0%	47.8%	49.2%	49.4%	48.9%	51.4%	55.1%	58.0%	59.3%	60.4%	56.1%	55.0%	55.8%
Venezuela new	35.2%	27.7%	28.3%	29.3%	30.3%	33.5%	33.3%	33.9%	52.3%	56.6%	51.5%	55.3%	52.6%	42.5%	43.7%	47.3%	44.9%	43.6%
LAC MEDIAN NEW	33.4%	36.0%	39.5%	40.2%	39.0%	46.4%	46.5%	49.2%	49.7%	50.9%	51.5%	52.4%	52.0%	50.8%	49.0%	52.4%	52.2%	52.9%
LAC AVERAGE NEW	34.0%	36.3%	38.5%	39.9%	40.7%	42.3%	43.2%	48.2%	50.7%	51.5%	50.1%	50.8%	50.7%	50.8%	50.1%	51.3%	51.4%	51.8%
Average LAC (1)	34.0%	36.3%	38.5%	39.9%	40.7%	43.4%	44.3%	48.5%	50.9%	51.8%	50.7%	51.3%	51.1%	51.2%	50.4%	51.4%	51.6%	51.8%
Median LAC (1)	33.4%	36.0%	39.5%	40.2%	39.0%	46.9%	46.9%	49.5%	50.4%	51.5%	51.7%	52.7%	52.3%	51.3%	49.5%	52.8%	52.5%	53.5%

Table 17.3
Financial and Fiscal Incentives to Production and Investment

	Loans for working capital	Loans for fixed assets and/or investment projects (1)	Equity investment	Loans to specific sectors (2)	Credit programs for particular regions	Horizontal tax incentives	Tax incentives to specific sectors	Tax incentives to particular regions	Subsidies to specific sectors	Subsidies to particular regions
Argentina	X	X(ip)		X	X		Mining, forestry		X (3)	
Bahamas						X (4)	Hotels, financial services, spirits and beer			
Barbados						X (5)	Financial services, insurance, information technology			
Belize						X	Mining			
Bolivia							Mining			
Brazil	X	X(ip)	X	Oil, natural gas, shipping, power sector, telecommunications, software, motion picture industry	X (6)			X (7)		
Chile	X	X			X	X (8)	Forestry, oil, nuclear materials	X	X	X
Colombia	X	X(ip)	X	Motion picture industry	X (9)			X (10)		
Costa Rica	X						Forestry, tourism			
Dominican Republic							Tourism, agribusiness			
Ecuador	X	X(ip)	X				Mining, Tourism			
El Salvador	X	X(ip)		Mining, services sector (11)						
Guatemala							Agribusiness			
Guyana						X (12)				
Haiti				Transport sector, shrimps						
Honduras	X	X								
Jamaica							Motion picture industry, tourism, bauxite, aluminum, factory construction			
Mexico	X	X(ip)	X	Motion picture industry		X (13)	Forestry, motion picture industry, air and maritime transportation, publishing industry		X (14)	
Nicaragua	X	X					Tourism			
Panama	X	X					Tourism, forestry			
Paraguay	X	X				X (15)		X (16)		
Peru	X	X					Tourism, mining, oil	X (17)		
Suriname						X (18)				
Trinidad & Tobago						X (19)	Hotels, construction,			
Uruguay	X	X(ip)				X (20)	Hydrocarbons, printing, shipping, forestry, military industry, airlines, newspapers, broadcasters, theaters, motion picture industry			
Venezuela	X	X(ip)				X (21)	Hydrocarbons and other primary sectors (22)			

Notes: 1) The notation X(ip) means that there are credit lines for entire investment projects and, a fortiori, for discrete capital goods. The plain X indicates that only loans for discrete sets of fixed assets are available.
2) Other than agriculture.

3) There have been subsidies financed from the national budget for agricultural and tourism projects in the provinces of Catamarca, La Rioja, San Luis, and San Juan.

4) Income is tax-free and imports to be used in investment projects are duty-free.

5) The tax incentive is for foreign investors. Offshore companies are taxed at a rate significantly below the rate for local companies.

6) The BNDES (through BNDESPAR) contributes with equity capital to two Regional Funds for Emerging Enterprises (in the states of Santa Catarina and Minas Gerais), which, in turn, lend to emerging firms. It also has special credit facilities for the North.

7) There are federal tax investment incentives for the Northeast and Amazon regions.

8) There are two main horizontal forms of tax incentive to investment (including re-investment of profits): 1) Accelerated depreciation is granted for new fixed assets acquired domestically and for imported fixed assets; 2) personal income tax and Adiff.

9) Colombia's Instituto de Fomento Industrial (IFI) has a credit line for firms located in border zones; and another for that part of the coffee-producing effected by the earthquake of January, 1999.

10) There are two special tax regimes that favour particular regions recently affected by natural disasters. They are the Pérez Law and the Quimbaya Law. The first is applicable to the zones affected by the flooding of the Pérez River in 1995 and the seco.

11) The services industries included with credit lines of their own are: tourism, transportation, software, and other services.

12) Haiti has a comprehensive tax-holiday scheme.

13) Through the Sector Promotion Program (PROSEC), firms in twenty-two industries in the manufacturing sector can import goods at a preferential rate to be used in the respective manufacturing sector to produce final goods either for the external or the

14) The tourism industry is subsidized through sale by the National Tourism Fund of developed land at favourable prices.

15) Paraguay has a five-year-duration tax-holiday for new investments.

16) The duration of the tax-holiday mentioned in footnote 15 is longer (ten years) if the company making the investment locates in the Departments of Guairá, Itapúa, Neembecú, Concepción, or in the Eastern Region.

17) Manufacturing enterprises operating in the border provinces and in the Amazon region are exempt from the income tax, the VAT, and the excise taxes.

18) According to the U.S. State Department, the Surinamese government has the legal power to grant tax holidays on a case-by-case basis.

19) Trinidad and Tobago grants comprehensive tax holidays of up to ten years.

20) A tax exemption is available on profits reinvested in manufacturing firms, farming, and hotel facilities. In addition, there is a partial relief from capital tax through computing the fiscal value of industrial equipment at fifty percent.

21) New investments in manufacturing industry, agriculture, fishing, fish farming, livestock, and tourism receive a tax rebate of 20 percent. Furthermore, the capital gains tax is one percent.

22) New investments in hydrocarbons production enjoy a tax rebate of 8 percent. The purchase of capital equipment and services for new investment in oil, mining, agriculture, and fisheries is exempt from the wholesale tax.
Source: IDB 2001, Table 17.3 in The Business of Growth. Economic and Social Progress in Latin America 2001 Report.