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Bolivian sub-national revenues: A review

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BOLIVIAN SUB-NATIONAL REVENUES: A REVIEW

by
Beatriz Muriel H.*

(February 2010)

Abstract

This papers reviews main topics concerning sub-national revenues (intergovernmental transfers and taxes) and discusses some policy options to develop own sub-national revenues. The review covers the political-legal framework and the fiscal outcomes, finding that: i) intergovernmental transfers policies have expanded over time, generating inequity problems, principally at the departmental level; ii) sub-national revenues depend mostly on intergovernmental transfers; this has generated high levels of vertical imbalances, mainly for department governments whose revenues rely mostly on the hydrocarbons sector; and iii) lack of adequate tax policies that promote fiscal effort and equity led to large horizontal imbalances in municipal per capita tax collection, unrelated to poverty or human development differences. In this regard, policy options were discussed to increase own sub-national revenues, taking into account political and social discussions, the economic, fiscal and legal base, and relevant tax principles. The main recommendations are: i) to promote in-kind contributions (materials and labour) at the municipal level, especially in poor rural municipalities; ii) to improve municipal tax administration supporting the continuation of the RUAT's work and improving the registry with the new census; and iii) to evaluate the possibility of redefining the RC-IVA as a personal income tax shared between the central government and the departments.

Keywords: Bolivia, fiscal decentralization, revenues, taxes, intergovernmental transfers
JEL Classification: H20, H71, H73, H77, K00

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I. INTRODUCTION

The Bolivian decentralization process started with the Popular Participation Law enacted in 1994, through which some central government spending responsibilities and financial resources were transferred to the municipalities. Additionally, in 1995, through the Administrative Decentralization Law, the central government delegated expenditure responsibilities and revenues to departmental governments.

In early 2000, some departmental governments initiated a wave of claims, seeking to deepen the Bolivian decentralization process; they were followed by municipalities and other prefectures looking for more political and fiscal independency. The result was a new legal framework established through the new National Political Constitution, enacted in 2009, and the Autonomy Framework Law, approved in 2010.

This paper reviews the main topics concerning sub-national revenues. Section II describes the sub-national revenues policies from 1994 to 2010, principally focused on taxes and intergovernmental transfers (that are derived from national taxes). The review is done from a political and legal point of view, highlighting the regulatory differences before and after the promulgation of the new constitution.

Section III analyzes the fiscal outcomes of the decentralization process, observing some relevant aspects. First, for the 10 main municipalities (capital cities plus El Alto), sub-national own revenues have been relatively important, but with a participation over total revenues that decreased over time – from a percentage of 54.3% in 2000 to 30.8% in 2008 –, displaced by intergovernmental transfers. In turn, intergovernmental transfers were increased through National Dialog Law in 2001, and the creation of the Direct Hydrocarbons Tax (IDH) in 2005 (through the promulgation of the new Hydrocarbons Law), which was accompanied by the growth in hydrocarbons prices. Second, for the rest of the municipalities, intergovernmental transfers have always been the main source of revenues, with percentage shares (over the corresponding total revenues) ranging from 66.7% in 2000 to 71.3% in 2008. Third, departmental governments, having been only de-concentrated, had few own resources being supported principally by intergovernmental transfers and royalties – 67.4% of all income in 2000 and 93.2% in 2008. Fourth, the intergovernmental transfers' dependency was reflected in higher levels of vertical imbalances, principally for departmental governments that mostly rely on the

hydrocarbons sector (prices and production). Finally, the analysis of horizontal imbalances shows high levels of inequality in the municipal per capita tax collection, which are not explained by poverty or human development differences, but by the inexistence of fiscal effort policies and the different capabilities of governance (among other reasons).

Given the review described above, Section IV discusses sub-national income generating policy options consistent with the current political and social discussion, the economic, fiscal, and legal Bolivian base and some relevant principles that should guide the tax assignment policy. The main recommendations are: i) to promote in-kind contributions (materials and labour) at municipal the level, especially in poor rural municipalities, which already have some successful experiences with the participation of communities in public investment tasks; ii) to improve municipal tax administration supporting the continuation of the work of RUAT (Sole Registry for Municipal Tax Administration) and improving the registry with the new census; and iii) to evaluate the possibility of redefining the RC-IVA as a personal income tax, being shared between the central government and the departments. Finally, the last section describes the most important conclusions.

II. POLITICAL AND LEGAL BACKGROUND

The Bolivian government initiated the decentralization process with the Popular Participation Law, enacted in 1994, in order to improve the quality of life of Bolivian citizens as well as to generate a more equitable and efficient use of public resources. The law allowed democratic elections of mayors and reassigned to municipalities central government expenditure responsibilities as well as resources. Additionally, in 1995, through the Administrative Decentralization Law, the central government delegated expenditures and revenues to prefectures (departmental governments).

The decentralization process promoted social, political and economic inclusion of Bolivian citizens, principally in areas that were somehow marginalized. However, the fiscal decentralization policies were in many cases established in an *ad hoc* manner, with shortcomings in terms of fiscal equilibriums, efficiency, fiscal enforcement, accountability and, in some cases, equity (see, for example, Ministerio de Hacienda 2006 for a discussion).

The expenses of sub-national governments were financed principally through three main sources: intergovernmental transfers, sub-national revenues and debt[1].

Intergovernmental transfers for municipalities began in 1994, with the transfer of the 20% of eight national taxes collection established by the Popular Participation Law (excluding fiscal values and customs administration costs)[2], and were reinforced with the HIPC (Heavily Indebted Poor Countries) debt relief resources since 2001, implemented by the National Dialog Law. In both cases, resources were distributed by equity criteria such as population and levels of poverty, being conditioned principally to social investment[3] under the guidelines of the central government social policies. Additionally, the National Dialogue Law created the National Compensation Policy (PNC), which tried to concentrate all international and (other) national non-reimbursable transfers resources in a basket for municipal social investment projects, being transferred by poverty criteria (see Table 1).

At that time, only a few municipal resources, such as mining and forestry patents, were transferred without any equity criteria, as they sought to compensate mining and forest exploitation in the affected regions. In 2005, however, the creation of the Direct Hydrocarbons Tax (IDH), through the promulgation of the new Hydrocarbons Law, generated a distortion in municipal resources allocation, which worsened during the last years because of the strong increase in oil prices favouring hydrocarbons producing regions. The benefited municipalities were mainly those belonging to the hydrocarbons producer departments, receiving 34.48% in 2005-2007 and 66.99% since 2008 from the corresponding departmental governments (see Table 1).

Municipalities' own revenues began with the formal assignment of the following taxes since 1994: the Motor Vehicles Property Tax (IPVA), the Real Estate Property Tax (IPBI), the Tax on Vehicle Property Transfers (ITVA), the Tax on Real Estate Property Transfers (ITI) and the Specific Consumption Tax on corn alcoholic drink. Municipalities could also apply fees, patents and especial contributions as own resources long before the promulgation of the Participation Law under previous regulations (see Table 1)[4].

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[1]Sub-national debt will not be analyzed in this paper.
[2]The fiscal values are payment certificates that are used as money to discount fiscal obligations (see Zapata 2005).
[3] Currently 85% should be destined to capital expenditures and the rest to current expenditures.
[4]The IPBI is taxed according to sworn declarations. The central government approves the zoning plans, valuation tables on land and buildings, value factor corrections, depreciation tables and tax scale.

Table 1: Bolivian Intergovernmental Transfers and Tax Policies by Level of Government

Resources	Central Government	Transfers to			By the Norm
		Municipalities	Departments	Other	
Intergovernmental Transfers					
Eight National Taxes: IVA (Value Added Tax), RC-IVA (Complementary to IVA Regime), IUE (Corporate Net Income Tax), IT (Tax to Transactions), ICE (Specific Consumption Tax), GA (Customs Tax), ISAE (Departure Outside Tax) and ITGB (Transmission Free Goods Tax)[(1)]	75%	20%; distributed by population size, and conditioned mainly to public investment and the central government health program		5% to Universities	GA modified by many reforms (see Muriel and Barja, 2006) and the rest created by the Tax Reform Law 843 (since 5/1986 and posterior modifications). The transfer policy were created by the Popular Participation Law (04/1994)
National Tax: Special Tax on Hydrocarbons and Derivatives (IEHD)	Up to 75%		25%: 50% distributed equally by territory and 50% by population size, plus up to 10% -The Compensatory Fund- to compensate departments with royalties below the national average per capita, and conditioned mainly to public investment	20% from the corresponding prefectural resources to universities	Created by the Law 1606 (12/1994) and transferred to Prefectures by the Administrative Decentralization Law (7/1995) and to universities by the Decree 25746 (4/2000).
National Tax: Direct Hydrocarbons Tax (IDH)	56.25% less compensation to producer departments, less the 5% of the reaming to the Compensatory Fund to municipalities and universities	66.99% (34.48% with the Decree 28421) from the corresponding prefectures resources distributed by population size, plus the 80% of the Compensatory Fund to the municipalities of La Paz, Santa Cruz and Cochabamba (because of the high population), conditioned to socioeconomic development programs	12.5% to producer departments distributed by their respective production, plus 31.25% to non-producer departments distributed by territory (6.25% each), plus a compensation to producer departments if the IDH resources are less compared with non-producer departments, and conditioned to socioeconomic development programs	8.62% from each Prefectural resources to corresponding universities plus the 20% of the Compensatory Fund to universities of La Paz, Santa Cruz and Cochabamba	Created the Hydrocarbon Law 3058 (5/2005), regulated by the Decree 28421 (10/2005) and amended by the Decree 29322 (10/2007)

