

*Case Study:*

**Topic 4.4. CIAT'S CONTRIBUTION FOR IMPROVING THE EFFECTIVENESS OF THE TAX ADMINISTRATIONS**

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## **1. INTRODUCTION**

The Inter-American Center of Tax Administrations (CIAT), is a public, nonprofit international organization established in 1967, with headquarters in the city of Panama, Republic of Panama, whose mission is to provide an integral service for the modernization of the tax Administrations of its member countries, by promoting their evolution, social acceptance and consolidation, within a framework of mutual cooperation, through the diffusion and exchange of knowledge and experiences, research, training and the rendering of specialized technical assistance services. To date, CIAT has 33 member countries: 28 from the American Continent and five European countries. The top-level authorities of its tax administration represent every country.

Within the framework of a Strategic Plan that is updated every two years, CIAT provides services through four main programs: International Projects, Information and Inquiries, Tax Studies and Technical Cooperation, thus creating the environment and conditions for executing, directly or indirectly, reform processes, and the strengthening and modernization of most of the tax administrations of the member countries.

In the past 15 years, CIAT, through its different programs and activities, and in particular, with the technical and financial collaboration of the IDB and the support of the missions of Germany, Spain and France and likewise working in close collaboration with the International Monetary Fund, has undertaken significant technical assistance efforts in most of the Latin American countries and the Caribbean, to strengthen and improve the effectiveness and efficiency of its tax administrations, thus achieving very important qualitative improvements in the countries of the region. Undoubtedly, the effort of the governments themselves, as well as the support of multilateral financial organizations and the European missions at CIAT has been key factors in the process for improving in recent years, the tax administrations in the Latin American and Caribbean countries.

CIAT's technical assistance efforts seek to provide the tax administrations an adequate managerial system for improving their efficiency and effectiveness, based on a model of innovative conception for the rendering of high quality services to the citizens, which may facilitate greater social acceptance and accordingly, better voluntary compliance with the tax obligations.

CIAT has vast experience in executing very complex technical cooperation projects in the countries of the region and has proved to be very efficient in carrying out these projects (effective and efficient hiring mechanism, compliance with the clauses agreed in the cooperation Agreements, effective administrative support system, provision of funds, progress reports, etc.), adapting itself to the administration procedures of the multilateral financial entities that have governed the operations carried out (auditing, rate of exchange, acquisitions, among others).

As a result of its almost two decades of involvement in the design, development and implementation of tax information systems and organizational changes, through the use of advanced computerized technology, CIAT currently has available a series of generic solutions in the form of models, standards and prototypes in the different functional areas of the administration. It also counts on a privileged experience and know-how in the management of complex projects and, what is most important, it coordinates a vast number of highly qualified consultants (specialists in different areas of tax management), willing to render their services in the tax administrations of the member countries.

We have learned that one of the most effective ways of taking advantage of technological solutions is through their reutilization. There are many levels at which reutilization may take place, from the use of conceptual models of information systems covering the entire administration, up to applications and/or generators of specific solutions in different functional areas and codes of computer programs.

CIAT has successfully applied this reutilization strategy, which is at present, a key factor for the effective development of the information systems. To this end, CIAT has an extensive inventory of models, standards and prototypes which under this concept, allow for providing technical counseling and developing information systems, with a high level of user satisfaction within a framework of proven efficiency and effectiveness.

## **2. THE TAX ADMINISTRATION REFORM IN LATIN AMERICA AND THE CARIBBEAN IN THE PAST DECADE: MODES AND ACHIEVEMENTS**

The past ten years of experiences in the area of reform of the tax Administration in the countries of Latin America and the Caribbean that are discussed in this document, are also experiences shared with the IDB, IMF and World Bank, the European missions of Germany, Spain and France established at CIAT and the almost totality of the CIAT member countries, since practically all of them participated in the efforts for reforming the tax administration, within the framework of technical cooperation projects, either as providers or beneficiaries thereof.

Tax administration reforms in Latin America and the Caribbean have adopted **different forms, scopes, intensity and likewise results**. A determinant factor in this process has been

the cultural, legal, political, economic and social context wherein the administrations perform and the development and evolution of the tax administrations in terms of: their tax systems, procedural norms, organization, human resources, organizational culture, as well as the stability of legislation, managerial capability and continuity of the reform policies and strategies.

