

# **“Tax Administration in Developing Countries: Management in an Uncertain Environment”**

## **INTRODUCTION**

Managing uncertainty has been, for a while, a challenging task which merits considerable attention. It is against this background that an in-depth examination of tax management in an uncertain environment is critical to all tax administrations in the region. With the rapidly changing global economy, islands in the Caribbean face special challenges. We share a number of common features. These include remoteness and isolation, susceptibility to natural disasters and environmental changes, limited diversification and capacity, income volatility and limited or difficult access to external capital. Many of these factors contribute to this uncertain environment.

Most small states like the islands of the Caribbean, are more vulnerable and experience greater income volatility than larger states, and the sources of this vulnerability are often the result of many changes including those from outside the region. A good example of how external factors have a profound impact on developing countries is the results and consequences of the events of September 11, 2001 in U.S.A. The negative effect on tourism in many member states was of such that receipts from tourism were drastically reduced and the concomitant rise in unemployment.

The 2001 Annual Report of the Central Bank of Barbados revealed that by year-end 2001 there was an increase in the rate of unemployment, led by net decreases in employment in the tourism sector, as well as in construction and manufacturing sectors. The Barbados' economy contracted 2.7% in 2001. The Report further stated that this outturn, which reflected decreases in both the traded and non-traded sectors, contrasts with an increase of 3% in 2000 and an average annual rise of 2.9% since the 1990-1992 recessionary period.

## **General Management**

Management includes activities of planning, implementing, monitoring, and controlling. It involves using the minimum resources to achieve the desired goals of the organization. These resources include the physical plant, the surroundings, financial and human capital. A good management philosophy suggests that the challenge of all managers is to co-ordinate all these resources in such a manner as to keep the organization a viable and effective entity.

## **Tax Management**

Tax management is not different from any other kind of management. Its managers are entrusted with the responsibility of ensuring that adequate measures and systems are put in place to guarantee that the government collects taxes due to the State by taxpayers. Given the limited resources available, tax managers are required to use their management skills to maximize the use of these resources. Unlike management of a company, failure to properly manage a tax organization can have a serious impact on the entire country and its citizens. It is for this reason that management of a tax organization presents challenges unknown to some other organizations and institutions.

The leadership must create an atmosphere where people thrive on challenges, including uncertainty. Such a culture leads to some measure of success. The onus of creating this mindset is squarely on the top management of the organization. A vision and a strategy consistently articulated by the leader and a strong motivated top management team who shares that vision, are critical factors for survival in today's environment.

## **General Impact of Uncertainty**

The aura of uncertainty affects member states in different ways. It reveals itself through an uncertain GDP. It undermines investor confidence in the economy. The issuing of bank loans is affected. There is reduced employment; difficulty in collecting taxes; and a major reduction in tax revenues. It is known that any major reduction in tax revenues impacts on the level of social services provided by the state.

Uncertainty impacts on management of a tax organization in many ways. It forces management to make strategic choices, streamline operations to reduce costs and utilize resources to achieve greater efficiency in the organization. During these times, management is challenged to make difficult decisions. Resources allocated to the organization are reduced but the volume of work remains constant or may even increase. In addition, the expectation of the stakeholders namely the government and taxpayers remains the same. Regardless of the resources, deadlines still have to be met.

Another type of uncertainty that could have a severe impact is that of a political nature. Investors coming to the islands of the Caribbean are encouraged to make investments based on the confidence they have in the political system. Therefore, a stable political climate is always a positive sign to investors and potential investors. The countries of the Caribbean depend on investors to develop new businesses in order to provide employment opportunities for its people. Failure to obtain investment in a country has a negative impact on the revenue collected and hence the tax consequence. In addition, it is likely to undermine the social fabric of the country by creating unemployment and the myriad problems that such unemployment produces.