Mining concession Patents	70% to the sector's institutions	30% to Municipalities where are the concessions			Created by the Mining Code (3/1997)
Exploitation and Clearance Forest Patents	40% by exploitation and 50% by clearance to the sector's institutions	25% by both exploitation and clearance transferred to affected Municipalities, non-conditioned	35% by exploitation and 25% by clearance transferred to affected Departments, non-conditioned		Created by the Forest Law 1700 (7/1996)
Heavily Indebted Poor Countries debt Relief	Municipal Solidarity Fund to pay items of public school and health	100% less the Municipal Solidarity Fund: The remaining 70% to productive and social infrastructure distributed by poverty, 10% to education according to school population and 20% to health by population size			Created by the National Dialog Law 2000 (7/2001)
National Compensation Policy (PNC): all non-reimbursable transfers from International Cooperation, Prefectures, Central Government, Non- Governmental Organizations and private entities that manage public resources or official aid to the country		100% by poverty criteria destined to public investment			Created by the National Dialog Law 2000 (7/2001)
Tax on Games (IJ)	100%				Created by the Law 971 (11/2010)
Tax on Games Participation (IPJ)	70%	15% on the corresponding collection	15% on the corresponding collection		Created by the Law 971 (11/2010)
Own Taxes					
Municipal Taxes: Motor Vehicles Property Tax (IPVA) and the Real Estate Property Tax (IPBI)		100%			Created by the Tax Reform Law 843 (5/1986) and considered municipal resources by the Popular Participation Law (04/1994)

Municipal Taxes: Tax on Vehicle Property Transfers (ITVA) and Tax on Real Estate Property Transfers (ITI)		100%			Created as municipal resources by the Law 1606 (12/1994)
Municipal Taxes: Specific Consumption Tax on Corn Alcoholic Drink		100%			Created as municipal resources by the Law 1606 (12/1994)
Municipal Taxes: User fees, patents and special contributions		100%			Previous Constitution and other norms
Departmental Taxes: User fees, patents and special contributions			100%		
National (other) Taxes: Financial Transaction Tax (ITF) and user fees, taxes and special contributions	100%				ITF was created by the Lay 3446
Hydrocarbons Royalties	33%		66% to hydrocarbon producing departments plus Pando and Beni departments		Consolidated by the Hydrocarbon Law 3058 (5/2005) and regulated by the Decree 28421 (10/2005)
Mining Royalties		15% to the producer Municipality and conditioned mainly to public investment	85% to the producer department and conditioned mainly to public investment		Consolidated by the Mining Code (3/1997) and modified by the Law 3787 (11/2007)

Source: Author's elaboration based on Bolivian regulation

Note: (1) In December of 2010 the central government approved an increase in the ICE rate to cigarettes and alcoholic beverages, but these new resources will not be co-participated with municipalities.

The previous Constitution[5], however, gave legal authority for creating and changing taxes only to the central government, being municipal taxes a kind of cession (derived power) with rates and tax bases regulated each year from it. Additionally, new municipal user fees and patents had to be approved by the national legislative power under the guidance of the national executive power, which meant that municipalities had to seek central government approval if they wanted to implement a new tax.

Intergovernmental transfers to prefectures, on the other hand, began with the transfer of 25% of the Special Tax on Hydrocarbons and Derivatives (IEHD) in 1995, with 50% distributed equally by territory, to the nine departments, and 50% by population size. In 2000, however, 20% of the departmental resources were transferred to the corresponding state(s) university(ies). Additionally, a Compensation Fund was created with the IEHD in order to compensate departments with hydrocarbons royalties below the national average per capita.[6]

Since 2005, the creation of the IDH gave to departments another important intergovernmental transfer source. The IDH was distributed, as in the case of municipalities, favoring hydrocarbon producing regions (see Table 1).

Departmental (prefecture) own revenues have been mainly royalties. This right was established long before the Popular Participation Law; however, it was rectified by this law. In the same way as for municipalities, these own revenues have been a kind of cession of the central government, but additionally they have been shared with other levels of governments and have been collected by the central government. Departmental governments have two main royalty resources: 66% of hydrocarbons royalties for producer departments (Tarija, Santa Cruz, Cochabamba, and Chuquisaca) plus Pando and Beni[7], with the rest being for the central government, and the 85% of mining royalties for producer departments, with 15% transferred to the producer municipalities.

[5]The new Constitution was promulgated in 2009.
[6] In this case also 85% should be destined to capital expenditures and the rest to current expenditures.
[7]These departments were favored in order to contribute to their development under equal conditions with the rest of departments (according to Law 981 of 1988).

II.1. DEEPENING FISCAL DECENTRALIZATION

In early 2000, the departments of Santa Cruz, Tarija, Beni, and Pando made a series of protests and requests, seeking to deepen the decentralization process towards the so-called autonomies. The result was a national referendum in 2006, where the population of four of the nine Bolivian departments – those who carried out the protests and demands – supported autonomies. Additionally, municipalities demanded more resources as well as more independence in terms of own revenues policies. The result was a new legal framework that deepened Bolivian decentralization, established through the new National Political Constitution, enacted in 2009, and the Autonomy Framework Law, approved a few months ago.

The new Constitution establishes Bolivia as a decentralized state with autonomies, understanding autonomies as: the direct election of authorities, management of economic resources and the exercising of the legislative, regulatory, supervisory and executive powers by the autonomous government bodies (legislative and executive) in their corresponding jurisdictions, responsibilities and attributions.[8] Sub-national governments are classified in four levels: i) departmental ii) regional (group of municipalities or provinces with geographical continuity within a department), iii) municipal, and iv) indigenous-native-peasant. In the case of Bolivia, it is worth noting that the deepening of decentralization focuses on cultural issues (besides the usual political, social and economic issues) derived from the indigenous-native-peasant autonomy and through the preservation of uses and customs developed in the territories before Spanish colonization (Articles 1, 2, 30, 272, and 290).[9]

The new Constitution also determines fiscal responsibilities. First, it establishes *exclusive*[10] municipal governments responsibilities for both the creation and administration of municipal-level taxes, provided that tax bases are not similar to those of any national or departmental tax; and the creation and administration of municipal-level user fees, patents for economic activities, and special contributions (Articles 302 and 323). Second, it establishes as *exclusive* departmental governments responsibilities the following: the creation and administration of departmental-level taxes, provided that tax

[8] The decentralization was not contemplated in the previous Constitution.
[9] The municipalities can change to regional autonomies or indigenous-native-peasant autonomies through democratic elections (Article 269).
[10] According to the new Constitution, the responsibilities of governments are exclusive when the governments can legislate, regulate and execute them. However, it is possible to delegate regulation and execution of responsibilities to other level of government.

bases are not similar to any national or municipal tax; the creation and administration of departmental-level user fees and special contributions; and the administration of their corresponding royalties under the framework of the national budget (Articles 300 and 323).[11] In this regard, taxes will be approved by their corresponding legislative bodies, however, the *Asamblea Legislativa Plurinacional* (Pluri-national Legislative Assembly), the central legislative level, is in charge of developing the basic regulations for the creation or modification of sub-national taxes (Article 299) as well as the definition and classification of taxes (Articles 323 and 340) corresponding to each government tax type (central, departmental and municipal). It is worth nothing that in any case (even at the central government level) small farming properties and community farming properties will not be subject to tax payment (Article 394).

Third, the new Constitution establishes that royalties, created by national law, are part of departmental revenues (being 11% for hydrocarbons producing departments, Articles 341 and 368). The Autonomy Framework Law complements sub-national revenues classification in detail for all levels of autonomies, following the new Constitution rules and maintaining provisionally the intergovernmental transfer policies as well as municipal taxes. However, it establishes the base to generate a Solidarity Productive Development Fund with resources coming from the IDH. The Fund will be implemented through three mechanisms: solidarity (to contribute to departments less favoured by the IDH), stability (to reduce the variability of resources coming from the hydrocarbons sector) and promotion of productive development.

Lastly, the new Constitution establishes that debt (internal and external) policies correspond to national government regulation as well as that new spending transfers responsibilities should be defined according to the specification of the resources to cover these expenses.

The new Constitution also establishes norms rules to conduct fiscal policies in general and tax policies in particular. Fiscal principles are *economic capacity, equity, progressiveness, proportionality, transparency, universality, control, administrative simplicity, and tax collection capacity* (Article 323) and the promotion of *equitable distribution policies of national wealth and economic resources, in order to avoid*

[11] Regions can have user fees and special contributions (Article 323); however, according to the Autonomy Framework Law, they will not have legislative power (Article 6). Indigenous-native-peasant autonomies can create and administrate user fees, patents and special contributions, and administrate taxes within their jurisdiction (Article 304).

inequality, social and economic exclusion, and to eradicate poverty in its multiple dimensions (Article 316). Additionally, the Autonomy Framework Law determines additional principles: i) the constitutional solidarity generic principle from a fiscal point of view, establishing the joint actions of all levels of government to satisfy collective needs and to use redistributive mechanisms to ensure the equitable use of resources; ii) financial sustainability in the provision of public services, guaranteed by the autonomies; and, iii) economic and financial autonomy to determine the use of resources and to exercise the powers of generating and increasing resources.

Tax policies are based also on vertical equity and universality in tax contribution, given that all Bolivian citizens have to pay taxes in proportion to their economic capacity (Article 108). Additionally, sub-national governments cannot create: i) taxes on goods, activities, rents or assets located outside of their territorial jurisdiction, other than for those generated by their citizens or firms outside the country; ii) taxes that hinder the free movement or establishment of persons, goods, activities or services within their territorial jurisdictions; and iii) taxes that generate privileges for residents, discriminating against non-residents..

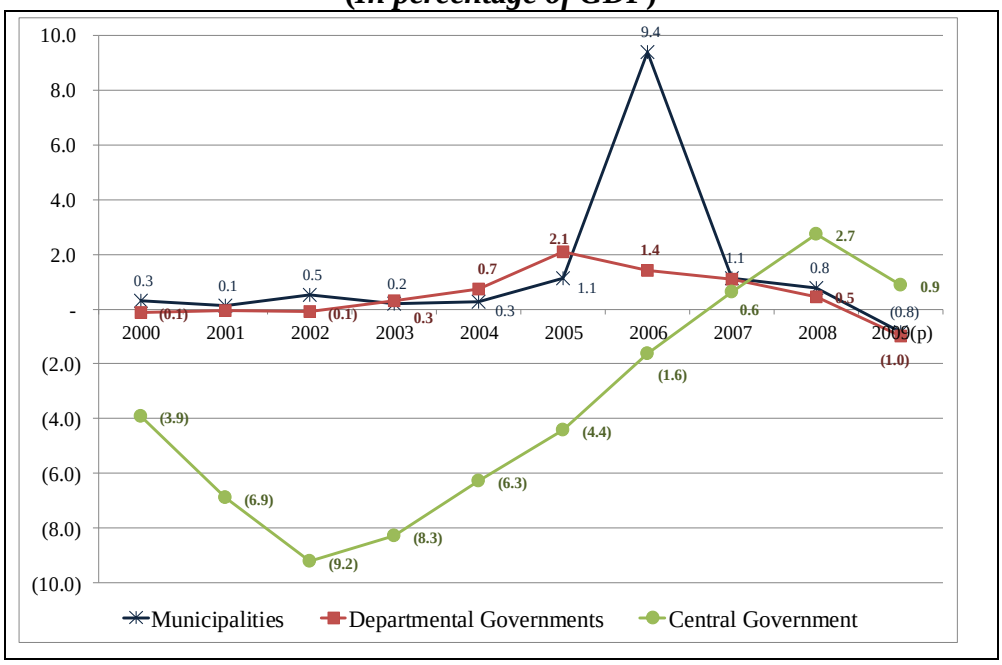
Finally, it is important to highlight the social participation and control of state activities, for eventually it could promote accountability, transparency, efficiency, and equity related to the collection and use of resources. In this regard, the new Constitution establishes that organized civil society will participate in the design of public policies and will control public management at all governmental levels (Articles 45, 242, and 309). Additionally, the Autonomy Framework Law guarantees social participation and control determining that all autonomies' basic regulation framework, called *Estatutos Autonómicos* (Autonomy Statutes) for departments and *Cartas Orgánicas* (Organic Charters) for municipalities, must have the mechanisms and forms of social participation and control[12].