Within this framework, one may identify three main modalities that characterize most of the reform processes undertaken in the countries of Latin America and the Caribbean.

**A first reform modality**, is that wherein a planned, gradual and systematic change took place, where improvement of legislation and, accordingly, of the related administrative processes and the administration itself, were carried out without any significant internal or external trauma for the organization, thus providing an important image of continuity and juridical security. In addition, these processes have been, in general, marked by important managerial continuity, development of human resources and the strengthening of the organizational environment with positive values. In this type of processes, the promotion of change has taken place within the organization and with its own resources, resorting to the hiring of external consulting services only for solving precise and specific problems. Examples of this modality of reform are the modernization processes carried out by the tax administrations of Brazil and Chile.

**A second modality of reforms** consists of reforms that have involved a radical and integral change of the administration, comprising aspects of reform of the tax system, the tax legislation in general, as well as of the administration. These reform processes have been financially and technically supported by such international organizations as the IDB, World Bank, IMF, the European missions and CIAT. The success of these reforms has been conditioned, to a great extent, to external as well as internal factors of the Administration, such as: the political support and availability of sufficient resources for their implementation; the capability and continuity of the managerial process, the quality and motivation of the human resources and the organizational culture and environment of the respective administration. Framed within this modality are the reforms undertaken in Barbados, Bolivia, Colombia, Costa Rica, Peru and Venezuela and recently begun in Argentina, Ecuador, Guatemala, Jamaica and Mexico.

**A third modality of reforms** is that in which the change processes have been centered above all on the use of information technology, the development of information systems and the re-engineering of processes in key areas of the administration (taxpayer file, collection and current account), intended mainly at controlling a special universe of taxpayers, the so-called main or large taxpayers, in order that the administration by controlling a small group of taxpayers may ensure the control of those responsible for a high percentage of collection. These reform processes have also been financially and technically supported by international organizations. Most of the Latin American and Caribbean countries are undergoing this type of reform.

### **Main achievements**

As previously indicated, the tax administration reform processes in the Latin American and Caribbean member countries of CIAT vary in various aspects and especially with regard to

results achieved. In any case, some areas may be identified wherein most of these countries achieve significant progress.

**a) *Management strategy***

It was in the past decade when the promotion of voluntary compliance was consolidated as a tax administration strategy. Previously, the role of the administration, and accordingly, its action strategy showed a distinctly repressive bias. Efforts were fundamentally aimed at inducing compliance with obligations by threatening with verification and sanctioning noncompliers, even though such attitude was not in keeping with actions, as regards the fulfillment of the threats and accordingly, did not achieve the expected results of inducing compliance. The authorities even used to undertake advertising campaigns, as the only social communications media by portraying the tax administration through different aggressive figures.

At present, regardless of recognizing the importance and need for exercising the tax administration control functions, it is understood that the promotion of voluntary compliance should comprise taxpayer assistance actions that may induce him to comply and facilitate his doing so, through the simplification of filing and payment procedures, orientation and information on the scope of the tax norms, and the concern for reducing the indirect tax burden to that which is essential.

**b) *Strategic planning***

It was also in the past decade when the use of strategic planning in the tax administrations was generalized, allowing them to act as an open system, which obtains feedback not only by observing its own processes and products in search for efficiency, but also by taking into consideration what takes place and what is to come within the social, political and economic context wherein they perform, in search also for effectiveness. That is, by setting guidelines and priorities based on the surrounding reality and the changes that may be anticipated to occur in that reality.

Within such planning, worth noting is the adoption of definitions of the mission of the tax administration which incorporate, in keeping with what has been previously stated with respect to strategy, the organization's notion of service.

**c) *Organizational structure***

With respect to the reforms introduced in the organizational structure, it is worthwhile to point out four relevant aspects taken into consideration by several of the countries on which this presentation is centered: autonomy, integration, large taxpayer units, taxpayer assistance entities.

- ◆ **Autonomy.** The adoption of greater autonomy of the tax administration, whose scope varies among the countries that adopted it, has allowed in many cases for significantly improving the human resources profile as, for example, in Peru and Venezuela, on

permitting the implementation of a policy for hiring and paying remunerations, compatible with the professional requirements demanded for carrying out the function. At the same time, on affording greater financial availability and flexibility for the acquisition of goods and services, it was possible to restore facilities and equipment in a more adequate and timely manner, than if they would have to undergo the cumbersome bureaucratic hiring procedures, common to every public administration.