## **SPECIFIC ISSUES**

### **Natural Disasters**

The Caribbean is located in a hurricane zone. We are therefore vulnerable to hurricanes and storms that can cause massive destruction to property and dislocation to citizens and businesses. Some islands may also face the eruption of volcanoes, as in the case of Montserrat when the volcano erupted and practically dislocated the entire island. In the case of Belize, Antigua, Dominica, St. Lucia and St. Vincent, hurricanes destroyed crops affecting the revenue collecting capacity of these countries, not to mention the resources required to replace and rebuild after such natural disasters. **See Appendices 1 and 2 to observe the frequency of hurricanes in the region and the associated costs of hurricane Lenny in 1999.**

In such an environment our economies can face massive shocks when natural disasters force tax departments to operate in a situation where office buildings and equipment may be damaged. Tax managers, not only have to deal with revenue loss due to dislocation, but also taxpayers who may have their own personal problems to consider. Although we may never be able to predict the intensity of a natural disaster, we surely can be proactive in planning for such an eventuality. Ensuring that computers and their data are well secured is critical to the smooth functioning of the organization subsequent to a hurricane or a storm. These situations do have an impact on revenue loss for islands in the region.

## **External Factors**

A climate of uncertainty also creates an economic impact on the management of tax departments in the region. By reason of international obligations the islands are forced to dismantle certain barriers that formerly protected some of the products and services produced locally from external/extra-regional competition. Groupings such as the World Trade Organization (WTO) and the Free Trade Agreement of the Americas (FTAA) demand that they compete on the world stage with players who have the resources to produce cheaper goods and services and therefore are able to offer better prices.

Reference can be made to the recent struggle by the Windward Islands to have Europe purchase their bananas at a price above the Chiquita brand produced in Latin America. Small islands such as St. Vincent and St. Lucia are unable to produce bananas at competitive prices when compared to larger countries which have more resources, cheaper labour and whose industries may even be subsidized by their governments.

With the advent of this new global movement, tax managers will be asked by the government for advice on a number of issues ranging from the likely impact on various decisions on tax revenues to what legislative procedures are required to protect our revenue base. It is important that the manager at every level of the organization be an important figure, capable of solving problems and making decisions concerning unexpected situations. In addition, tax managers must be knowledgeable about the legal framework in which the organization operates.

## **Human Resources**

In an era of uncertainty, education is one area on which emphasis is required. Tax managers are currently facing enormous pressure to attract officers of a certain level to move their organizations forward in this changing age. Training of competent tax officers takes time and some of the trained officers are lured to the private sector by the offer of better salaries while other officers seek their fortunes outside the region. It would appear that more incentives would have to be offered to officers who have potential and who are desirous of working in the tax department of government. Clear career paths need to be set out so that young officers view the tax profession as a preferred career choice. Without a clear career path and a stated policy that makes the ability to do the job more important than the age or years of service of the officer, frustration will develop.

The tax officer has to keep abreast of what is happening locally, regionally and internationally. With the present environment, tax managers are challenged to guide their organization through this period of uncertainty. This can be done through appropriate training and educational opportunities. Tax managers themselves must also pursue educational opportunities in order to broaden their horizons and help them to understand and function in this changing and uncertain environment.

## **Technology and Service**

We live in information age, where computer technology and the internet are used to bring people and businesses closer. The same technology can be used to enhance the customer service offered by tax departments. For example, Barbados is actively pursuing the possibility of introducing electronic services, including electronic-filing. It is expected that this feature will enhance the services presently offered to taxpayers. Whenever possible, computers should be used to obtain information which would help management to make decisions. When information is required on a timely basis by tax managers the use of the computer will make this a reality.

In these times, tax administrators must ensure that all relevant information is provided to the taxpayer to improve voluntary compliance. Taxpayers must be accorded maximum courtesy and cooperation in their attempt to fulfil their tax obligations. Management has to expose officers to all levels of training which will not only enhance their technical skills but also their interpersonal skills. It is only through a process of education that officers will share the mission of the organization to provide optimum service to all taxpayers.