[12]The Popular Participation Law, however, already formalized civil societies, *Organizaciones Territoriales de Base* (Grassroots Territorial Organizations), for participating in public works and services, and to have access to information on the resources.

III. FISCAL OUTCOMES

The revenues legal framework described above, jointly with the expenditure responsibilities and their changes, led to different patterns of fiscal disequilibrium as show in Chart 1. In 2000-2006, the central government was permanently in deficit, while sub-national governments had fiscal surpluses. These fiscal disparities have been usually explained by: i) the increase in intergovernmental transfers (first the HIPC and then the IDH) to municipalities, highlighting the important contribution of the IDH in 2006, derived from Law No. 3058 of 2005, and as a result of the considerable increase in the price of oil; ii) deficiencies in public management capabilities in some sub-national governments, leading to expenditures below those programmed; and iii) the high burden of public expenditures of the central government.

Chart 1: Fiscal Surplus by Level of Government
(*In percentage of GDP*)



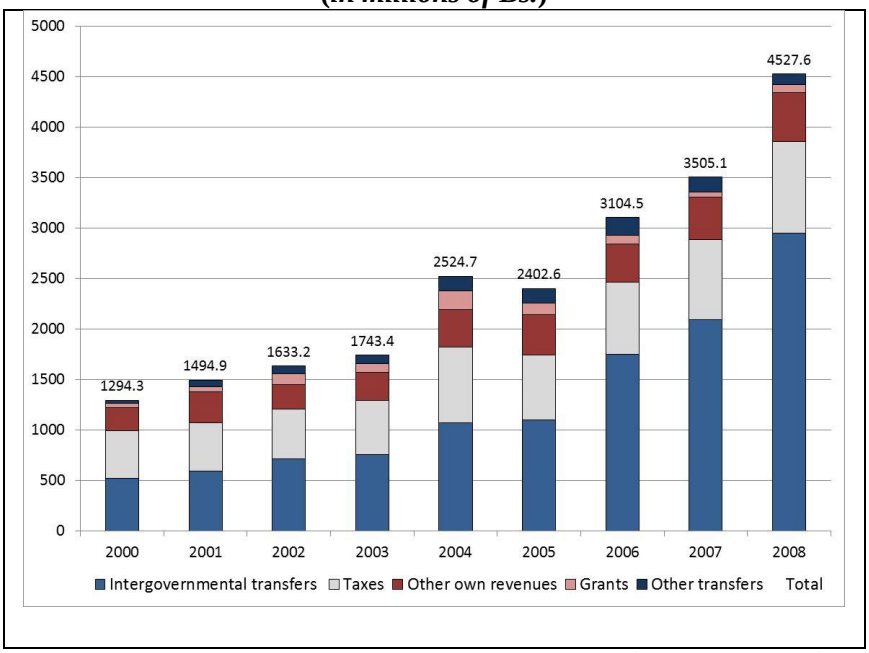
Source: UDAPE (Unidad de Análisis de Políticas Sociales y Económicas).
Note: i) used cash flow data; ii) central government includes state companies and social security.

In 2007-2009 the tendency was reversed: the central government began experiencing fiscal surpluses with rates higher than those of the sub-national governments. In this case the central government was favoured by: i) more resources from hydrocarbons royalties and the IDH; ii) a kind of re-transfer of the 30% of the IDH collection belonging

to sub-national governments to the central government since 2008 for paying the non-contributive older persons' pension (*Renta Dignidad*); and iii) the debt write-offs of the International Monetary Fund, the World Bank and the Inter-American Development Bank, negotiated in 2004-2006, becoming effective in 2006-2007 (achieving USD 2,787.5 million in debt write-off). However, central government expenses also increased over time due principally to both social transfers – such as Juancito Pinto for primary level students and Juana Azurduy de Padilla for pregnant women and newborns – and the "nationalization" of capitalized state companies[13].

Sub-national revenues, on the other hand, have been composed largely of intergovernmental transfers; however, they have different structures, as is shown in Charts 2 to 4. Chart 2 shows the trend and composition of total revenues for the ten main municipalities (the nine capital cities plus El Alto) in 2000-2008.

Chart 2: Revenues Composition of the Ten Main Municipalities (*in millions of Bs.*)



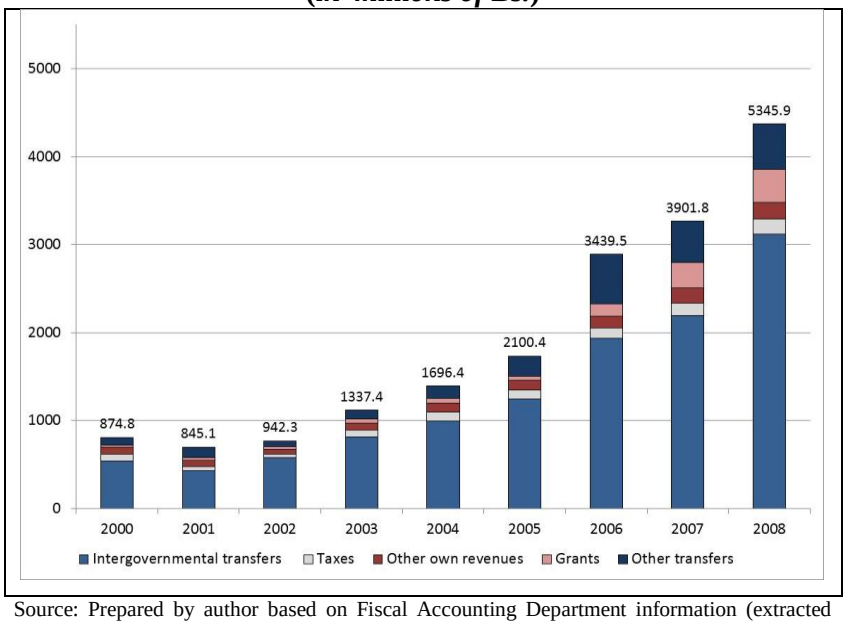
Source: Prepared by author based on Fiscal Accounting Department information (extracted from www.forodac.org.bo)
Notes: i) Taxes includes IPBI, IPVA, ITI, ITVA, and other minor taxes; ii) other own revenues includes user fees, goods and services sales, interest and rental income, and other non-tax revenues.

[13] In 1994-1997, the largest state enterprises were capitalized by increasing stock with foreign investment (see Muriel and Barja 2006)

In 2000 own sub-national revenues were the most important source of income, having a participation of 54.3% over total revenues – taxes, 36.5%, plus other revenues, 17.7% –, more than intergovernmental transfers (40.2%). Nevertheless, in 2008 the situation changed and own sub-national revenues reached only 30.8% of total revenues (Bs. 1.395 billion, or USD 192.0 million), less than a half of intergovernmental transfers, 65.1% (Bs. 2.947 billions, or USD 405.6 million). The change in intergovernmental transfers participation was reflected in a high growth rate, 24.2% per year on average (17.6% in real terms[14]), compared with own sub-national revenues, 9.0% (3.2% in real terms).

Chart 3 shows revenues trend and composition for the remaining 250 municipalities that have information for the period analyzed[15].

Chart 3: Composition of Revenues of Remaining Municipalities (*in millions of Bs.*)



Source: Prepared by author based on Fiscal Accounting Department information (extracted from www.forodac.org.bo).
Notes: i) Taxes includes IPBI, IPVA, ITI, ITVA and other minor taxes; ii) other own revenues includes user fees, goods and services sales, interest and rental income, and other non-tax revenues.

It is worth noting than these revenues represent only 70% of the ten main municipalities' revenues on average in 2000-2008. In this case, intergovernmental transfers are the most important resources for all the years analyzed, with percentage

[14] It means discounting by the inflation rate.
[15] The Popular Participation Law created 314 municipalities that increased over time; however, many of them are very small and did not report their corresponding budgets and others that were divided after 2000 were included as if they had not been divided.

shares ranging from 66.7% in 2000 to 71.3% in 2008, and a rate of growth of 24.5% on average by year (17.9% in real terms). In contrast, the share of own resources was 19.0% of total income in 2000 and 8.4% in 2008; however, these revenues have an important relative growth rate between 2000 and 2008, 11.4% (5.5% in real terms), that seems to be associated with improvements in tax collection[16].