- ◆ **Integration.** Integration in the organizational structure of the tax administration took place in two directions. On the one hand, in the Dominican Republic, for example, there was integration not only of the administration of different internal taxes that were previously managed by different organizations, but also of functions corresponding to the administration of the same tax that had been performed separately.

Besides, another form of integration that has taken place in recent years was the concentration in a single organization of the management of internal taxes and customs duties, such as for example, in Argentina, Colombia, Mexico and Venezuela and, in some case, as that of Argentina, also of social security contributions. A precedent in this form of integration is the case of the tax administration of Brazil, wherein it was undertaken in the late sixties.

The reasons behind this integration were mainly for obtaining economies of scale in the tax administration and improving controls, through a more integral vision of taxpayer behaviour.

- ◆ **Large taxpayers management units.** The trend toward the establishment of units for the differentiated management of large taxpayers was maintained and reaffirmed, to thus exercise closer and effective control of those who are responsible for the greater part of tax collection.

This trend also responds to a tactic that has proved to be satisfactory in the development of tax administration modernization projects. It deals with selectively initiating the improvement of the administration's functions, with respect to a reduced number of taxpayers formed by the most important ones, so that gradually the improvements introduced may be extended until covering the entire taxpayer universe.

This tactic is being applied in most of the countries that undertook tax administration modernization projects.

- ◆ **Taxpayer assistance entities.** To a certain extent, as corollary to what has been commented in relation to the change of strategy in favor of the promotion of voluntary compliance, and the consecration of the notion of service introduced in the definition of the tax administration's mission, specific entities were created for providing taxpayer assistance, at times, at the managerial level.

#### **d) *Management***

Significant efforts were devoted to increasing the managerial capability of the tax administration which ranged from numerous training activities, up to the introduction of modern management techniques, such as “total quality”.

In this field, achievements differ considerably; however, it may be concluded that, regardless of the results obtained, which in many cases are far from being satisfactory, almost all of the administrations became aware of the fact that the search for an adequate managerial capability constitutes a priority goal for arriving at acceptable levels of efficiency and effectiveness in the tax administration’s action.

***e) Engineering of tax processes***

In terms of administrative processes and procedures, several countries undertook real re-engineering efforts, intended to improve the levels of efficiency. This contributed to the simplification of taxpayer compliance with their obligations and the development of functions common to the administration. In many cases, these re-engineering efforts were undertaken to adapt the administration’s action to a broader use of information technology.

Among the actions undertaken, worth noting is the generalized use of the banking network for the filing and payment of taxes and, in many cases, with real time transmission of information.

In some cases, progress was achieved in the filing of returns through magnetic media and, in the case of Brazil, Internet was used for such purpose. In this country, the number of income tax returns filed through Internet in 1997, although it was an experimental activity, was approximately half a million.

***f) Information systems and information technology***

Progress achieved in the use of modern information technology took place in relation to "hardware" as well as "software".

Most of the administrations significantly expanded the capability and number of computerized equipment used, which allowed them to establish network systems that increased the flow and availability of information between and for the various units and regions of those administrations.

On the other hand, the corresponding information systems were developed or improved, mainly with respect to the collection functions. Many countries consolidated the taxpayer file and integral tax current account, thus being able to notify the filing of returns and payments automatically.

In this field, many of the efforts undertaken were based on the application of successful experiences and of standards and prototypes which CIAT has developed and documented for the purpose of facilitating and accelerating the modernization processes.

***g) Human resources and training***

In the area of human resources, the greatest achievements correspond to those countries, which at the same time were able to obtain better conditions for managing those resources with greater autonomy.

Although most of the countries still have a lot to do in this field, there is already evident a greater concern for all aspects dealing with the human capital of the tax administrations.

In particular, training actions are being carried out in a more systematic and consistent manner. In this respect, it is worthwhile mentioning the acceptance by the 18 Latin American countries for which it is intended, of the program for strengthening the tax training centers, sponsored by the IDB, Mexico, CIAT and the State Agency of Tax Administration of Spain.