## **Planning**

Planning is an ongoing process that is vital especially during periods of uncertainty. It is even more critical at this time. Although long-term planning cannot be ignored, tax managers will find that short-term planning will occupy a lot of their energies. With things changing so rapidly, we have to adapt our strategies to fit the times.

A Strategic Plan for a tax department is essential. Given that the future is uncertain, management will always need to plan in order to develop the procedures and operations necessary to achieve the changing requirements. With a well-conceived strategic plan, tax managers will be more forward thinking in their approach in an era of uncertainty. The Barbados experience in the preparation of our Strategic Plan 2001-2006 reinforces the point that a strategic plan is an important document to guide any tax department on the way forward. It provides a mechanism to pool ideas from each level of the organization. Such collaboration and cooperation can only benefit the entire organization.

In the Barbados Inland Revenue Department Strategic Plan 2001-2006, one of the goals is to maximize the provision of services through technology. The objective is to be on the cutting edge of technology. To achieve this objective it was determined that specific actions are to be taken to implement electronic filing of taxpayers' returns and continue to develop and enhance current procedures and programs using technology wherever possible. Each action is given a time frame in which it is to be accomplished. The cost of each action was also estimated and persons/sections were given responsibility for the execution of each action. This type of planning is essential as it gives specific persons in the organization the responsibility to be accountable for the implementation or required change of actions as outlined in the Strategic Plan.

Adequate planning will help management to find the preferred way of achieving a particular objective. In addition, it allows the administration to examine areas that can be improved, including better use of resources available. For example, it may be recognized that joint assignments by tax collections agencies may be a better utilization of resources than for each organization to do an assignment independently.

Proper planning lends itself to more integration and synergies within the tax administration. Revenue collection is the main purpose of all tax departments. Therefore, any decision that will enhance that process should be examined.

It is also important to have early warning systems in place to pinpoint changes in the environment that will require an internal reorientation. There should be a section within the tax department where information of an external nature could be channelled and monitored. For example, if it is apparent that there will be a storm or hurricane in a country, this information should be sent to this section that in turn would provide the department with guidance and direction in the circumstances.

The section's activities should not be confined to natural disasters. Relevant Intelligence information should also be collected. With such information management can be proactive rather than reactive to situations. For example, if it is recognized that laws which may have a negative impact on tax revenues are being considered by countries from which most of the International Business Companies (IBCs) in the region originate, this information should be filtered through to management. In this way a determination can be made on what measures can be taken to safeguard any potential revenue loss.

Critical to this monitoring system is the availability of current information and its effects. Lectures and talks from the private sector or other government agencies could assist in this exercise. In Barbados, persons were invited to the department to speak on current issues including the World Trade Organisation (W.T.O.) and the impact of its decisions on trade in Barbados.

Flexibility, or the ability to adapt, is critical. Being flexible in approach demands that the organization has broad and directional plans. With adequate planning, including that for contingencies, the organization is better prepared to cope with most challenges which accompany periods of uncertainty.

## **OTHER FACET OF PROPER MANAGEMENT**

### **Innovation**

Developing states are usually slow in implementing new strategies and techniques to deal with old problems and old ways of doing business. In an era of uncertainty, we have to be innovative. We have to find new ways to do business. It is customary for persons to visit the tax department to pay their taxes and generally to ascertain details of outstanding amounts. Given the technology available, taxpayers should be able to access their account and have queries answered on line. Items such as allowances, balances, deadlines for filing and paying specific taxes, penalties and interest should all be answered on line. Information presented by the tax department to the public should be in a format that is simple, captivating and easy to understand.

Payments in electronic form must be accepted if the tax departments are to offer improved services to customers. Tax managers would be failing in their duties if they refuse to implement procedures and systems which make payment of taxes more customer- friendly. Furthermore, for the administration to gain the highest respect and public confidence, it is necessary to introduce innovative ideas and practices that will strengthen the entire collection process even in times of uncertainty.