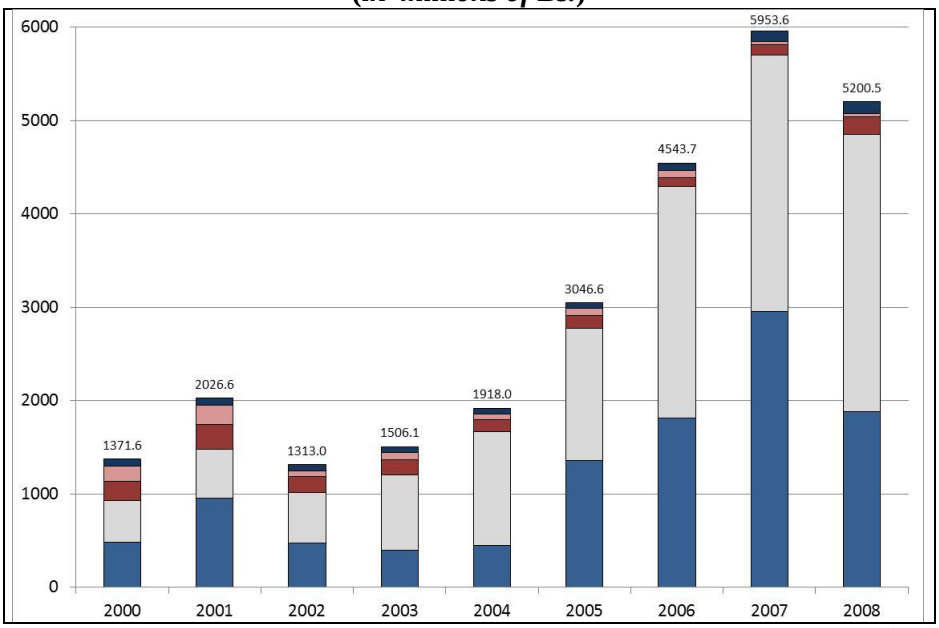
Municipalities' taxes are mostly composed of the Real Estate Property Tax (IPBI) collections, representing on average, in 2000-2008, 59.1% of all taxes in the ten main municipalities, and 50.9% in the remaining municipalities. The next most important tax is the Motor Vehicles Property Tax (IPVA) with a participation of 19.1% in the ten main municipalities, and 23.5% in the remaining ones.

Chart 4 shows revenues trend and composition of departmental governments. As expected, intergovernmental transfers and royalties make up most of departmental revenues, and increasingly so, representing 67.4% of all income in 2000 and 93.2% in 2008, with a growth rate of 23.0% on average by year (16.5% in real terms). In contrast, the (rest of) own revenues had a very low participation, 5.7% in 2000 and 2.5% in 2008, derived from operating revenues, sales of goods and services, interest and property rent taxes, fees, patents and contributions.

Royalties, on the other hand, were mostly composed of hydrocarbon royalties, derived principally from gas sales to Brazil and Argentina. Nevertheless, mining royalties have been increasing in importance since 2006, responding to both the price increases of these commodities and the changes of the tax base for more collection since 2007. Additionally, until 2004 intergovernmental transfers have been mostly composed of the IEHD (with a participation of 56.8% on average in 2000-2004); however, the promulgation of the Hydrocarbons Law in 2005 (together with higher oil prices) made the IDH to be the most important source of income, with a participation of 58.2% on average in 2005-2008, positioning the IEHD transfers in second place (with a participation of 31.9%).

[16] As will be discussed later, municipalities had the support of the RUAT (Municipal Tax Administration Registry Office), which provided tax administration systems to both register and collect taxes and to reduce administrative costs.

Chart 4: Revenues Composition of Departmental Governments
(*in millions of Bs.*)



Source: Prepared by author based on Fiscal Accounting Department information (extracted from www.forodac.org.bo).
Notes: i) Own revenues includes user fees, goods and services sales, interest and rental income, and other non-tax revenues; ii) exclude transfers for paying earnings to health and education sectors.

Finally, Table 2 indicates the problems of unequal distribution of intergovernmental transfers at the department level (in per capita terms) discussed above, being higher in 2008. In particular, Tarija receives the highest amount of these funds; in per capita terms, 28.9 times the amount received by residents of the department of La Paz, that is the least favoured department in per capita terms.

Table 2: Per capita Intergovernmental Transfers (Including Royalties) by Department

Year/Department	2000		2008	
	Bs.	Tarija=100	Bs.	Tarija=100
Tarija	373.8	100.00	4,107.1	100.00
Pando	559.4	149.68	3,904.8	95.08
Potosí	78.5	21.00	773.2	18.83
Beni	128.9	34.48	686.5	16.71
Oruro	128.3	34.31	603.6	14.70
Chuquisaca	111.9	29.93	564.7	13.75
Santa Cruz	103.9	27.79	341.4	8.31
Cochabamba	118.5	31.71	273.3	6.65
La Paz	58.7	15.71	141.9	3.46
Bolivia	109.7	29.34	575.3	14.01

Source: Prepared by author based on Fiscal Accounting Department information (extracted from www.forodac.org.bo) and UDAPE dossier.
Note: Excludes transfers for paying earnings to health and education sectors.

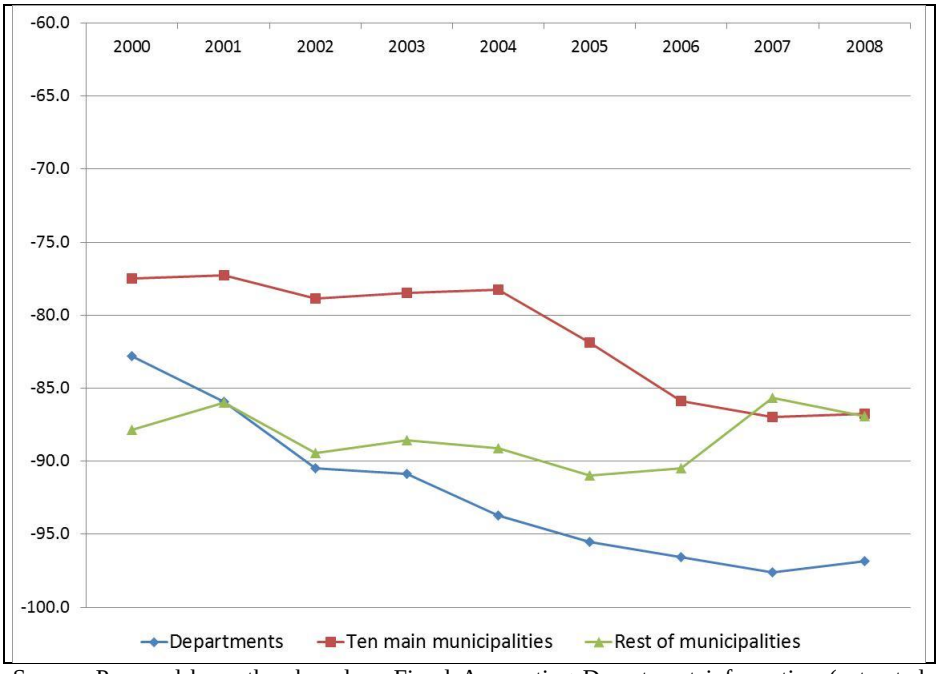
III.1. VERTICAL AND HORIZONTAL IMBALANCES

The dependency on intergovernmental transfers has been reflected directly by vertical imbalances (understood as the insufficiency of own sub-national resources to finance sub-national expenditure). Following Bird (2002), vertical imbalances (*VI*) can be defined as:

(1) $$VI = \left[\frac{Own\,Revenues + Grants}{Expenditures + Lending} - 1 \right] \times 100$$

which can be understood as the rate between own revenues (including grants) and expenditures (accounting also by fiscal surplus). At the extreme, a value of 0 shows that there are no intergovernmental transfers and that all expenses are financed by own resources. At the other extreme, a value of -100 means that there are no own revenues (or grants) to finance expenses. Chart 5 shows the results of the calculation of the vertical imbalances for the period 2000-2008.

Chart 5: Municipalities and Departments Vertical Imbalances



Source: Prepared by author based on Fiscal Accounting Department information (extracted from www.forodac.org.bo).

The ten main municipalities' vertical imbalances are less high as compared to the departments and the rest of municipalities, but are far from and equilibrium. Over time the imbalance increases from -78.9 in 2000 to -87.3 in 2008 as a result of more

intergovernmental transfers. For the rest of the municipalities, the rate presents a value that ranges around -88.3 in 2000-2008, but decreases in 2006-2008 as a result of the strong increase of grants. Lastly, departments' vertical imbalances increase over most of the period, going from -82.8 in 2000 to -6.9 in 2008, which means that in 2008 practically all expenses were financed by intergovernmental transfers. This result also reflects the focus of the Bolivian political, social, and economic issues on intergovernmental transfers – discussed in the political and legal background – giving marginal importance to sub-national own income generation.

Besides the dependency on intergovernmental transfers, horizontal imbalances are another topic of main concern at the municipal level because of the different capabilities and efforts to generate own sub-national income. Table 3 shows these disparities in terms of some relevant indicators.

Table 3: Horizontal Imbalance Indicators of Municipal Per Capita Tax Collection (*in Bs.*)

Statistics/Year	2000	2004	2008
Mean	12.708	15.825	23.252
Median	2.099	3.085	5.677
Maximum	214.89	291.44	409.44
Minimum	0.000	0.000	0.000
Coefficient of variance	2.203	2.270	2.147
Gini coefficient	0.829	0.797	0.844
Concentration index(1)	0.002	0.003	0.002
Concentration index(2)	0.002	0.003	0.002

Source: Prepared by author based on Fiscal Accounting Department information (extracted from www.forodac.org.bo) and INE (National Institute of Statistics).
Notes: (1) considers the Human Development Index and (2) the poverty index based on Unsatisfied Basic Needs

The coefficient of variance is, for all the years analyzed, very high, showing that the standard deviation represents more than two times the corresponding average. This is corroborated with the first statistics described in the table. The average of the per capita tax payment was Bs. 12.71 in 2000 and increased to Bs. 23.25 in 2008, with a growth rate of 7.8% per year (2.1% in real terms); however, in both these extreme years the maximum payment was around 17 times the average, and the minimum payment was zero (no payment at all). Additionally, the Gini coefficient – that measures the inequality of the

distribution of the relevant variable, with zero representing total equality, and one representing total inequality – is also very high, close to 0.8.

One possibility is to attribute the high inequality in tax collection to wealth (or income) inequalities at the municipal level. The concentration index is calculated in order to evaluate this possibility; this index captures the inequality relative to the distribution of a socioeconomic relevant variable. It fluctuates between -1 and 1, where a negative value means that inequality is consistent with a progressive concentration, higher per capita tax collection in richer municipalities. A positive value means the opposite (regressive concentration) and zero means no inequality relative to the socioeconomic relevant variable. Table 2 shows the index using two proxies for income: poverty index (measured by Unsatisfied Basic Needs) and the Human Development Index. In both cases the coefficient is slightly progressive (positive) in all years analyzed, showing that inequality in per capita municipal tax collection is practically unrelated to differences in wealth or income. This result can also be seen in Chart 6.