### **3. CHALLENGES FOR THE TAX ADMINISTRATION**

As already stated, the tax administrations are directly influenced by their own political, cultural, economic, social and technological environment, as well as by the evolution and trends in the world environment. The forecasts, which in general may be made with respect to the next decade, is that it will be one of ever more radical, accelerated and in depth changes than those experienced up till now.

Such changes will promote permanent instability and ever more complex and interdependent relationships between the Administration and society that will undoubtedly demand, adaptation of the forms of management, highly qualified human resources and new forms of management and organizational structures, capable of responding and adapting themselves to the changes and to the new requirements of society.

We may say that in the remainder of this decade and the next one, the tax Administrations will face the following challenges:

- ◆ Further simplify the tax system, legislation and tax processes.
- ◆ Reduce the levels of tax evasion.
- ◆ Promote greater juridical security in the treasury/taxpayer relationships.
- ◆ Respond to the demands of globalization of the economic systems.
- ◆ Control the tax effects of social phenomena of an illegal nature.
- ◆ Follow up the evolution of information technology and communications.
- ◆ Control electronic commerce.
- ◆ Observe and implement the tax decentralization trends.
- ◆ Adapt themselves to the new organizational trends and managerial practices of the tax Administration.
- ◆ Participate in the tax harmonization efforts of the economic integration processes.
- ◆ Professionalize and train the human resources of the tax administrations.
- ◆ Implement a new management philosophy and service attitude of the administrations vis-a-vis society that may facilitate responses to the previously described challenges.

## THE AGENDA FOR THE FUTURE

The Agenda for the future is certainly extensive, complex, will change and will depend on the variables of the Tax Administration's environment. The success of the long path yet to be trodden especially by the Latin American and Caribbean tax administrations for obtaining acceptable levels in their management processes, to a great extent will be conditioned to the balanced progress achieved in the modernization of the following key aspects of the axes on which a modern, efficient and effective tax Administration is based: (i) the tax system, tax legislation and the powers of the Administration, (ii) information technology and the information systems, (iii) the re-engineering of processes and the simplification of procedures, (iv) tax management, organization, human resources and organizational culture, (v) the administration's relationships with the taxpayers and the level of acceptance of taxes by society and (vi) international taxation.

Briefly listed below is a series of aspects and statements (without intending to be exhaustive), that generates important and varied problems to the management of the tax administrations and accordingly, must be borne in mind in the reflections of the managers:

1. Inadequacy of the Tax Code in certain subject areas such as: effective sanctioning regime (including formal noncompliances); domicile; official discharges; possibility for obtaining tax information for the control of taxes.
2. Need to have forms with contents adapted to the importance of the taxpayers. Promote the use of information returns (fundamentally for control).
3. Insufficiency of massive controls for the elimination of generalized noncompliances and errors (voluntary or involuntary), through computerized verification of all sworn returns; and obtaining provisional assessments by crosschecking the information available. The verification presence of the tax Administration achieved through the use of these controls is very high.
4. The taxpayer information and assistance situation. It must be analyzed, strengthened, even by undertaking surveys of very diverse contents.
5. Analysis and re-engineering of processes and procedures used in the tax cycle for performing the administrative tasks.
6. Administrative enforced collection must be effective. To have available an adequate normative framework (as a General Regulation for administrative Collection and Recovery) would be an essential requirement for achieving this objective. Of course, the stratification of debts and the follow-up of the delinquent portfolio, prioritizing attention to the larger amounts, are valuable aids for achieving the collection, institutional presence and seriousness and tax education objectives.
7. The system of guarantees in administrative action must be speeded up. In legal action, the progress of procedures must be controlled.