## **POINTS TO REMEMBER**

### **What Must be Managed:**

- **Culture**
  - X Directs the organisation

## POINTS TO REMEMBER

### What Must be Managed: (cont'd)

- **Human Resources**
  - X Determine quality of decisions
- **Vigilance**
  - X Monitors positive and negative aspects
- **Planning Process**
  - X Facilitates resource allocation, strategies and flexibility
- **Policies and Procedures**
  - X Direct all activities
- **Technology**
  - X Improves information and decisions
- **Services**
  - X Encourage voluntary compliance

## CONCLUSION

The Caribbean is a region in which some member states depend heavily on tourism to earn foreign exchange. Others islands depend on agriculture in the form of sugar cane production, bananas, nutmeg and coffee to a lesser extent. What is common about this diversity is that each island must rethink its strategies to deal with the uncertainty of the times. Each island has to examine what is the best path to travel.

The strategies adopted by tax managers must recognize the global competition and the ability of small states to maintain some kind of equilibrium. Much is uncertain and strategies used must be adapted to existing conditions.

Regardless of our area of expertise, we are required to ensure that all resources under our management are working at full capacity. Productivity is the buzzword and it will be for sometime. We must be dynamic and proactive

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**APPENDIX 1**

	<b><u>NAME</u></b>	<b><u>YEAR</u></b>	<b><u>COUNTRIES AFFECTED</u></b>
1.	Hugo	1989	Montserrat
2.	Bret	1993	Trinidad & Tobago
3.	Cindy	1993	St. Maarten
4.	Debby	1994	St. Lucia
5.	Iris	1995	Barbados, Martinique, Guadeloupe, Antigua, St. Kitts
6.	Marilyn	1995	Barbados, U.S. Virgin Islands, Puerto Rico, Antigua, Martinique
7.	Luis	1995	Antigua, Montserrat, Guadeloupe, St. Maarten
8.	Cesar	1996	Nicaragua, Honduras, El Salvador, Curacao, Aruba
9.	Hortense	1996	Puerto Rico
10.	Georges	1998	U.S. Virgin Islands, Puerto Rico, Montserrat, Cuba, Dominican Republic, Haiti
11.	Mitch	1998	Honduras, Nicaragua, Belize, Guatemala, El Salvador, Costa Rica
12.	Jose	1999	Antigua, St. Maarten, Puerto Rico
13.	Lenny	1999	U.S. Virgin Islands, Antigua, Puerto Rico, Dutch St. Maarten, Guadeloupe, Martinique, St. Vincent, Grenada, entire Lesser Antilles
14.	Debbie	2000	British Virgin Islands
15.	Keith	2000	Belize
16.	Iris	2001	Belize
17.	Michelle	2001	Cuba

## APPENDIX 2

<b>PRELIMINARY ESTIMATES OF COSTS ASSOCIATED WITH HURRICANE LENNY ON CDERA PARTICIPATING STATES</b>		
<b>COUNTRY</b>	<b>EC\$ COSTS</b>	<b>US\$ COSTS</b>
Anguilla	\$199,350,000	\$75,226,415
Antigua and Barbuda	\$136,021,000	\$51,328,679
British Virgin Islands	\$ 13,668,787	\$ 5,158,033
Dominica	\$ 57,084,750	\$21,541,415
Grenada	\$250,000,000	\$94,339,623
Saint Lucia	\$ 17,437,000	\$ 6,580,000
St. Vincent and the Grenadines	\$ 33,421,250	\$12,611,792
Montserrat		
St. Kitts-Nevis	\$ 19,207,757	\$ 7,248,210
<b>TOTAL</b>	<b>\$726,190,544</b>	<b>\$274,034,167</b>

**SOURCES:**

1. 2001 Annual Report of Central Bank of Barbados
2. Caribbean Disaster Emergency Response Agency (CDERA)
3. Barbados Meteorology Services.

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