Chart 6a shows that La Paz is the municipality with the highest tax collection in per capita terms, being on average, for 2000, 2004, and 2008 close to Bs. 357 at 2008 prices, markedly higher than both Cochabamba and Santa Cruz, although the levels of human development are similar for the three municipalities. Porongo is another municipality with a high level of per capita tax collection; it ranks in third place even though in terms of human development it is in position number 90.

Additionally, Chart 6b highlights Poroma, Acasio, and Mizque because they are municipalities with low human development indexes but with considerable levels of per capita tax collection compared to the rest of municipalities. Caranavi also stands out for its level of per capita tax collection; because it does not belong to the ten main municipalities, it has a human development index that is lower compared to these, but has higher tax collection compared to El Alto, Trinidad and Cobija.

In summary, the high levels of vertical and horizontal imbalances related to tax payments (responsibilities) reflect, among other things: i) lack of policies to promote tax equity and fiscal effort; ii) different management capabilities between municipalities in tax administration; iii) different tax bases, especially for real estate properties, which are valued higher in the more populated municipalities; and iv) different degrees of

urbanization that limit own tax revenues, mainly in the rural municipalities (with this factor apparently not being adequately related to the poverty indicator).

Chart 6a: Municipal Per Capita Tax Collection vs. Human Development Index
(average, 2000, 2004, 2008)

Chart 6a: All Municipalities Analyzed

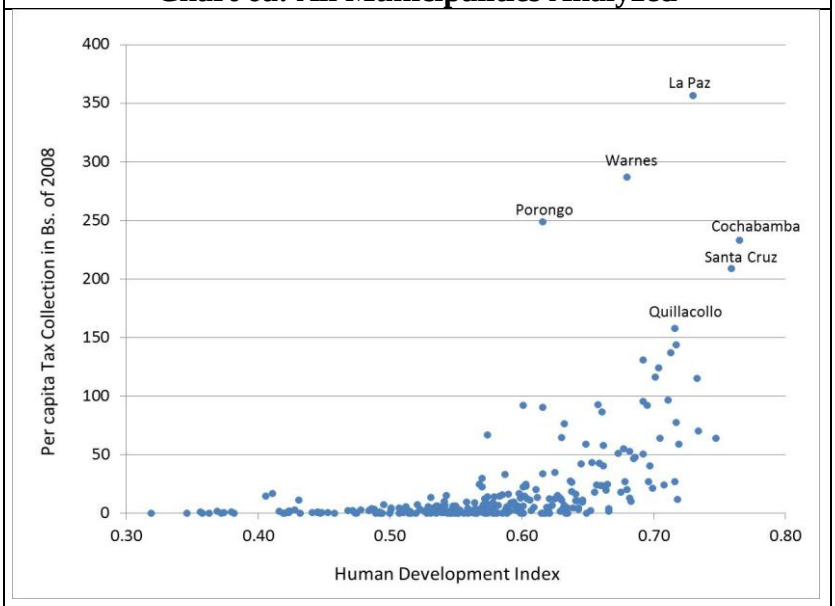
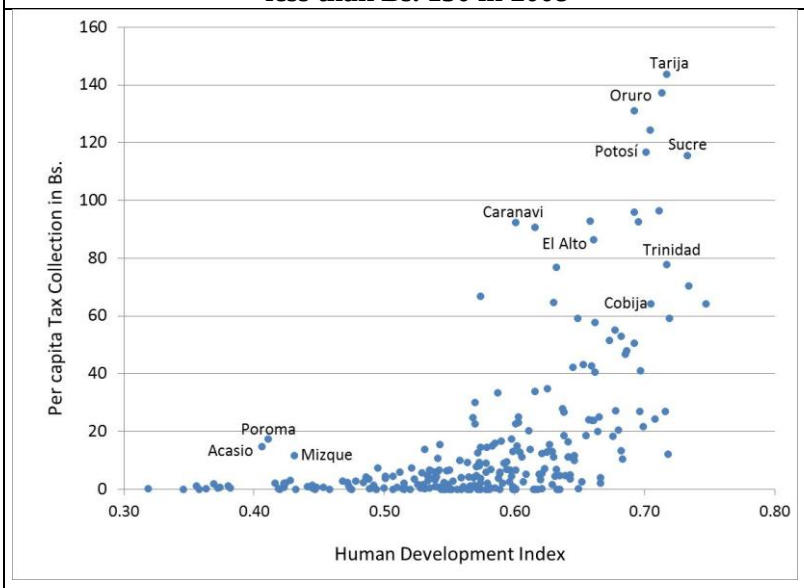


Chart 6b: Municipalities with Per Capita Tax Collection less than Bs. 150 in 2008



Source: Prepared by author based on Fiscal Accounting Department information (extracted from www.forodac.org.bo) and INE (National Institute of Statistics).
Note: Some municipalities have been grouped together because they were divided after 2000 (they did not exist previously).

IV. SUBNATIONAL REVENUES MOBILIZATION POLICY OPTIONS

IV.1. POLITICAL ECONOMIC BASE

According to Section II, one important challenge for the Bolivian government in the years to come will be to develop both the legal framework for regulating sub-national taxes and the legal framework for classifying taxes by level of government.

In this regard, the new constitution has clear and specific rules defining sub-national taxes. First, sub-national governments can create and administrate "sub-national-type taxes", provided that their tax bases are not similar to any other sub-national tax in force. In practice, it gives very few possibilities to generate new taxes at the sub-national level. The central government taxes currently cover most tax bases: hydrocarbons, forestry and mining resources (royalties, taxes and patents), the Value-added Tax (IVA), the Specific Consumption Tax (ICE) for final goods and services sales, the Transactions Tax on all gross income (IT) – except for employees –, the Regime Complementary to IVA (RC-IVA) on labour and capital income, the IEHD on hydrocarbons and derivatives sales, the IDH on hydrocarbons gross value, current municipal taxes on properties and vehicles (transferred by the central government as *derived taxing power*), among others that are less relevant (see Table A.1 in Annex 1 for a detailed description of taxes). Nevertheless, taxes collected at the municipal level are a kind of right acquired by municipalities, which means that they belong to municipalities (avoiding potential political conflicts); however, taking into account the new constitution, these rights would be *derived taxing powers*, and not *original taxing power*. In this regard, in legal terms, it would still be possible for the central government to derive other taxes to sub-national governments or to share some taxes with them. However, it would give less negotiation power to sub-national governments.

Second, the previous evaluation shows the relevance of promoting own sub-national income generation, basically for the following reasons:

- Departmental governments are at present almost entirely dependent on intergovernmental transfers that are based principally on hydrocarbons production and prices, which generates many problems; among these are: central government dependence on hydrocarbons sector investment for increasing these resources;

hydrocarbons prices volatility; some revenues conditioned to social programs; and, unequal distribution between departments.

- Municipalities present an increasing intergovernmental transfer dependency, confronting the same problems described previously for departments. Additionally, the high levels of horizontal imbalances analysis shows the need to think of more effective and equitable sub-national own income generating policies.

At the social and political discussion level, there is consensus on the need for increasing own sub-national revenues through taxes, fees and in-kind contributions. The Bolivian Federation of Municipalities (2007, 2008) – that groups together all municipal associations from the nine departments – and the Tarija Association of Municipalities (2006) explain that their members raise the need for consolidating municipal autonomies by (among others) having own resources (and transfers) sufficient to meet their corresponding institutional functions and spending responsibilities. In this regard, they propose creating taxes on property and transfers of property for medium and large rural farm properties and green taxes, reducing tax incentives and exemptions, and co-participating all central taxes and royalties (with less conditionality). Additionally, recognized is the need for strengthening municipal tax administration and to break the link with vulnerabilities caused by changes in central government policy. Finally, a Fiscal Pact is proposed that would be a fiscal solidarity regime based on cohesion, compensation, and equalization in order to promote more even development and less horizontal and vertical imbalances.

Departments are still less organized than municipalities because four of the nine departments – Santa Cruz, Tarija, Beni, and Pando – democratically became autonomies only in 2006, and the rest of the departments in 2009. Additionally the *Estatutos Autonómicos* (Autonomy Statues) – that will define tax policies among other rules – were developed and approved in Santa Cruz, Tarija, Beni, and Pando in 2008, before the new constitution was approved, which means that they have to be restructured. The rest of departments are still developing their corresponding *Estatutos Autonómicos.* However, there is the perception, from the proposals found in the *Estatutos Autonómicos*, that most departments would like to share or co-participate current national taxes and create new taxes, such as especial contributions, new taxes for mining and forestry, and new patents for hydrocarbons.

Additionally, some authors have proposed as departmental resources, the Income Tax on Individuals (Cossío 2005, Zapata 2005, Pereira 2006, Dorado 2009, Medinacelli 2010, and Barrios 2010), the Sales Tax on Gasoline and Diesel or, alternatively, a surcharge on the IEHD (World Bank 2006, and Pereira 2006), a surcharge on the Specific Consumption Tax (ICE) (World Bank 2006, and Pereira 2006), a surcharge on vehicles and urban properties (Pereira 2006, and Zapata 2006) and the reallocation of the Corporate Net Income Tax (IUE) (Villarroel, 2010).

Lastly, as mentioned in Section II, the new constitution already establishes some principles regarding the tax assignment problem by levels of government discussed in the literature. They can be summarized in *the prohibition on taxing non-residents or discriminating against them (in terms of taxes) and on taxes that limit freedom of movement*. Additionally, the previous evaluation leads us to propose the following principles usually found in the literature (see Ambrosanio and Bordignon 2004, and Bird 2008) for choosing sub-national revenue options:

1. *Classifying sub-national taxes that are as closely related as possible to the benefits derived from spending them*. This option could allow progress in Bolivian social control policies established by the new constitution; where citizens would perceive tax results and, hence, would be more willing to fulfil their tax obligations and be better able to control their expenses. This behaviour, in turn, would promote more accountability.
2. *Maintaining taxes on unevenly distributed tax bases (such as natural resources) at the central level*, such as hydrocarbons and mining taxes and royalties (that already cause imbalances between departments).
3. *Payments of taxes that serve to generate credits towards the payment of other taxes should be a responsibility of the central government*.
4. *Implementing a basic tax regulation for avoiding "tax wars" and revenue erosion problems*.
5. *Implementing tax policies that are as simple as possible regarding collection and comprehension at all government levels*.