8. It is of fundamental importance to have an integrated information system for the management and control of taxes in the tax administration.
9. Large taxpayers must be treated with a more integrating optics.
10. Greater sensitivity toward the staff policy: Selection, initial and permanent training, incentives, ethics, mobility.
11. Specialized training of large taxpayer auditors.
12. Tax amnesties. Fully discourage them, due to their detrimental effect on compliant taxpayers.
13. Ethics of tax accountants and their collaboration with the tax administration.
14. Tax documents file.
15. The search for the most adequate model of tax administration for each stage of development of the country, among others, model for Verification and Collection and which will obviously not generate social litigation.
16. The managerial attitudes and abilities; the decision-making mechanisms; the decentralization of decisions at the territorial level (solution of appeals; local verification plans...); disposal and use of statistics for daily management.
17. The control of invoices. Seriously analyze and select the most adequate model.
18. The procedure to follow up administrative acts.
19. The nonexistence of essential mechanisms of internal control.
20. The unclear differentiation of taxpayers according to size (e.g. by volume of operations) causes significant deficiencies for their follow-up and control.
21. The situation of interdepartmental and interinstitutional relationships (Municipalities, Chambers of Commerce, Professional Associations...) does not allow for achieving the desired results.
22. Bank secrecy versus tax secrecy. Analysis and future evolution.
23. The bank collaboration policy. In many cases, collaboration agreements must be revised.

24. International taxation. In order to face sophisticated international tax evasion and avoidance problems mainly derived from the globalization process, such as transfer prices in operations between related companies, use of tax havens and others, it will be necessary to train a select team of officials and develop with them verification programs for combatting these forms of evasion and avoidance, in collaboration with other tax administrations, to which end it will be necessary to look for ways of further strengthening international mutual cooperation.

## CONCLUSIONS

The process of reform and modernization of the tax administrations is a complex, difficult and long-range task, wherein there intervene a series of factors, internal as well as external to the organization. In sum, the success of this process will depend on the balance existing in the modernization achievements in key aspects of the administration. On the one hand, the legislation, organizational structure, information systems and processes and procedures, and on the other, the continuity of management, the development of human resources and the development of an organizational culture favoring ethical and professional values and the taxpayer service attitude.

Highlighted within this framework are the achievements of countries where the tax administrations have had sustained political support and managerial continuity in the reform process (Brazil and Chile); have achieved autonomy in the management of their human, financial resources and wherein the reform processes have been integral (Peru and Venezuela).

In all Latin American and Caribbean countries one observes significant qualitative achievements in key areas of the administration. However, such achievements are still far from implying a sustained change in the way of managing taxes. In this sense, we visualize that CIAT and other international cooperation organizations, have a very important role to play to support the strengthening of the Latin American and Caribbean tax administrations, within the framework of the Agenda for the future traced in this paper.

We wish to highlight the importance of international cooperation for facing problems derived from the globalization of the economy and world trade. In this sense, it would be important to consider the possibility, for example, of setting up an International Verification Committee, formed by representatives of the member countries, with headquarters at CIAT, in order to develop plans and coordinate the application of measures intended to identify and combat international fraud in a sustained manner. This Committee could work in close coordination with special committees for the struggle against tax fraud, to be established at the national level and it could report to the CIAT Executive Council through its Executive Secretariat.

An important step for the development of mechanisms of mutual cooperation between the tax administrations of the CIAT member countries, is the Working Group on international taxation established within the framework of the CIAT/Italy Technical Cooperation Agreement, one of whose objectives is to render feasible the conclusion and application of information exchange agreements, which are considered of vital importance for combatting

every form of international tax evasion and which, nevertheless, have not been used as much as desired by the CIAT member countries, especially those of Latin America. In this sense, the actions of the Working Group are aimed at establishing parameters that go beyond the existence of a Model Agreement, seeking also to support and provide solutions for its effective implementation, such as determining the organizational needs for carrying out information exchange activities and identifying and scheduling technical assistance and training mechanisms that may facilitate such exchange.

Lastly, for all of the above, we would wish the IFIs to include (when making their valuable recommendations to the Governments of the CIAT member countries) the need for a new working philosophy with greater rigor and professionalism, at least in the following tasks and fundamental areas:

- Tax code: adequate legal framework.
- Taxpayer Information and Assistance: professionalized.
- Taxpayer file: significantly improved.
- Control of voluntary collection: banks and electronic media.
- Massive control of noncompliance (tax presence).
- In-depth verifications of large taxpayers: new optics.
- Effective enforced collection: stratification of debts.
- Design of forms adapted to the taxpayer size.
- Design of information return forms.
- System of integral information for the tax administration.
- Greater sensitivity toward the staff policy: selection; training; compensation and motivation; continuity of officials; separating from political changes the mobility of staff at the levels of apolitical performance. The staff is the most valuable resource of any organization.

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