Additionally, other general tax policy principles – some of which are considered in the new decentralization regulations as described above – should also be taken into

account, *such as vertical and horizontal equity*, *seeking minimal distortions on agents' decisions*, and *avoiding double base taxation* (principally on savings).

IV.2. POLICY OPTIONS DISCUSSION

This Sub-section briefly discusses the sub-national own revenues policy options described above.

At the municipal and departmental levels, a proposal was made to implement green taxes (also called environmental taxes or ecological taxes) which are related to sustainable development. In this regard, green taxes are part of environmental policies, meaning that they should be established by the (levels of) government responsible of these policies, which is not yet clearly established in all regards[17]. However, currently the mining and forestry patents are similar to these kinds of taxes (because their intention is to compensate the affected regions), under the responsibility of the central government. Waste treatment is a municipal responsibility, with specific fees[18]. Additionally, it could be possible to apply fees on camping, hiking, fishing and hunting; probably at the municipal level (however many municipalities will have limitations because of deficient management capabilities).

At the municipal level (other kind of) fees are certainly desirable instruments to improve own revenues, and the perceivable benefits generated come quite close to the costs in the case of sub-national goods and services provisions. The proposal for the creation of taxes on property and transfers of property on medium and large rural farm properties cannot be applied in most of the highlands of Bolivia because the properties are small and, according to the new constitution, they are not subject to any tax. In the lowlands, however, this policy could be applied because there are medium and large rural farm properties. In this scenario, however, many problems arise. First, the implementation of this tax policy would be another source of tax burden inequality – given that the tax base is unevenly distributed among municipalities – which would benefit the richer rural municipalities. Second, if it were applied, it would require a proper definition of small, medium and large properties, which can become complicated, and may give rise to tax

[17] According to the new regulation, the central government is responsible for the design, approval, and implementation of general biodiversity and environmental policies. However, several specific functions are under the responsibility of various levels of government; for example, the regulation and execution of solid waste, industrial and toxic policies; and environmental and wildlife protection, maintaining the ecological balance, and controlling pollution.

[18] See, for example, http://en.wikipedia.org/wiki/Ecotax, for green taxes classification.

evasion because it would establish who pays this tax. Finally, it would require a new tax collection system for the benefited municipalities, which currently are rural and with low public administration capacities. Therefore, at the municipal level the present discussion concentrates on the two most promising policies: in-kind contributions and improvements in tax administration.

In-kind contributions – of materials and labour – can be highly favourable for increasing own sub-national resources collection, especially for poor municipalities where the main activity is traditional agriculture. In terms of *economics and fiscal results*, Roduner (2003) estimated that in-kind contributions, from the communities to their respective municipalities (not registered or valued), represent at least 30% of the cost of investments in infrastructure in northern Potosí – the poorest region of the country – and 24% in the Chaco. Additionally, they represent between 2% and 13% of total municipalities' revenues and at least 14% of their corresponding own revenues.

In terms of *administrative feasibility*, Roduner developed a pilot test in two municipalities applying a proposal methodology for valuing, registration, and inclusion of these contributions as non-tax revenue to the municipal budget, and gave the basis for their implementation. He showed that it is possible to take into account these revenues by both changing some sub-national budget guidelines established by the central government and by applying a proper methodology to account for these revenues.

In terms of *political and social feasibility*, the participation of communities in public investment tasks (education, housing, health, etc.) was defined in the Popular Participation Law as a duty. In practice, however, it has not been applied in a compulsory way, but voluntarily, and has had some successful results, for example, in the education sector. In this regard, it is possible to take advantage of the strong Bolivian social organization structures, mainly developed in rural areas, to encourage citizens to contribute with labour or materials. In this context, Roduner points out the need for formalizing these community contributions by the local authorities, through a formal agreement and non-monetary recognition, in order to distinguish these contributions.

Finally, in terms of *tax assignment principles* and good practices, it is worth noting the multiple advantages of this policy as: i) effective in terms of cost-benefit (where communities are the main beneficiaries of public investments); ii) the promotion of

vertical and horizontal equity; and, iii) greater accountability and empowerment for the work of municipalities.

Improving ***tax administration*** can certainly decrease the horizontal imbalances described above, promoting the constitutional principle related to vertical equity (contribution according to economic capacity). In this regard, the RUAT (*Registro Único para la Administración Tributaria Municipal*, Sole Municipal Tax Administration Registry) was created, which began operating in 1998, initially as RUA (*Registro Único Automotor,* Sole Vehicle Registry), supporting municipalities with the use of the national vehicles records, as well as with the design, development, and management of information technology systems for the registration and payment of taxes on vehicles (IPVA and ITVA). The record has been updated by the customs office for the registration of imports. The system has been improved over time, correcting the duplication of licence plates and implementing high-security stickers, among others.

Since 2004, through a request by the municipalities, the RUAT expanded its work to help the municipalities with real estate taxes collection (IPBI and ITBI), and other minor collections. The RUAT developed and managed registration and collection systems, taking into account the differences in the tax base specifications of each municipality (that use specific parameters according to their respective regions).

The RUAT's work had several positive results, among of them: i) gains in terms of economies of scale (reducing administrative costs) through the development and use of the information technology systems by the affiliated municipalities, in terms of collection – since the RUAT established contracts with all banks with levels of commissions that would not be given to the municipalities – and in terms of information generation for payment and collection, among others; ii) streamlining and simplifying tax payment information for taxpayers; iii) increasing coverage of taxpayers; iv) generating positive externalities in poor municipalities that could not have this kind of system independently; and v) the use and standardization of tools that are increasingly modern and sophisticated.

According to the RUAT members, the difficulties that they find are: i) differences in the tax base determination at the municipal level; ii) lack of registries to adequately determine tax bases, which in turn are currently derived from sworn declarations; iii) deficient technical records, partly as a result of the previous point (there were duplicated records, some undocumented or incomplete records, and false statements regarding

housing characteristics; for example, some are still registered as land); and, iv) low levels of fiscal controls at the municipal level.

Other municipalities (usually rural and small) that are not registered in the RUAT, manage a basic system (*Sistema Integrado de Ingresos Municipales,* Integrated Municipal Income System) for collecting taxes; however, this system has many limitations in terms of technology and coverage of requirements (see Terán 2007).

Although there is no information to estimate the levels of tax evasion, RUAT members estimate that the evasion of vehicle taxes is between 20% and 25%, and improvements in the registry and in tax administration could increase real estate tax collection by up to three times in some cases. This observation can be supported by the data. According to the Household Survey of 2003-2004, only 18.14% of Bolivian households pay the IPBI and 4.66% pay the IPVA, representing, respectively, 0.9% and 0.4% of their annual incomes. Furthermore, these tax collections represented around 1% of GDP in 2000-2008.

In this regard, it seems necessary to continue improving the municipal tax administration. This will require actions such as: i) a specific diagnostic for each case (municipality) in order to implement appropriate policies to improve tax administration[19]; ii) the generation of better registries; and iii) continued support for RUAT's work. In particular, registries could be improved (at least for fiscal control) by using the new Census, which collects much information on housing characteristics for the entire country. The Census questions can be redefined or complemented according to the requirements of the municipalities' tax base determination.

At the department level, as mentioned before, there was a proposal to create new taxes (or surcharges) on mining, forestry, and hydrocarbons; to place a surcharge on the ICE; to implement a surcharge on vehicles and urban real estates property taxes, to reallocate the IUE, and to create a personal income tax. Each case will be briefly discussed below, emphasizing personal income tax more strongly.

In the mining sector, Table 1 showed that there are already patents, royalties and taxes on production and sales of the sector (IT, IUE and IVA). Additionally, they are currently central government taxes and part of them are used as intergovernmental transfer resources. Furthermore, the creation of a new tax on the sector (with a "new kind of tax

[19] See Terán (2007) for an evaluation of this topic.

base”) would imply more inequity because this natural resource is unevenly distributed between departments. A similar observation applies to the forestry sector, which has patents and taxes on production and sales (IT, IUE, and IVA).

In the hydrocarbons sector, on the other hand, there are also limitations for implementing other taxes. First because it already has a wide range of taxes on exploitation, production, and sales – royalties, IDH, IUE, IVA, IT, and EHD – used also as part of the intergovernmental transfers system as discussed in Table 1. Second, because one of the main problems (described above) of departmental resources, is their dependency on hydrocarbons, and the possible consequences on fiscal instability. Finally, because the hydrocarbons resources are unevenly distributed among regions, which means that inequity problems will increase. In this regard, the proposed Sales Tax on Gasoline and Diesel (similar to the IEHD), or, alternatively, a surcharge on the IEHD, could avoid, in some way, equity problems (if taxed in the corresponding departments). However, the IEHD is not used only for transfers to departments but also as a stabilizing tool for hydrocarbons derivatives domestic prices (such as gasoline and diesel). In particular in the Bolivian case, the stability of these prices is related to both domestic price stability and socio-political stability, which means that it has to be managed carefully by the central government because it is related to macro policies. Nevertheless, the IEHD could be transferred to departments in a more equitable way (for example by considering the consumption of hydrocarbons derivatives by department).

A surcharge on the ICE has also been evaluated as a departmental own resource (it applies to vehicles, tobacco products, alcoholic beverages, and soft drinks). However, it has two limitations: it has some *mobility* problems with regards to the tax base (mainly on tobacco products, alcoholic beverages, and soft drinks), and it is already used as part of municipalities’ transfers. Additionally, the collection of ICE in 2000-2008 represented 3.8% on average of the total central government collection, and a surcharge of 20% (under the hypothesis of inelastic demands) would represent only 3.9% of the total departmental resources (considering data of 2000-2008).

The reallocation of IUE to departmental governments has already been evaluated by the Ministry of the Economy (2006). The main drawbacks found are: i) The tax is not necessarily collected where the companies are located (because there are many companies with dispersed locations and the collection is done at the main location of the firms, that

could belong to a department different from those of the other locations); ii) The tax is related to the IVA and the IT, with the IUE being a fiscal credit for the IT (which would demand the complicated work of matching these two tax collections between departments), and being directly related to the IVA through sales and the costs of production levels; iii) Different tax rates between departments would imply fiscal wars; and iv) The administration of the IUE is relatively complicated, which would complicate its management at departmental level.

Surcharges on real estate and vehicle taxes are other possibilities for generating departmental tax revenues. The advantage relies on the use of the current tax administration system, and the possible help of departmental governments to improve tax administration in small and rural municipalities. However, this proposal could be disapproved by two important social groups, the municipalities (associations) that would see the IPBI and the IPVA tax bases and collections affected, and citizens' associations; and it would not be clear who would collect the taxes, with the need for negotiations between departments and municipalities. Finally, tax collection does not seem to be significant; for example, surcharges representing an increase of 20% of total collection would represent only 4.8% of the total departmental resources (considering the data of 2000-2008 for the calculation). However, improving tax administration, as mentioned before, could triple this percentage.

Lastly, with respect to the ***personal income tax***, it is important to note that Bolivia has the RC-IVA that can could be considered similar to this tax, because it applies to individuals and inheritances (*sucesiones indivisas*), additional to employee labour income and capital rents, with a 13% tax rate. However, in the case of formal salaried workers, they can deduct four minimum salaries, their pension contributions, and all purchases that include the IVA payment through IVA invoices declarations. In practice, the RC-IVA has been useful for increasing the payment of the IVA in an economy that is highly informal – the purchase of most basic goods and services does not have IVA included in the payment because they are produced by micro and small firms that are illegal or subject to special tax regimes (which means that do not pay any tax at all, see Jiménez et al. 2001). And the possibility of deducting the entire RC-IVA tax by presenting invoices has also generated a secondary market for IVA invoices, with the existence of false invoices.

The collection of the RC-IVA has been very low (0.2% of GDP on average in 2000-2009), with taxpayers wasting their time (on average around USD 115 of loss per employee per year according to Jenkins and Arroyo, 2003) because they have to declare all IVA payments, by individual invoices.

Besides the RC-IVA, the government applies taxes to the rents of independent professionals and the rental of properties, treating them as companies, which means that they are subject to the IVA, the IT and the IUE, assuming that the net benefits are 50% of gross income! Independent professionals have to make monthly declarations of the IVA (13%) and the IT (3%), but they may also deduct the IVA by declaring IVA invoices, which also gives an incentive to the existence of a secondary market for invoices and implies loss of time. Additionally, once a year they must declare the IUE on gross income minus 13% for the IVA, with the remaining income being subject to the IUE, but 50% can be deducted with IVA invoices declarations again, paying the other 50%. The 50% IUE payment, in turn, serves to deduct IT payments in the future. Property rentals follow a similar process; however, most properties that are rented usually do not pay these taxes.

In this context, it is possible to modify the RC-IVA, and independent professionals and property rental taxes by:

a. Establishing than only a percentage of employees' "net labour income" be deduced from the RC-IVA through presenting IVA invoices, which would be applied to labour incomes above a certain minimal amount, maintaining the previous RC-IVA declaration for the rest of formal salaried workers; Additionally "net labour income" would be determined deducting only two minimum salaries and pension contributions (the two minimum salaries discount would give a certain progressive nature to the tax without incurring in considerable tax administration problems).
b. Applying the RC-IVA to independent professionals and giving non-professionals the same treatment; In the case of independent professionals, the proposal would lead to exclusion of the IT and IUE payments, and lower the amount of IVA invoices declarations. In the case of independent non-professionals, it would mean excluding them in some cases of special regimes (that do not pay any taxes on their income) and in other cases from the IT and IUE payments (see Jiménez et al. 2001).
c. Applying to the RC-IVA the treatment described previously for property rentals

d. Establishing a low and flat tax rate in order to avoid sub-declarations and political problems; The RC-IVA tax rate should be shared by the central government and the departments, for example 40% of the tax for the central government and 60% for the departments.
e. Establishing the tax administration at the national level for two main reasons: i) it is currently a national tax, which means that it cannot be created by departmental governments; and ii) it is related to the collection of IVA, which is a central tax.

In terms of *social and political feasibility*, the implementation of this modification of the RC-IVA has the advantages that follow. It would be favourable for the central government because: i) as is seen below, it would maintain (or even increase) the present level of the RC-IVA collection, compensating the IUE collection loss from independent workers; ii) it would reduce the administrative costs related to the preparation of IVA invoice declarations (that are done invoice by invoice) as well as the IT and IUE declarations, and iii) the secondary market of IVA bills would be reduced, decreasing illegal actions. Additionally, the announcement of a reformulation of the RC-IVA scheme by the central government would be less "dramatic" than an announcement of a tax on personal income.

For employees, the RC-IVA policy would mean more tax payments; however, since it would be a low flat tax rate, it can be evaluated in relation to the benefits associated with the IVA invoices declarations. For the formal independent professionals, it would mean not only less transaction costs but also less tax payments (that is currently around 8% of their gross labour income) and could imply an incentive to declare more labour income (through their own IVA invoices issued). Finally, for independent non-professionals, it would mean, in some cases, to pay taxes (for people under the special regimes) and, in other cases, to pay less taxes with the benefit of less transaction costs. However, it is important here to remember that the RC-IVA would be applied only to labour incomes above a certain minimal amount, which corresponds (as we will see in the economic evaluation below) to earnings in the 9th and 10th deciles.

Finally, because departmental governments, as mentioned before, have raised the need of having own resources, they could support this policy to the extent that this tax announcement does not involve social dissatisfaction (which must be associated with a clear and simple explanation to taxpayers).

In terms of *tax administration feasibility*, the tax policy would have the following advantages: i) exclusion of other possible tax bases on personal income that are difficult to tax in practice in the Bolivian case (see, for a discussion, Cossío 2005); ii) reduction of administrative costs related to IVA invoices, IT and IUE; iii) simplified administration through the implementation of a flat tax, avoiding tax complexities and tax evasion problems; iv) use of the current tax administration system; and iv) possible approval by departmental governments, which would not have the need to develop a tax administration system.

Additionally, it is possible to promote making the RC-IVA payment universal (avoiding the usual tax evasion) by designing creative policies, such as for example, establishing that all bank loans be supported by RC-IVA declarations.

In terms of *economic and fiscal results*, the Household Surveys of 2003-2004[20] allow estimating the RC-IVA collections according to the proposed policy. In this regard, it is assumed that:

- The minimum labour income is determined using the poverty threshold, considering the highest poverty threshold per capita from the nine departments (because they differ according to the variation of the cost of the consumer basket) multiplied by the national average number of household members (4.2) – assuming implicitly that only one member of the family works to sustain the family. This minimum income that the family requires in a month constitutes the minimum salary, and was Bs. 1,600 (USD 203) in 2003-2004, which corresponds to the workers that have earnings in the 9th and 10th deciles.
- RC-IVA is applied to the entire employed population; that is, salaried workers, independent professionals, and self-employed workers (for non-professionals), with the remainder being employers, bosses, and cooperative members that do not receive salaries (and hence should pay taxes as companies). This employed population was of 508,074 workers in 2003-2004, which corresponds to 12.1% of the entire employed population.

We obtain the "net labour income" and calculate four scenarios: i) a tax rate of 5% applied to 60% of the tax base (the remainder being deducted through IVA invoices); ii) a

[20] We propose using the 2003-2004 survey because, it being continuous over one year, it has richer information than the surveys implemented in other years (that are applied only to one month).

tax rate of 8% applied to 60%; iii) maintaining the tax rate of 13% applied to 30% of the tax base; and iv) maintaining the tax rate of 13% applied to 40% of the tax base. The estimations of Nina (2006) show that on average the payment of IVA by household is 7% of the total household income, approximately 15% of the "net labour income", which means that simulations cover all IVA controls made of current IVA invoices declarations. The following Table shows the results of these scenarios by departments.

Table 4: RC-IVA Modification as an approximation of a Personal Income Tax

Tax rate	5%	8%	13%	13%
On "net labor income" and rental properties	60%	60%	30%	40%
Tax Collection (Thousand Bs./year)				
Chuquisaca	30968	49549	40258	53678
La Paz	140120	224193	182157	242875
Cochabamba	85536	136857	111196	148262
Oruro	16665	26664	21665	28886
Potosi	24990	39985	32487	43317
Tarija	22878	36605	29742	39656
Santa Cruz	157867	252587	205227	273636
Beni	17821	28513	23167	30889
Pando	4893	7829	6361	8481
Total	501739	802782	652260	869680
As a percentage of GDP	0.8%	1.2%	1.0%	1.3%
For departmanets (60%)	0.5%	0.7%	0.6%	0.8%
The 60% as % of departmental revenues	18%	28%	23%	30%

Source: Prepared by author based on 2003-2004 Household Survey.

The simulation results show that for all departments, the collection would imply a range from a minimum of 18% of current total revenues (a tax rate of 5% applied over 60% of the tax base) to a maximum of 30% (maintaining the tax rate of 13% applied to 40% of the tax base), which means significant own departmental resources, although the tax burden is not significant at the national level (around % of GDP). In per capita terms, however, richer departments (such as Santa Cruz) would collect more taxes compared with poorer departments (such as Oruro and Potosí), which can be corrected with specific national programs to increase earnings in less-benefited departments (by supporting productive development).

V. CONCLUSIONS

This paper reviews sub-national revenues – taxes and intergovernmental transfers – in the Bolivian decentralization process, disusing some possible policy options in order to increase own sub-national revenues.

The first discussion is on sub-national revenues policies from a political-legal point of view. In terms of own revenues, municipalities inherited national taxes (IPVA, IPBI, ITVA, ITI and the Specific Consumption Tax on Corn Alcoholic Drink) and could implement user fees and patents through approval by the central government. Departments received as "own revenues" part of royalties for the exploitation of natural resources (hydrocarbons and mining); however, they were unevenly distributed among them (favouring producer departments).

Municipalities began to receive intergovernmental transfers in 1994, with the transfer of 20% of the collection of eight national taxes, being reinforced with the HIPC (Heavily Indebted Poor Countries) debt relief resources since 2001. In both cases, resources were distributed by equity criteria, such as population size and poverty levels, and only a few municipal resources, such as those of mining and forestry patents, were transferred without any equity criteria, since they sought to compensate for mining and forest exploitation in the affected regions. In 2005, however, the transfers of the Direct Hydrocarbons Tax (IDH) – and a part of the royalties – generated a distortion on municipal resources allocation benefiting municipalities belonging to hydrocarbons producer departments.

Departments' intergovernmental transfers began in 1995, through part of the IEHD collection. Since 2005, the creation of the IDH provided another important source of income. In both cases, however, equity criteria were only taken into account marginally.

Taxes and intergovernmental transfers have not changed yet; nevertheless, the new National Political Constitution and the Autonomy Framework Law provide the basis for a new sub-national revenues structure, which may contribute to generating more efficient and equitable sub-national revenues policies. In this regard, it is worth emphasizing that municipalities and departments: i) may create and administrate their own taxes, provided that the tax bases are not similar to those of any other level of government – under a basic regulation for the creation, modification, and definition of sub-national taxes; ii) may

negotiate mechanisms in order to redistribute and ensure the equitable use of resources; iii) may promote economic and financial autonomy to determine the use of their resources and to exercise powers for generating and increasing their resources; and iv) may establish social participation rules for controlling public management.

In terms of fiscal outcomes, many shortcomings have been observed. First, fiscal disequilibrium had different patterns by level or government. In 2000-2006, the central government was permanently in deficit, while sub-national governments had fiscal surpluses, attributed to more intergovernmental transfers; there were public management capabilities limitations for spending in some sub-national governments, and a high burden of public expenditures for the central government. In 2007-2009 the previous tendency was reversed; the central government was favoured by more resources from hydrocarbons exploitation, the re-transfer of 30% of the IDH from the sub-national governments, and debt write-offs by multinational organizations. However, central government expenses also increased over time due principally to both social programs and the "nationalization" of capitalized state enterprises.

Second, for the ten main municipalities (capital cities plus El Alto), sub-national own revenues have been relatively important; however, with a participation over total revenues that decreased over time – from a percentage of 54.3% in 2000 to 30.8% in 2008 –being displaced by intergovernmental transfers. In turn, intergovernmental transfers grew through the National Dialog Law in 2001, and the creation of the IDH in 2005, which was accompanied by a considerable increase in hydrocarbons prices. For the rest of the municipalities (that have information for the period analyzed), intergovernmental transfers and royalties have always been the main source of revenues, with percentage shares ranging from 67.7% in 2000 to 71.3% in 2008. These outcomes generated high levels of vertical imbalances, principally for the rest of the municipalities, which jointly had a rate that ranged around -88.3 in 2000-2008, compared with the ten main municipalities, which over time had a rate that increased from -78.9 in 2000 to -87.3 in 2008.

Third, departmental governments, having been only de-concentrated, had few own resources, being supported principally by intergovernmental transfers and royalties – 67.4% of all income in 2000 and 93.2% in 2008 – mostly relying on the hydrocarbons sector (prices and production). Over time, departments' vertical imbalances increased, going from -82.8 in 2000 to -96.9 in 2008.

Finally, the analysis of horizontal imbalances showed high levels of inequality in municipal per capita tax collection, with the Gini coefficient being close to 0.8. Inequality was also evaluated by taking in to account poverty and human development differences (as proxies of income or wealth), by using the Concentration Index. This index, however, showed that tax collection is practically not related with differences in these proxies of income or wealth. In this regard, La Paz stands out as the municipality with the highest tax collection, and Poroma, Acasio, and Mizque as municipalities with low human development indexes but with considerable levels of per capita tax collection compared with the rest of the municipalities.

The horizontal imbalances observed may reflect several aspects, among of them: i) a lack of policies to promote tax equity and fiscal effort; ii) different management capabilities between municipalities in tax administration; iii) different tax bases, especially for real estate properties, which are valued higher in more populated municipalities; and iv) different degrees of urbanization that limit tax revenues, mainly in the rural municipalities (apparently not being adequately considered by the current poverty indicator).

Lastly, the discussion centres on sub-national income-generating policy options consistent with the current political and social discussion, the economic, fiscal, and legal Bolivian base, and some relevant principles that should guide the tax assignment policy. In this regard, the main recommendations are: i) to promote in-kind contributions (materials and labour) at the municipal level, especially in poor rural municipalities, that already have some successful experiences with the participation of communities in public investment tasks; ii) to improve municipal tax administration supporting the continuation of the RUAT's work and improving the registry with the new Census; and iii) to evaluate the possibility of redefining the RC-IVA as a personal income tax, being shared between the central government and the departments, that could generate considerable own resources for the departments.

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Table A.1: Taxes Description

Tax	Acronym in Spanish	Taxable event	Tax base	Taxable person	Tax rate	Exemptions
Value Added Tax	IVA	Regular sales of movable property. Leasing & Sub-leasing of real estate & movable property. Services in general. Final imports. Financial leasing (movable property)	Net sales	Natural or legal persons	13%	Exports. Imports-Diplomatic Staff. "Bonafide" Imports up to $US 1000. Free trade zones. Portfolio transfers. Securities listed on the stock market. Assets subject to securitization. Art work
Value Added Tax Complementary Regime	RC- IVA	Income deriving form a Bolivian source of individuals and undivided estates originating from work, capital investment or application of both.	For dependent employees: difference between income earned and permitted deductions. For direct taxpayers: total amount of income received.	Natural persons and undivided states	13%	Natural persons who receive retirement pensions and elderly pensions. Social benefits. Subsidies. Natural persons and undivided estates liable to pay the IUE. Natural persons resident in the country who receive profits or dividends.
Transaction Tax	IT	Accrued Gross Income obtained during the year from any activity, whether profit making or not: commerce, industry , profession, trade, leasing of goods, works & services, non-sale transfer of real estate & movable property and rights	Accrued gross income	All natural or legal persons who carry out the activities mentioned in the taxable event. Natural persons who carry out independent professions or trades.	3%	Dependent workers. Civil service workers. Services rendered by national, departmental & municipal governments. Interest on deposits in savings, fixed term and current accounts. Private educational establishments using the official curriculum. Publication & import of books & newspapers. Trading of shares & securities. Diplomatic services. Trading of minerals, metals, oil & natural gas in the internal market. Portfolio transfers. Exports

Tax on corporate profits	IUE	Net Profit	For enterprises: Gross profit less deductible expenses. For independent Professionals or trades. Presumed Profit: 50% of the total amount of the income received after deduction of the IVA declared and paid during the taxable year. Overseas beneficiaries. Profits from Bolivian sources remitted overseas. Activities partially carried out in the country.	Public and private enterprises, including professional business. Overseas beneficiaries.	Enterprises: 25% on net profits. Independent professionals or trades: 25% on presumed profits. Overseas beneficiaries (who receive income from Bolivian sources) 25%. Activities partially carried our in the country (remittances from overseas): 4%. Extractive activities pay an additional tax rate of 25%, after deduction of up to 33% of accumulated investments or 45% of net income obtained for each extractive operation.	National and municipal governments, public universities. Associations, foundations and legally authorized non-profit institutions.
Special tax on Hydrocarbons and derivatives	IEHD	Imports and sales of hydrocarbons and their derivatives in the internal market	Produced or imported volume	Natural or legal persons who import and sell the mentioned products	Specific rates by unit of measure to be updated annually.	None. ICE paid on products contained in hydrocarbons mix is tax credit that can by used as payment on account of this tax.
Specific Consumption Tax	ICE	Sales in the internal market and final imports of goods for ultimate consumption. Cigarettes and tobacco, motor vehicles, non-alcoholic beverages, beer, maize beer, alcoholic drinks.	Cigarettes, tobacco and motor vehicles: sale price. Beverages: produced or imported volume.	Independent or third party manufacturers and importers and legal or natural persons financially linked to the wholesale trade or distribution.	Cigarettes and tobacco:50%. Motor vehicles:16%. Alcoholic and non-alcoholic beverages: specific rates	Retailers
Tax on non-sale transfer of goods	TGB	Non-sale transfers of personal and real property, shares and goods that can be registered		Appraised value of the good or right transferred	Parents, children & spouse: 1%. Siblings and descendants: 10%. Joint inheritors, legatees:20%	Central government. Municipal Governments. Non-profit associations, foundations, or institutions (authorized). War veterans.

Tax on air flights with an international destination	ISAE	International air flights	Specific rate	All Bolivians and foreign residents who travel by plane to an international destination	Specific rate to be updated annually	Persons with diplomatic passport. Children under age of 2. War veterans
Complimentary Mining Tax	ICM	Mining extraction	Gross sale value.	Natural or legal persons who carry out prospecting, exploration, smelting, refining and or commercialization of minerals and metals.	Determined periodically based on the international price of each mineral	None.
Direct Tax on Hydrocarbons	IDH	Production	Production of hydrocarbons.	Natural or legal persons who produce hydrocarbons.	32% of hydrocarbons production at wellhead	None.
Tax on financial transactions	ITF	Financial transactions	Total amount withdrawn or transferred	Owners of savings and current accounts. Persons who make payments or transfer of funds. Persons who cash all types of checks	0.25%	Public accounts. Deposits or withdrawals by natural persons in national currency. Deposits or withdrawals by natural persons under 1000 US$. Transfers to Pension Funds accounts. Debit or credit to accounts belonging to financial institutions. Debit or credit to accounts belonging to ATM network administrators. Transfers made through accounts destined to tax payment, authorized by the National Tax Service.

Taxes on real estate property	IPBI	Ownership of real estate property	Appraised value of the real estate property	Owners of real estate property	Progressive, as a function of the appraised value of the real estate property. Between 0.35 and 1.5%	Real estate property owned by: Central Government, Non-profit associations, institutions and foundations, Diplomatic missions, Small plots of land, & real estate owned by small farming communities, Rural real estate not devoted to commercial or industrial activities. War veterans or widows. Hotels (50% discount on tax base value). Industrial buildings in El Alto for up to 3 years. Heritage buildings from Sucre (discounts between 30 & 70%)
Motor vehicle property tax	IPV	Ownership of motor vehicles	Customs value	Owners of motor vehicles	Progressive, as a function of the accrued value of the motor vehicle property. Between 1.5 and 5%	Vehicles owned by: Central Government, Diplomatic missions
Municipal Transfers Tax	IMT	Transfers of real estate property and vehicles	In case of real estate: Total amount of the transfer or fiscal value (whichever is higher). In case of motor vehicles: Total amount of the transfer or value (whichever is higher)	Owner, when it's a 2nd or subsequent sale	3% of the total amount of the transfer	

Source: National Tax Service Office (SIN)